CORE PRINCIPLES OF INTERNATIONAL MARKETING



Babu John-Mariadoss
Texas Tech University

LibreTexts™

Texas Tech University

Core Principles of International Marketing

Babu John-Mariadoss

This text is disseminated via the Open Education Resource (OER) LibreTexts Project (https://LibreTexts.org) and like the thousands of other texts available within this powerful platform, it is freely available for reading, printing, and "consuming."

The LibreTexts mission is to bring together students, faculty, and scholars in a collaborative effort to provide an accessible, and comprehensive platform that empowers our community to develop, curate, adapt, and adopt openly licensed resources and technologies; through these efforts we can reduce the financial burden born from traditional educational resource costs, ensuring education is more accessible for students and communities worldwide.

Most, but not all, pages in the library have licenses that may allow individuals to make changes, save, and print this book. Carefully consult the applicable license(s) before pursuing such effects. Instructors can adopt existing LibreTexts texts or Remix them to quickly build course-specific resources to meet the needs of their students. Unlike traditional textbooks, LibreTexts' web based origins allow powerful integration of advanced features and new technologies to support learning.



LibreTexts is the adaptable, user-friendly non-profit open education resource platform that educators trust for creating, customizing, and sharing accessible, interactive textbooks, adaptive homework, and ancillary materials. We collaborate with individuals and organizations to champion open education initiatives, support institutional publishing programs, drive curriculum development projects, and more.

The LibreTexts libraries are Powered by NICE CXone Expert and was supported by the Department of Education Open Textbook Pilot Project, the California Education Learning Lab, the UC Davis Office of the Provost, the UC Davis Library, the California State University Affordable Learning Solutions Program, and Merlot. This material is based upon work supported by the National Science Foundation under Grant No. 1246120, 1525057, and 1413739.

Any opinions, findings, and conclusions or recommendations expressed in this material are those of the author(s) and do not necessarily reflect the views of the National Science Foundation nor the US Department of Education.

Have questions or comments? For information about adoptions or adaptions contact info@LibreTexts.org or visit our main website at https://LibreTexts.org.

This text was compiled on 05/05/2026

TABLE OF CONTENTS

Acknowledgements

Licensing

Dedication

Introduction

1: Introduction to International Marketing

- 1.1: Introduction to International Marketing Summary
- 1.2: Defining Marketing
- 1.3: Defining International Marketing
- 1.4: The Motivation for International Marketing
- 1.5: Stages in International Marketing
- 1.6: Why International Marketing Matters
- 1.7: Challenges of Global Marketing
- 1.8: What is Globalization
- 1.9: The Globalization Debate
- 1.10: Standardization and Customization

2: International Business and Trade

- 2.1: International Business and Trade Summary
- 2.2: International Trade
- 2.3: International Economic Cooperation among Nations
- 2.4: Understanding Tariffs
- 2.5: Regional Economic Integration
- 2.6: The United Nations and the Impact on Trade
- 2.7: Trade Controversies
- 2.8: Foreign Direct Investment

3: Social and Cultural Environment

- 3.1: Social and Cultural Environment Summary
- 3.2: Factors Shaping the Global Marketing Environment
- 3.3: The Social and Cultural Environment
- 3.4: Importance of Culture on Markets
- 3.5: What is Culture
- 3.6: Describing Culture
- 3.7: Marketing Across Cultures

4: The Economic and Political Environment

- 4.1: The Economic and Political Environment Summary
- 4.2: The Economic Environment
- 4.3: The Political Environment
- 4.4: Political Risk
- 4.5: Legal Risk

5: Economic Development in the World

- 5.1: Chapter 5- Economic Development in the World
- 5.2: World Economies
- 5.3: Classifying World Economies
- 5.4: Understanding the Developed World
- 5.5: The Developing World
- 5.6: Emerging Markets

6: Global Market Planning

- 6.1: Global Market Planning Summary
- 6.2: Measuring Market Attractiveness
- 6.3: Global Market Opportunity Assessment – PESTEL Analysis
- 6.4: Global Market Opportunity Assessment – CAGE Analysis
- 6.5: Global Market Opportunity Assessment – Scenario Planning and Analysis
- 6.6: Selecting the Countries to Enter
- 6.7: Global Market Segmentation
- 6.8: Using Demographics to Guide Global Marketing Strategy
- 6.9: Target Market Selection
- 6.10: Global Positioning
- 6.11: Basics of Positioning

7: Global Market Entry Modes

- 7.1: Global Market Entry Modes Summary
- 7.2: International Entry Modes
- 7.3: 7.02- Exporting
- 7.4: Licensing
- 7.5: Franchising
- 7.6: Contract Manufacturing
- 7.7: Joint Ventures

8: Global Products

- 8.1: Global Products Summary
- 8.2: Global Product Development
- 8.3: Global Products and Services
- 8.4: Product Adaptation Decisions
- 8.5: Global Innovation
- 8.6: Global Innovation at the BOP

9: Global Branding

- 9.1: Global Branding Summary
- 9.2: Formulating a Global Brand Strategy
- 9.3: Global Branding
- 9.4: Global Brand Structures
- 9.5: Determinants of Global Brand Structure
- 9.6: Managing Key Strategic Brands

10: Global Channels and Supply Chains

- 10.1: Global Channels and Supply Chains Summary
- 10.2: Basics of Distribution Channels
- 10.3: Global Supply Chains
- 10.4: Global Sourcing and Distribution
- 10.5: Organizing The Channel

11: Global Promotions

- 11.1: Global Promotions Summary
- 11.2: Changes in Promotion
- 11.3: Global Communication Platform
- 11.4: Global Communication Strategies

12: Global Pricing

- 12.1: Global Pricing Summary
- 12.2: Basics of Pricing
- 12.3: Introduction to Global Pricing
- 12.4: Global Pricing Approaches
- 12.5: Currency Fluctuations and Global Pricing
- 12.6: Tariffs and Global Pricing
- 12.7: Quotas and Dumping

13: The International Marketing Plan

- 13.1: Marketing Plan Basics
- 13.2: Writing the International Marketing Plan

Index

Glossary

Detailed Licensing

Welcome to the Business Library. This Living Library is a principal hub of the LibreTexts project, which is a multi-institutional collaborative venture to develop the next generation of open-access texts to improve postsecondary education at all levels of higher learning. The LibreTexts approach is highly collaborative where an Open Access textbook environment is under constant revision by students, faculty, and outside experts to supplant conventional paper-based books.

Licensing

*A detailed breakdown of this resource's licensing can be found in **Back Matter/Detailed Licensing**.*

Dedication

TO MY UNCLE AND AUNT

S. ARULANANDARAJ AND A. CHRISTIE THERESE

Introduction

‘Core Principles of International Marketing’ is my second Open Education Resources (OER) textbook effort, which follows my other OER textbook title ‘Core Principles of Marketing’, published in 2017. I have edited this book using own content, and content from a variety of OER sources, and under a Creative Commons Attribution NonCommercial ShareAlike license. This textbook can be used for an introductory level International Marketing course, and I encourage instructors teaching an undergraduate International Marketing course to adopt this textbook and provide me feedback on the content. Although the term ‘International Marketing’ has used throughout the book, the content will pretty much be as applicable if they are read in the context of a ‘Global Marketing’ course. Therefore, the textbook can also be used for an introductory level course in ‘Global Marketing’, and I encourage instructors of the undergraduate ‘Global Marketing’ course to adopt this textbook.

Although it is generally assumed that students will have already taken an introductory course in ‘International Business’ before enrolling into the introductory ‘International Marketing’ course, most undergraduate textbooks on International Marketing dedicate considerable space on discussing the basics of the International Business Environments. Therefore I have maintained the same focus while editing this textbook. I have also relaxed the generally held assumption that students will have prior exposure to the introductory principles of Marketing; therefore, this textbook also dedicates considerable space to introducing basic marketing concepts such as its definition, segmentation, positioning, pricing, etc., before applying them in an international context.

I thank the instructors and students who are using this textbook for their course. Please feel free to contact me with your comments and feedback on improving this textbook. If I make changes to this textbook based on your comments, they will be duly acknowledged for your contribution in making this better. Best wishes for a great semester!

CHAPTER OVERVIEW

1: Introduction to International Marketing

1.1: Introduction to International Marketing Summary
1.2: Defining Marketing
1.3: Defining International Marketing
1.4: The Motivation for International Marketing
1.5: Stages in International Marketing
1.6: Why International Marketing Matters
1.7: Challenges of Global Marketing
1.8: What is Globalization
1.9: The Globalization Debate
1.10: Standardization and Customization

This page titled 1: Introduction to International Marketing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

1.1: Introduction to International Marketing Summary

Marketing is an organizational function and a set of processes for creating, communicating, and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stakeholders. A company that engages in global marketing focuses resources on global market opportunities and threats. Successful global marketers such as Nestle, Coca-Cola, and Honda use familiar marketing mix elements – the four Ps – to create global marketing programs.

Marketing, R&D, manufacturing, and other activities comprise a firm's value chain; the value equation (V =B/P) expresses the relationship between values and the marketing mix.

Global companies also maintain strategic focus while pursuing competitive advantage. The marketing mix, value chain, competitive advantage, and focus are universal in their applicability, irrespective of whether a company does business only in the home country or has a presence in many markets around the world. However, in a global industry, companies that fail to pursue global opportunities risk being pushed aside by stronger global competitors.

A firm's global marketing strategy (GMS) can enhance its worldwide performance. The GMS addresses several issues. First is nature of the marketing program in terms of the balance between a standardization (extension) approach to the marketing mix and a localization (adaptation) approach that is responsive to country or regional differences. Second is the concentration of marketing activities in a few countries or the dispersal of such activities across many countries. Companies that engage in global marketing can also engage in coordination of marketing activities. Finally, a firm's GMS will address the issue of global market participation.

The importance of global marketing today can be seen in the company rankings compiled by the Wall Street Journal, Fortune, Financial Times, and other publications. Whether ranked by revenues, market capitalization, or some other measure, most of the world's major corporations are active regionally or globally. The size of global markets for individual industries or product categories helps explain why companies "go global". Global markets for some product categories represent hundreds of billions of dollars in annual sales; other markets are much smaller. Whatever the size of the opportunity, successful industry competitors find that increasing revenues and profits means seeking markets outside the home country.

Company management can be classified in terms of its orientation toward the world: ethnocentric, polycentric, regiocentric, or geocentric. The terms reflect progressive levels of development or evolution. An ethnocentric orientation characterizes domestic and international companies; international companies pursue marketing opportunities outside the home market by extending various elements of the marketing mix. A polycentric worldview predominates at a multinational company, where the marketing mix is adapted by country managers operating autonomously. Managers at global and transnational companies are regiocentric or geocentric in their orientation and pursue both extension and adaptation strategies in global markets.

The dynamic interplay of several driving and restraining forces shapes the importance of global marketing. Driving forces include market needs and wants, technology, transportation and communication improvements, product costs, quality, world economic trends, and recognition of opportunities to develop leverage by operating globally. Restraining forces include market differences, management myopia, organizational culture, and national controls such as nontariff barriers (NTBs).

Source

The above note was adapted from the course note from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM). 'Introduction to Global Marketing' is Copyright (c) by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license

This page titled 1.1: Introduction to International Marketing Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

1.2: Defining Marketing

Learning Objectives

After reading this section, students should be able to …

1. Recall the definition of 'Marketing' learned in their previous marketing courses.

While we are attempting to understand and define International Marketing, it may help to go back to our basic definitions of 'Marketing', and the concepts that we learned in one of our introductory marketing courses.

Noted Harvard Professor of Business Theodore Levitt, states that the purpose of all business is to "find and keep customers". Furthermore, the only way you can achieve this objective is to create a competitive advantage. That is, you must convince buyers (potential customers) that what you have to offer them comes closest to meeting their particular need or want at that point in time. Hopefully, you will be able to provide this advantage consistently, so that eventually the customer will no longer consider other alternatives and will purchase your product out of habit. This loyal behavior is exhibited by people in the US who drive only Fords, brush their teeth only with Crest, buy only Dell computers, and have their plumbing fixed only by "Samson Plumbing—On Call 24 hours, 7 days a week". Creating this blind commitment—without consideration of alternatives—to a particular brand, store, person, or idea is the dream of all businesses. It is unlikely to occur, however, without the support of an effective marketing program. In fact, the specific role of marketing is to provide assistance in identifying, satisfying and retaining customers.

While the general tasks of marketing are somewhat straightforward, attaching an acceptable definition to the concept has been difficult. A textbook writer once noted, "Marketing is not easy to define. No one has yet been able to formulate a clear, concise definition that finds universal acceptance". Yet a definition of some sort is necessary if we are to lay out the boundaries of what is properly to be considered "marketing". How do marketing activities differ from non-marketing activities? What activities should one refer to as marketing activities? What institutions should one refer to as marketing institutions?

Marketing is advertising to advertising agencies, events to event marketers, knocking on doors to salespeople, direct mail to direct mailers. In other words, to a person with a hammer, everything looks like a nail. In reality, marketing is a way of thinking about business, rather than a bundle of techniques. It is much more than just selling stuff and collecting money. It is the connection between people and products, customers and companies. Like organic tissue, this kind of connection—or relationship—is always growing or dying. It can never be in a steady state. And like tissue paper, this kind of connection is fragile. Customer relationships, even long-standing ones, are contingent on the last thing that happened.

Tracing the evolution of the various definitions of marketing proposed during the last thirty years reveals two trends: (1) expansion of the application of marketing to non-profit and non-business institutions; e.g. charities, education, or health care; and (2) expansion of the responsibilities of marketing beyond the personal survival of the individual firm, to include the betterment of society as a whole. These two factors are reflected in the official American Marketing Association definition published in 1988.

"Marketing is the process of planning and executing the conception. pricing, promotion, and distribution of ideas, goods, and services to create exchanges that satisfy individual (customer) and organizational objectives."

While this definition can help us better comprehend the parameters of marketing, it does not provide a full picture. Definitions of marketing cannot flesh out specific transactions and other relationships among these elements. The following propositions are offered to supplement this definition and better position marketing within the firm.

The overall directive for any organization is the mission statement or some equivalent statement of organizational goals. It reflects the inherent business philosophy of the organization.

Every organization has a set of functional areas (e.g. accounting, production, finance, data processing, marketing) in which tasks that are necessary for the success of the organization are performed. These functional areas must be managed if they are to achieve maximum performance.

Every functional area is guided by a philosophy (derived from the mission statement or company goals) that governs its approach toward its ultimate set of tasks.

Marketing differs from the other functional areas in that its primary concern is with exchanges that take place in markets, outside the organization (called a transaction).

Marketing is most successful when the philosophy, tasks, and manner of implementing available technology are coordinated and complementary.

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at http://cnx.org/contents/6fdb38de-3019-4843-8ffd-2b204bc45c29@4

Section 1.1 Defining Marketing is also adapted from the chapter section of the same title appearing in 'Chapter 1: What is Marketing?' of the textbook 'Principles of Marketing,' authored by University of Minnesota Libraries Publishing edition, 2015 – this book was adapted from a work originally produced in 2010 by a publisher who has requested that it not receive attribution.

The following changes were made to the most recent edition: Created new title for Figure 1.1: Marketing activities; Created new title for Figure 1.2: Creating Offerings That Have Value – BMW versus CRV; Created new title for Figure 1.3: Creating Offerings That Have Value – Social media sites; Added learning objectives.

This page titled 1.2: Defining Marketing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

1.3: Defining International Marketing

Learning Objectives

After reading this section, students should be able to …

1. Extend the definition of 'Marekting' to 'International Marketing'
2. Define 'International Marketing'

Case: Toyota has a vehicle for every market

Each market has unique cultural characteristics and contextual circumstances that must be considered. For example, in the United States roads tend to be wide; highways can accommodate a broad array of vehicles with a high number of lanes, and people demand a mix of cars based on their needs. Conversely, in Europe roads tend to be narrow, and the market demands smaller, more fuel-efficient vehicles. Therefore, while a Toyota 4Runner tends to sell extremely well in the United States, it would not be a very popular model in Europe for these very reasons. As a result, Toyota invests billions of dollars every year into market research and market development to make sure they meet the needs and wants of its customers, in each specific country that they sell their vehicles in. This has led to Toyota's success in the US automotive market, as our earlier case suggested. With their #1 selling sedan, Toyota Camry, a wide array of hybrid models, trucks, and SUVs to meet the United States constantly-changing expectations, Toyota is, arguably, the strongest player in the automotive industry.

Now that the world has entered the next millennium, we are seeing the emergence of an interdependent global economy that is characterized by faster communication, transportation, and financial flows, all of which are creating new marketing opportunities and challenges. Given these circumstances, it could be argued that companies face a deceptively straightforward and stark choice: they must either respond to the challenges posed by this new environment or recognize and accept the long-term consequences of failing to do so. This need to respond is not confined to firms of a certain size or particular industries. It is a change that to a greater or lesser extent will ultimately affect companies of all sizes in virtually all markets. The pressures of the international environment are now so great, and the bases of competition within many markets are changing so fundamentally, that the opportunities to survive with a purely domestic strategy are increasingly limited to small and medium-sized companies in local niche markets.

Perhaps partly because of the rapid evolution of international marketing, a vast array of terms have emerged that suggest various facets of international marketing. Clarification of these terms is a necessary first step before we can discuss this topic more thoroughly.

Let us begin with the assumption that the marketing process that you have learned in any basic marketing course is just as applicable to domestic marketing as to international marketing. In both markets, we are goal-driven, do necessary marketing research, select target markets, employ the various tools of marketing (i.e. product, pricing, distribution, communication), develop a budget, and check our results. However, the uncontrollable factors such as culture, social, legal, and economic factors, along with the political and competitive environment, all create the need for a myriad of adjustments in the marketing management process.

One of the inevitable questions that surfaces concerning international marketing are: how does international marketing truly differ from domestic marketing, if at all? There has historically been much discussion over commonalities and differences between global and domestic marketing, but the three most common points of view upon which scholars agree are the following. First, all marketing is about the formulation and implementation of the basic policies known as the 4 P's: Product, Price, Place, and Promotion. Second, international marketing, unlike domestic marketing, is understood to be carried out "across borders". Third, international marketing is not synonymous with international trade (Perry, 1990). Perhaps the best way to distinguish between the two is simply to focus on the textbook definition of international marketing. One comprehensive definition states that, "international marketing means identifying needs and wants of customers in different markets and cultures, providing products, services, technologies, and ideas to give the firm a competitive marketing advantage, communicating information about these products and services and distributing and exchanging them internationally through one or a combination of foreign market entry modes" (Bradley, 2005)

At its simplest level, international marketing involves the firm in making one or more marketing decisions across national boundaries. At its most complex, it involves the firm in establishing manufacturing and marketing facilities overseas and coordinating marketing strategies across markets. Thus, how international marketing is defined and interpreted depends on the level of involvement of the company in the international marketplace.

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at http://cnx.org/contents/6fdb38de-3019-4843-8ffd-2b204bc45c29@4

This page titled 1.3: Defining International Marketing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

1.4: The Motivation for International Marketing

Learning Objectives

After reading this section, students should be able to …

1. appreciate why firms enter international markets
2. explain why firms may want to avoind entering international markets

Reasons for entering international markets

Many marketers have found the international marketplace to be extremely hostile. A study by Baker and Kynak, for example, found that less than 20 per cent of firms in Texas with export potential actually carried out business in international markets. But although many firms view in markets with trepidation, others still make the decision to go international. Why?

In one study, the following motivating factors were given for initiating overseas marketing involvement (in order of importance):

- large market size
- stability through diversification
- profit potential
- unsolicited orders
- proximity of market
- excess capacity
- offer by foreign distributor
- increasing growth rate
- smoothing out business cycles

Other empirical studies over a number of years have pointed to a wide variety of reasons why companies initiate international involvement. These include the saturation of the domestic market, which leads firms either to seek other less competitive markets or to take on the competitor in its home markets; the emergence of new markets, particularly in the developing world; government incentives to export; tax incentives offered by foreign governments to establish manufacturing plants in their countries in order to create jobs; the availability of cheaper or more skilled labor; and an attempt to minimize the risks of a recession in the home country and spread risk.

Reasons to avoid international markets

Despite attractive opportunities, most businesses do not enter foreign markets. The reasons given for not going international are numerous. The biggest barrier to entering foreign markets is seen to be a fear by these companies that their products are not marketable overseas, and a consequent preoccupation with the domestic market. The following points were highlighted by the findings in the previously mentioned study by Barker and Kaynak, who listed the most important barriers:

- too much red tape
- trade barriers
- transportation difficulties
- lack of trained personnel
- lack of incentives
- lack of coordinated assistance
- unfavorable conditions overseas
- slow payments by buyers
- lack of competitive products
- payment defaults
- language barriers

It is the combination of these factors that determines not only whether companies become involved in international markets, but also the degree of any involvement.

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at http://cnx.org/contents/6fdb38de-3019-4843-8ffd-2b204bc45c29@4

This page titled 1.4: The Motivation for International Marketing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

1.5: Stages in International Marketing

Learning Objectives

After reading this section, students should be able to …

1. define domestic marketing, international marketing, export marketing, multinational marketing, and global marketing
2. explain the difference between domestic marketing, international marketing, export marketing, multinational marketing, and global marketing

Earlier in our discussion on definitions, we identified several terms that relate to how committed a firm is to being international. Here we expand on these concepts and explain the rationale behind this process. Two points should be noted. First, the process tends to be ranked in order of "least risk and investment" to "greatest involvement". Second, these are not necessarily sequential steps, even though exporting is apparently most common as an initial entry.

Firms typically approach involvement in international marketing rather cautiously, and there appears to exist an underlying lifecycle that has a series of critical success factors that change as a firm moves through each stage. For small and medium-sized firms, in particular, exporting remains the most promising alternative to a full-blooded international marketing effort, since it appears to offer a degree of control over risk, cost, and resource commitment. Indeed, exporting, especially by the smaller firms, is often initiated as a response to an unsolicited overseas order-these are often perceived to be less risky. Therefore, the following possibilities exist:

Domestic marketing.

This involves the company manipulating a series of controllable variables, such as price, advertising, distribution, and the product, in a largely uncontrollable external environment that is made up of different economic structures, competitors, cultural values, and legal infrastructure within specific political or geographic country boundaries.

International marketing.

This involves the company operating across several markets in which not only do the uncontrollable variables differ significantly between one market and another, but the controllable factor in the form of cost and price structures, opportunities for advertising, and distributive infrastructure are also likely to differ significantly.

Export marketing.

In this case the firm markets its goods and/or services across national/political boundaries. In general, exporting is a simple and low risk-approach to entering foreign markets. Firms may choose to export products for several reasons. First, products in the maturity stage of their domestic life cycle may find new growth opportunities overseas, as Perrier chose to do in the US. Second, some firms find it less risky and more profitable to expand by exporting current products instead of developing new products. Third, firms who face seasonal domestic demand may choose to sell their products to foreign markets when those products are "in season" there. Finally, some firms may elect to export products because there is less competition overseas.

A firm can export its products in one of three ways: indirect exporting, semi-direct exporting, and direct exporting. Indirect exporting is a common practice among firms that are just beginning their exporting. Sales, whether foreign or domestic, are treated as domestic sales. All sales are made through the firm's domestic sales department, as there is no export department. Indirect exporting involves very little investment, as no overseas sales force or other types of contacts need to be developed. Indirect exporting also involves little risk, as international marketing intermediaries have knowledge of markets and will make fewer mistakes than sellers.

In semi-direct exporting, an American exporter usually initiates the contact through agents, merchant middlemen, or other manufacturers in the US. Such semi-direct exporting can be handled in a variety of ways: (a) a combination export manager, a domestic agent intermediary that acts as an exporting department for several noncompeting firms; (b) the manufacturer's export agent (MEA) operates very much like a manufacturer's agent in domestic marketing settings; (c) a Webb-Pomerene Export Association may choose to limit cooperation to advertising, or it may handle the exporting of the products of the association's

members and; (d) piggyback exporting, in which one manufacturer (carrier) that has export facilities and overseas channels of distribution handles the exporting of another firm (rider) noncompeting but complementary products.

When direct exporting is the means of entry into a foreign market, the manufacturer establishes an export department to sell directly to a foreign film. The exporting manufacturer conducts market research, establishes physical distribution, and obtains all necessary export documentation. Direct exporting requires greater investment and also carries a greater risk. However, it also provides greater potential return and greater control of its marketing program.

Multinational marketing.

Here the marketing activities of an organization include activities, interests, or operations in more than one country, and where there is some kind of influence or control of marketing activities from outside the country in which the goods or services will actually be sold. Each of these markets is typically perceived to be independent and a profit center in its own right.

Global marketing.

The entire organization focuses on the selection and exploration of global marketing opportunities and marshals resources around the globe with the objective of achieving a global competitive advantage. The primary objective of the company is to achieve synergy in the overall operation, so that by taking advantage of different exchange rates, tax rates, labor rates, skill levels, and market opportunities, the organization as a whole will be greater than the sum of its parts.

Thus Toyota Motors started out as a domestic marketer, eventually exported its cars to a few regional markets, grew to become a multinational marketer, and today is a true global marketer, building manufacturing plants in the foreign country as well as hiring local labor, using local ad agencies, and complying to that country's cultural mores. As it moved from one level to the next, it also revised attitudes toward marketing and the underlying philosophy of business.

Ultimately, the successful marketer is the one who is best able to manipulate the controllable tools of the marketing mix within the uncontrollable environment. The principal reason for failure in international marketing results from a company not conducting the necessary research, and as a consequence, misunderstanding the differences and nuances of the marketing environment within the country that has been targeted.

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at http://cnx.org/contents/6fdb38de-3019-4843-8ffd-2b204bc45c29@4

This page titled 1.5: Stages in International Marketing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

1.6: Why International Marketing Matters

Learning Objectives

After reading this section, students should be able to …

1. explain why international marketing matters to firms and marketing managers

Why It Matters

Suppose you're in the marketing department for a highly successful snack food company in the U.S. You're in a brainstorming meeting about expanding into China, and the discussion is starting to get heated. Should you lead with your company's best-selling nacho-cheese-flavored snacks to take China by storm? Or would it be better to start out with the ranch-dressing-flavored snack instead, because it's so quintessentially American and it'd be a great way to introduce the Chinese to the tastes Americans love?

Or would something else be a better fit?

It's time to vote: your manager wants everyone on the team to name the flavor they want to lead with. What are you going to choose?

Set aside your top pick while you watch this short but very interesting video.



Video:https://youtu.be/BA8bCNiKZsg

You can read a transcript of the video **here**.

So . . . how did you do? How close did you come to favorite flavors in the video? Were you in the ballpark? Are you ready for a career developing snack foods for global markets?

If you're like most Americans, your recommendation probably wasn't very close to the mark, and you're probably thinking that many of the flavors that are delicious to Chinese consumers sound a bit odd to you. Well, now you know how a lot of Chinese consumers probably feel when presented with Cheetos Crunchy Flamin' Hot Limon Cheese Flavored Snacks or Zapp's Spicy Cajun Crawtator potato chips. A little queasy.

Hopefully this scenario helps highlight some of the challenges of global marketing, as companies start selling products in other countries. How should you enter a new market? Are you offering products that consumers in other countries will want to buy? What should you do to make sure your product–and the rest of your marketing mix–is a good fit for the global customers you want to attract?

Global marketing is a complex and fascinating business. The rest of the sections will introduce key challenges, opportunities, and factors to consider when marketing to target audiences outside your home country.

Source

The above content was adapted from textbook content provided by: Lumen Learning. License: CC BY: Attribution, titled “Why It Matters: Marketing Globally”. CC LICENSED CONTENT, SHARED PREVIOUSLY

Chinese Flavors for American Snacks. Provided by: BBC. Located at: https://youtu.be/BA8bCNiKZsg. License: CC BY-NC-ND: Attribution-NonCommercial-NoDerivatives

---

This page titled 1.6: Why International Marketing Matters is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

1.7: Challenges of Global Marketing

Learning Objectives

After reading this section, students should be able to …

1. appreciate the challenges and opportunities presented by global markets
2. explain the challenges and opportunities presented by globalization

A global company is generally referred to as a multinational corporation (MNC). An MNC is a company that operates in two or more countries, leveraging the global environment to approach varying markets in attaining revenue generation. These international operations are pursued as a result of the strategic potential provided by technological developments, making new markets a more convenient and profitable pursuit both in sourcing production and pursuing growth.

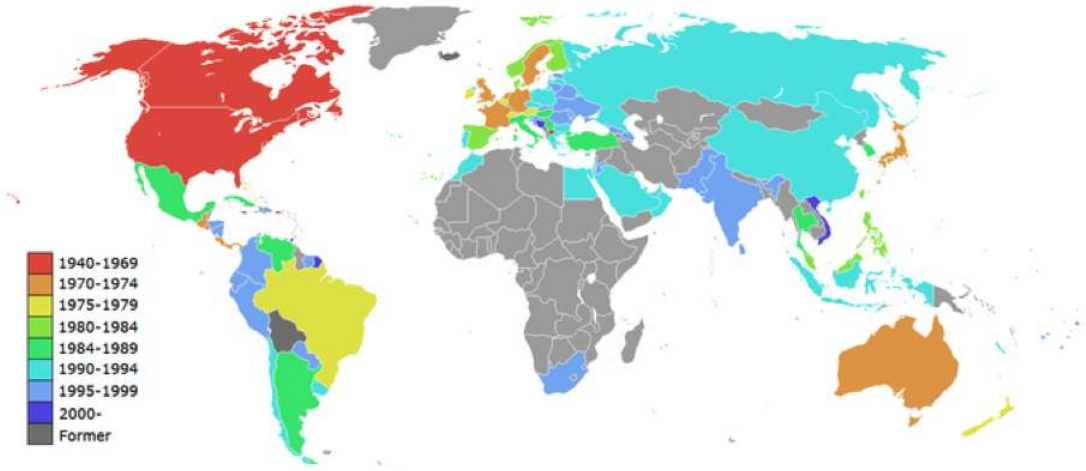


Figure 1.7.1: McDonald's Locations: Over the last 70 years, McDonald's has become a global corporation. (CC-BY-SA; Wikimedia)

*McDonald's Locations: Over the last 70 years, McDonald's has become a global corporation.*International operations are therefore a direct result of either achieving higher levels of revenue or a lower cost structure within the operations or value-chain. MNC operations often attain economies of scale, through mass producing in external markets at substantially cheaper costs, or economies of scope, through horizontal expansion into new geographic markets. If successful, these both result in positive effects on the income statement (either larger revenues or stronger margins), but contain the innate risk in developing these new opportunities.

Opportunities

As gross domestic product (GDP) growth migrates from mature economies, such as the US and EU member states, to developing economies, such as China and India, it becomes highly relevant to capture growth in higher growth markets. It is a particularly strong visual representation of the advantages a global corporation stands to capture, where the darker green areas reppresent where the highest GDP growth potential resides. High growth in the external environment is a strong opportunity for most incumbents in the market.

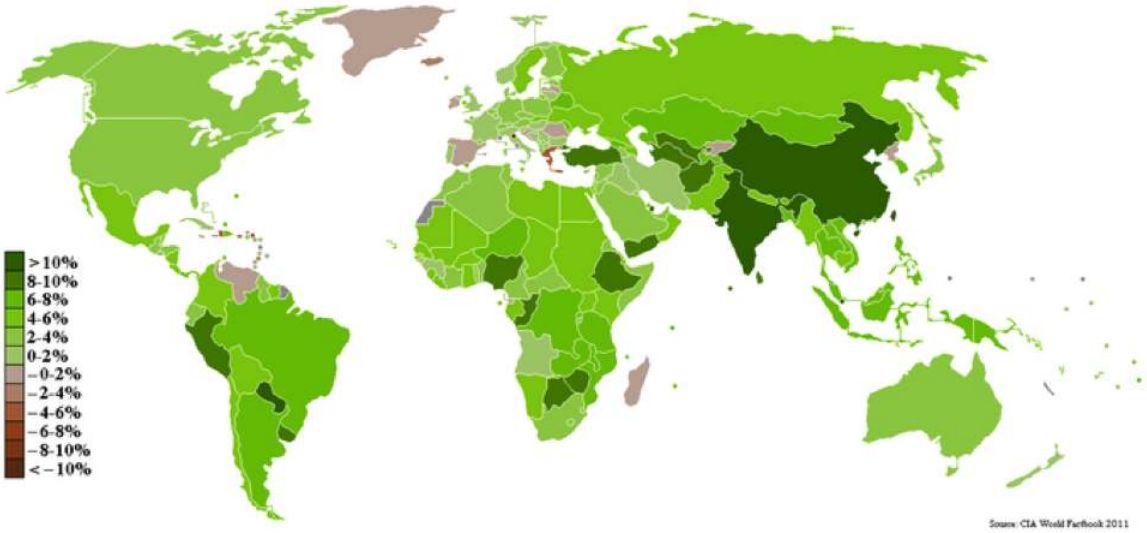


Figure 1.7.2: **GDP Growth Rate**: This map highlights (via dark green) where the strongest growth opportunities currently are as of 2010.. (CC-BY-SA; (CC-BY-SA, Wikimedia)

Challenges

However, despite the general opportunities a global market provides, there are significant challenges MNCs face in penetrating these markets. These challenges can loosely be defined through four factors:

- Public Relations: Public image and branding are critical components of most businesses. Building this public relations potential in a new geographic region is an enormous challenge, both in effectively localizing the message and in the capital expenditures necessary to create momentum.
- Ethics: Arguably the most substantial of the challenges faced by MNCs, ethics have historically played a dramatic role in the success or failure of global players. For example, Nike had its brand image hugely damaged through utilizing ‘sweat shops’ and low wage workers in developing countries. Maintaining the highest ethical standards while operating in developing countries is an important consideration for all MNCs.
- Organizational Structure: Another significant hurdle is the ability to efficiently and effectively incorporate new regions within the value chain and corporate structure. International expansion requires enormous capital investments in many cases, along with the development of a specific strategic business unit (SBU) in order to manage these accounts and operations. Finding a way to capture value despite this fixed organizational investment is an important initiative for global corporations.
- Leadership: The final factor worth noting is attaining effective leaders with the appropriate knowledge base to approach a given geographic market. There are differences in strategies and approaches in every geographic location worldwide, and attracting talented managers with high intercultural competence is a critical step in developing an efficient global strategy.

Combining these four challenges for global corporations with the inherent opportunities presented by a global economy, companies are encouraged to chase the opportunities while carefully controlling the risks to capture the optimal amount of value. Through effectively maintaining ethics and a strong public image, companies should create strategic business units with strong international leadership in order to capture value in a constantly expanding global market.

Globalization

Opportunities

Those in favor of globalization theorize that a wider array of products, services, technologies, medicines, and knowledge will become available and that these developments will have the potential to reach significantly larger customer bases. This means larger volumes of sales and exchange, larger growth rates in GDP, and more empowerment of individuals and political systems through acquiring additional resources and capital. These benefits of globalization are viewed as utilitarian, providing the best possible benefits for the largest number of people.

Challenges

Along with arguments supporting the benefits of a more globally-connected economy, there are criticisms that question the profits that are captured. Opponents argue that the expansion of global trade creates unfair exchanges between larger and smaller economies, arguing that developed economies capture significantly more value because of financial leverage. Other commonly raised concerns include damage to the environment, decreased food safety, unethical labor practices in sweatshops, increased consumerism, and the weakening of traditional cultural values.

Source

The above content was adapted from textbook content provided by: Lumen Learning. License: CC BY: Attribution, titled "Introduction to Global Marketing".

CC LICENSED CONTENT, SHARED PREVIOUSLY

- Curation and Revision. **Provided by**: Boundless.com. **License**: CC BY-SA: Attribution-ShareAlike

CC LICENSED CONTENT, SPECIFIC ATTRIBUTION

- Globalization. **Provided by**: Wikipedia. **Located at**: http://en.Wikipedia.org/wiki/Globalization. **License**: CC BY-SA: Attribution-ShareAlike
- Multinational corporation. **Provided by**: Wikipedia. **Located at**: http://en.Wikipedia.org/wiki/Multinational_corporation. **License**: CC BY-SA: Attribution-ShareAlike
- International marketing. **Provided by**: Dropbox. **Located at**: http://dl.dropbox.com/u/31779972/Introducing%20Marketing.pdf. **License**: CC BY: Attribution
- Mcdonalds World locations. **Provided by**: Wikimedia Commons. **Located at**: http://commons.wikimedia.org/wiki/File:Mcdonalds_World_locations_map.PNG. **License**: CC BY-SA: Attribution-ShareAlike
- Provided by: Wikimedia. **Located at**: http://upload.wikimedia.org/Wikipedia/commons/e/e7/GDP_real_growth_rate_CIA_Factbook.PNG. **License**: **CC BY-SA: Attribution-ShareAlike**
- Competitive advantage. **Provided by**: Wiktionary. **Located at**: http://en.wiktionary.org/wiki/competitive_advantage. **License**: CC BY-SA: Attribution-ShareAlike
- Introducing Marketing by John Burnett. **Provided by**: Global Text Project. **Located at**: https://dl.dropboxusercontent.com/u/31779972/Introducing%20Marketing.pdf. **License**: CC BY: Attribution
- World Trade Organization. **Provided by**: Wikimedia. **Located at**: http://upload.wikimedia.org/Wikipedia/commons/3/32/WTO_map_2005en.png. **License**: CC BY-SA:
- Attribution-ShareAlike

This page titled 1.7: Challenges of Global Marketing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

1.8: What is Globalization

Learning Objectives

After reading this section, students should be able to …

1. list the elements of economic globalization
2. explain the positive and negative effects of globalization

Case: United States Domestic Automaker, Ford

Nowhere are the effects of globalization seen more drastically than in the automobile industry, especially for the United States "Big 3" automakers: General Motors, Chrysler, and Ford.

Ford's history dates back to the Model T created by Henry Ford, with the goal of building a car for every family. Today, Ford is in dire competition with not only their domestic competitors, but also now foreign car manufacturers such as Toyota, Volkswagen and Hyundai.

At the current pace, the automotive market is approaching a 50/50 split between United States and overseas-based control of the US market. As a result, Ford is challenged to constantly reevaluate and revamp its market strategy. This is evident, as Ford decided that it was more cost-effective to buy existing networks than to start from scratch, by bringing Jaguar, Volvo, Mazda, Aston Martin and Land Rover under its control. However, Ford has recently decided to sell its stake in both Jaguar and Land Rover to the Indian automaker, Tata, and may divest other divisions as well.

Today, Ford faces a number of important questions. As the globalization of the auto industry continues, how should Ford market its vehicles? What target markets should Ford appeal to? How can it continue to improve production and quality and adhere to the needs of even more demanding customers? And, how should Ford position itself, as a company, in the face of formidable competition?

While the future of Ford is uncertain, one thing is clear, globalization will continue to affect the way domestic and foreign companies do business.

Globalization is difficult to define because it has many dimensions—economic, political, cultural and environmental. The focus here is on the economic dimension of globalization. Economic globalization refers to the "quickly rising share of economic activity in the world [that] seems to be taking place between people in different countries" (World Bank Briefing Paper, 2001). More specifically, economic globalization is the result of the increasing integration of economies around the world, particularly through trade and financial flows and the movement of people and knowledge across international borders (IMF Issue Brief, 2000).

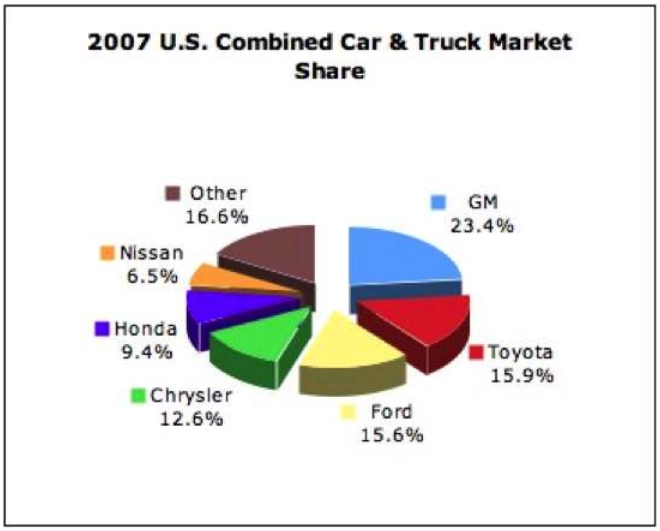


Figure 1.8.1: Global Market Share, 2007-2008 (Edmunds.com, 2007)

As this figure suggests, the “Big Three” must adapt to changes in the market and globalization factors to remain key players in the automotive market. At one point in 2007, for the first time in history, US automaker’s share of their home market fell below 50 percent.

Elements of economic globalization

The growth in cross-border economic activities takes five principal forms: (1) international trade; (2) foreign direct investment; (3) capital market flows; (4) migration (movement of labor); and (5) diffusion of technology (Stiglitz, 2003).

International trade:

An increasing share of spending on goods and services is devoted to imports and an increasing share of what countries produce is sold as exports. Between 1990 and 2001, the percentage of exports and imports in total economic output (GDP) rose from 32.3 per cent to 37.9 per cent in industrialized countries, and from 33.8 per cent to 48.9 per cent in low and middle-income countries (World Briefing Paper, 2001). In the 1980s, about 20 per cent of industrialized countries’ exports went to less industrialized countries; today, this share has risen to about 25 per cent, and it appears likely to exceed 33 per cent by 2010 (Qureshi, 1996).

The importance of International trade lies at the root of a country’s economy. In the constant changing business market, countries are now more interdependent than ever on their partners for exporting, importing, thereby keeping the home country’s economy afloat and healthy. For example, China’s economy is heavily dependent on the exportation of goods to the United States, and the United States customer base who will buy these products.

Foreign Direct Investment (FDI):

According to the United Nations, FDI is defined as “investment made to acquire lasting interest in enterprises operating outside of the economy of the investor”.

Direct investment in constructing production facilities, is distinguished from portfolio investment, which can take the form of short-term capital flows (e.g. loans), or long-term capital flows (e.g. bonds) (Stiglitz, 2003). Since 1980, global flows of foreign direct investment have more than doubled relative to GDP (World Briefing, Paper, 2001).

Capital market flows:

In many countries, particularly in the developed world, investors have increasingly diversified their portfolios to include foreign financial assets, such as international bonds, stocks or mutual funds, and borrowers have increasingly turned to foreign sources of funds (World Briefing, Paper, 2001). Capital market flows also include remittances from migration, which typically flow from industrialized to less industrialized countries. In essence, the entrepreneur has a number of sources for funding a business.

Migration:

Whether it is physicians who emigrate from India and Pakistan to Great Britain or seasonal farm workers emigrating from Mexico to the United States, labor is increasingly mobile. Migration can benefit developing economies when migrants who acquired education and know-how abroad return home to establish new enterprises. However, migration can also hurt the economy through “brain drain”, the loss of skilled workers who are essential for economic growth (Stiglitz, 2003).

Diffusion of technology:

Innovations in telecommunications, information technology, and computing have lowered communication costs and facilitated the cross-border flow of ideas, including technical knowledge as well as more fundamental concepts such as democracy and free markets (Stiglitz, 2003). The rapid growth and adoption of information technology, however, is not evenly distributed around the world—this gap between the information technology is often referred to as the “digital divide”.

As a result, for less industrialized countries this means it is more difficult to advance their businesses without the technical system and knowledge in place such as the Internet, data tracking, and technical resources already existing in many industrialized countries.

Negative effects of globalization for developing country business

Critics of global economic integration warn that: (Watkins, 2002, Yusuf, 2001)

- the growth of international trade is exacerbating income inequalities, both between and within industrialized and less industrialized nations
- global commerce is increasingly dominated by transnational corporations which seek to maximize profits without regard for the development needs of individual countries or the local populations
- protectionist policies in industrialized countries prevent many producers in the Third World from accessing export markets;
- the volume and volatility of capital flows increases the risks of banking and currency crises, especially in countries with weak financial institutions
- competition among developing countries to attract foreign investment leads to a “race to the bottom” in which countries dangerously lower environmental standards
- cultural uniqueness is lost in favor of homogenization and a “universal culture” that draws heavily from American culture

Critics of economic integration often point to Latin America as an example where increased openness to international trade had a negative economic effect. Many governments in Latin America (e.g. Peru) liberalized imports far more rapidly than in other regions. In much of Latin America, import liberalization has been credited with increasing the number of people living below the USD $1 a day poverty line and has perpetuated already existing inequalities (Watkins, 2002).

Positive effects of globalization for developing country business

Conversely, globalization can create new opportunities, new ideas, and open new markets that an entrepreneur may have not had in their home country. As a result, there are a number of positives associated with globalization:

- it creates greater opportunities for firms in less industrialized countries to tap into more and larger markets around the world
- this can lead to more access to capital flows, technology, human capital, cheaper imports and larger export markets
- it allows businesses in less industrialized countries to become part of international production networks and supply chains that are the main conduits of trade

For example, the experience of the East Asian economies demonstrates the positive effect of globalization on economic growth and shows that at least under some circumstances globalization decreases poverty. The spectacular growth in East Asia, which increased GDP per capita by eightfold and raised millions of people out of poverty, was based largely on globalization—export-led growth and closing the technology gap with industrialized countries (Stiglitz, 2003). Generally, economies that globalize have higher growth rates than non-globalizers (Bhagwati and Srinivasan, 2002).

Also, the role of developing country firms in the value chain is becoming increasingly sophisticated as these firms expand beyond manufacturing into services. For example, it is now commonplace for businesses in industrialized countries to outsource functions such as data processing, customer service and reading x-rays to India and other less industrialized countries (Bhagwati et al, 2004). Advanced telecommunications and the Internet are facilitating the transfer of these service jobs from industrialized to less industrialized and making it easier and cheaper for less industrialized country firms to enter global markets. In addition to bringing in capital, outsourcing helps prevent “brain drain” because skilled workers may choose to remain in their home country rather than having to migrate to an industrialized country to find work.

Further, some of the allegations made by critics of globalization are very much in dispute—for example, that globalization necessarily leads to growing income inequality or harm to the environment. While there are some countries in which economic integration has led to increased inequality—China, for instance—there is no worldwide trend (Dollar, 2003). With regard to the environment, international trade and foreign direct investment can provide less industrialized countries with the incentive to adopt, and the access to, new technologies that may be more ecologically sound (World Bank Briefing Paper, 2001). Transnational corporations may also help the environment by exporting higher standards and best practices to less industrialized countries.

In the fortune at the bottom of the pyramid, Prahalad and Stuart point out that

> *C.K. Prahalad and Stuart L. Hart have suggested that the four billion people in the world whose per capita income is less than U-S- $1500 (the people "at the bottom of the pyramid ") represent an enormous opportunity for business. Their theory is that the poor in developing countries comprise a vast, untapped market for goods and services,*

> *including basic needs as well as more advanced offerings such as financial services, cellular telephones and inexpensive computers.*
>
> *An example of a successful business that services this market is the Crameen Bank Ltd. in Bangladesh. Founded by Nobel Prize winner Muhammad Yunus, Grameen Bank extends small loans ("micro-credit") to low- income customers. Cirameen Bank charges high interest rates of approximately 20% a year, but does not require collateral, which enables even the very poor to obtain credit and gain an opportunity to participate in the formal economy. Grameen Bank's success has stimulated interest in micro-credit around the world.*
>
> *Although Prahalad and Hart mostly discuss "the bottom of the pyramid" as a potential market for transnational corporations ("TNCs") based in developed countries, this market also offers opportunities to businesses in developing countries. These firms, either alone or in partnership with TNCs, can use their understanding of the needs, and obstacles faced by, the poor to create sustainable enterprises, which will have the added benefit of helping to alleviate poverty.*

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at Download for free at http://cnx.org/contents/d6db603c-cd31-4ca4-be19-d29734673b90@4.3.

This page titled 1.8: What is Globalization is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

1.9: The Globalization Debate

Learning Objectives

After reading this section, students should be able to …

1. Understand the flattening world perspective in the globalization debate.
2. Understand the multidomestic perspective in the globalization debate.
3. Know the dimensions of the CAGE analytical framework.

In today's global economy, everyone is accustomed to buying goods from other countries—electronics from Taiwan, vegetables from Mexico, clothing from China, cars from Korea, and skirts from India. Most modern shoppers take the "Made in [a foreign country]" stickers on their products for granted. Long-distance commerce wasn't always this common, although foreign trade—the movement of goods from one geographic region to another—has been a key factor in human affairs since prehistoric times. Thousands of years ago, merchants transported only the most precious items—silk, gold and other precious metals and jewels, spices, porcelains, and medicines—via ancient, extended land and sea trade routes, including the famed Silk Road through central Asia. Moving goods great distances was simply too hard and costly to waste the effort on ordinary products, although people often carted grain and other foods over shorter distances from farms to market towns.[1]

What is the globalization debate? Well, it's not so much a debate as it is a stark difference of opinion on how the internationalization of businesses is affecting countries' cultural, consumer, and national identities—and whether these changes are desirable. For instance, the ubiquity of such food purveyors as Coca-Cola and McDonald's in practically every country reflects the fact that some consumer tastes are converging, though at the likely expense of local beverages and foods. Remember, globalization refers to the shift toward a more interdependent and integrated global economy. This shift is fueled largely by (1) declining trade and investment barriers and (2) new technologies, such as the Internet. The globalization debate surrounds whether and how fast markets are actually merging together.

We Live in a Flat World

The flat-world view is largely credited to Thomas Friedman and his 2005 best seller, The World Is Flat. Although the next section provides you with an alternative way of thinking about the world (a multidomestic view), it is nonetheless important to understand the flat-world perspective. Friedman covers the world for the New York Times, and his access to important local authorities, corporate executives, local Times bureaus and researchers, the Internet, and a voice recorder enabled him to compile a huge amount of information. Many people consider globalization a modern phenomenon, but according to Friedman, this is its third stage. The first stage of global development, what Friedman calls "Globalization 1.0," started with Columbus's discovery of the New World and ran from 1492 to about 1800. Driven by nationalism and religion, this lengthy stage was characterized by how much industrial power countries could produce and apply.

"Globalization 2.0," from about 1800 to 2000, was disrupted by the Great Depression and both World Wars and was largely shaped by the emerging power of huge, multinational corporations. Globalization 2.0 grew with the European mercantile stock companies as they expanded in search of new markets, cheap labor, and raw materials. It continued with subsequent advances in sea and rail transportation. This period saw the introduction of modern communications and cheaper shipping costs. "Globalization 3.0" began around 2000, with advances in global electronic interconnectivity that allowed individuals to communicate as never before.

In Globalization 1.0, nations dominated global expansion. Globalization 2.0 was driven by the ascension of multinational companies, which pushed global development. In Globalization 3.0, major software advances have allowed an unprecedented number of people worldwide to work together with unlimited potential.

The Mumbai Taxman

What shape will globalization take in the third phase? Friedman asks us to consider the friendly local accountants who do your taxes. They can easily outsource your work via a server to a tax team in Mumbai, India. This increasingly popular outsourcing trend has its benefits. As Friedman notes, in 2003, about 25,000 US tax returns were done in India.[2] By 2004, it

was some 100,000 returns, with 400,000 anticipated in 2005. A software program specifically designed to let midsized US tax firms outsource their files enabled this development, giving better job prospects to the 70,000 accounting students who graduate annually in India. At a starting salary of $100 per month, these accountants are completing US returns and competing with US tax preparers.

Chris C. Got It Wrong?

In 1492, Christopher Columbus set sail for India, going west. He had the Niña, the Pinta, and the Santa María. He never did find India, but he called the people he met "Indians" and came home and reported to his king and queen: "The world is round." I set off for India 512 years later. I knew just which direction I was going in—I went east. I was in Lufthansa business class, and I came home and reported only to my wife and only in a whisper: "The world is flat."

And therein lies a tale of technology and geoeconomics that is fundamentally reshaping our lives—much, much more quickly than many people realize. It all happened while we were sleeping, or rather while we were focused on 9/11, the dot-com bust, and Enron—which even prompted some to wonder whether globalization was over. Actually, just the opposite was true, which is why it's time to wake up and prepare ourselves for this flat world, because others already are, and there is no time to waste.[3]

This job competition is not restricted to accountants. Companies can outsource any service or business that can be broken down to its key components and converted to computerized operations. This includes everything from making restaurant reservations to reporting corporate earnings to reading x-rays. And it doesn't stop at basic services. With the "globalization of innovation," multinationals in India are filing increasing numbers of US patent applications, ranging from aircraft-engine designs to transportation systems and microprocessor chips. Japanese-speaking Chinese nationals in Dailian, China, now answer call-center questions from Japanese consumers. Due to Dailian's location near Japan and Korea, as well as its numerous universities, hospitals, and golf courses, some 2,800 Japanese companies outsource operations there. While many companies are outsourcing to other countries, some are using "home sourcing"—allowing people to work at home. JetBlue uses home sourcing for reservation clerks. Today, about 16 percent of the US workforce works from home. In many ways, outsourcing and home sourcing are related; both allow people to work from anywhere.

How the World Got Flat

Friedman identifies ten major events that helped reshape the modern world and make it flat:[4]



Figure 1.9.1:Infosys Bangalore Hall Infosys is a multibillion-dollar global IT and consulting firm headquartered in India. (Copyright 2011, Infosys.)

1. 11/9/89: When the walls came down and the windows went up. The fall of the Berlin Wall ended old-style communism and planned economies. Capitalism ascended.

2. 8/9/95: When Netscape went public. Internet browsing and e-mail helped propel the Internet by making it commercially viable and user friendly.

3. Work-flow software: Let's do lunch. Have your application talk to my application. With more powerful, easier-to-use software and improved connectivity, more people can share work. Thus, complex projects with more interdependent parts can be worked on collaboratively from anywhere.

4. Open-sourcing: Self-organizing, collaborative communities. Providing basic software online for free gives everyone source code, thus accelerating collaboration and software development.

5. Outsourcing: Y2K. The Internet lets firms use employees worldwide and send specific work to the most qualified, cheapest labor, wherever it is. Enter India, with educated and talented people who work at a fraction of US or European wages. Indian technicians and software experts built an international reputation during the Y2K millennium event. The feared computer-system breakdown never happened, but the Indian IT industry began handling e-commerce and related businesses worldwide.

6. Offshoring: Running with gazelles, eating with lions. When it comes to jobs leaving and factories being built in cheaper places, people think of China, Malaysia, Thailand, Mexico, Ireland, Brazil, and Vietnam. But going offshore isn't just moving part of a manufacturing or service process. It means creating a new business model to make more goods for non-US sale, thus increasing US exports.

7. Supply-chaining: Eating sushi in Arkansas. Walmart demonstrates that improved acquisition and distribution can lower costs and make suppliers boost quality.

8. Insourcing: What the guys in funny brown shorts are really doing. This kind of service collaboration happens when firms devise new service combinations to improve service. Take United Parcel Service (UPS). The "brown" company delivers packages globally, but it also repairs Toshiba computers and organizes delivery routes for Papa John's pizza. With insourcing, UPS uses its logistics expertise to help clients create new businesses.

9. Informing: Google, Yahoo!, MSN Web Search. Google revolutionized information searching. Its users conduct some one billion searches annually. This search methodology and the wide access to knowledge on the Internet transforms information into a commodity people can use to spawn entirely new businesses.

10. The steroids: Digital, mobile, personal, and virtual. Technological advances range from wireless communication to processing, resulting in extremely powerful computing capability and transmission. One new Intel chip processes some 11 million instructions per second (MIPS), compared to 60,000 MIPS in 1971.

These ten factors had powerful roles in making the world smaller, but each worked in isolation until, Freidman writes, the convergence of three more powerful forces: (1) new software and increased public familiarity with the Internet, (2) the incorporation of that knowledge into business and personal communication, and (3) the market influx of billions of people from Asia and the former Soviet Union who want to become more prosperous—fast. Converging, these factors generated their own critical mass. The benefits of each event became greater as it merged with another event. Increased global collaboration by talented people without regard to geographic boundaries, language, or time zones created opportunity for billions of people.

Political allegiances are also shifting. While critics say outsourcing costs US jobs, it can also work the other way. When the state of Indiana bid for a new contract to overhaul its employment claims processing system, a computer firm in India won. The company's bid would have saved Indiana $8 million, but local political forces made the state cancel the contract. In such situations, the line between the exploited and the exploiter becomes blurred.

Corporate nationality is also blurring. Hewlett-Packard (HP) is based in California, but it has employees in 178 countries. HP manufactures parts wherever it's cheapest to do so. Multinationals like HP do what's best for them, not what's best for their home countries. This leads to critical issues about job loss versus the benefits of globalization.

Since the world's flattening can't be stopped, new workers and those facing dislocation should refine their skills and capitalize on new opportunities. One key is to become an expert in a job that can't be delegated offshore. This ranges from local barbers and plumbers to professionals such as surgeons and specialized lawyers.

We Live in a Multidomestic World, Not a Flat One!

International business professor Pankaj Ghemawat takes strong issue with the view that the world is flat and instead espouses a world he characterizes as "semiglobalized" and "multidomestic." If the world were flat, international business and global strategy would be easy. According to Ghemawat, it would be domestic strategy applied to a bigger market. In the semiglobalized world, however, global strategy begins with noticing national differences.[5]

Ghemawat's research suggests that to study "barriers to cross-border economic activity" you will use a "CAGE" analysis. The CAGE framework covers these four factors:[6]

1. Culture.

Generally, cultural differences between two countries reduce their economic exchange. Culture refers to a people's norms, common beliefs, and practices. Cultural distance refers to differences based in language, norms, national or ethnic identity, levels of trust, tolerance, respect for entrepreneurship and social networks, or other country-specific qualities. Some products have a strong national identification, such as the Molson beer company in Canada (see Molson's "I am Canadian" ad campaign).[7] Conversely, genetically modified foods (GMOs) are commonly accepted in North America but highly disdained in Western Europe. Such cultural distance for GMOs would make it easier to sell GMO corn in the United States but impossible to sell in Germany. Some differences are surprisingly specific (such as the Chinese dislike of dark beverages, which Coca-Cola marketers discovered too late).

2. Administration.

Bilateral trade flows show that administratively similar countries trade much more with each other. Administrative distance refers to historical governmental ties, such as those between India and the United Kingdom. This makes sense; they have the same sorts of laws, regulations, institutions, and policies. Membership in the same trading block is also a key similarity. Conversely, the greater the administrative differences between nations, the more difficult the trading relationship—whether at the national or corporate level. It can also refer simply to the level and nature of government involvement in one industry versus another. Farming, for instance, is subsidized in many countries, and this creates similar conditions.

3. Geography.

This is perhaps the most obvious difference between countries. You can see that the market for a product in Los Angeles is separated from the market for that same product in Singapore by thousands of miles. Generally, as distance goes up, trade goes down, since distance usually increases the cost of transportation. Geographic differences also include time zones, access to ocean ports, shared borders, topography, and climate. You may recall from the opening case that even Google was affected by geographic distance when it felt the speed of the Internet connection to Google.com was slowed down because the Chinese were accessing server farms in other countries, as none were set up in China (prior to the setup of Google.cn).

4. Economics.

Economic distance refers to differences in demographic and socioeconomic conditions. The most obvious economic difference between countries is size (as compared by gross domestic product, or GDP). Another is per capita income. This distance is likely to have the greatest effect when (1) the nature of demand varies with income level, (2) economies of scale are limited, (3) cost differences are significant, (4) the distribution or business systems are different, or (5) organizations have to be highly responsive to their customers' concerns. Disassembling a company's economy reveals other differences, such as labor costs, capital costs, human capital (e.g., education or skills), land value, cheap natural resources, transportation networks, communication infrastructure, and access to capital.

Each of these CAGE dimensions shares the common notion of distance. CAGE differences are likely to matter most when the CAGE distance is great. That is, when CAGE differences are small, there will likely be a greater opportunity to see business being conducted across borders. A CAGE analysis also requires examining an organization's particular industry and products in each of these areas. When looking at culture, consider how culturally sensitive the products are. When looking at

administration, consider whether other countries coddle certain industries or support “national champions.” When looking at geography, consider whether products will survive in a different climate. When looking at economics, consider such issues as the effect of per capita income on demand.

An Amusing Anecdote

Pankaj Ghemawat provides this anecdote in partial support of his multidomestic (or anti-flat-world) view. “It takes an aroused man to make a chicken affectionate” is probably not the best marketing slogan ever devised. But that’s the one Perdue Chicken used to market its fryers in Mexico. Mexicans were nonplussed, to say the least, and probably wondered what was going on in founder Frank Perdue’s henhouse. How did the slogan get approved? Simple: it’s a literal translation of Perdue’s more appetizing North American slogan “It takes a tough man to make a tender chicken.” As Perdue discovered, at least through his experience with the literal translation of his company motto into Spanish, cultural and economic globalization have yet to arrive. Consider the market for capital. Some say capital “knows no boundaries.” Recent data, however, suggests capital knows its geography quite well and is sticking close to home. For every dollar of capital investment globally, only a dime comes from firms investing “outside their home countries.” For every $100 US investors put in the stock market, they spend $15 on international stocks. For every one hundred students in the Organisation for Economic Co-operation (OECD) universities, perhaps five are foreigners. These and other key measures of internationalization show that the world isn’t flat. It’s 90 percent round, like a rugby ball.[8]

References

1. William J. Bernstein, A Splendid Exchange: How Trade Shaped the World, New York: Atlantic Monthly Press, 2008

2. Thomas L. Friedman, The World Is Flat (New York: Farrar, Straus and Giroux, 2005).

3. Thomas L. Friedman, “It’s a Flat World, After All,” New York Times Magazine, April 3, 2005, accessed June 2, 2010, http://www.nytimes.com/2005/04/03/magazine/03DOMINANCE.html.

4. Thomas L. Friedman, The World Is Flat (New York: Farrar, Straus and Giro1.10: Standardization and Customizationux, 2005), 48–159.

5. Pankaj Ghemawat, “Distance Still Matters,” Harvard Business Review 79, no. 8 (2001): 137–47.

6. Pankaj Ghemawat, “Distance Still Matters,” Harvard Business Review 79, no. 8 (2001): 137–47.

7. “I Am Canadian,” YouTube video, posted by “vinko,” May 22, 2006, accessed May 4, 2011, http://www.youtube.com/watch?v=BRI-A3vakVg.

8. Pankaj Ghemawat, Redefining Global Strategy: Crossing Borders in a World Where Differences Still Matter(Boston: Harvard Business School Press, 2007), 42.

Source

The above content was adapted from textbook content provided in the chapter “The Globalization Debate”, section 1.4 from the book Challenges and Opportunities in International Business (v. 1.0), published by publishers and authors who would like to remain anonymous. Their book was licensed under a Creative Commons by-nc-sa 3.0 license.

This page titled 1.9: The Globalization Debate is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

1.10: Standardization and Customization

Learning Objectives

After reading this section, students should be able to …

1. make the argument for standardized marketing
2. make the argument to localize marketing
3. make the case for blending standardization and localization

Most of the basic principles for effective marketing apply equally well to domestic and global marketing activity. However, globalization introduces a number of challenges that are unique to operating simultaneously in different countries and global markets. What is the best way to enter a global market? When should you adjust a product's features to customize it to consumer needs in a different global market? How do you manage the costs and complexities of product promotion when it must take place in different locations, with different languages, cultural sensitivities and consumer expectations? What considerations should go into product pricing, when a good is offered in different markets using different currencies and exchange rates?

In 1983, Harvard marketing professor Theodore Levitt wrote an article entitled, "The Globalization of Markets", and nothing about marketing has been the same since. According to Levitt, a new economic reality-the emergence of global consumer markets for single standard products-has been triggered in part by technological developments. Worldwide communications ensure the instant diffusion of new lifestyles and pave the way for a wholesale transfer of goods and services.

Adopting this global strategy provides a competitive advantage in cost and effectiveness. In contrast to multinational companies, standardized (global) corporations view the world or its major regions as one entity instead of a collection of national markets. These world marketers compete on a basis of appropriate value: i.e. an optimal combination of price, quality, reliability, and delivery of products that are identical in design and function. Ultimately, consumers tend to prefer a good price/quality ratio to a highly customized but less cost-effective item.

Levitt distinguished between products and brands. While the global product itself is standardized or sold with only minor modifications, the branding, positioning, and promotion may have to reflect local conditions.

Critics of Levitt's perspective suggest that his argument for global standardization is incorrect and that each market strategy should be customized for each country. Kotler notes that one study found that 80 per cent of US exports required one or more adaptations. Furthermore, the average product requires at least four to five adaptations out of a set of eleven marketing elements: labeling, packaging, materials, colors, name, product features, advertising themes, media, execution, price, and sales promotion. Kotler suggests that all eleven factors should be evaluated before standardization is considered.

To date, no one has empirically validated either perspective. While critics of Levitt can offer thousands of anecdotes contradicting the validity of standardization, a more careful read of Levitt's ideas indicate that he offers standardization as a strategic option, not a fact. Although global marketing has its pitfalls, it can also yield impressive advantages. Standardized products can lower operating costs. Even more important, effective coordination can exploit a company's best product and marketing ideas.

Too often, executives view global marketing as an either/or proposition-either full standardization or local control. But when a global approach can fall anywhere on a spectrum-from tight worldwide coordination on programming details to loose agreements on a product ideas-there is no reason for this extreme view. In applying the global marketing concept and making it work, flexibility is essential. The big issue today is not whether to go global, but how to tailor the global marketing concept to fit each business and how to make it work.

Global Marketing Strategies

U.S. firms choose to engage in international marketing for many reasons, the most attractive of which are market expansion and new profit opportunities. When a firm chooses to market internationally, it must decide whether to adjust its domestic marketing program—depending on how much centralized control a firm wishes to maintain over its marketing. If an organization wants to maintain strong centralized control and uniformity in its products and marketing activities, it is choosing a strategy called *standardization*. If an organization wants to adjust products, messaging, and marketing activities to fit the needs and preferences of

local markets around the world, it is choosing a *localization* strategy. You'll recall our earlier discussion of the unique flavors of Oreo cookies developed for the Chinese market: that's an example of a localization strategy.

Global Standardization: The Argument for Standardized Marketing

To the extent that global consumers desire standardized products, companies can pursue a global standardization strategy. Using this approach, a product and the way in which it is marketed are largely uniform across the world, with little variation in the marketing mix from country to country. Advocates of standardization strategy argue that companies can achieve competitive advantage by offering the optimal combination of price, quality, and reliability with products that are identical in design and function throughout the world; they also claim that consumers will prefer this standardized product to a highly localized product that is also more expensive.

Standardization can translate into lower operating costs because there aren't extra costs associated with developing and marketing unique products tailored to local market needs. It also expands the customer base receptive to a common global product. There is no need to adjust product features, naming, or other attributes for each new market, and marketing materials themselves can be repurposed across different world regions. Below are the primary benefits of a global standardization strategy:

Marketers can use the same approach for developing, promoting, and delivering products and services worldwide, creating lower operating costs and economies of scale in product development and marketing

The ability to develop and invest in a unified brand and/or company identity throughout the world, along with the opportunity to develop brand awareness and brand equity that give a competitive advantage

Product lines that consist of a small number of global brands rather than a plethora of localized product brands and extensions, along with cost savings and improved efficiencies associated with managing a smaller total number of brands

Companies that pursue this approach assume that consumer needs are relatively homogenous around the world and that the same basic marketing mix will work across global markets. These organizations typically have a centralized approach to the marketing function and try to minimize the need for developing localized marketing strategies.

The case for a standardization strategy was made by Harvard marketing professor Theodore Levitt in his 1983 article, "The Globalization of Markets." He argued that technology and worldwide communications have helped trigger the emergence of global consumer markets that are receptive to single, standardized global products. According to Levitt, adopting a standardized global strategy provides a competitive advantage in cost and effectiveness.

Localization: The Argument to Localize Marketing

On the other end of the spectrum is localization strategy, in which firms adjust their products and marketing mix for each target market. Advocates of localization argue that, in reality, global standardization doesn't work, and in fact nearly all exported products require one or more adaptations to be successful. In work by Kotler, one study found that 80 percent of U.S. exports require one or more adaptations, and the average product requires at least four to five adaptations out of eleven different elements: labeling, packaging, materials, colors, name, product features, advertising themes, media, execution, price, and sales promotion.

Localization strategy recognizes that diversity exists in global markets and that marketers need to understand and respond to this diversity in the goods they offer and the way they market to consumers in these markets. Language, culture, customs, the physical environment, the degree of economic development, societal institutions, and other factors all contribute to how well a product fits a local market's needs. Localization may involve: 1) altering existing products to fit the needs of the local target market, or 2) creating completely new products to fit the needs of the local target market.

Although localization does increase the cost and complexity associated with developing and marketing tailored products, its supporters argue that it results in products and marketing strategy that are a better fit for local market needs and ultimately a greater sales success. A localized approach can protect companies from high-profile, disastrous consequences when a standardized product fails. Standardization is often responsible for marketing misfires like offensive marketing images, catastrophic naming, and product-design glitches. Its critics argue that standardization strategy overestimates how well any single, uniform product and marketing approach will succeed in markets all over the world.

The Middle Ground: Blending Standardization and Localization

In reality, global marketing is not an either/or proposition requiring either full standardization or localized control of product and marketing. In fact, a successful global approach can fall anywhere on a spectrum–from tight worldwide coordination on programing details to loose agreements on product ideas. Most organizations find that flexibility is essential in order to allow organizations to capitalize global opportunities available to them. The right answer for each business depends on organizational structure, leadership and operations; the product category; the markets in question; and other factors. Both strategies offer attractive benefits as well as costs and risks. Most organizations find ways to balance the options available to them with a focus on how to maximize success in their target markets.



Few would disagree that fast-food chain McDonald's is a master of global marketing. As you watch this video, look for ways that McDonald's has blended elements of global standardization strategy with localization strategy to penetrate global markets and offer products that align perfectly with local appetites and preferences.

Source

The above content was adapted from textbook content provided by: Lumen Learning. License: CC BY-SA: Attribution-ShareAlike and textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. (Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at http://cnx.org/contents/6fdb38de-3019-4843-8ffd-2b204bc45c29@4)

CC LICENSED CONTENT, SHARED PREVIOUSLY

- Introduction to Global Marketing. **Provided by**: Lumen Learning. **Located at**: https://courses.candelalearning.com/principlesmktg1x2kscope/chapter/13-1-introduction-to-global-marketing/. **License**: CC BY-SA: Attribution-ShareAlike
- Global Marketing: Points of Controversy. **Provided by**: Lumen Learning. **Located at**: https://courses.candelalearning.com/principlesmktg1x2kscope/chapter/global-marketing-points-of-controversy/. **License**: CC BY-SA: Attribution-ShareAlike
- McDonald's. **Provided by**: BBC. **Located at**: https://youtu.be/4hQwdIVyi2s. **License**: CC BY-NC-ND: Attribution-NonCommercial-NoDerivatives

This page titled 1.10: Standardization and Customization is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

2: International Business and Trade

2.1: International Business and Trade Summary
2.2: International Trade
2.3: International Economic Cooperation among Nations
2.4: Understanding Tariffs
2.5: Regional Economic Integration
2.6: The United Nations and the Impact on Trade
2.7: Trade Controversies
2.8: Foreign Direct Investment

This page titled 2: International Business and Trade is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

2.1: International Business and Trade Summary

Summary

It's easy to think that trade is just about business interests in each country. But global trade is much more. There's a convergence and, at times, a conflict of the interests of the different stakeholders—from businesses to governments to local citizens. In recent years, advancements in technology, a renewed enthusiasm for entrepreneurship, and a global sentiment that favors free trade have further connected people, businesses, and markets—all flatteners that are helping expand global trade and investment. An essential part of international business is understanding the history of international trade and what motivates countries to encourage or discourage trade within their borders. In this chapter we'll look at the evolution of international trade theory to our modern time. We'll explore the political and legal factors impacting international trade. This chapter will provide an introduction to the concept and role of foreign direct investment, which can take many forms of incentives, regulations, and policies. Companies react to these business incentives and regulations as they evaluate with which countries to do business and in which to invest. Governments often encourage foreign investment in their own country or in another country by providing loans and incentives to businesses in their home country as well as businesses in the recipient country in order to pave the way for investment and trade in the country. The opening case study in the next section shows how and why China is investing in the continent of Africa.

A country's balance of payments is a record of its economic transactions with the rest of the world; this record shows whether a country has a trade surplus (value of exports exceeds value of imports) or a trade deficit (value of imports exceeds value of exports). Trade figures can be further divided into merchandise trade and services trade accounts; a country can run a surplus in both accounts, a deficit in both accounts, or a combination of the two. The U.S. merchandise trade deficit was $819 billion in 2007. However, the U.S.enjoys an annual service trade surplus. Overall, however, the United Statesis a debtor; Japanenjoys an overall trade surplus and serves as a creditor nation.

Foreign exchange provides a means for settling accounts across borders. The dynamics of international finance can have a significant impact on a nation's economy as well as the fortunes of individual companies. Currencies can be subject to devaluation or revaluation as a result of actions taken by a country's central banker. Currency trading by international speculators can also lead to devaluation. When a country's economy is strong or when demand for its goods is high, its currency tends to appreciate in value. When currency values fluctuate, global firms face various types of economic exposure. Firms can manage exchange rate exposure by hedging.

Source

The above note was adapted from the following sources (i) course note from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM). 'International Business and Trade' is Copyright (c) by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license, and (ii) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor. I would like to thank Andy Schmitz for his work in maintaining and improving the HTML versions of these textbooks. This textbook is adapted from his HTML version, and his project can be found here.

This page titled 2.1: International Business and Trade Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

2.2: International Trade

Learning Objectives

After reading this section, students should be able to …

1. Define international trade.
2. Compare and contrast different trade theories.
3. Determine which international trade theory is most relevant today and how it continues to evolve.

Opening Case: China in Africa

Foreign companies have been doing business in Africa for centuries. Much of the trade history of past centuries has been colored by European colonial powers promoting and preserving their economic interests throughout the African continent.[1] After World War II and since independence for many African nations, the continent has not fared as well as other former colonial countries in Asia. Africa remains a continent plagued by a continued combination of factors, including competing colonial political and economic interests; poor and corrupt local leadership; war, famine, and disease; and a chronic shortage of resources, infrastructure, and political, economic, and social will.[2] And yet, through the bleak assessments, progress is emerging, led in large part by the successful emergence of a free and locally powerful South Africa. The continent generates a lot of interest on both the corporate and humanitarian levels, as well as from other countries. In particular in the past decade, Africa has caught the interest of the world's second largest economy, China.[3]

At home, over the past few decades, China has undergone its own miracle, managing to move hundreds of millions of its people out of poverty by combining state intervention with economic incentives to attract private investment. Today, China is involved in economic engagement, bringing its success story to the continent of Africa. As professor and author Deborah Brautigam notes, China's "current experiment in Africa mixes a hard-nosed but clear-eyed self-interest with the lessons of China's own successful development and of decades of its failed aid projects in Africa." [4]

According to *CNN*, "China has increasingly turned to resource-rich Africa as China's booming economy has demanded more and more oil and raw materials."[5] Trade between the African continent and China reached $106.8 billion in 2008, and over the past decade, Chinese investments and the country's development aid to Africa have been increasing steadily."China-Africa Trade up 45 percent in 2008 to $107 Billion," [6] "Chinese activities in Africa are highly diverse, ranging from government to government relations and large state owned companies (SOE) investing in Africa financed by China's policy banks, to private entrepreneurs entering African countries at their own initiative to pursue commercial activities."[7]

Since 2004, eager for access to resources, oil, diamonds, minerals, and commodities, China has entered into arrangements with resource-rich countries in Africa for a total of nearly $14 billion in resource deals alone. In one example with Angola, China provided loans to the country secured by oil. With this investment, Angola hired Chinese companies to build much-needed roads, railways, hospitals, schools, and water systems. Similarly, China provided nearby Nigeria with oil-backed loans to finance projects that use gas to generate electricity. In the Republic of the Congo, Chinese teams are building a hydropower project funded by a Chinese government loan, which will be repaid in oil. In Ghana, a Chinese government loan will be repaid in cocoa beans.[8]

The Export-Import Bank of China (Ex-Im Bank of China) has funded and has provided these loans at market rates, rather than as foreign aid. While these loans certainly promote development, the risk for the local countries is that the Chinese bids to provide the work aren't competitive. Furthermore, the benefit to local workers may be diminished as Chinese companies bring in some of their own workers, keeping local wages and working standards low.

In 2007, the UNCTAD (United Nations Conference on Trade and Development) Press Office noted the following:

Over the past few years, China has become one of Africa´s important partners for trade and economic cooperation. Trade (exports and imports) between Africa and China increased from US$11 billion in 2000 to US$56 billion in 2006….with Chinese companies present in 48 African countries, although Africa still accounts for only 3 percent of China´s outward FDI

[foreign direct investment]. A few African countries have attracted the bulk of China´s FDI in Africa: Sudan is the largest recipient (and the 9th largest recipient of Chinese FDI worldwide), followed by Algeria (18th) and Zambia (19th).[9]

Observers note that African governments can learn from the development history of China and many Asian countries, which now enjoy high economic growth and upgraded industrial activity. These Asian countries made strategic investments in education and infrastructure that were crucial not only for promoting economic development in general but also for attracting and benefiting from efficiency-seeking and export-oriented FDI.[10]



Figure 2.2.1: Source: "China in Africa: Developing Ties," BBC News, last updated November 26, 2007, accessed June 3, 2011, *http://news.bbc.co.uk/2/hi/africa/7086777.stm* .

Criticized by some and applauded by others, it's clear that China's investment is encouraging development in Africa. China is accused by some of ignoring human rights crises in the continent and doing business with repressive regimes. China's success in Africa is due in large part to the local political environment in each country, where either one or a small handful of leaders often control the power and decision making. While the countries often open bids to many foreign investors, Chinese firms are able to provide low-cost options thanks in large part to their government's project support. The ability to forge a government-level partnership has enabled Chinese businesses to have long-term investment perspectives in the region. China even hosted a summit in 2006 for African leaders, pledging to increase trade, investment, and aid over the coming decade.[11] The 2008 global recession has led China to be more selective in its African investments, looking for good deals as well as political stability in target countries. Nevertheless, whether to access the region's rich resources or develop local markets for Chinese goods and services, China intends to be a key foreign investor in Africa for the foreseeable future.[12]

What Is International Trade?

International trade theories are simply different theories to explain international trade. Trade is the concept of exchanging goods and services between two people or entities. *International trade* is then the concept of this exchange between people or entities in two different countries.

People or entities trade because they believe that they benefit from the exchange. They may need or want the goods or services. While at the surface, this many sound very simple, there is a great deal of theory, policy, and business strategy that constitutes international trade.

> *"Around 5,200 years ago, Uruk, in southern Mesopotamia, was probably the first city the world had ever seen, housing more than 50,000 people within its six miles of wall. Uruk,*

> *its agriculture made prosperous by sophisticated irrigation canals, was home to the first class of middlemen, trade intermediaries. A cooperative trade network…set the pattern that would endure for the next 6,000 years."*[1]

Mercantilism

Developed in the sixteenth century, mercantilism was one of the earliest efforts to develop an economic theory. This theory stated that a country's wealth was determined by the amount of its gold and silver holdings. In it's simplest sense, mercantilists believed that a country should increase its holdings of gold and silver by promoting exports and discouraging imports. In other words, if people in other countries buy more from you (exports) than they sell to you (imports), then they have to pay you the difference in gold and silver. The objective of each country was to have a trade surplus, or a situation where the value of exports are greater than the value of imports, and to avoid a trade deficit, or a situation where the value of imports is greater than the value of exports.

A closer look at world history from the 1500s to the late 1800s helps explain why mercantilism flourished. The 1500s marked the rise of new nation-states, whose rulers wanted to strengthen their nations by building larger armies and national institutions. By increasing exports and trade, these rulers were able to amass more gold and wealth for their countries. One way that many of these new nations promoted exports was to impose restrictions on imports. This strategy is called protectionism and is still used today.

Nations expanded their wealth by using their colonies around the world in an effort to control more trade and amass more riches. The British colonial empire was one of the more successful examples; it sought to increase its wealth by using raw materials from places ranging from what are now the Americas and India. France, the Netherlands, Portugal, and Spain were also successful in building large colonial empires that generated extensive wealth for their governing nations.

Although mercantilism is one of the oldest trade theories, it remains part of modern thinking. Countries such as Japan, China, Singapore, Taiwan, and even Germany still favor exports and discourage imports through a form of neo-mercantilism in which the countries promote a combination of protectionist policies and restrictions and domestic-industry subsidies. Nearly every country, at one point or another, has implemented some form of protectionist policy to guard key industries in its economy. While export-oriented companies usually support protectionist policies that favor their industries or firms, other companies and consumers are hurt by protectionism. Taxpayers pay for government subsidies of select exports in the form of higher taxes. Import restrictions lead to higher prices for consumers, who pay more for foreign-made goods or services. Free-trade advocates highlight how free trade benefits all members of the global community, while mercantilism's protectionist policies only benefit select industries, at the expense of both consumers and other companies, within and outside of the industry.

Absolute Advantage

In 1776, Adam Smith questioned the leading mercantile theory of the time in *The Wealth of Nations*.Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (London: W. Strahan and T. Cadell, 1776). Recent versions have been edited by scholars and economists. Smith offered a new trade theory called absolute advantage, which focused on the ability of a country to produce a good more efficiently than another nation. Smith reasoned that trade between countries shouldn't be regulated or restricted by government policy or intervention. He stated that trade should flow naturally according to market forces. In a hypothetical two-country world, if Country A could produce a good cheaper or faster (or both) than Country B, then Country A had the advantage and could focus on specializing on producing that good. Similarly, if Country B was better at producing another good, it could focus on specialization as well. By specialization, countries would generate efficiencies, because their labor force would become more skilled by doing the same tasks. Production would also become more efficient, because there would be an incentive to create faster and better production methods to increase the specialization.

Smith's theory reasoned that with increased efficiencies, people in both countries would benefit and trade should be encouraged. His theory stated that a nation's wealth shouldn't be judged by how much gold and silver it had but rather by the living standards of its people.

Comparative Advantage

The challenge to the absolute advantage theory was that some countries may be better at producing both goods and, therefore, have an advantage in *many* areas. In contrast, another country may not have *any* useful absolute advantages. To answer this challenge, David Ricardo, an English economist, introduced the theory of comparative advantage in 1817. Ricardo reasoned that even if

Country A had the absolute advantage in the production of *both* products, specialization and trade could still occur between two countries.

Comparative advantage occurs when a country cannot produce a product more efficiently than the other country; however, it *can* produce that product better and more efficiently than it does other goods. The difference between these two theories is subtle. Comparative advantage focuses on the relative productivity differences, whereas absolute advantage looks at the absolute productivity.

Let's look at a simplified hypothetical example to illustrate the subtle difference between these principles. Miranda is a Wall Street lawyer who charges $500 per hour for her legal services. It turns out that Miranda can also type faster than the administrative assistants in her office, who are paid $40 per hour. Even though Miranda clearly has the absolute advantage in both skill sets, should she do both jobs? No. For every hour Miranda decides to type instead of do legal work, she would be giving up $460 in income. Her productivity and income will be highest if she specializes in the higher-paid legal services and hires the most qualified administrative assistant, who can type fast, although a little slower than Miranda. By having both Miranda and her assistant concentrate on their respective tasks, their overall productivity as a team is higher. This is comparative advantage. A person or a country will specialize in doing what they do *relatively* better. In reality, the world economy is more complex and consists of more than two countries and products. Barriers to trade may exist, and goods must be transported, stored, and distributed. However, this simplistic example demonstrates the basis of the comparative advantage theory.

Modern or Firm-Based Trade Theories

In contrast to classical, country-based trade theories, the category of modern, firm-based theories emerged after World War II and was developed in large part by business school professors, not economists. The firm-based theories evolved with the growth of the multinational company (MNC). The country-based theories couldn't adequately address the expansion of either MNCs or intraindustry trade, which refers to trade between two countries of goods produced in the same industry. For example, Japan exports Toyota vehicles to Germany and imports Mercedes-Benz automobiles from Germany.

Unlike the country-based theories, firm-based theories incorporate other product and service factors, including brand and customer loyalty, technology, and quality, into the understanding of trade flows.

Country Similarity Theory

Swedish economist Steffan Linder developed the country similarity theory in 1961, as he tried to explain the concept of intraindustry trade. Linder's theory proposed that consumers in countries that are in the same or similar stage of development would have similar preferences. In this firm-based theory, Linder suggested that companies first produce for domestic consumption. When they explore exporting, the companies often find that markets that look similar to their domestic one, in terms of customer preferences, offer the most potential for success. Linder's country similarity theory then states that most trade in manufactured goods will be between countries with similar per capita incomes, and intraindustry trade will be common. This theory is often most useful in understanding trade in goods where brand names and product reputations are important factors in the buyers' decision-making and purchasing processes.

Product Life Cycle Theory

Raymond Vernon, a Harvard Business School professor, developed the product life cycle theory in the 1960s. The theory, originating in the field of marketing, stated that a product life cycle has three distinct stages: (1) new product, (2) maturing product, and (3) standardized product. The theory assumed that production of the new product will occur completely in the home country of its innovation. In the 1960s this was a useful theory to explain the manufacturing success of the United States. US manufacturing was the globally dominant producer in many industries after World War II.

It has also been used to describe how the personal computer (PC) went through its product cycle. The PC was a new product in the 1970s and developed into a mature product during the 1980s and 1990s. Today, the PC is in the standardized product stage, and the majority of manufacturing and production process is done in low-cost countries in Asia and Mexico.

The product life cycle theory has been less able to explain current trade patterns where innovation and manufacturing occur around the world. For example, global companies even conduct research and development in developing markets where highly skilled labor and facilities are usually cheaper. Even though research and development is typically associated with the first or new product

stage and therefore completed in the home country, these developing or emerging-market countries, such as India and China, offer both highly skilled labor and new research facilities at a substantial cost advantage for global firms.

Global Strategic Rivalry Theory

Global strategic rivalry theory emerged in the 1980s and was based on the work of economists Paul Krugman and Kelvin Lancaster. Their theory focused on MNCs and their efforts to gain a competitive advantage against other global firms in their industry. Firms will encounter global competition in their industries and in order to prosper, they must develop competitive advantages. The critical ways that firms can obtain a sustainable competitive advantage are called the barriers to entry for that industry. The barriers to entry refer to the obstacles a new firm may face when trying to enter into an industry or new market. The barriers to entry that corporations may seek to optimize include:

- research and development,
- the ownership of intellectual property rights,
- economies of scale,
- unique business processes or methods as well as extensive experience in the industry, and
- the control of resources or favorable access to raw materials.

Porter's National Competitive Advantage Theory

In the continuing evolution of international trade theories, Michael Porter of Harvard Business School developed a new model to explain national competitive advantage in 1990. Porter's theory stated that a nation's competitiveness in an industry depends on the capacity of the industry to innovate and upgrade. His theory focused on explaining why some nations are more competitive in certain industries. To explain his theory, Porter identified four determinants that he linked together. The four determinants are (1) local market resources and capabilities, (2) local market demand conditions, (3) local suppliers and complementary industries, and (4) local firm characteristics.



Figure 2.2.2: Porter's four determinants of industrial competitiveness (1) local market resources and capabilities, (2) local market demand conditions, (3) local suppliers and complementary industries, and (4) local firm characteristics.

1. **Local market resources and capabilities (factor conditions).** Porter recognized the value of the factor proportions theory, which considers a nation's resources (e.g., natural resources and available labor) as key factors in determining what products a country will import or export. Porter added to these basic factors a new list of advanced factors, which he defined as skilled labor, investments in education, technology, and infrastructure. He perceived these advanced factors as providing a country with a sustainable competitive advantage.
2. **Local market demand conditions.** Porter believed that a sophisticated home market is critical to ensuring ongoing innovation, thereby creating a sustainable competitive advantage. Companies whose domestic markets are sophisticated, trendsetting, and demanding forces continuous innovation and the development of new products and technologies. Many sources credit the demanding US consumer with forcing US software companies to continuously innovate, thus creating a sustainable competitive advantage in software products and services.

3. **Local suppliers and complementary industries.** To remain competitive, large global firms benefit from having strong, efficient supporting and related industries to provide the inputs required by the industry. Certain industries cluster geographically, which provides efficiencies and productivity.
4. **Local firm characteristics.** Local firm characteristics include firm strategy, industry structure, and industry rivalry. Local strategy affects a firm's competitiveness. A healthy level of rivalry between local firms will spur innovation and competitiveness.

In addition to the four determinants of the diamond, Porter also noted that government and chance play a part in the national competitiveness of industries. Governments can, by their actions and policies, increase the competitiveness of firms and occasionally entire industries.

Porter's theory, along with the other modern, firm-based theories, offers an interesting interpretation of international trade trends. Nevertheless, they remain relatively new and minimally tested theories.

References

1. Martin Meredith, The Fate of Africa (New York: Public Affairs, 2005).

2. "Why Africa Is Poor: Ghana Beats Up on Its Biggest Foreign Investors," Wall Street Journal, February 18, 2010, accessed February 16, 2011, http://online.wsj.com/article/SB10001424052748704804204575069511746613890.html .

3. Andrew Rice, "Why Is Africa Still Poor?," The Nation, October 24, 2005, accessed December 20, 2010, http://www.thenation.com/article/why-africa-still-poor?page=0,1 .

4. Deborah Brautigam, "Africa's Eastern Promise: What the West Can Learn from Chinese Investment in Africa," Foreign Affairs, January 5, 2010, accessed December 20, 2010, http://www.foreignaffairs.com/articles/65916/deborah-brautigam/africa%E2%80%99s-eastern-promise .

5. "China: Trade with Africa on Track to New Record," CNN, October 15, 2010, accessed April 23, 2011, http://articles.cnn.com/2010-10-15/world/china.africa.trade_1_china-and-africa-link-trade-largest-trade-partner?_s=PM:WORLD .

6. China Daily, February 11, 2009, accessed April 23, 2011, http://www.chinadaily.com.cn/china/2009-02/11/content_7467460.htm .

7. Tracy Hon, Johanna Jansson, Garth Shelton, Liu Haifang, Christopher Burke, and Carine Kiala, Evaluating China's FOCAC Commitments to Africa and Mapping the Way Ahead(Stellenbosch, South Africa: Centre for Chinese Studies, University of Stellenbosch, 2010), 1, accessed December 20, 2010, http://www.ccs.org.za/wp-content/uploads/2010/03/ENGLISH-Evaluating-Chinas-FOCAC-commitments-to-Africa-2010.pdf .

8. Deborah Brautigam, "Africa's Eastern Promise: What the West Can Learn from Chinese Investment in Africa," Foreign Affairs, January 5, 2010, accessed December 20, 2010, http://www.foreignaffairs.com/articles/65916/deborah-brautigam/africa%E2%80%99s-eastern-promise .

9. United Nations Conference on Trade and Development, "Asian Foreign Direct Investment in Africa: United Nations Report Points to a New Era of Cooperation among Developing Countries," press release, March 27, 2007, accessed December 20, 2010, http://www.unctad.org/Templates/Webflyer.asp?docID=8172&intItemID=3971&lang=1 .

10. United Nations Conference on Trade and Development, "Foreign Direct Investment in Africa Remains Buoyant, Sustained by Interest in Natural Resources," press release, September 29, 2005, accessed December 20, 2010, http://news.bbc.co.uk/2/hi/africa/7086777.stm .

11. "Summit Shows China's Africa Clout," BBC News, November 6, 2006, accessed December 20, 2010, http://news.bbc.co.uk/2/hi/business/6120500.stm .

12. "China in Africa: Developing Ties," BBC News, November 26, 2007, accessed December 20, 2010, http://news.bbc.co.uk/2/hi/africa/7086777.stm .

13. Matt Ridley, "Humans: Why They Triumphed," Wall Street Journal, May 22, 2010, accessed December 20, 2010, http://online.wsj.com/article/SB1000...386933138.html.

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 2.2: International Trade is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

2.3: International Economic Cooperation among Nations

Learning Objectives

After reading this section, students should be able to …

1. Understand the global trading system.
2. Explain how and why the GATT was created and what its historical role in international trade is.
3. Know what the WTO is and what its current impact on international trade is.

In the post–World War II environment, countries came to realize that a major component of achieving any level of global peace was global cooperation—politically, economically, and socially. The intent was to level the trade playing field and reduce economic areas of disagreement, since inequality in these areas could lead to more serious conflicts. Among the initiatives, nations agreed to work together to promote free trade, entering into bilateral and multilateral agreements. The General Agreement on Tariffs and Trade (GATT) resulted from these agreements. In this section, you'll review GATT—why it was created and what its historical successes and challenges are. You'll then look at the World Trade Organization (WTO), which replaced GATT in 1995, and study the impact of both these organizations on international trade. While GATT started as a set of rules between countries, the WTO has become an institution overseeing international trade.

General Agreement on Tariffs and Trade (GATT)

The General Agreement on Tariffs and Trade (GATT) is a series of rules governing trade that were first created in 1947 by twenty-three countries. By the time it was replaced with the WTO, there were 125 member nations. GATT has been credited with substantially expanding global trade, primarily through the reduction of tariffs.

The basic underlying principle of GATT was that trade should be free and equal. In other words, countries should open their markets equally to member nations, and there should be neither discrimination nor preferential treatment. One of GATT's key provisions was the most-favored-nation clause (MFN). It required that once a benefit, usually a tariff reduction, was agreed on between two or more countries, it was automatically extended to all other member countries. GATT's initial focus was on tariffs, which are taxes placed on imports or exports.

Did You Know?

MFN Is Everywhere

As a concept, MFN can be seen in many aspects of business; it's an important provision. Companies require MFN of their trading partners for pricing, access, and other provisions. Corporate or government customers require it of the company from which they purchase goods or services. Venture capitalists (VC) require it of the companies in which they invest. For example, a VC wants to make sure that it has negotiated the best price for equity and will ask for this provision in case another financier negotiates a cheaper purchase price for the equity. The idea behind the concept of MFN is that the country, company, or entity that has MFN status shouldn't be disadvantaged in comparison with others in similar roles as a trading partner, buyer, or investor. In practice, the result is that the signing party given MFN status benefits from any better negotiation and receives the cheaper price point or better term. This terminology is also used in sales contracts or other business legal agreements.

Gradually, the GATT member countries turned their attention to other nontariff trade barriers. These included government procurement and bidding, industrial standards, subsidies, duties and customs, taxes, and licensing. GATT countries agreed to limit or remove trade barriers in these areas. The only agreed-on export subsidies were for agricultural products. Countries agreed to permit a wider range of imported products to enter their home markets by simplifying licensing guidelines and developing consistent product standards between imports and domestically produced goods. Duties had to result from uniform and consistent procedures for the same foreign and domestically produced items.

The initial successes in these categories led some countries to get more creative with developing barriers to trade as well as entering into bilateral agreements and providing more creative subsidies for select industries. The challenge for the member

countries of GATT was enforcement. Other than complaining and retaliating, there was little else that a country could do to register disapproval of another country's actions and trade barriers.

Gradually, trade became more complex, leading to the Uruguay Round beginning in 1986 and ending in 1994. These trade meetings were called rounds in reference to the series of meetings among global peers held at a "roundtable." Prior to a round, each series of trade discussions began in one country. The round of discussions was then named after that country. It sometimes took several years to conclude the topic discussions for a round. The Uruguay Round took eight years and actually resulted in the end of GATT and the creation of the World Trade Organization (WTO). The current Doha Development Round began in 2001 and is actually considered part of the WTO.

World Trade Organization (WTO)

Brief History and Purpose

The World Trade Organization (WTO) developed as a result of the Uruguay Round of GATT. Formed officially on January 1, 1995, the concept of the WTO had been in development for several years. When the WTO replaced GATT, it absorbed all of GATT's standing agreements. In contrast to GATT, which was a series of agreements, the WTO was designed to be an actual institution charged with the mission of promoting free and fair trade. As explained on its website, the WTO "is the only global international organization dealing with the rules of trade between nations. At its heart are the WTO agreements, negotiated and signed by the bulk of the world's trading nations and ratified in their parliaments. The goal is to help producers of goods and services, exporters, and importers conduct their business."[1]

The global focus on multilateral trade agreements and cooperation has expanded trade exponentially. "The past 50 years have seen an exceptional growth in world trade. Merchandise exports grew on average by 6 percent annually. Total trade in 2000 was 22-times the level of 1950. GATT and the WTO have helped to create a strong and prosperous trading system contributing to unprecedented growth."[2]

The WTO's primary purpose is to serve as a negotiating forum for member nations to dispute, discuss, and debate trade-related matters. More than just a series of trade agreements, as it was under GATT, the WTO undertakes discussions on issues related to globalization and its impact on people and the environment, as well as trade-specific matters. It doesn't necessarily establish formal agreements in all of these areas but does provide a forum to discuss how global trade impacts other aspects of the world.

Headquartered in Geneva, Switzerland, the current round is called the Doha Round and began in 2001. With 153 member nations, the WTO is the largest, global trade organization. Thirty nations have observer status, and many of these are seeking membership. With so many member nations, the concept of MFN has been eased into a new principle of normal trade relations (NTR). Advocates say that no nation really has a favored nation status; rather, all interact with each other as a normal part of global trade.

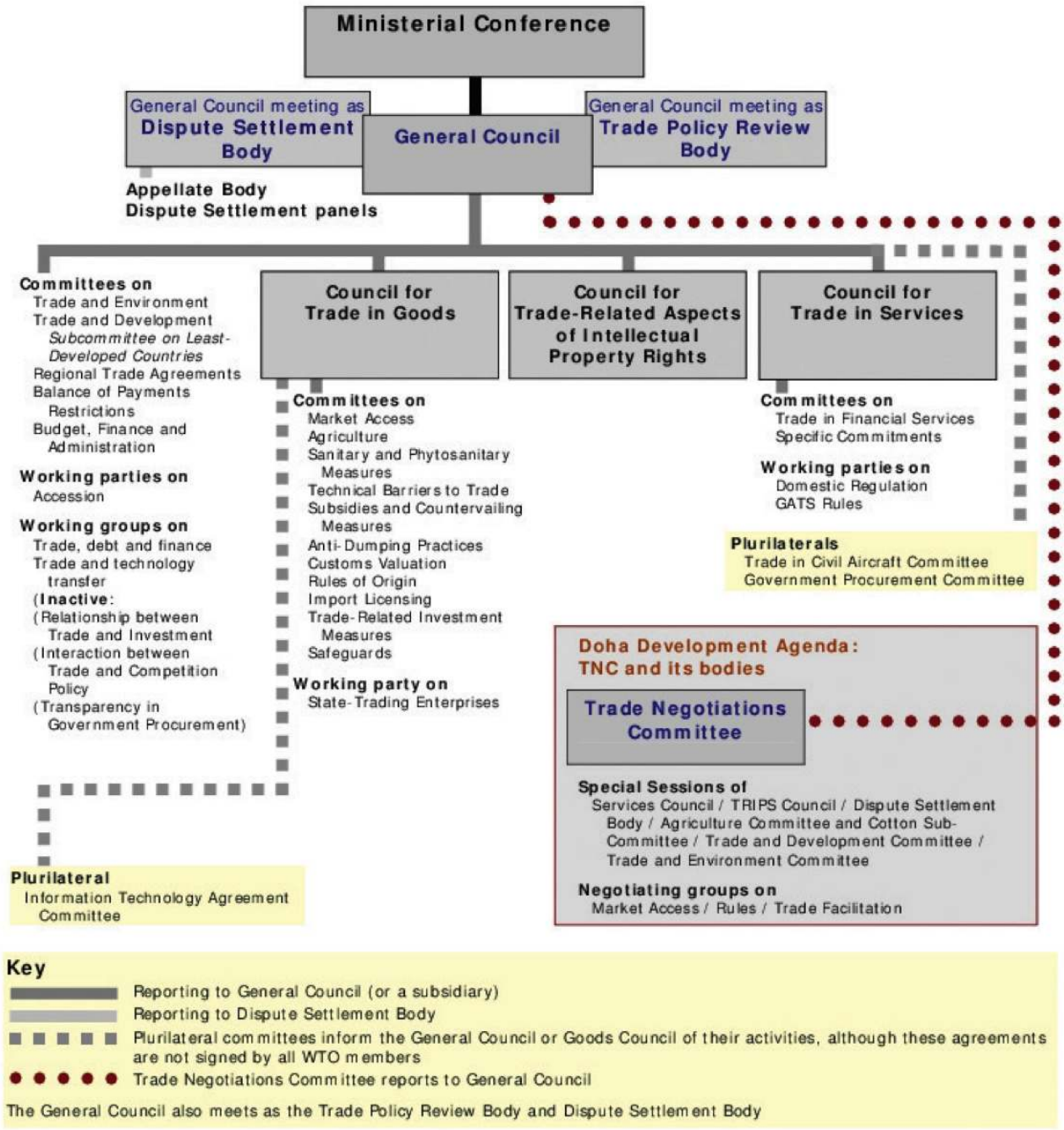


Figure 2.3.1: The Structure of the WTO Source: World Trade Organization, 2011.

The biggest change from GATT to the WTO is the provision for the settlement of disputes. If a country finds another country's trade practices unfair or discriminatory, it may bring the charges to the WTO, which will hear from both countries and mediate a solution.

The WTO has also undertaken the effort to focus on services rather than just goods. Resulting from the Uruguay Round, the General Agreement on Trade in Services (GATS) seeks to reduce the barriers to trade in services. Following the GATT commitment to nondiscrimination, GATS requires member nations to treat foreign service companies as they would domestic ones. For example, if a country requires banks to maintain 10 percent of deposits as reserves, then this percentage should be the same for foreign and domestic banks. Services have proven to be more complex to both define and regulate, and the member nations are continuing the discussions.

Similar to GATS is the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). Intellectual property refers to just about anything that a person or entity creates with the mind. It includes inventions, music, art, and writing, as well as words, phrases, sayings, and graphics—to name a few. The basic premise of intellectual property rights (IPR) law is that the creator of the property has the right to financially benefit from his or her creation. This is particularly important for protecting the development for the creation, known as the research and development (R&D) costs. Companies can also own the intellectual property that their employees generate. This section focuses on the protection that countries agree to give to intellectual property created in another country.

Over the past few decades, companies have become increasingly diligent in protecting their intellectual property and pursuing abusers. Whether it's the knock-off designer handbag from China that lands on the sidewalks of New York or the writer protecting her thoughts in the written words of a book (commonly understood as content), or the global software company combating piracy of its technical know-how, IPR is now formally a part of the WTO agreements and ongoing dialogue.

Current Challenges and Opportunities

Agriculture and textiles are two key sectors in which the WTO faces challenges. Trade in agriculture has been impacted by export-country subsidies, import-country tariffs and restrictions, and nontariff barriers. Whether the United States provides low-cost loans and subsidies to its farmers or Japan restricts the beef imports, agriculture trade barriers are an ongoing challenge for the WTO. Global companies and trade groups that support private-sector firms seek to have their governments raise critical trade issues on their behalf through the WTO.

For example, Japan's ban of beef imports in response to mad cow disease has had a heavy impact on the US beef industry.

At the moment, unfortunately there's some distance between Japan and the U.S.," Japan Agriculture Minister Hirotaka Akamatsu told reporters in 2010 after meeting [US Agriculture Secretary Tom] Vilsack in Tokyo. "For us, food safety based on Japan's scientific standards is the priority. The OIE standards are different from the Japanese scientific ones.

The U.S. beef industry is losing about $1 billion a year in sales because of the restrictions, according to the National Cattlemen's Beef Association, [a trade group supporting the interests of American beef producers]. Japan was the largest foreign buyer of U.S. beef before it banned all imports when the first case of the brain-wasting disease, also known bovine spongiform encephalopathy [i.e., mad cow disease], was discovered in the U.S.

The ban was eased in 2005 to allow meat from cattle aged 20 months or less, which scientists say are less likely to have contracted the fatal illness….

Japan was the third-largest destination for U.S. beef [in 2009], with trade totaling $470 million, up from $383 million in 2008, according to the U.S. Meat Export Federation. That compares with $1.39 billion in 2003.

Mexico and Canada were the biggest buyers of U.S. beef [in 2009].[3]

The role of the WTO is to facilitate agreements in difficult bilateral and multilateral trade disputes, but this certainly isn't easy. Japan's reluctance for American beef may appear to be the result of mad cow disease, but business observers note Japan's historical cultural preference for Japanese goods, which the country often claims are superior. A similar trade conflict was triggered in the 1980s when Japan discouraged the import of rice from other countries. The prevailing Japanese thought was that its local rice was easier for the Japanese to digest. After extensive discussions in the Uruguay Round, on "December 14, 1993 the Japanese government accepted a limited opening of the rice market under the GATT plan."[4]

Antidumping is another area on which the WTO has focused its attention. Dumping occurs when a company exports to a foreign market at a price that is either lower than the domestic prices in that country or less than the cost of production. Antidumping charges can be harder to settle, as the charge is against a company and not a country. One example is in India, which has, in the

past, accused Japan and Thailand of dumping acetone, a chemical used in drugs and explosives, in the Indian market. In an effort to protect domestic manufacturers, India has raised the issue with the WTO. In fact, India was second only to Argentina among the G-20 (or Group of Twenty) nations in initiating antidumping investigations during 2009, according to a recent WTO report.[5]

Future Outlook

While the end of the Doha Round is uncertain, the future for the WTO and any related organizations remains strong. With companies and countries facing a broader array of trade issues than ever before, the WTO plays a critical role in promoting and ensuring free and fair trade. Many observers expect that the WTO will have to emphasize the impact of the Internet on trade. In most cases, the WTO provides companies and countries with the best options to dispute, discuss, and settle unfair business and trade practices.

? Key Takeaways

- The General Agreement on Tariffs and Trade (GATT) is a series of rules governing trade that were first created in 1947 by twenty-three countries. It remained in force until 1995, when it was replaced by the WTO.
- The World Trade Organization (WTO) is the only global, international organization dealing with the rules of trade between nations. The WTO agreements that have been negotiated and signed by the organization's 153 member nations and ratified in their parliaments are the heart of the organization. Its goal is to help the producers, exporters, and importers of goods and services conduct business. The current round of the WTO is called the Doha Round.

References

1. "What Is the WTO?," World Trade Organization, accessed December 29, 2010, http://www.wto.org/english/thewto_e/whatis_e/whatis_e.htm.

2. "The Multilateral Trading System—Past, Present and Future," World Trade Organization, accessed December 29, 2010, http://www.wto.org/english/thewto_e/whatis_e/inbrief_e/inbr01_e.htm .

3. Jae Hur and Ichiro Suzuki, "Japan, U.S. to Continue Dialogue on Beef Import Curbs (Update 1)," BusinessWeek, April 7, 2010, accessed December 29, 2010, http://www.businessweek.com/news/2010-04-07/japan-u-s-to-continue-dialogue-on-beef-import-curbs-update1-.html.

4. "Japan Rice Trade," case study on American University website, accessed January 2, 2010, http://www1.american.edu/ted/japrice.htm.

<. Press Trust of India, "Govt Initiates Anti-Dumping Probe against Acetone Imports," Business Standard, November 3, 2009, accessed December 29, 2010, http://www.business-standard.com/india/news/govt-initiates-anti-dumping-probe-against-acetone-imports/375153/ .

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 2.3: International Economic Cooperation among Nations is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

2.4: Understanding Tariffs

Learning Objectives

After reading this section, students should be able to …

1. Learn the different methods used to assess a tariff.
2. Measure, interpret, and compare average tariffs around the world.

The most common way to protect one's economy from import competition is to implement a tariff: a tax on imports. Generally speaking, a tariff is any tax or fee collected by a government. Sometimes the term "tariff" is used in a nontrade context, as in railroad tariffs. However, the term is much more commonly used to refer to a tax on imported goods.

Tariffs have been applied by countries for centuries and have been one of the most common methods used to collect revenue for governments. Largely this is because it is relatively simple to place customs officials at the border of a country and collect a fee on goods that enter. Administratively, a tariff is probably one of the easiest taxes to collect. (Of course, high tariffs may induce smuggling of goods through nontraditional entry points, but we will ignore that problem here.)

Tariffs represent the primary way in which countries either liberalize trade or protect their economies. It isn't the only way, though, since countries also implement subsidies, quotas, and other types of regulations that can affect trade flows between countries. When people talk about trade liberalization, they generally mean reducing the tariffs on imported goods, thereby allowing the products to enter at a lower cost. Since lowering the cost of trade makes it more profitable, it will make trade freer. Complete elimination of tariffs and other barriers to trade is what economists and others mean by free trade. In contrast, any increase in tariffs is referred to as protection or protectionism. Because tariffs raise the cost of importing products from abroad but not from domestic firms, they have the effect of protecting the domestic firms that compete with imported products. These domestic firms are called import competitors.

There are two basic ways in which tariffs may be levied: specific tariffs and ad valorem tariffs. A specific tariff is levied as a fixed charge per unit of imports. For example, the U.S. government levies a $0.51 specific tariff on every wristwatch imported into the United States. Thus, if one thousand watches are imported, the U.S. government collects $510 in tariff revenue. In this case, $510 is collected whether the watch is a $40 Swatch or a $5,000 Rolex.

An ad valorem tariff is levied as a fixed percentage of the value of the commodity imported. "Ad valorem" is Latin for "on value" or "in proportion to the value." The United States currently levies a 2.5 percent ad valorem tariff on imported automobiles. Thus, if $100,000 worth of automobiles is imported, the U.S. government collects $2,500 in tariff revenue. In this case, $2,500 is collected whether two $50,000 BMWs or ten $10,000 Hyundais are imported.

Occasionally, both a specific and an ad valorem tariff are levied on the same product simultaneously. This is known as a two-part tariff. For example, wristwatches imported into the United States face the $0.51 specific tariff as well as a 6.25 percent ad valorem tariff on the case and the strap and a 5.3 percent ad valorem tariff on the battery. Perhaps this should be called a three-part tariff!

As the above examples suggest, different tariffs are generally applied to different commodities. Governments rarely apply the same tariff to all goods and services imported into the country. Several countries prove the exception, though. For example, Chile levies a 6 percent tariff on every imported good, regardless of the category. Similarly, the United Arab Emirates sets a 5 percent tariff on almost all items, while Bolivia levies tariffs either at 0 percent, 2.5 percent, 5 percent, 7.5 percent, or 10 percent. Nonetheless, simple and constant tariffs such as these are uncommon.

Thus, instead of one tariff rate, countries have a tariff schedule that specifies the tariff collected on every particular good and service. In the United States, the tariff schedule is called the Harmonized Tariff Schedule (HTS) of the United States. The commodity classifications are based on the international Harmonized Commodity Coding and Classification System (or the Harmonized System) established by the World Customs Organization.

Measuring Protectionism: Average Tariff Rates around the World

One method used to measure the degree of protectionism within an economy is the average tariff rate. Since tariffs generally reduce imports of foreign products, the higher the tariff, the greater the protection afforded to the country's import-competing industries.

At one time, tariffs were perhaps the most commonly applied trade policy. Many countries used tariffs as a primary source of funds for their government budgets. However, as trade liberalization advanced in the second half of the twentieth century, many other types of nontariff barriers became more prominent.

Table 2.4.1 "Average Tariffs in Selected Countries (2009)" provides a list of average tariff rates in selected countries around the world. These rates were calculated as the simple average tariff across more than five thousand product categories in each country's applied tariff schedule located on the World Trade Organization (WTO) Web site. The countries are ordered by highest to lowest per capita income.

Table 2.4.1 Average Tariffs in Selected Countries (2009)

Country	Average Tariff Rates (%)
United States	3.6
Canada	3.6
European Community (EC)	4.3
Japan	3.1
South Korea	11.3
Mexico	12.5
Chile	6.0 (uniform)
Argentina	11.2
Brazil	13.6
Thailand	9.1
China	9.95
Egypt	17.0
Philippines	6.3
India	15.0
Kenya	12.7
Ghana	13.1

Generally speaking, average tariff rates are less than 20 percent in most countries, although they are often quite a bit higher for agricultural commodities. In the most developed countries, average tariffs are less than 10 percent and often less than 5 percent. On average, less-developed countries maintain higher tariff barriers, but many countries that have recently joined the WTO have reduced their tariffs substantially to gain entry.

Problems Using Average Tariffs as a Measure of Protection

The first problem with using average tariffs as a measure of protection in a country is that there are several different ways to calculate an average tariff rate, and each method can give a very different impression about the level of protection.

The tariffs in Table 2.4.1 "Average Tariffs in Selected Countries (2009)" are calculated as a simple average. To calculate this rate, one simply adds up all the tariff rates and divides by the number of import categories. One problem with this method arises if a country has most of its trade in a few categories with zero tariffs but has high tariffs in many categories it would never find advantageous to import. In this case, the average tariff may overstate the degree of protection in the economy.

This problem can be avoided, to a certain extent, if one calculates the trade-weighted average tariff. This measure weighs each tariff by the share of total imports in that import category. Thus, if a country has most of its imports in a category with very low tariffs but has many import categories with high tariffs and virtually no imports, then the trade-weighted average tariff would indicate a low level of protection. The simple way to calculate a trade-weighted average tariff rate is to divide the total tariff revenue by the total value of imports. Since these data are regularly reported by many countries, this is a common way to report average tariffs. To illustrate the difference, the United States is listed in Table 2.4.1 "Average Tariffs in Selected Countries (2009)" with a simple average tariff of 3.6 percent. However, in 2008 the U.S. tariff revenue collected came to $29.2 billion from imports of goods totaling $2,126 billion, meaning that the U.S. trade-weighted average tariff was a mere 1.4 percent.

Nonetheless, the trade-weighted average tariff is not without flaws. For example, suppose a country has relatively little trade because it has prohibitive tariffs (i.e., tariffs set so high as to eliminate imports) in many import categories. If it has some trade in a few import categories with relatively low tariffs, then the trade-weighted average tariff would be relatively low. After all, there would be no tariff revenue in the categories with prohibitive tariffs. In this case, a low average tariff could be reported for a highly protectionist country. Also, in this case, the simple average tariff would register as a higher average tariff and might be a better indicator of the level of protection in the economy.

Of course, the best way to overstate the degree of protection is to use the average tariff rate on *dutiable* imports. This alternative measure, which is sometimes reported, only considers categories in which a tariff is actually levied and ignores all categories in which the tariff is set to zero. Since many countries today have many categories of goods with zero tariffs applied, this measure would give a higher estimate of average tariffs than most of the other measures.

The second major problem with using average tariff rates to measure the degree of protection is that tariffs are not the only trade policy used by countries. Countries also implement quotas, import licenses, voluntary export restraints, export taxes, export subsidies, government procurement policies, domestic content rules, and much more. In addition, there are a variety of domestic regulations that, for large economies at least, can and do have an impact on trade flows. None of these regulations, restrictions, or impediments to trade, affecting both imports and exports, would be captured using any of the average tariff measures. Nevertheless, these nontariff barriers can have a much greater effect on trade flows than tariffs themselves.

? Key Takeaways

- Specific tariffs are assessed as a money charge per unit of the imported good.
- Ad valorem tariffs are assessed as a percentage of the value of the imported good.
- Average tariffs can be measured as a simple average across product categories or can be weighted by the level of imports.
- Although average tariffs are used to measure the degree of protection or openness of a country, neither measure is best because each measure has unique problems.
- In general, average tariffs are higher in developing countries and lower in developed countries.

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 2.4: Understanding Tariffs is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

2.5: Regional Economic Integration

Learning Objectives

After reading this section, students should be able to …

1. Understand regional economic integration.
2. Identify the major regional economic areas of cooperation.

What Is Regional Economic Integration?

Regional economic integration has enabled countries to focus on issues that are relevant to their stage of development as well as encourage trade between neighbors.

There are four main types of regional economic integration.

1. **Free trade area.** This is the most basic form of economic cooperation. Member countries remove all barriers to trade between themselves but are free to independently determine trade policies with nonmember nations. An example is the North American Free Trade Agreement (NAFTA).
2. **Customs union.** This type provides for economic cooperation as in a free-trade zone. Barriers to trade are removed between member countries. The primary difference from the free trade area is that members agree to treat trade with nonmember countries in a similar manner.[1]
3. **Common market.** This type allows for the creation of economically integrated markets between member countries. Trade barriers are removed, as are any restrictions on the movement of labor and capital between member countries. Like customs unions, there is a common trade policy for trade with nonmember nations. The primary advantage to workers is that they no longer need a visa or work permit to work in another member country of a common market. An example is the Common Market for Eastern and Southern Africa (COMESA).[2]
4. **Economic union.** This type is created when countries enter into an economic agreement to remove barriers to trade and adopt common economic policies. An example is the European Union (EU).[3]

In the past decade, there has been an increase in these trading blocs with more than one hundred agreements in place and more in discussion. A trade bloc is basically a free-trade zone, or near-free-trade zone, formed by one or more tax, tariff, and trade agreements between two or more countries. Some trading blocs have resulted in agreements that have been more substantive than others in creating economic cooperation. Of course, there are pros and cons for creating regional agreements.

Pros

The pros of creating regional agreements include the following:

- **Trade creation.** These agreements create more opportunities for countries to trade with one another by removing the barriers to trade and investment. Due to a reduction or removal of tariffs, cooperation results in cheaper prices for consumers in the bloc countries. Studies indicate that regional economic integration significantly contributes to the relatively high growth rates in the less-developed countries.
- **Employment opportunities.** By removing restrictions on labor movement, economic integration can help expand job opportunities.
- **Consensus and cooperation.** Member nations may find it easier to agree with smaller numbers of countries. Regional understanding and similarities may also facilitate closer political cooperation.

Cons

The cons involved in creating regional agreements include the following:

- **Trade diversion.** The flip side to trade creation is trade diversion. Member countries may trade more with each other than with nonmember nations. This may mean increased trade with a less efficient or more expensive producer because it is in a member country. In this sense, weaker companies can be protected inadvertently with the bloc agreement acting as a trade barrier. In essence, regional agreements have formed new trade barriers with countries outside of the trading bloc.

- **Employment shifts and reductions.** Countries may move production to cheaper labor markets in member countries. Similarly, workers may move to gain access to better jobs and wages. Sudden shifts in employment can tax the resources of member countries.
- **Loss of national sovereignty.** With each new round of discussions and agreements within a regional bloc, nations may find that they have to give up more of their political and economic rights. In the opening case study, you learned how the economic crisis in Greece is threatening not only the EU in general but also the rights of Greece and other member nations to determine their own domestic economic policies.

Major Areas of Regional Economic Integration and Cooperation

There are more than one hundred regional trade agreements in place, a number that is continuously evolving as countries reconfigure their economic and political interests and priorities. Additionally, the expansion of the World Trade Organization (WTO) has caused smaller regional agreements to become obsolete. Some of the regional blocs also created side agreements with other regional groups leading to a web of trade agreements and understandings.

North America: NAFTA

Brief History and Purpose

The North American Free Trade Agreement (NAFTA) came into being during a period when free trade and trading blocs were popular and positively perceived. In 1988, the United States and Canada signed the Canada–United States Free Trade Agreement. Shortly after it was approved and implemented, the United States started to negotiate a similar agreement with Mexico. When Canada asked to be party to any negotiations to preserve its rights under the most-favored-nation clause (MFN), the negotiations began for NAFTA, which was finally signed in 1992 and implemented in 1994.

The goal of NAFTA has been to encourage trade between Canada, the United States, and Mexico. By reducing tariffs and trade barriers, the countries hope to create a free-trade zone where companies can benefit from the transfer of goods. In the 1980s, Mexico had tariffs as high as 100 percent on select goods. Over the first decade of the agreement, almost all tariffs between Mexico, Canada, and the United States were phased out.

The rules governing origin of content are key to NAFTA. As a free trade agreement, the member countries can establish their own trading rules for nonmember countries. NAFTA's rules ensure that a foreign exporter won't just ship to the NAFTA country with the lowest tariff for nonmember countries. NAFTA rules require that at least 50 percent of the net cost of most products must come from or be incurred in the NAFTA region. There are higher requirements for footwear and cars. For example, this origin of content rule has ensured that cheap Asian manufacturers wouldn't negotiate lower tariffs with one NAFTA country, such as Mexico, and dump cheap products into Canada and the United States. Mexican *maquiladoras* have fared well in this arrangement by being the final production stop before entering the United States or Canada. *Maquiladoras* are production facilities located in border towns in Mexico that take imported materials and produce the finished good for export, primarily to Canada or the United States.

Current Challenges and Opportunities

Canadian and US consumers have benefited from the lower-cost Mexican agricultural products. Similarly, Canadian and US companies have sought to enter the expanding Mexican domestic market. Many Canadian and US companies have chosen to locate their manufacturing or production facilities in Mexico rather than Asia, which was geographically far from their North American bases.

When it was introduced, NAFTA was highly controversial, particularly in the United States, where many felt it would send US jobs to Mexico. In the long run, NAFTA hasn't been as impactful as its supporters had hoped nor as detrimental to workers and companies as its critics had feared. As part of NAFTA, two side agreements addressing labor and environmental standards were put into place. The expectation was that these side agreements would ensure that Mexico had to move toward improving working conditions.

Mexico has fared the best from NAFTA as trade has increased dramatically. *Maquiladoras* in Mexico have seen a 15 percent annual increase in income. By and large, Canadians have been supportive of NAFTA and exports to the region have increased in the period since implementation. "Tri-lateral [merchandise] trade has nearly tripled since NAFTA came into force in 1994. It topped $1 trillion in 2008."[4]

Future Outlook

Given the 2008 global economic recession and challenging impact on the EU, it isn't likely that NAFTA will move beyond the free-trade zone status to anything more comprehensive (e.g., the EU's economic union). In the opening case study, you read about the pressures on the EU and the resistance by each of the governments in Europe to make policy adjustments to address the recession. The United States, as the largest country member in NAFTA, won't give up its rights to independently determine its economic and trade policies. Observers note that there may be the opportunity for NAFTA to expand to include other countries in Latin America.[5] Chile was originally supposed to be part of NAFTA in 1994, but President Clinton was hampered by Congress in his ability to formalize that decision.[6] Since then, Canada, Mexico, and the United States have each negotiated bilateral trade agreements with Chile, but there is still occasional mention that Chile may one day join NAFTA.[7]

Did You Know?

Mexico, NAFTA, and the *Maquiladoras*

The Mexican economy has undergone dramatic changes during the last decade and a half as the country has become integrated into the global marketplace. Once highly protected, Mexico is now open for business. Successive governments have instituted far-reaching economic reforms, which have had a major impact on the way business is conducted. The scale of business has changed as well. Forced to compete with large multinationals and Mexican conglomerates, many traditional family-owned firms have had to close because they were unable to compete in the global marketplace.

NAFTA has added to the already-strong US influence on Mexico's corporate and business practices. In particular, competitiveness and efficiency have become higher priorities, although company owners and managers still like to surround themselves with people they know and to groom their sons and sometimes their daughters to be their successors. US influence is also pervasive in the products and services offered throughout Mexico.

Mexico has always had a strong entrepreneurial business culture, but until NAFTA, it was protected from the pressures of international finance and the global marketplace. Business and particularly interpersonal business relationships were viewed as something that should be pleasurable, like other important aspects of life.

Long-term relationships are still the foundation on which trust is established and business is built. In Mexico, patience and the willingness to wait are still highly valued—and necessary—in business transactions. This is slowly changing, spurred in part by an aggressive cadre of young professionals who pursued graduate education in the United States.

Since the mid-1960s, production facilities known as *maquiladoras* have been a regular feature of Mexican border towns, especially along the Texas and New Mexico borders. US multinational companies, such as John Deere, Zenith, Mattel, and Xerox, run the majority of the more than 3,600 maquiladoras in northern Mexico. Billions of dollars' worth of products—from televisions to clothes to auto parts—are assembled in maquiladoras and then shipped back, tax free, to the United States for sale to US consumers.

Maquiladoras employ more than a million Mexicans, mostly unskilled women in their twenties and early thirties who work long hours. Wages and benefits are generally poor but much better than in the rest of Mexico. The huge growth in trade between the United States and Mexico has greatly expanded the role—and scale—of these assembly operations.

Along with the benefits, challenges have also come with the increased trade. A large number of Mexicans are concerned that wealth is distributed more unevenly than ever. For example, many commentators see the political situation in the state of Chiapas as underscoring the alienation large groups have suffered as a result of the opening of the Mexican economy to global forces. A rural region in southern Mexico, Chiapas is home to extremely poor Mayan, Ch'ol, Zoque, and Lacandón Indians. Although it is the poorest state in Mexico, Chiapas has the richest natural resources, including oil, minerals, and electrical power.

On January 1, 1994, the day NAFTA officially took effect, a group of Indian peasants, commanded by Subcomandante Marcos, rose up in armed rebellion. This was shocking not only to Mexico's leadership but to the international community. The unrest in Chiapas stems from long-standing economic and social injustice in the region and from the Indians' isolation and exploitation by the local oligarchy of landowners and mestizo bosses (*caciques*). While NAFTA clearly advanced the goals of free trade, global businesses are often forced to deal with local economic, political, and social realities within a country.

The Mexican government has indicated that improving the social conditions in the region is a high priority. However, only partial accords have been reached between the government and the peasants. At the same time, the army continues to exert tight control over the state, particularly in and around towns where residents are known to support the rebels.

The low standard of living in Chiapas and of Indians throughout Mexico remains a significant challenge for the Mexican government. In the years following the Chiapas uprising, poverty in southern Mexico has risen to about 40 percent, while in the north, poverty has decreased thanks to closer economic links with the United States.[8]

South America: MERCOSUR

The Common Market of the South, Mercado Común del Sur or MERCOSUR, was originally established in 1988 as a regional trade agreement between Brazil and Argentina and then was expanded in 1991 to include Uruguay and Paraguay. Over the past decade, Bolivia, Chile, Colombia, Ecuador, and Peru have become associate members, and Venezuela is in the process for full membership.

MERCOSUR constituents compose nearly half of the wealth created in all of Latin America as well as 40 percent of the population. Now the world's fourth-largest trading bloc after the EU, NAFTA, and the Association of South East Asian Nations (ASEAN),[9] the group has been strategically oriented to develop the economies of its constituents, helping them become more internationally competitive so that they would not have to rely on the closed market arena. MERCOSUR has brought nations with long-standing rivalries together. Although this is an economic trade initiative, it has also been designed with clear political goals. MERCOSUR is committed to the consolidation of democracy and the maintenance of peace throughout the southern cone. For example, it has taken stride to reach agreements between Brazil and Argentina in the nuclear field.[10]

MERCOSUR has emerged as one of the most dynamic and imaginative initiatives in the region. Surging trade, rising investment, and expanding output are the economic indicators that point to the group's remarkable achievement. More than this, the integration is helping transform national relations among South American nations and with the world as a whole, forging a new sense of shared leadership and shared purpose, which is sending ripples of hope across the continent and beyond.

Other Trade Agreements in the Americas

CARICOM and Andean Community

The Caribbean Community and Common Market (CARICOM), or simply the Caribbean Community, was formed in 1973 by countries in the Caribbean with the intent of creating a single market with the free flow of goods, services, labor, and investment.[11] The Andean Community (called the Andean Pact until 1996)[12] is a free trade agreement signed in 1969 between Bolivia, Chile, Colombia, Ecuador, and Peru. Eventually Chile dropped out, while Venezuela joined for about twenty years and left in 2006. This trading bloc had limited impact for the first two decades of its existence but has experienced a renewal of interest after MERCOSUR's implementation. In 2007, MERCOSUR members became associate members of the Andean Community, and more cooperative interaction between the trading groups is expected.[13]

CAFTA-DR

The Dominican Republic–Central America–United States Free Trade Agreement (CAFTA-DR) is a free trade agreement signed into existence in 2005. Originally, the agreement (then called the Central America Free Trade Agreement, or CAFTA) encompassed discussions between the US and the Central American countries of Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua. A year before the official signing, the Dominican Republic joined the negotiations, and the agreement was renamed CAFTA-DR.[14]

The goal of the agreement is the creation of a free trade area similar to NAFTA. For free trade advocates, the CAFTA-DR is also seen as a stepping stone toward the eventual establishment of the Free Trade Area of the Americas (FTAA)—the more ambitious grouping for a free trade agreement that would encompass all the South American and Caribbean nations as well as those of North and Central America (except Cuba). Canada is currently negotiating a similar treaty called the Canada Central American Free Trade Agreement. It's likely that any resulting agreements will have to reconcile differences in rules and regulations with NAFTA as well as any other existing agreements.[15]

Did You Know?

As a result of CAFTA-DR, more than 80 percent of goods exported from the United States into the region are no longer subject to tariffs.[16] Given its physical proximity, Florida is the main investment gateway to the CAFTA-DR countries: about three hundred multinational firms have their Latin American and Caribbean regional headquarters in Florida. In all, more than two thousand companies headquartered outside the United States operate in Florida.

US companies, for example, sell more than $25 billion in products to the Latin American and Caribbean regions annually, ranking it among the top US export markets. With the removal of virtually all tariffs and other barriers to trade, the CAFTA-DR agreement is making commerce with these countries even easier, opening opportunities to a range of industries. At the same time, it's making the CAFTA-DR countries richer and increasing the purchasing power of their citizens.

For international companies looking to access these markets, the United States, recognized worldwide for its stable regulatory and legal framework and for its robust infrastructure, is the most logical place to set up operations. And within the United States, no location is as well positioned as Florida to act as the gateway to the CAFTA-DR markets. For a variety of reasons—from geography and language to well-developed business and family connections—this is a role that Florida has been playing very successfully for a number of years and which, with the implementation of CAFTA-DR, is only gaining in importance.[17]

Europe: EU

Brief History and Purpose

The European Union (EU) is the most integrated form of economic cooperation. As you learned in the opening case study, the EU originally began in 1950 to end the frequent wars between neighboring countries in the Europe. The six founding nations were France, West Germany, Italy, and the Benelux countries (Belgium, Luxembourg, and the Netherlands), all of which signed a treaty to run their coal and steel industries under a common management. The focus was on the development of the coal and steel industries for peaceful purposes.

In 1957, the six nations signed the Treaty of Rome, which established the European Economic Community (EEC) and created a common market between the members. Over the next fifty years, the EEC added nine more members and changed its name twice—to European Community (EC) in the 1970s and the European Union (EU) in 1993.[18]

The entire history of the transformation of the EEC to the EU has been an evolutionary process. However, the Treaty of Maastricht in 1993 stands out as an important moment; it's when the *real*economic union was created. With this treaty, the EU identified three aims. The first was to establish a single, common currency, which went into effect in 1999. The second was to set up monetary and fiscal targets for member countries. Third, the treaty called for a political union, which would include the development of a common foreign and defense policy and common citizenship. The opening case study addressed some of the current challenges the EU is facing as a result of the impact of these aims. Despite the challenges, the EU is likely to endure given its historic legacy. Furthermore, a primary goal for the development of the EU was that Europeans realized that they needed a larger trading platform to compete against the US and the emerging markets of China and India. Individually, the European countries would never have the economic power they now have collectively as the EU.

Today, the EU has twenty-seven member countries. Croatia, Iceland, Macedonia, and Turkey are the next set of candidates for future membership. In 2009, the twenty-seven EU countries signed the Treaty of Lisbon, which amends the previous treaties. It is designed to make the EU more democratic, efficient, and transparent and to tackle global challenges, such as climate change, security, and sustainable development.

The European Economic Area (EEA) was established on January 1, 1994, following an agreement between the member states of the European Free Trade Association (EFTA) and the EC (later the EU). Specifically, it has allowed Iceland (now an EU candidate), Liechtenstein, and Norway to participate in the EU's single market without a conventional EU membership. Switzerland has also chosen to not join the EU, although it is part of similar bilateral agreements.

Countries in the EU (as May 1,2011)

Austria
Belgium

Bulgaria
Cyprus
Czech Republic
Denmark
Estonia
Finland
France
Greece
Hungary
Ireland
Italy
Latvia
Lithuania
Luxembourg
Malta
Netherlands
Poland
Portugal
Romania
Slovakia
Slovenia
Sweden
United Kingdom

Candidate Countries

Croatia
The former Yugoslav Republic of Macedonia
Turkey
Iceland

Potential Candidate Countries

Albania
Bosnia and Herzegovina
Kosovo under UN Security Council Resolution 1244
Montenegro
Serbia

Source: "The Member Countries of the European Union," Europa, accessed May 1, 2011, http://europa.eu/about-eu/member-cou...s/index_en.htm .

CEFTA

Central European Free Trade Agreement (CEFTA) is a trade agreement between non-EU countries in Central and Southeastern Europe, which currently includes Albania, Bosnia and Herzegovina, Croatia, Macedonia, Moldova, Montenegro, Serbia, and the United Nations Interim Administration Mission on behalf of Kosovo (UNMIK)—all of whom joined in 2006.[19]

Originally signed in 1992, CEFTA's founding members were the Visegrad Group, also called the Visegrad Four or V4, which is an alliance of four Central European states—the Czech Republic, Hungary, Poland, and Slovakia. All of the Visegrad Group have relatively developed free-market economies and have formal ties.[20]

Many of the Central European nations have left CEFTA to become members of the EU. In fact, CEFTA has served as a preparation for full EU membership and a large proportion of CEFTA foreign trade is with EU countries. Poland, the Czech

Republic, Hungary, Slovakia, and Slovenia joined the EU on May 1, 2004, with Bulgaria and Romania following suit on January 1, 2007.[21] Croatia and Macedonia are in the process of becoming EU members.[22]

Amusing Anecdote

There are twenty-three official and working languages within the EU, and all official documents and legislation are translated into all of these languages. With this in mind, it's easy to see why so many Europeans see the need to speak more than one language fluently!

Official and Working Languages of the EU

Bulgarian
Czech
Danish
Dutch
English
Estonian
Finnish
French
German
Greek
Hungarian
Italian
Irish
Latvian
Lithuanian
Maltese
Polish
Portuguese
Romanian
Slovene
Spanish
Swedish

EU Governance

The EU is a unique organization in that it is not a single country but a group of countries that have agreed to closely cooperate and coordinate key aspects of their economic policy. Accordingly, the organization has its own governing and decision-making institutions.

- **European Council.** The European Council provides the political leadership for the EU. The European Council meets four times per year, and each member has a representative, usually the head of its government. Collectively it functions as the EU's "Head of State."
- **European Commission.** The European Commission provides the day-to-day leadership and initiates legislation. It's the EU's executive arm.
- **European Parliament.** The European Parliament forms one-half of the EU's legislative body. The parliament consists of 751 members, who are elected by popular vote in their respective countries. The term for each member is five years. The purpose of the parliament is to debate and amend legislation proposed by the European Commission.
- **Council of the European Union.** The Council of the European Union functions as the other half of the EU's legislative body. It's sometimes called the Council or the Council of Ministers and should not be confused with the European Council above. The Council of the European Union consists of a government minister from each member country and its representatives may change depending on the topic being discussed.
- **Court of Justice.** The Court of Justice makes up the judicial branch of the EU. Consisting of three different courts, it reviews, interprets, and applies the treaties and laws of the EU.[23]

Current Challenges and Opportunities

The biggest advantage of EU membership is the monetary union. Today, sixteen member countries use the euro. Since its launch, the euro has become the world's second-largest reserve currency behind the US dollar. It's important to remember several distinctions. First, the EU doesn't consist of the same countries as the continent of Europe. Second, there are more EU member countries than there are countries using the euro. Euro markets, or euro countries, are the countries using the euro.

The European single market is the foremost advantage of being a member of EU. According to Europa, which is the official website of the EU (http://europa.eu), the EU member states have formed a single market with more than five hundred million people, representing 7 percent of the world's population. This single market permits the free flow of goods, service, capital, and people within the EU.[24] Although there is a single tariff on goods entering an EU country, once in the market, no additional tariffs or taxes can be levied on the goods.[25]

Businesses conducting business with one country in the EU now find it easier and cheaper, in many cases, to transact business with the other EU countries. There's no longer a currency–exchange rate risk, and the elimination of the need to convert currencies within euro markets reduces transaction costs. Further, having a single currency makes pricing more transparent and consistent between countries and markets.

Despite the perceived benefits, economic policymakers in the EU admit that the Union's labor markets are suffering from rigidity, regulation, and tax structures that have contributed to high unemployment and low employment responsiveness to economic growth. This is the case, particularly, for relatively low-skilled labor.

Future Outlook

Europe's economy faces a deeper recession and a slower recovery than the United States or other parts of the world. Because the EU's $18.4 trillion economy makes up 30 percent of the world economy, its poor prospects are likely to rebound on the United States, Asia, and other regions.[26] Fixing the EU's banking system is particularly tricky, because sixteen of the twenty-seven countries share the euro currency and a central bank, but banking regulation mostly remains under the control of the national governments.[27]

The Europe 2020 strategy put forth by the European Commission sets out a vision of the EU's social market economy for the twenty-first century. It shows how the EU can come out stronger from this crisis and how it can be turned into a smart, sustainable, and inclusive economy delivering high levels of employment, productivity, and social cohesion. It calls for stronger economic governance in order to deliver rapid and lasting results.[28]

Asia: ASEAN

The Association of Southeast Asian Nations (ASEAN) was created in 1967 by five founding-member countries: Malaysia, Thailand, Indonesia, Singapore, and the Philippines. Since inception, Myanmar (Burma), Vietnam, Cambodia, Laos, and Brunei have joined the association.[29]

ASEAN's primary focus is on economic, social, cultural, and technical cooperation as well as promoting regional peace and stability. Although less emphasized today, one of the primary early missions of ASEAN was to prevent the domination of Southeast Asia by external powers—specifically China, Japan, India, and the United States.

In 2002, ASEAN and China signed a free trade agreement that went into effect in 2010 as the ASEAN–China Free Trade Area (ACFTA). In 2009, ASEAN and India also signed the ASEAN–India Free Trade Agreement (FTA). In 2009, ASEAN signed a free trade agreement with New Zealand and Australia. It also hopes to create an ASEAN Economic Community by 2015.[30] While the focus and function remains in discussion, the intent is to forge even closer ties among the ten member nations, enabling them to negotiate more effectively with global powers like the EU and the United States.[31]

Asia: APEC

The Asia–Pacific Economic Cooperation (APEC) was founded in 1989 by twelve countries as an informal forum. It now has twenty-one member economies on both sides of the Pacific Ocean. APEC is the only regional trading group that uses the term *member economies*, rather than countries, in deference to China. Taiwan was allowed to join the forum, but only under the name Chinese Taipei.[32]

As a result of the Pacific Ocean connection, this geographic grouping includes the United States, Canada, Mexico, Chile, Peru, Russia, Papua New Guinea, New Zealand, and Australia with their Asia Pacific Rim counterparts.[33] This assortment of economies and cultures has, at times, made for interesting and heated discussions. Focused primarily on economic growth and cooperation, the regional group has met with success in liberalizing and promoting free trade as well as facilitating business, economic, and technical cooperation between member economies. With the Doha Round of the WTO dragging, APEC members have been discussing establishing a free-trade zone. Given its broader membership than ASEAN, APEC has found good success—once its member countries agree. The two organizations often share common goals and seek to coordinate their efforts.

China Seeks to Create a Trading Bloc

On June 29, 2010, China and Taiwan signed the Economic Cooperation Framework Agreement (ECFA), a preferential trade agreement between the two governments that aims to reduce tariffs and commercial barriers between the two sides. It's the most significant agreement since the two countries split at the end of the Chinese Civil War in 1949.[34] It will boost the current $110 billion bilateral trade between both sides. China already absorbed Hong Kong in 1999, after the hundred-year lease to Britain ended. While Hong Kong is now managed by China as a Special Administrative Region (SAR), it continues to enjoy special economic status. China is eager for Hong Kong and Taiwan to serve as gateways to its massive market. Taiwan's motivation for signing the agreement was in large part an effort to get China to stop pressuring other countries from signing trade agreements with it.[35]

"An economically stronger Taiwan would not only gain clout with the mainland but also have more money to entice allies other than the 23 nations around the globe that currently recognize the island as an independent state. Beijing is hoping closer economic ties will draw Taiwan further into its orbit."[36] While opposition in Taiwan sees the agreement as a cover for reunification with China, the agreement does reduce tariffs on both sides, enabling businesses from both countries to engage in more trade.

Middle East and Africa: GCC

The Cooperation Council for the Arab States of the Gulf, also known as the Gulf Cooperation Council (GCC), was created in 1981. The six member states are Bahrain, Kuwait, Saudi Arabia, Oman, Qatar, and the United Arab Emirates (UAE). As a political and economic organization, the group focuses on trade, economic, and social issues.[37] The GCC has become as much a political organization as an economic one. Among its various initiatives, the GCC calls for the coordination of a unified military presence in the form of a Peninsula Shield Force.[38]

In 1989, the GCC and the EU signed a cooperation agreement. "Trade between the EU and the GCC countries totalled €79 billion in 2009 and should increase under the FTA. And while strong economic relations remain the basis for mutual ties, the EU and the GCC also share common interests in areas such as the promotion of alternative energy, thus contributing to the resolution of climate change and other pressing environmental concerns; the promotion of proper reform for the global economic and financial policies; and the enhancement of a comprehensive rules-based international system."[39]

In 2008, the GCC formed a common market, enabling free flow of trade, investment, and workers.[40] In December 2009, Bahrain, Saudi Arabia, Kuwait, and Qatar created a monetary council with the intent of eventually creating a shared currency.[41] Since its creation, the GCC has contributed not only to the expansion of trade but also to the development of its countries and the welfare of its citizens, as well as promoting peace and stability in the region.[42]

Middle East and Africa: AEC

The African Economic Community (AEC) is an organization of the African Union states. Signed in 1991 and implemented in 1994, it provides for a staged integration of the regional economic agreements. Several regional agreements function as pillars of the AEC:[43]

- Community of Sahel-Saharan States (CEN-SAD)
- Common Market for Eastern and Southern Africa (COMESA)
- East African Community (EAC)
- Economic Community of Central African States (ECCAS/CEEAC)

- Economic Community of West African States (ECOWAS)
- Intergovernmental Authority on Development (IGAD)
- Southern African Development Community (SADC)
- Arab Maghreb Union (AMU/UMA)

Economists argue that free trade zones are particularly suited to African countries which were created under colonial occupation when land was divided up, often with little regard for the economic sustainability of the newly created plot.

Plus, post-independence conflict in Africa has left much of the continent with a legacy of poor governance and a lack of political integration which free trade zones aim to address….

[In October 2008,] plans were agreed to create a "super" free trade zone encompassing 26 African countries, stretching from Libya in the north to South Africa. The GDP of this group of nations is put at $624bn (£382.9bn).[44]

Ambitiously, in 2017 and after, the AEC intends to foster the creation of a free-trade zone and customs union in its regional blocs. Beyond that, there are hopes for a shared currency and eventual economic and monetary union.

How Do These Trade Agreements and Efforts Impact Business?

Overall, global businesses have benefited from the regional trade agreements by having more consistent criteria for investment and trade as well as reduced barriers to entry. Companies that choose to manufacture in one country find it easier and cheaper to move goods between member countries in that trading bloc without incurring tariffs or additional regulations.

The challenges for businesses include finding themselves outside of a new trading bloc or having the "rules" for their industry change as a result of new trade agreements. Over the past few decades, there has been an increase in bilateral and multilateral trade agreements. It's often called a "spaghetti bowl" of global bilateral and multilateral trade agreements, because the agreements are not linear strands lining up neatly; instead they are a messy mix of crisscrossing strands, like a bowl of spaghetti, that link countries and trading blocs in self-benefiting trading alliances. Businesses have to monitor and navigate these evolving trade agreements to make sure that one or more agreements don't negatively impact their businesses in key countries. This is one reason why global businesses have teams of in-house professionals monitoring the WTO as well as the regional trade alliances.

For example, American companies doing business in one of the ASEAN countries often choose to become members of the US–ASEAN Business Council, so that they can monitor and possibly influence new trade regulations as well as advance their business interests with government entities.

The US–ASEAN Business Council is the premiere advocacy organization for U.S. corporations operating within the dynamic Association of Southeast Asian Nations (ASEAN). ASEAN represents nearly 600 million people and a combined GDP of USD $1.5 trillion across Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam. The Council's members include the largest U.S. companies working in ASEAN, and range from newcomers to the region to companies that have been working in Southeast Asia for over 100 years….

The Council leads major business missions to key economies; convenes multiple meetings with ASEAN heads of state and ministers; and is the only U.S. organization to be given the privilege of raising member company concerns in consultations with the ASEAN Finance and Economic Ministers, as well as with the ASEAN Customs Directors-General at their annual meetings. Having long-established personal and professional relationships with key ASEAN decision makers, the Council is able to arrange genuine dialogues, solve problems and facilitate opportunities in all types of market conditions, and provide market entry and exclusive advisory services.[45]

US–ASEAN member companies read like the *Fortune* Global 500 and include AT&T, Coca-Cola, Microsoft, Johnson & Johnson, Chevron, Ford Motor Company, and General Electric. While other countries and the EU have ongoing dialogues with ASEAN, the US–ASEAN Business Council is the most formal approach. [46]

It's easy to see how complicated the relationships can be with just one trading bloc. A global firm with operations in North America, the EU, and Asia could easily find itself at the crosshairs of competing trade interests. Staffed with lawyers in an advocacy department, global firms work to maintain relationships with all of the interested parties. If you are curious about a business career in trade, then you may want to consider combining a business degree with a legal degree for the most impact.

Key Takeaways

- Regional economic integration refers to efforts to promote free and fair trade on a regional basis.

There are four main types of economic integration:

1. *Free trade area*is the most basic form of economic cooperation. Member countries remove all barriers to trade between themselves, but are free to independently determine trade policies with nonmember nations.
2. *Customs union*provides for economic cooperation. Barriers to trade are removed between member countries, and members agree to treat trade with nonmember countries in a similar manner.
3. *Common market*allows for the creation of an economically integrated market between member countries. Trade barriers and any restrictions on the movement of labor and capital between member countries are removed. There is a common trade policy for trade with nonmember nations, and workers no longer need a visa or work permit to work in another member country of a common market.
4. *Economic union*is created when countries enter into an economic agreement to remove barriers to trade and adopt common economic policies.

- The largest regional trade cooperative agreements are the European Union (EU), the North American Free Trade Agreement (NAFTA), and the Asia–Pacific Economic Cooperation (APEC). The African Economic Community (AEC) has more member countries than the EU, NAFTA, and APEC but represents a substantially smaller portion of global trade than these other cooperatives.

References

1. The Gulf Cooperation Council (GCC) Cooperation Council for the Arab States of the Gulf website, accessed April 30, 2011, http://www.gcc-sg.org/eng/index.html. is an example.

2. Common Market for Eastern and Southern Africa website, accessed April 30, 2011, http://www.comesa.int .

3. Europa, the Official Website of the European Union, accessed April 30, 2011, http://europa.eu .

4. Foreign Affairs and International Trade Canada, “Fast Facts: North American Free Trade Agreement,” December 15, 2009, accessed December 30, 2010, http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/nafta-alena/fast_facts-faits_saillants.aspx?lang=eng .

5. William M. Pride, Robert James Hughes, and Jack R. Kapoor, Business, 9th ed. (Boston: Houghton Mifflin, 2008), 89, accessed April 30, 2011, http://books.google.com/books?id=z2t...oin+nafta+2009&source=bl&ots=iohSe7YV0E&sig=BjQr2KOx0lsrAGhv5vMqeb9LhFU&hl=en&ei=hLu8TZ3LPNDAgQeZusjqBQ&sa=X&oi=book_result&ct=result&resnum=6&ved=0CDoQ6AEwBQ#v=onepage&q=will%20chile%20join%20nafta%202009&f=false.

6. David A. Sanger, “Chile Is Admitted as North American Free Trade Partner,” New York Times, December 12, 1994, accessed April 30, 2011, http://www.nytimes.com/1994/12/12/world/chile-is-admitted-as-north-american-free-trade-partner.html .

7. Anthony DePalma, “Passing the Torch on a Chile Trade Deal,” New York Times, January 7, 2001, accessed April 30, 2011, http://www.nytimes.com/2001/01/07/business/economic-view-passing-the-torch-on-a-chile-trade-deal.html .

8. CultureQuest Doing Business in Mexico (New York: Atma Global, 2011).

9. Joanna Klonsky and Stephanie Hanson, “Mercosur: South America’s Fractious Trade Bloc,” Council on Foreign Relations, August 20, 2009, accessed April 30, 2011, http://www.cfr.org/trade/mercosur-south-americas-fractious-trade-bloc/p12762 .

10. Joanna Klonsky and Stephanie Hanson, “Mercosur: South America’s Fractious Trade Bloc,” Council on Foreign Relations, August 20, 2009, accessed April 30, 2011, http://www.cfr.org/trade/mercosur-south-americas-fractious-trade-bloc/p12762 .

11. Caribbean Community (CARICOM) Secretariat website, accessed April 30, 2011, http://www.caricom.org/index.jsp .

12. Andean Community of Nations—Andean Pact website, accessed April 30, 2011, http://www.grouplamerica.com/andean_pact.htm .

13. European Commission, “Andean Community Regional Strategy Paper 2007–2013,” December 4, 2007, accessed April 30, 2011, http://www.eeas.europa.eu/andean/rsp/07_13_en.pdf .

14. “Dominican Republic–Central America–United States Free Trade Agreement (CAFTA-DR),” Export.gov, accessed April 30, 2011, http://www.export.gov/FTA/cafta-dr/index.asp .

15. “What Is CAFTA?,” CAFTA Intelligence Center, accessed April 30, 2011, http://www.caftaintelligencecenter.com/subpages/What_is_CAFTA.asp .

16. “Dominican Republic–Central America–United States Free Trade Agreement (CAFTA-DR),” Export.gov, accessed April 30, 2011, http://www.export.gov/FTA/cafta-dr/index.asp .

17. Enterprise Florida, “Your Business: International,” The CAFTA Intelligence Center, accessed December 30, 2010, http://www.caftaintelligencecenter.com/subpages/location-International.asp .

18. “History of the European Union,” Europa, accessed April 30, 2011, http://europa.eu/abc/history/index_en.htm .

19. Andzej Arendarski, Ludovit Cernak, Vladimir Dlouhy, and Bela Kadar, “Central European Free Trade Agreement,” December 21, 1992, accessed April 30, 2011, http://www.worldtradelaw.net/fta/agreements/cefta.pdf .

20. “About the Visegrad Group,” International Visegrad Fund, accessed December 30, 2010, http://visegradgroup.eu/main.php?folderID=858.

21. “About CEFTA,” Central European Free Trade Agreement, accessed April 30, 2011, http://cefta.net.

22. “About CEFTA,” Central European Free Trade Agreement, accessed April 30, 2011, http://cefta.net; Andzej Arendarski, Ludovit Cernak, Vladimir Dlouhy, and Bela Kadar, “Central European Free Trade Agreement,” December 21, 1992, accessed April 30, 2011, http://www.worldtradelaw.net/fta/agreements/cefta.pdf; Wikipedia, s.v. “Central European Free Trade Agreement,” last modified February 12, 2011, accessed February 16, 2011, http://en.Wikipedia.org/wiki/Central_European_Free_Trade_Agreement.

23. “Institutions and Bodies of the European Union,” Europa, accessed April 30, 2011, http://europa.eu/about-eu/institutions-bodies/index_en.htm.

24. “Four Market Freedom Which Benefit Us All,” Europa, accessed December 30, 2010, http://europa.eu/pol/singl/index_en.htm.

25. “Basic Information on the European Union,” Europa, accessed April 30, 2011, http://europa.eu/about-eu/basic-information/index_en.htm.

26. “Staring into the Abyss,” Economist, July 8, 2010, accessed December 28, 2010, http://www.economist.com/node/16536898.

27. Liz Alderman, “Contemplating the Future of the European Union,” New York Times, February 13, 2010, accessed April 30, 2011, http://www.nytimes.com/2010/02/14/weekinreview/14alderman.html .

28. “Future for Europe,” Europa, accessed April 30, 2011, http://europa.eu/abc/12lessons/lesson_12/index_en.htm .

29. Sanjyot P. Dunung, Doing Business in Asia: The Complete Guide, 2nd ed. (San Francisco: Jossey-Bass, 1998).

30. “ASEAN Countries to Integrate Regional Capital Markets by 2015,” Asia Economic Institute, accessed April 30, 2011, http://www.asiaecon.org/special_arti.../read_sp/12174.

31. “About ASEAN,” Association of Southeast Asian Nations, accessed April 30, 2011, http://www.aseansec.org/about_ASEAN.html .

32. Sanjyot P. Dunung, Doing Business in Asia: The Complete Guide, 2nd ed. (San Francisco: Jossey-Bass, 1998).

33. “About APEC: History,” Asia–Pacific Economic Cooperation, accessed April 30, 2011, http://www.apec.org/About-Us/About-APEC/History.aspx .

34. Keith B. Richburg, “China, Taiwan Sign Trade Pact,” Washington Post, June 30, 2010, accessed April 30, 2011, http://www.washingtonpost.com/wp-dyn/content/article/2010/06/29/AR2010062900163.html .

35. Lucy Hornby, “Taiwan and China Sign Trade Pact,” Reuters, June 29, 2010, accessed April 30, 2011, http://www.reuters.com/article/2010/06/29/us-china-taiwan-signing-idUSTRE65S17Z20100629 .

36. Isaac Stone Fish, “Taiwan Inks Risky Deal with China,” Newsweek, July 2, 2010, accessed December 31, 2010, http://www.newsweek.com/2010/07/02/taiwan-inks-a-risky-deal-with-china.html .

37. Cooperation Council for the Arab States of the Gulf website, accessed April 30, 2011, http://www.gcc-sg.org/eng/index.html .

38. “Stop Meddling in Our Affairs: GCC Countries Tell Iran,” The Middle East Times, April 4, 2011, accessed April 30, 2011, http://www.mideast-times.com/left_news.php?newsid=1628 .

39. Gonzalo de Benito, Luigi Narbone, and Christian Koch, “The Bonds between the GCC and EU Grow Deeper,” The National, June 12, 2010, accessed May 23, 2011, http://www.grc.ae/index.php?frm_modu...pe_id=&op_lang=en&override=Articles+%3E+The+Bonds+between+the+GCC+and+EU+Grow+Deeper&sec=Contents&frm_title=&book_id=69542.

40. P. K. Abdul Ghafour, “GCC Common Market Becomes a Reality,” Arab News, January 2, 2008, accessed April 30, 2011, http://archive.arabnews.com/?page=1&section=0&article=105173&d=1&m=1&y=2008 .

41. Mohsin Khan, “The GCC Monetary Union: Choice of Exchange Rate Regime,” Peterson Institute for International Economics, April 2009, accessed April 30, 2011, http://www.iie.com/publications/wp/wp09-1.pdf .

42. Nadim Kawach, “Unrest Will Not Affect GCC Monetary Union: Bahrain Central Bank Governor Says Union Remains Open for Other Members,” Emirates 24/7, March 12, 2011, accessed April 30, 2011, http://www.emirates247.com/2.266/finance/unrest-will-not-affect-gcc-monetary-union-2011-03-12-1.366972 .

43. Wikipedia, s.v. “African Economic Community,” accessed April 30, 2011, http://en.Wikipedia.org/wiki/African_Economic_Community .

44. Louise Greenwood, “Q&A: Free Trade Zones in Africa,” BBC Africa Business Report, BBC News, August 21, 2009, accessed December 31, 2010, http://news.bbc.co.uk/2/hi/business/8208254.stm .

45. “About the US–ASEAN Business Council,” US–ASEAN Business Council, accessed December 31, 2010, http://www.usasean.org/Aboutus/index.asp .

46. For a list of ongoing ASEAN relationships with key trading partners, visit http://www.aseansec.org/9731.htm .

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

This page titled 2.5: Regional Economic Integration is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

2.6: The United Nations and the Impact on Trade

Learning Objectives

After reading this section, students should be able to …

1. Understand how and why peace impacts business.
2. Describe the role of the United Nations.
3. Identify how global businesses benefit from political and economic stability

The final section in this chapter reviews an institution, the United Nations, whose primary purpose is to promote peace between countries. Peace fosters stability and that stability provides the framework for the expansion of business interests and trade.

Why Does Peace Impact Business?

The opening case study demonstrated how political, economic, and military instability in Europe led to two world wars and eventually the development of the EU. It's clear that conflict between countries significantly reduces international trade and seriously damages national and global economic welfare.

It's worth noting that there is a wide range of businesses that benefit from war—for example, companies in industries that manufacture arms, plastics, clothing (uniforms), and a wide range of supplies and logistics. Companies such as BAE Systems, Lockheed Martin, Finmeccanica, Thales Group, General Dynamics, KBR (Halliburton), Rolls-Royce, Boeing, and Honeywell are just some of the world's largest companies in this sector, and all receive benefits that are woven into economic and trade policy from their respective governments directly as well as through general preferences in trade policies and agreements.

Did You Know?

Industrialized countries negotiate free trade and investment agreements with other countries, but exempt military spending from the liberalizing demands of the agreement. Since only the wealthy countries can afford to devote billions on military spending, they will always be able to give their corporations hidden subsidies through defence contracts, and maintain a technologically advanced industrial capacity.

And so, in every international trade and investment agreement one will find a clause which exempts government programs and policies deemed vital for national security.[1]

Nevertheless, military conflict can be extremely disruptive to economic activity and impede long-term economic performance. As a result, most global businesses find that operating in stable environments leads to the best business operations for a range of reasons:

- **Staffing.** It's easier to recruit skilled labor if the in-country conditions are stable and relatively risk-free. Look at the challenges companies have in recruiting nonmilitary personnel to work in the fledging private sectors of Iraq or Afghanistan. Even development organizations have been challenged to send in skilled talent to develop banking-, finance-, and service-sector initiatives. Historically, regardless of which country or conflict, development staff has only been sent into a country after stability has been secured by military force. Companies have to pay even higher levels of hardship and risk pay and may still not necessarily be able to bring in the best talent.
- **Operations.** In unstable environments, companies fear loss or damage to property and investment. For example, goods in transit can easily be stolen, and factories or warehouses can be damaged.
- **Regulations.** Unclear and constantly changing business rules make it hard for firms to plan for the long term.
- **Currency convertibility and free-flowing capital.** Often countries experiencing conflict often impose capital controls (i.e., restrictions on money going in and out of their countries) as well as find that their currency may be devalued or illiquid. Financial management is a key component of global business management.

While bilateral or multilateral trade doesn't always dissuade countries from pursuing military options, countries that are engaged in trade discussions are more likely to use these forums to discuss other conflict areas. Furthermore, the largest global companies—

Siemens, General Electric, Boeing, Airbus, and others—have the economic might to influence governments to promote initiatives to benefit their companies or industries.

Ethics in Action

Business in Conflict Zones: Angola and Conflict Diamonds

Angola, located in southern Africa, is a country that faced internal devastation from an intense civil war raging from its independence in 1975 until 2002. For many businesspeople, Angola may seem a relatively obscure country. However, it is the second-largest petroleum and diamond producer in sub-Saharan Africa. While the oil has brought economic success, the diamonds, known as conflict or blood diamonds, have garnered global attention. Even Hollywood has called attention to this illicit trade in a 2006 movie entitled *Blood Diamond* as well as numerous other movie plots focusing on conflict diamonds, including one in the James Bond franchise.

So what are conflict diamonds? The United Nations (UN) defines them as follows:

Conflict diamonds are diamonds that originate from areas controlled by forces or factions opposed to legitimate and internationally recognized governments, and are used to fund military action in opposition to those governments, or in contravention of the decisions of the Security Council….

Rough diamond caches have often been used by rebel forces to finance arms purchases and other illegal activities. Neighbouring and other countries can be used as trading and transit grounds for illicit diamonds. Once diamonds are brought to market, their origin is difficult to trace and once polished, they can no longer be identified.[2]

First discovered in 1912, diamonds are a key industry for Angola. During its twenty-seven years of conflict, which cost up to 1.5 million lives, rebel groups in Angola traded diamonds to fund armed conflict, hence the term *conflict diamonds*. Some estimate that Angola's main rebel group, National Union for the Total Independence of Angola (UNITA), sold more than $3.72 billion in conflict diamonds to finance its war against the government.[3]

These morally tainted conflict diamonds, along with those from other conflict countries, were bad for the global diamond industry—damaging the reputation and integrity of their key commodity product.

In 1999, the UN applied sanctions to ban the Angolan rebels' trade in conflict diamonds, but a portion of diamonds continued to be traded by the rebels. The UN conducted extensive investigations. "The Security Council's diamond campaign is part of an ongoing UN effort to make sanctions more selective, better targeted and more rigorously enforced instruments for maintaining international peace and security."[4]

Eventually, the UN, various governments, the diamond industry, and nongovernmental organizations, including Global Witness, Amnesty International, and Partnership Africa Canada (PAC), recognized the need for a global system to prevent conflict diamonds from entering the legitimate diamond supply chain and thus helping fund conflicts. The process that was established in 2003 provides for certification process to assure consumers that by purchasing certified diamonds they weren't financing war and human rights abuses. As a result, seventy-four governments have adopted the Kimberley Process certification system, and more than 99 percent of the world's diamonds are from conflict- free sources.[5]

The Kimberley Process and global attention have addressed a critical global-business ethics issue. By taking collective ethical action, the global diamond industry, including firms such as De Beers, Cartier, and Zale, have not only done the right thing but have also helped preserve and grow their businesses while restoring the reputation of their industry.

For example, South African De Beers is the world's largest diamond mining and trading company. Prior to UN action and the Kimberley Process, De Beers was buying conflict diamonds from guerilla movements in three African countries, thereby financing regional conflicts. One UN investigation in Angola found that rebel forces bartered uncut diamonds for weaponry, thereby allowing the civil war to continue in 1998 despite international economic and diplomatic sanctions. In 1999, under UN pressure, De Beers decided to stop buying any outside diamonds in order to guarantee the conflict-free status of its diamond.[6]

Today, De Beers states that 100 percent of the diamonds it sells are conflict-free and that all De Beers diamonds are purchased in compliance with national law, the Kimberley Process, and its own Best Practice Principles.[7]

Angola is still dealing with the loss and devastation of an almost thirty-year conflict with its quality of life among the worst in the world in terms of life expectancy and infant mortality. Nevertheless, the country has made rapid economic strides since 2002 and is now one of the fastest-growing economies in Africa. Conflict diamonds are no longer traded in Angola. The country is a Kimberley Process participant and currently produces approximately 9 percent of the world's diamonds.[8]

The United Nations

The United Nations (UN) was formed in 1945 at the end of World War II to replace the League of Nations, which had been formed in 1919. Its original goals remain the same today: to maintain international peace and security; to develop friendly relations between nations; and to foster international cooperation in solving economic, social, humanitarian, and cultural issues. There is an underlying premise of human rights and equality. Almost all of the world's countries are members—currently 192 nations—with only a few smaller territories and Taiwan, out of deference to China, given observer status and not membership. The UN is funded by member countries' assessments and contributions.

The work of the UN reaches every corner of the globe. Throughout the world, the UN and its agencies assist refugees, set up programs to clear landmines, help expand food production, and lead the fight against AIDS. They also help protect the environment, fight diseases, reduce poverty, and strive for better living standards and human rights. Although the UN is often best known for peacekeeping, peace building, conflict prevention, and humanitarian assistance, the organization also works on a broad range of fundamental social, economic, environment, and health issues. In the Ethics in Action sidebar on Angola, you learned how the UN led the way to resolving the problem of conflict diamonds and partnered with the global diamond industry to develop a long-term solution to a thorny ethical trading problem and promote peace and stability in former conflict countries like Angola.

A secretary-general leads the UN and serves for a five-year term. Structurally, the UN consists of six main bodies:

1. **General Assembly.** This is the deliberative body of the UN and consists of all of the member countries that meet in regular sessions throughout the year. All of the members have an equal vote in the General Assembly.
2. **Security Council.** This body is responsible for addressing issues related to peace and security. It has fifteen members, five of which are permanent country representations—the United States, the United Kingdom, Russia, China, and France. The remaining ten are elected by the General Assembly every two years. As you may expect, there's a great deal of political wrangling by countries to be on the Security Council, which is deemed to have significant power. All decisions by the Security Council are supposed to be binding on the rest of the member nations of the UN.
3. **Economic and Social Council (ECOSOC).** This body is responsible for issues related to economics, human rights, and social matters. A number of smaller commissions and specialized agencies carry out this council's work. The ECOSOC works closely with the World Bank and the International Monetary Fund.
4. **Secretariat.** The Secretariat oversees the operations of the UN and is technically headed by the Secretary-General
5. **International Court of Justice.** Located in The Hague, this body hears disputes between nations. The court consists of fifteen judges who are elected by the General Assembly and the Security Council. The court reviews cases concerning war crimes, genocide, ethnic cleansing, and illegal interference by one country in the affairs of another, among others.
6. **UN Trusteeship Council.** While an official part of the UN Charter charged with overseeing all trustee territories under UN custody, this body is currently inactive.

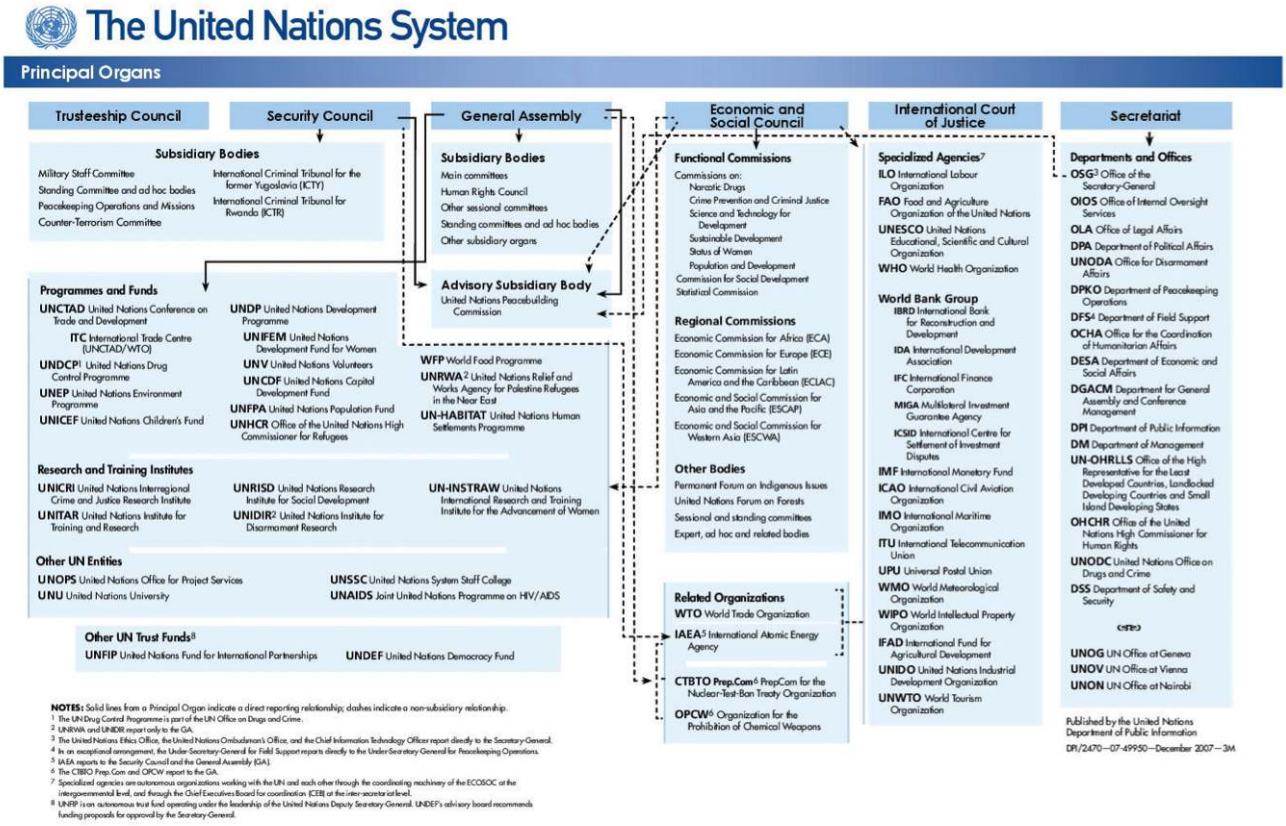


Figure 2.6.1:*The United Nations System Source: The United Nations*

Did You Know?

A strong UN is the world's most effective voice for international cooperation on behalf of peace, development, human rights, and the environment. The UN has also sought to forge partnerships outside of the traditional diplomatic arena. One such partnership that is of growing interest to private sector businesses is the UN Global Compact. This is a strategic policy initiative for businesses that are committed to aligning their operations and strategies with ten universally accepted principles. Why would companies want to align their businesses with these principles? For starters, some businesses see it as a way to be a good global corporate citizen, a label that they can use to attract and retain the best workforce as well as use in marketing efforts to exhibit their global corporate responsibility. The UN is motivated to engage the private sector in helping solve the world's most pressing problems, often with for-profit solutions.

The United Nations Global Compact presents a unique strategic platform for participants to advance their commitments to sustainability and corporate citizenship. Structured as a public-private initiative, the Global Compact offers a policy framework for the development, implementation, and disclosure of sustainability principles and practices related to its four core areas: human rights, labour, the environment and anti-corruption. Indeed, managing the enterprise risks and opportunities related to these areas is today a widely understood aspect of long-term "value creation"—value creation that can simultaneously benefit the private sector and societies at large.

With over 7700 business participants and other stakeholders from more than 130 countries, the Global Compact offers participants a wide spectrum of specialized work streams, management tools and resources, and topical programs and projects —all designed to help advance sustainable business models and markets in order to contribute to the initiative's overarching objective of helping to build a more sustainable and inclusive global economy.[9]

Companies use their participation in the UN Global Compact to illustrate that they are good global corporate citizens, in an effort to satisfy the objectives of consumers, suppliers, and investors as well as government and nongovernment entities—all of whose

support a global company needs to achieve its global business objectives.

One example is Coca-Cola and its adherence to maintaining its good global business citizenship also earns it the ability to influence trade and economic policy with governments and organizations that can positively impact its business interests in select markets around the world. For example, Coca-Cola highlights its commitment on its website and in global reports. The company explains on its website, "In March 2006, The Coca-Cola Company became a signatory to the United Nations (UN) Global Compact, affirming our commitment to the advancement of its 10 universal accepted principles…in the areas of human rights, labor, the environment and anti-corruption. Several of our bottling partners are also signatories."[10]

? The Ten Principles of the UN Global Compact

Human Rights

- Principle 1: Businesses should support and respect the protection of internationally proclaimed human rights; and
- Principle 2: make sure that they are not complicit in human rights abuses.

Labour

- Principle 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining;
- Principle 4: the elimination of all forms of forced and compulsory labour;
- Principle 5: the effective abolition of child labour; and
- Principle 6: the elimination of discrimination in respect of employment and occupation.

Environment

- Principle 7: Businesses should support a precautionary approach to environmental challenges;
- Principle 8: undertake initiatives to promote greater environmental responsibility; and
- Principle 9: encourage the development and diffusion of environmentally friendly technologies.

Anti-Corruption

- Principle 10: Businesses should work against corruption in all its forms, including extortion and bribery.[11]

UN as a Business Partner

The UN has a very clear diplomatic role on the global stage. It's also important to remember that it works closely with the private sector, which actually carries out the vast amount of services and projects around the world. Global businesses sell to the UN just as they do to their own governments and public-sector organizations. Each arm of the UN has a procurement office. The UN Procurement Division does business with vendors from all over the world and is actively working to increase its sources of supply from developing countries and countries with economies in transition.

? Key Takeaways

- While certain industries (e.g., defense companies) benefit from conflict, in general global firms prosper best in peaceful times. The primary impact for businesses is in the areas of staffing, operations, regulations, and currency convertibility and financial management.
- The United Nations (UN) was formed at the end of World War II in 1945. Its original intent remains the same: to maintain international peace and security; to develop friendly relations between nations; and to foster international cooperation in solving economic, social, humanitarian, and cultural issues.
- The six main bodies of the UN are the (1) Secretariat, (2) Security Council, (3) General Assembly, (4) Economic and Social Council, (5) International Court of Justice, and (6) UN Trusteeship Council. The Secretary-General leads the UN.

References

1. Stephen Staples, "Confronting the Military-Corporate Complex" (presented at the Hague Appeal for Peace, The Hague, May 12, 1999).

2. United Nations Department of Public Information in cooperation with the Sanctions Branch, Security Council Affairs Division, Department of Political Affairs, “Conflict Diamonds: Sanctions and War,” United Nations, March 21, 2001, accessed December 31, 2010, http://www.un.org/peace/africa/Diamond.html.

3. Wikipedia , s.v. “Blood diamond,” last modified February 9, 2011, accessed February 15, 2011, http://en.Wikipedia.org/wiki/Blood_diamond.

4. Michael Fleshman, “Targeting ‘Conflict Diamonds’ in Africa,” Africa Recovery 14, no. 4 (January 2001): 6, accessed December 31, 2010, http://www.un.org/ecosocdev/geninfo/afrec/subjindx/144diam.htm.

5. World Diamond Council, “Eliminating Conflict Diamonds,” accessed December 31, 2010, http://diamondfacts.org/conflict/eliminating_conflict_diamonds.html#kim.

6. Dick Durham, “De Beers Sees Threat of Blood Diamonds,” January 18, 2001, accessed April 30, 2011, http://www.cnnstudentnews.cnn.com/2001/WORLD/africa/01/18/diamonds.debeers/index.html.

7. De Beers Group, “FAQs: What Has De Beers Done about Conflict Diamonds?,” 2008, accessed December 31, 2010, http://www.debeersgroup.com/en/Global/FAQs/#Section755.

8. Wikipedia , s.v. “Angola,” last modified February 13, 2011, accessed February 16, 2011, http://en.Wikipedia.org/wiki/Angola.

9. “How to Participate,” United Nations Global Compact, accessed January 1, 2011, http://www.unglobalcompact.org/HowToParticipate/Business_Participation/index.html.

10. “UN Global Compact,” Coca-Cola Company, accessed January 1, 2011, http://www.thecoca-colacompany.com/citizenship/un_global_compact.html.

11. “The Ten Principles,” United Nations Global Compact, accessed April 30, 2011, http://www.unglobalcompact.org/AboutTheGC/TheTenPrinciples/index.html.

This page titled 2.6: The United Nations and the Impact on Trade is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

2.7: Trade Controversies

Learning Objectives

After reading this section, students should be able to …

1. Identify some of the ways the world has stepped closer to free trade recently.
2. Identify some of the ways the world has stepped further from free trade recently.

In the spring of 2009, the world was in the midst of the largest economic downturn since the early 1980s. Economic production was falling and unemployment was rising. International trade had fallen substantially everywhere in the world, while investment both domestically and internationally dried up.

The source of these problems was the bursting of a real estate bubble. Bubbles are fairly common in both real estate and stock markets. A bubble describes a steady and persistent increase in prices in a market—in this case, in the real estate markets in the United States and abroad. When bubbles are developing, many market observers argue that the prices are reflective of true values despite a sharp and unexpected increase. These justifications fool many people into buying the products in the hope that the prices will continue to rise and generate a profit.

When the bubble bursts, the demand driving the price increases ceases and a large number of participants begin to sell off their product to realize their profit. When this occurs, prices quickly plummet. The dramatic drop in real estate prices in the United States in 2007 and 2008 left many financial institutions near bankruptcy. These financial market instabilities finally spilled over into the *real sector* (i.e., the sector where goods and services are produced), contributing not only to a world recession but also to a new popular attitude that capitalism and free markets may not be working very well. This attitude change may fuel the antiglobalization sentiments that were growing during the previous decade.

As the current economic crisis unfolded, there were numerous suggestions about similarities between this recession and the Great Depression in the 1930s. One big concern was that countries might revert to protectionism to try to save jobs for domestic workers. This is precisely what many countries did at the onset of the Great Depression, and it is widely believed that that reaction made the Depression worse rather than better.

Since the economic crisis began in late 2008, national leaders have regularly vowed to avoid protectionist pressures and maintain current trade liberalization commitments made under the World Trade Organization (WTO) and individual free trade agreements. However, at the same time, countries have raised barriers to trade in a variety of subtle ways. For example, the United States revoked a promise to maintain a program allowing Mexican trucks to enter the United States under the North American Free Trade Agreement (NAFTA), it included “Buy American” provisions it its economic stimulus package, it initiated a special safeguards action against Chinese tire imports, and it brought a case against China at the WTO. Although many of these actions are legal and allowable under U.S. international commitments, they are nevertheless irritating to U.S. trading partners and indicative of the rising pressure to implement policies favorable to domestic businesses and workers. Most other countries have taken similar, albeit subtle, protectionist actions as well.

Nevertheless, this rising protectionism runs counter to a second popular sentiment among people seeking to achieve greater liberalization and openness in international markets. For example, as the recession began, the United States had several free trade areas waiting to be approved by the U.S. Congress: one with South Korea, another with Colombia, and a third with Panama. In addition, the United States has participated in talks recently with many Pacific Rim countries to forge a Trans-Pacific Partnership (TPP) that could liberalize trade around the region. Simultaneously, free trade area discussions continue among many other country pairings around the world.

This current ambivalence among countries and policymakers is nothing new. Since the Great Depression, trade policymaking around the world can be seen as a tug of war between proponents and opponents of trade liberalization. Even as free trade advocates have achieved trade expansions and liberalizations, free trade opponents have often achieved market-closing policies at the same time; three steps forward toward trade liberalization are often coupled with two steps back at the same time.

To illustrate this point, we continue with a discussion of both recent initiatives for trade liberalization and some of the efforts to resist these liberalization movements. We’ll also look back to see how the current policies and discussions have been shaped by

events in the past century.

Doha and WTO

The Doha Round is the name of the current round of trade liberalization negotiations undertaken by WTO member countries. The objective is for all participating countries to reduce trade barriers from their present levels for trade in goods, services, and agricultural products; to promote international investment; and to protect intellectual property rights. In addition, member countries discuss improvements in procedures that outline the rights and responsibilities of the member countries. Member countries decided that a final agreement should place special emphasis on changes targeting the needs of developing countries and the world's poor and disadvantaged. As a result, the Doha Round is sometimes called the Doha Development Agenda, or DDA.

The Doha Round was begun at the WTO ministerial meeting held in Doha, Qatar, in November 2001. It is the first round of trade liberalization talks under the auspices of the WTO, which was founded in 1994 in the final General Agreement on Tariffs and Trade (GATT) round of talks, the Uruguay Round. Because missed deadlines are commonplace in the history of GATT talks, an old joke is that GATT really means the "General Agreement to Talk and Talk."

In anticipation, WTO members decided to place strict deadlines for different phases of the agreement. By adhering to the deadlines, countries were more assured that the talks would be completed on schedule in the summer of 2005—but the talks weren't. So members pushed off the deadline to 2006, and then to 2007, and then to 2008, always reporting that an agreement was near. As of 2009, the Doha Round has still not been completed, testifying to the difficulty of getting 153 member countries to conceive of a trade liberalization agreement that all countries can accept mutually.

This is an important point: WTO rounds (and the GATT rounds before them) are never finalized until every member country agrees to the terms and conditions. Each country offers a set of trade-liberalizing commitments, or promises, and in return receives the trade-liberalizing commitments made by its 152 potential trading partners. This is a much stronger requirement than majority voting, wherein coalitions can force other members into undesirable outcomes. Thus one reason this round has so far failed is because some countries believe that the others are offering too little liberalization relative to the liberalization they themselves are offering.

The DDA is especially complex, not only because 153 countries must reach a consensus, but also because there are so many trade-related issues under discussion. Countries discuss not only tariff reductions on manufactured goods but also changes in agricultural support programs, regulations affecting services trade, intellectual property rights policy and enforcement, and procedures involving trade remedy laws, to name just a few. Reaching an agreement that every country is happy about across all these issues may be more than the system can handle. We'll have to wait to see whether the Doha Round ever finishes to know if it is possible. Even then, there is some chance an agreement that is achievable may be so watered down that it doesn't result in much trade liberalization.

The primary stumbling block in the Doha Round (and the previous Uruguay Round too) has been insufficient commitments on agricultural liberalization, especially by the developed countries. Today, agriculture remains the most heavily protected industry around the world. In addition to high tariffs at the borders, most countries offer subsidies to farmers and dairy producers, all of which affects world prices and international trade. Developing countries believe that the low world prices for farm products caused by subsidies in rich countries both prevents them from realizing their comparative advantages and stymies economic development. However, convincing developed country farmers to give up long-standing handouts from their governments has been a difficult to impossible endeavor.

To their credit, developed countries have suggested that they may be willing to accept greater reductions in agricultural subsidies if developing countries would substantially reduce their very high tariff bindings on imported goods *and* bind most or all of their imported products. Developing countries have argued, however, that because this is the Doha "Development" Round, they shouldn't be asked to make many changes at all to their trade policies; rather, they argue that changes should be tilted toward greater market access from developing into developed country markets.

Of course, this is not the only impasse in the discussions, as there are many other issues on the agenda. Nevertheless, agricultural liberalization will surely remain one of the major stumbling blocks to continued trade liberalization efforts. And the Doha Round is not dead yet, since continuing discussions behind the spotlight reflect at least some sentiment around the world that further trade liberalization is a worthy goal. But this is not a sentiment shared by all, and indeed opponents almost prevented this WTO round

from beginning in the first place. To understand why, we need to go back two years to the Doha Round commencement in Seattle, Washington, in December 1999.

The WTO Seattle Ministerial—1999

Every two years, the WTO members agreed to hold a ministerial meeting bringing together, at minimum, the trade ministers of the member countries to discuss WTO issues. In 1999, the ministerial was held in Seattle, Washington, in the United States, and because it was over five years since the last round of trade discussions had finished, many members thought it was time to begin a new round of trade talks. There is a well-known "bicycle theory" about international trade talks that says that forward momentum must be maintained or else, like a bicycle, liberalization efforts will stall.

And so the WTO countries decided by 1999 to begin a new "Millennial Round" of trade liberalization talks and to kick off the discussions in Seattle in December 1999. However, two things happened, the first attesting to the difficulty of getting agreement among so many countries and the second attesting to the growing opposition to the principles of free trade itself.

Shortly before the ministers met, they realized that there was not even sufficient agreement among governments about what the countries should discuss in the new round. For example, the United States was opposed to any discussion about trade remedy laws, whereas many developing countries were eager to discuss revisions. Consequently, because no agreement—even about what to talk about—could be reached, the start of the round was postponed.

The second result of the meeting was a cacophony of complaints that rose up from the thousands of protesters who gathered outside the meetings. This result was more profound if only because the resulting disturbances, including property damage and numerous arrests, brought the issues of trade and the WTO to the international stage. Suddenly, the world saw that there was substantial opposition to the principles of the WTO in promoting trade and expanded globalization.

These protests at the Seattle Ministerial were perhaps directed not solely at the WTO itself but instead at a variety of issues brought to the forefront by globalization. Some protesters were there to protest environmental degradation and were worried that current development was unsustainable, others were protesting child labor and unsafe working conditions in developing countries, and still others were concerned about the loss of domestic jobs due to international competition. In many ways, the protesters were an eclectic group consisting of students, labor union members, environmentalists, and even some anarchists.

After Seattle, groups sometimes labeled "antiglobalization groups" began organizing protests at other prominent international governmental meetings, including the biannual World Bank and International Monetary Fund (IMF) meetings, the meeting of the G8 countries, and the World Economic Forum at Davos, Switzerland. The opposition to freer trade, and globalization more generally, was on the rise. At the same time, though, national governments continued to press for more international trade and investment through other means.

Ambivalence about Globalization since the Uruguay Round

Objectively speaking, ambivalence about trade and globalization seems to best characterize the decades of the 1990s and 2000s. Although this was a time of rising protests and opposition to globalization, it was also a time in which substantial movements to freer trade occurred. What follows are some events of the last few decades highlighting this ambivalence.

First off, trade liberalization became all the rage around the world by the late 1980s. The remarkable success of outward-oriented economies such as South Korea, Taiwan, Hong Kong, and Singapore—known collectively as the East Asian Tigers—combined with the relatively poor performance of inward-oriented economies in Latin America, Africa, India, and elsewhere led to a resurgence of support for trade.

Because the Uruguay Round of the GATT was on its way to creating the WTO, many countries decided to jump on the liberalizing bandwagon by joining the negotiations to become founding members of the WTO. One hundred twenty-three countries were members of the WTO upon its inception in 1995, only to grow to 153 members by 2009.

Perhaps the most important new entrant into the WTO was China in 2001. China had wanted to be a founding member of the WTO in 1995 but was unable to overcome the accession hurdle. You see, any country that is already a WTO member has the right to demand trade liberalization concessions from newly acceding members. Since producers around the world were fearful of competition from China, most countries demanded more stringent liberalization commitments than were usually expected from

other acceding countries at a similar level of economic development. As a result, it took longer for China to gain entry than for most other countries.

But at the same time that many developing countries were eager to join the WTO, beliefs in freer trade and the WTO were reversing in the United States. Perhaps the best example was the struggle for the U.S. president to secure trade-negotiating authority. First, a little history.

Article 1, section 8 of the U.S. Constitution states, "The Congress shall have the power…to regulate commerce with foreign nations." This means that decisions about trade policies must be made by the U.S. Senate and House of Representatives, and *not* by the U.S. president. Despite this, the central agency in trade negotiations today is the United States Trade Representative (USTR), an executive branch (or presidential) agency. The reason for this arrangement is that the U.S. Congress has ceded authority for these activities to the USTR. One such piece of enabling legislation is known as trade promotion authority (TPA).

TPA enables the U.S. president, or more specifically the USTR, to negotiate trade liberalization agreements with other countries. The legislation is known as *fast-track authority* because it provides for expedited procedures in the approval process by the U.S. Congress. More specifically, for any trade agreement the president presents to the Congress, Congress will vote the agreement, in its entirety, up or down in a yea or nay vote. Congress agrees not to amend or change in any way the contents of the negotiated agreement. The fast-track procedure provides added credibility to U.S. negotiators since trade agreement partners will know the U.S. Congress cannot change the details upon review.

TPA has been given to the U.S. president in various guises since the 1930s. In the post–World War II era, authority was granted to the president to negotiate successive GATT rounds. A more recent incarnation was granted to the president in the Trade Act of 1974. TPA enabled negotiations for the U.S.-Israel free trade area (FTA) in 1985 and NAFTA in 1993. However, this authority expired in 1994 under President Clinton and was never reinstated during the remainder of his presidency. The failure to extend TPA signified the growing discontent, especially in the U.S. House of Representatives, with trade liberalization.

When George W. Bush became president, he wanted to push for more trade liberalization through the expansion of FTAs with regional and strategic trade partners. He managed to gain a renewal of TPA in 2001 (with passage in the House by just one vote, 216 to 215). This enabled President Bush to negotiate and implement a series of FTAs with Chile, Singapore, Australia, Morocco, Jordan, Bahrain, Oman, Central America and the Dominican Republic, and Peru. Awaiting congressional approval (as of December 2009) are FTAs with South Korea, Colombia, and Panama.

Despite these advances toward trade liberalization, TPA expired in 2007 and has not yet been renewed by the U.S. Congress, again representing the ambivalence of U.S. policymakers to embrace freer trade. Another indication is the fact that the FTAs with South Korea, Colombia, and Panama were submitted for approval to Congress before the deadline for TPA expired in 2007 and these agreements still have not been brought forward for a vote by the U.S. Congress.

While the United States slows its advance toward freer trade, other countries around the world continue to push forward. There are new FTAs between China and the Association of Southeast Asian Nations (ASEAN) countries, Japan and the Philippines, Thailand and Chile, Pakistan and China, and Malaysia and Sri Lanka, along with several other new pairings.

Future prospects for trade liberalization versus trade protections are quite likely to depend on the length and severity of the present economic crisis. If the crisis abates soon, trade liberalization may return to its past prominence. However, if the crisis continues for several more years and if unemployment rates remain much higher than usual for an extended time, then demands for more trade protection may increase significantly. Economic crises have proved in the past to be a major contributor to high levels of protection. Indeed, as was mentioned previously, there is keen awareness today that the world may stumble into the trade policy mistakes of the Great Depression. Much of the trade liberalization that has occurred since then can be traced to the desire to reverse the effects of the Smoot-Hawley Tariff Act of 1930. Thus to better understand the current references to our past history, the story of the Great Depression is told next.

? Key Takeaways

- Recent support for trade liberalization is seen in the establishment of numerous free trade areas and the participation of many countries in the Doha Round of trade talks.
- Recent opposition to trade liberalization is seen in national responses to the financial crisis, the protest movement at the Seattle Ministerial and other venues, and the failure in the United States to grant trade promotion authority to the president.

This page titled 2.7: Trade Controversies is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

2.8: Foreign Direct Investment

Learning Objectives

After reading this section, students should be able to …

1. Understand the types of international investments.
2. Identify the factors that influence foreign direct investment (FDI).
3. Explain why and how governments encourage FDI in their countries.

Understand the Types of International Investments

There are two main categories of international investment—portfolio investment and foreign direct investment. Portfolio investment refers to the investment in a company's stocks, bonds, or assets, but not for the purpose of controlling or directing the firm's operations or management. Typically, investors in this category are looking for a financial rate of return as well as diversifying investment risk through multiple markets.

Foreign direct investment (FDI) refers to an investment in or the acquisition of foreign assets with the intent to control and manage them. Companies can make an FDI in several ways, including purchasing the assets of a foreign company; investing in the company or in new property, plants, or equipment; or participating in a joint venture with a foreign company, which typically involves an investment of capital or know-how. FDI is primarily a long-term strategy. Companies usually expect to benefit through access to local markets and resources, often in exchange for expertise, technical know-how, and capital. A country's FDI can be both inward and outward. As the terms would suggest, inward FDI refers to investments coming into the country and outward FDI are investments made by companies from that country into foreign companies in other countries. The difference between inward and outward is called the net FDI inflow, which can be either positive or negative.

Governments want to be able to control and regulate the flow of FDI so that local political and economic concerns are addressed. Global businesses are most interested in using FDI to benefit their companies. As a result, these two players—governments and companies—can at times be at odds. It's important to understand why companies use FDI as a business strategy and how governments regulate and manage FDI.

Factors That Influence a Company's Decision to Invest

Let's look at why and how companies choose to invest in foreign markets. Simply purchasing goods and services or deciding to invest in a local market depends on a business's needs and overall strategy. Direct investment in a country occurs when a company chooses to set up facilities to produce or market their products; or seeks to partner with, invest in, or purchase a local company for control and access to the local market, production, or resources. Many considerations influence its decisions:

- **Cost.** Is it cheaper to produce in the local market than elsewhere?
- **Logistics.** Is it cheaper to produce locally if the transportation costs are significant?
- **Market.** Has the company identified a significant local market?
- **Natural resources.** Is the company interested in obtaining access to local resources or commodities?
- **Know-how.** Does the company want access to local technology or business process knowledge?
- **Customers and competitors.** Does the company's clients or competitors operate in the country?
- **Policy.** Are there local incentives (cash and noncash) for investing in one country versus another?
- **Ease.** Is it relatively straightforward to invest and/or set up operations in the country, or is there another country in which setup might be easier?
- **Culture.** Is the workforce or labor pool already skilled for the company's needs or will extensive training be required?
- **Impact.** How will this investment impact the company's revenue and profitability?
- **Expatriation of funds.** Can the company easily take profits out of the country, or are there local restrictions?
- **Exit.** Can the company easily and orderly exit from a local investment, or are local laws and regulations cumbersome and expensive?

These are just a few of the many factors that might influence a company's decision. Keep in mind that a company doesn't need to sell in the local market in order to deem it a good option for direct investment. For example, companies set up manufacturing facilities in low-cost countries but export the products to other markets.

There are two forms of FDI—horizontal and vertical. Horizontal FDI occurs when a company is trying to open up a new market—a retailer, for example, that builds a store in a new country to sell to the local market. Vertical FDI is when a company invests internationally to provide input into its core operations—usually in its home country. A firm may invest in production facilities in another country. When a firm brings the goods or components back to its home country (i.e., acting as a supplier), this is referred to as backward vertical FDI. When a firm sells the goods into the local or regional market (i.e., acting as a distributor), this is termed forward vertical FDI. The largest global companies often engage in both backward and forward vertical FDI depending on their industry.

Many firms engage in backward vertical FDI. The auto, oil, and infrastructure (which includes industries related to enhancing the infrastructure of a country—that is, energy, communications, and transportation) industries are good examples of this. Firms from these industries invest in production or plant facilities in a country in order to supply raw materials, parts, or finished products to their home country. In recent years, these same industries have also started to provide forward FDI by supplying raw materials, parts, or finished products to newly emerging local or regional markets.

There are different kinds of FDI, two of which—greenfield and brownfield—are increasingly applicable to global firms. Greenfield FDIs occur when multinational corporations enter into developing countries to build new factories or stores. These new facilities are built from scratch—usually in an area where no previous facilities existed. The name originates from the idea of building a facility on a green field, such as farmland or a forested area. In addition to building new facilities that best meet their needs, the firms also create new long-term jobs in the foreign country by hiring new employees. Countries often offer prospective companies tax breaks, subsidies, and other incentives to set up greenfield investments.

A brownfield FDI is when a company or government entity purchases or leases existing production facilities to launch a new production activity. One application of this strategy is where a commercial site used for an "unclean" business purpose, such as a steel mill or oil refinery, is cleaned up and used for a less polluting purpose, such as commercial office space or a residential area. Brownfield investment is usually less expensive and can be implemented faster; however, a company may have to deal with many challenges, including existing employees, outdated equipment, entrenched processes, and cultural differences.

You should note that the terms *greenfield* and *brownfield* are not exclusive to FDI; you may hear them in various business contexts. In general, greenfield refers to starting from the beginning, and brownfield refers to modifying or upgrading existing plans or projects.

Why and How Governments Encourage FDI

Many governments encourage FDI in their countries as a way to create jobs, expand local technical knowledge, and increase their overall economic standards. Countries like Hong Kong and Singapore long ago realized that both global trade and FDI would help them grow exponentially and improve the standard of living for their citizens. As a result, Hong Kong (before its return to China) was one of the easiest places to set up a new company. Guidelines were clearly available, and businesses could set up a new office within days. Similarly, Singapore, while a bit more discriminatory on the size and type of business, offered foreign companies a clear, streamlined process for setting up a new company.

In contrast, for decades, many other countries in Asia (e.g., India, China, Pakistan, the Philippines, and Indonesia) restricted or controlled FDI in their countries by requiring extensive paperwork and bureaucratic approvals as well as local partners for any new foreign business. These policies created disincentives for many global companies. By the 1990s (and earlier for China), many of the countries in Asia had caught the global trade bug and were actively trying to modify their policies to encourage more FDI. Some were more successful than others, often as a result of internal political issues and pressures rather than from any repercussions of global trade.[1]

How Governments Discourage or Restrict FDI

In most instances, governments seek to limit or control foreign direct investment to protect local industries and key resources (oil, minerals, etc.), preserve the national and local culture, protect segments of their domestic population, maintain political and

economic independence, and manage or control economic growth. A government use various policies and rules:

- **Ownership restrictions.** Host governments can specify ownership restrictions if they want to keep the control of local markets or industries in their citizens' hands. Some countries, such as Malaysia, go even further and encourage that ownership be maintained by a person of Malay origin, known locally as *bumiputra*. Although the country's Foreign Investment Committee guidelines are being relaxed, most foreign businesses understand that having a *bumiputra*partner will improve their chances of obtaining favorable contracts in Malaysia.
- **Tax rates and sanctions.** A company's home government usually imposes these restrictions in an effort to persuade companies to invest in the domestic market rather than a foreign one.

How Governments Encourage FDI

Governments seek to promote FDI when they are eager to expand their domestic economy and attract new technologies, business know-how, and capital to their country. In these instances, many governments still try to manage and control the type, quantity, and even the nationality of the FDI to achieve their domestic, economic, political, and social goals.

- **Financial incentives.** Host countries offer businesses a combination of tax incentives and loans to invest. Home-country governments may also offer a combination of insurance, loans, and tax breaks in an effort to promote their companies' overseas investments. The opening case on China in Africa illustrated these types of incentives.
- **Infrastructure.** Host governments improve or enhance local infrastructure—in energy, transportation, and communications—to encourage specific industries to invest. This also serves to improve the local conditions for domestic firms.
- **Administrative processes and regulatory environment.** Host-country governments streamline the process of establishing offices or production in their countries. By reducing bureaucracy and regulatory environments, these countries appear more attractive to foreign firms.
- **Invest in education.** Countries seek to improve their workforce through education and job training. An educated and skilled workforce is an important investment criterion for many global businesses.
- **Political, economic, and legal stability.** Host-country governments seek to reassure businesses that the local operating conditions are stable, transparent (i.e., policies are clearly stated and in the public domain), and unlikely to change.

✔ Ethics in Action

Encouraging Foreign Investment

Governments seek to encourage FDI for a variety of reasons. On occasion, though, the process can cross the lines of ethics and legality. In November 2010, seven global companies paid the US Justice Department "a combined $236 million in fines to settle allegations that they or their contractors bribed foreign officials to smooth the way for importing equipment and materials into several countries."[2] The companies included Shell and contractors Transocean, Noble, Pride International, Global Santa Fe, Tidewater, and Panalpina World Transport. The bribes were paid to officials in oil-rich countries—Nigeria, Brazil, Azerbaijan, Russia, Turkmenistan, Kazakhstan, and Angola. In the United States, global firms—including ones headquartered elsewhere, but trading on any of the US stock exchanges—are prohibited from paying or even offering to pay bribes to foreign government officials or employees of state-owned businesses with the intent of currying business favors. While the law and the business ethics are clear, in many cases, the penalty fines remain much less onerous than losing critical long-term business revenues.[3]

? Did You Know?

Hong Kong: From Junks to Jets? The Rise of a Global Powerhouse

Policies of openness to FDI and international trade have enabled countries around the world to leapfrog economically over their neighbors. The historical rise of Hong Kong is one example. Hong Kong's economic strengths can be traced to a combination of factors, including its business-friendly laws and policies, a local population that is culturally oriented to transacting trade and business, and Hong Kong's geographic proximity to the major economies of China, Japan, and Taiwan.

Hong Kong has always been open to global trade. Many people, from the Chinese to the Japanese to the British, have occupied Hong Kong over the centuries, and all of them have contributed to its development as one of the world's great ports and trading

centers.

In 1997, Hong Kong reverted back to Chinese control; however, free enterprise will be governed under the agreement of Basic Law, which established Hong Kong as a separate Special Administrative Region (SAR) of China. Under its Basic Law, in force until 2047, Hong Kong will retain its legal, social, economic, and political systems apart from China's. Thus, Hong Kong is guaranteed the right to its own monetary system and financial autonomy. Hong Kong is allowed to work independently with the international community; to control trade in strategic commodities, drugs, and illegal transshipments; and to protect intellectual property rights. Under the Basic Law, the Hong Kong SAR maintains an independent tax system and the right to free trade.

Hong Kong has an open business structure, which freely encourages foreign direct investment. Any company that wishes to do business here is free to do so as long as it complies with local laws. Hong Kong's legal and institutional framework combined with its good banking and financial facilities and business-friendly tax systems have encouraged foreign direct investment as many multinationals located their regional headquarters in Hong Kong.

As a base for doing business with China, Hong Kong now accounts for half of all direct investments in the mainland and is China's main conduit for investment and trade. China has also become a major investor in Hong Kong.

Culturally, many foreign firms are attracted to Hong Kong by its skilled workforce and the fact that Hong Kong still conducts business in English, a remnant of its British colonial influence. The imprint of the early British trading firms, known as *hongs*, is particularly strong today in the area of property development. Jardine Matheson and Company, for instance, founded by trader William Jardine, remains one of Hong Kong's preeminent firms. In many of these companies, British management practices remain firmly in place. Every aspect of Hong Kong's business laws—whether pertaining to contracts, taxes, or trusts—bears striking similarities to the laws in Britain. All these factors contribute to a business culture that is familiar to people in many multinationals.

Chinese cultural influences have always affected business and are increasingly so today. Many pundits claim that Hong Kong already resembles China's free-trade zone. And, indeed, the two economies are becoming increasingly intertwined. Much of this economic commingling began in the 1990s, when Hong Kong companies began relocating production centers to the mainland—especially to Guangdong province.

Because of the shift in production to mainland China and other Asian countries, there is not much manufacturing left in Hong Kong. What remains is light in nature and veers toward high-value-added products. In fact, 80 percent of Hong Kong's gross domestic product now comes from its high value-added service sector: finance, business and legal services, brokerage services, the shipping and cargo industries, and the hotel, food, and beverage industry.

Local Hong Kong companies, as well as foreign businesses based there, are uniquely positioned to play important roles as brokers and intermediaries between the mainland and global corporations. Doing business in China is not only complex and daunting but also requires connections, locally known as *guanxi*, to influential people and an understanding of local laws and protocol. Developing these relationships and this knowledge is almost impossible without the assistance of an insider. It is in this role that the Hong Kong business community stands to contribute enormously.

Hong Kong's openness to foreign investment coupled with its proximity to China will ensure its global economic competitiveness for decades to come.

? Key Takeaways

- There are two main categories of international investment: portfolio investment and foreign direct investment (FDI). Portfolio investment refers to the investment in a company's stocks, bonds, or assets, but not for the purpose of controlling or directing the firm's operations or management. FDI refers to an investment in or the acquisition of foreign assets with the intent to control and manage them.
- Direct investment in a country occurs when a company chooses to set up facilities to produce or market its products or seeks to partner with, invest in, or purchase a local company for control and access to the local market, production, or resources. Many considerations can influence the company's decisions, including cost, logistics, market, natural resources, know-how, customers and competitors, policy, ease of entry and exit, culture, impact on revenue and profitability, and expatriation of funds.

- Governments discourage or restrict FDI through ownership restrictions, tax rates, and sanctions. Governments encourage FDI through financial incentives; well-established infrastructure; desirable administrative processes and regulatory environment; educational investment; and political, economic, and legal stability.

References

1. UNCTAD compiles statistics on foreign direct investment (FDI): “Foreign Direct Investment database,” UNCTAD United Nations Conference on Trade and Development, accessed February 16, 2011, http://unctadstat.unctad.org/ReportFolders/reportFolders.aspx?sRF_ActivePath=P,5,27&sRF_Expanded=,P,5,27&sCS_ChosenLang=en.
2. Kara Scannell, “Shell, Six Other Firms Settle Foreign-Bribery Probe,” Wall Street Journal, November 5, 2010, accessed December 23, 2010, http://online.wsj.com/article/SB1000...301043920.html.
3. Kara Scannell, “Shell, Six Other Firms Settle Foreign-Bribery Probe,” Wall Street Journal, November 5, 2010, accessed December 23, 2010, http://online.wsj.com/article/SB1000...301043920.html.

This page titled 2.8: Foreign Direct Investment is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

3: Social and Cultural Environment

3.1: Social and Cultural Environment Summary
3.2: Factors Shaping the Global Marketing Environment
3.3: The Social and Cultural Environment
3.4: Importance of Culture on Markets
3.5: What is Culture
3.6: Describing Culture
3.7: Marketing Across Cultures

This page titled 3: Social and Cultural Environment is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

3.1: Social and Cultural Environment Summary

Summary

Most people hear about culture and business and immediately think about protocol—a list of dos and don'ts by country. For example, don't show the sole of your foot in Saudi Arabia; know how to bow in Japan. While these practices are certainly useful to know, they are just the tip of the iceberg. We often underestimate how critical local culture, values, and customs can be in the business environment. We assume, usually incorrectly, that business is the same everywhere. Culture does matter, and more and more people are realizing its impact on their business interactions.

Culture, in the broadest sense, refers to how and why we think and function. It encompasses all sorts of things—how we eat, play, dress, work, think, interact, and communicate. Everything we do, in essence, has been shaped by the cultures in which we are raised. Similarly, a person in another country is also shaped by his or her cultural influences. These cultural influences impact how we think and communicate.

Culture, a society's "programming of the mind," has both a pervasive and changing influence on each national market environment. Global marketers must recognize the influence of culture and be prepared to either respond to it or change it. Human behavior is a function of a person's own unique personality and that person's interaction with the collective forces of the particular society and culture in which he or she has lived. In particular, attitudes, values, and beliefs can vary significantly from country to country.

Also, differences pertaining to religion, aesthetics, dietary customs, and language and communication can affect local reaction to brands or products as well as the ability of company personnel to function effectively in different cultures. A number of concepts and theoretical frameworks provide insights into these and other cultural issues.

Cultures can be classified as high- or low-context; communication and negotiation styles can differ from country to country. Hofstede's social value typology sheds light on national cultures in terms of power distance, individualism vs. collectivism, masculinityvs. femininity, uncertainty avoidance, and long-versus short-term orientation. By understanding the self-reference criterion, global marketers can overcome the unconscious tendency for perceptual blockage and distortion.

Source

The above note was adapted from the course note from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM) ('Social and Cultural Environments' is Copyright (c) by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license.), and under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 3.1: Social and Cultural Environment Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

3.2: Factors Shaping the Global Marketing Environment

Learning Objectives

After reading this section, students should be able to …

1. appreciate the role of external environmental factors that shape the global marketing environment

While the same basic domestic marketing principles apply to global marketing, there are additional layers of complexity for marketers to consider when working across markets in different countries and world regions. Much of this complexity centers the need to develop a keen understanding of the consumer and the target market—a task essential for effective marketing, whether global or domestic. But in the global environment, there are additional questions to ask and issues to consider in order to fully appreciate the consumer and the marketing opportunities in a target market.

Additional complexity resides in the business environment created by government, regulatory bodies, and other societal institutions that shape the behaviors of individuals and institutions. This business environment is somewhat unique to every country and target market. Understanding these dynamics can help marketers work more effectively to achieve their organizations' business objectives.

This page titled 3.2: Factors Shaping the Global Marketing Environment is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

3.3: The Social and Cultural Environment

Learning Objectives

After reading this section, students should be able to …

1. list the various elements in a firm's cultural environment

The cultural environment consists of the influence of religious, family, educational, and social systems in the marketing system. Marketers who intend to market their products overseas may be very sensitive to foreign cultures. While the differences between our cultural background in the United States and those of foreign nations may seem small, marketers who ignore these differences risk failure in implementing marketing programs. Failure to consider cultural differences is one of the primary reasons for marketing failures overseas.

This task is not as easy as it sounds as various features of a culture can create an illusion of similarity. Even a common language does not guarantee similarity of interpretation. For example, in the US we purchase "cans" of various grocery products, but the British purchase "tins". A number of cultural differences can cause marketers problems in attempting to market their products overseas. These include: (a) language, (b) color, (c) customs and taboos, (d) values, (e) aesthetics, (f) time, (g) business norms, (h) religion, and (i) social structures. Each is discussed in the following sections.

Student Example

I travel out of the country to Mexico almost every year. I can see the immense cultural differences between Mexico and the United States, from the language to colors, to the values, religious beliefs, and business norms. As soon as I step out of the plane in Mexico, I feel like I am in a different world. In terms of the language, the primary is obviously Spanish; however, in the past few years, I have noticed signs in the airport with translations to English and Chinese. In terms of values, they seem to focus more on survival. For example, marketing food, shelter products, and clothing. Their religious beliefs are centered around Catholicism.

Elizabeth Garcia

Class of 2020

Language

The importance of language differences cannot be overemphasized, as there are almost 3,000 languages in the world. Language differences cause many problems for marketers in designing advertising campaigns and product labels. Language problems become even more serious once the people of a country speak several languages. For example, in Canada, labels must be in both English and French. In India, there are over 200 different dialects, and a similar situation exists in China.

Student Example

I believe language is very important in marketing, advertising, and product labels. In the United States, I have noticed that most products have product labels in English and often you can peel off for a Spanish label under. Although I have heard many people complain about the fact that there are two languages on every product in America, it is very necessary. In the United States, we have many individuals who speak Spanish, or a language very similar to that, especially since we are so close to South America. Companies and organizations have come to terms with the fact that their product may be in the hands of an individual whose primary language is Spanish; thus, they provide a label in Spanish to properly cater to their consumers.

Natalie Vazquez-Lopez

Class of 2020

Colors

Colors also have different meanings in different cultures. For example, in Egypt, the country's national color of green is considered unacceptable for packaging, because religious leaders once wore it. In Japan, black and white are colors of mourning and should not be used on a product's package. Similarly, purple is unacceptable in Hispanic nations because it is associated with death.

Consider how the following examples could be used in development of international marketing programs:

- In Russia, it is acceptable for men to greet each other with a kiss, but this custom is not acceptable in the US.
- Germans prefer their salad dressing in a tube, while Americans prefer it in a bottle.
- In France, wine is served with most meals, but in America, milk, tea, water, and soft drinks are popular.

McDonalds Corporation has opened 20 restaurants in India. Since 80 percent of Indians are Hindu, McDonald's will use a non-beef meat substitute for its traditional hamburger. The likely beef substitute will be lamb, a very popular meat in India. In anticipation of its restaurant openings, McDonald's conducted extensive market research, site selection studies, and developed a relationship with India's largest chicken supplier. McDonald's has opted to market its product in India, largely because India's population of more than 900 million represents one-sixth of the world's population.

Values

An individual's values arise from his/her moral or religious beliefs and are learned through experiences. For example, in America, we place a very high value on material well-being and are much more likely to purchase status symbols than people in India. Similarly, in India, the Hindu religion forbids the consumption of beef, and fast-food restaurants such as McDonald's and Burger King would encounter tremendous difficulties without product modification. Americans spend large amounts of money on soap, deodorant, and mouthwash because of the value placed on personal cleanliness. In Italy, salespeople call on women only if their husbands are at home.

Aesthetics

The term *aesthetics* is used to refer to the concepts of beauty and good taste. The phrase, "Beauty is in the eye of the beholder" is a very appropriate description for the differences in aesthetics that exist between cultures. For example, Americans believe that suntans are attractive, youthful, and healthy. However, the Japanese do not.

Time

Americans seem to be fanatical about time when compared to other cultures. Punctuality and deadlines are routine business practices in the US. However, salespeople who set definite appointments for sales calls in the Middle East and Latin America will have a lot of time on their hands, as business people from both of these cultures are far less bound by time constraints. To many of these cultures, setting a deadline such as "I have to know next week" is considered pushy and rude.

Student Example

While traveling this past summer I was able to spend time in Italy. It took me a while to get used to having to plan around their typical schedule. During lunch they take what is called a riposo, or an extended lunch break where they go home to eat and spend time with their families and relax. This is in direct contrast to the culture in America, where I have on many occasions worked through lunch breaks. In the world of business, this would be something people would need to be sensitive to so that there would be no issues with trying to schedule meetings or even work lunches.

Brittney Harvey

Class of 2020

Business Norms

The norms of conducting business also vary from one country to the next. Here are several examples of foreign business behavior that differ from US business behavior:

- In France, wholesalers do not like to promote products. They are mainly interested in supplying retailers with the products they need.
- In Russia, plans of any kind must be approved by a seemingly endless string of committees. As a result, business negotiations may take years.
- South Americans like to talk business “nose to nose”. This desire for close physical proximity causes American businesspeople to back away from the constantly forward-moving South Americans.
- In Japan, business people have mastered the tactic of silence in negotiations. Americans are not prepared for this, and they panic because they think something has gone wrong. The result is that Americans become impatient, push for a closure, and often make business concessions they later regret.

These norms are reflected in the difficulty of introducing the Web into Europe.

Religious Beliefs

A person’s religious beliefs can affect shopping patterns and products purchased in addition to his/her values, as discussed earlier. In the United States and other Christian nations, Christmastime is a major sales period. But for other religions, religious holidays do not serve as popular times for purchasing products. Women do not participate in household buying decisions in countries in which religion serves as opposition to women’s rights movements.

Every culture has a social structure, but some seem less widely defined than others. That is, it is more difficult to move upward in a social structure that is rigid. For example, in the US, the two-wage earner family has led to the development of a more affluent set of consumers. But in other cultures, it is considered unacceptable for women to work outside the home.

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at Download for free at http://cnx.org/contents/65dfa6e7-819...dae5f033aece@4

This page titled 3.3: The Social and Cultural Environment is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

3.4: Importance of Culture on Markets

Learning Objectives

After reading this section, students should be able to …

1. appreciate the importance of culture on markets

Because international marketing is closely correlated to the cultures in which a firm wishes to sell its product, culture itself must be analyzed to understand the best way to integrate into both existing and emerging foreign markets. There are five essential areas within which culture must be continually studied in order to achieve success in dealing with culture as it affects international marketing.

These are: (Tian, 2008)

- culture impacts on marketing (international versus domestic)
- cross-cultural dimensions of marketing research
- cross-cultural aspects of the marketing mix (products, price, promotion, and place)
- cross-cultural marketing education and professional training
- and cross-cultural practice in electronic marketing

Cross-cultural marketing occurs when a consumer's culture differs from that of the marketer's own culture.

Consumer behavior diverges across country lines with increased wealth, globalization, and technology; it does not converge (De Mooij, 2005).

Student Example

McDonald's has done a great job introducing its chain around the world and moving into numerous markets and cultures. One location that I think is a great example of cross-cultural marketing is McDonald's in France. The French have a very different culture than the United States. They live their life at a much slower pace and their meals are more about socializing and enjoying the time with people rather than eating and getting out. McDonald's has created some new menu items for their French locations such as an Alpine burger and the McBaguette. McDonald's also designed the French chains so that they are more spacious and decorated tastefully so that it does encourage the French to sit down and enjoy their meal at their own pace. There are also separate McCafe locations around France that are decorated with big comfortable chairs and couches to encourage socialization. In addition, the coffee is served in real coffee mugs and not it to-go cups.

Before entering the country, McDonald's surely did their research because they not only added French-like items to the menu, but they also incorporated a French-like atmosphere. I think this is a very good example of cross-cultural marketing because these locations really encourage a dine-in and more relaxed experience compared to the fast pace take-out that Americans are used to. Many French people have actually commented on the fact that McDonald's in France does not feel like a fast-food restaurant at all. With this information, I think it is easy to say that their research and cross-cultural marketing plan for France has been a success.

Courtney Kent

Class of 2020

This simple fact proves the importance of cultural knowledge in cross-cultural marketing endeavors. In fact, the importance of cross-cultural study has inspired a definition separate from that of international marketing. Cross-cultural marketing is defined as the strategic process of marketing among consumers whose culture differs from that of the marketer's own culture at least in one of the fundamental cultural aspects, such as language, religion, social norms and values, education, and the living style (Tian, 2008).

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at Download for free at http://cnx.org/contents/22ef0f57-703...dd1287d17e0a@5

This page titled 3.4: Importance of Culture on Markets is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

3.5: What is Culture

Learning Objectives

After reading this section, students should be able to …

1. Understand what is meant by *culture*.
2. Know that there are different kinds of culture.
3. Identify several different kinds of culture.

Opening Case: Dunkin' Brands

Dunkin' Donuts and Baskin-Robbins: Making Local Global

High-tech and digital news may dominate our attention globally, but no matter where you go, people still need to eat. Food is a key part of many cultures. It is part of the bonds of our childhood, creating warm memories of comfort food or favorite foods that continue to whet our appetites. So it's no surprise that sugar and sweets are a key part of our food focus, no matter what the culture. Two of the most visible American exports are the twin brands of Dunkin' Donuts and Baskin-Robbins.

Owned today by a consortium of private equity firms known as the Dunkin' Brands, Dunkin' Donuts and Baskin-Robbins have been sold globally for more than thirty-five years. Today, the firm has more than 14,800 points of distribution in forty-four countries with $6.9 billion in global sales.

After an eleven-year hiatus, Dunkin' Donuts returned to Russia in 2010 with the opening of twenty new stores. Under a new partnership, "the planned store openings come 11 years after Dunkin' Donuts pulled out of Russia, following three years of losses exacerbated by a rogue franchisee who sold liquor and meat pies alongside coffee and crullers."[1] Each culture has different engrained habits, particularly in the choices of food and what foods are appropriate for what meals. The more globally aware businesses are mindful of these issues and monitor their overseas operations and partners. One of the key challenges for many companies operating globally with different resellers, franchisees, and wholly owned subsidiaries is the ability to control local operations.

This wasn't the first time that Dunkin' had encountered an overzealous local partner who tried to customize operations to meet local preferences and demands. In Indonesia in the 1990s, the company was surprised to find that local operators were sprinkling a mild, white cheese on a custard-filled donut. The company eventually approved the local customization since it was a huge success.[2]

Dunkin' Donuts and Baskin-Robbins have not always been owned by the same firm. They eventually came under one entity in the late 1980s—an entity that sought to leverage the two brands. One of the overall strategies was to have the morning market covered by Dunkin' Donuts and the afternoon-snack market covered by Baskin-Robbins. It is a strategy that worked well in the United States and was one the company employed as it started operating and expanding in different countries. The company was initially unprepared for the wide range of local cultural preferences and habits that would culturally impact its business. In Russia, Japan, China, and most of Asia, donuts, if they were known at all, were regarded more as a sweet type of bakery treat, like an éclair or cream puff. Locals primarily purchased and consumed them at shopping malls as an "impulse purchase" afternoon-snack item and not as a breakfast food.

In fact, in China, there was no equivalent word for "donut" in Mandarin, and European-style baked pastries were not common outside the Shanghai and Hong Kong markets. To further complicate Dunkin' Donuts's entry into China, which took place initially in Beijing, the company name could not even be phonetically spelled in Chinese characters that made any sense, as Baskin-Robbins had been able to do in Taiwan. After extensive discussion and research, company executives decided that the best name and translation for *Dunkin' Donuts* in China would read *Sweet Sweet Ring* in Chinese characters.

Local cultures also impacted flavors and preferences. For Baskin-Robbins, the flavor library is controlled in the United States, but local operators in each country have been the source of new flavor suggestions. In many cases, flavors that were customized for local cultures were added a decade later to the main menus in major markets, including the United States.

Mango and green tea were early custom ice cream flavors in the 1990s for the Asian market. In Latin America, *dulce de leche* became a favorite flavor. Today, these flavors are staples of the North American flavor menu.

One flavor suggestion from Southeast Asia never quite made it onto the menu. The durian fruit is a favorite in parts of Southeast Asia, but it has a strong, pungent odor. Baskin-Robbins management was concerned that the strong odor would overwhelm factory operations. (The odor of the durian fruit is so strong that the fruit is often banned in upscale hotels in several Asian countries.) While the durian never became a flavor, the company did concede to making ice cream flavored after the *ube*, a sweetened purple yam, for the Philippine market. It was already offered in Japan, and the company extended it to the Philippines. In Japan, sweet corn and red bean ice cream were approved for local sale and became hot sellers, but the two flavors never made it outside the country.

When reviewing local suggestions, management conducts a market analysis to determine if the global market for the flavor is large enough to justify the investment in research and development and eventual production. In addition to the market analysis, the company always has to make sure they have access to sourcing quality flavors and fruit. Mango proved to be a challenge, as finding the correct fruit puree differed by country or culture. Samples from India, Hawaii, Pakistan, Mexico, the Philippines, and Puerto Rico were taste-tested in the mainland United States. It seems that the mango is culturally regarded as a national treasure in every country where it is grown, and every country thinks its mango is the best. Eventually the company settled on one particular flavor of mango.

A challenging balance for Dunkin' Brands is to enable local operators to customize flavors and food product offerings without diminishing the overall brand of the companies. Russians, for example, are largely unfamiliar with donuts, so Dunkin' has created several items that specifically appeal to Russian flavor preferences for scalded cream and raspberry jam.[3] In some markets, one of the company's brands may establish a market presence first. In Russia, the overall "Dunkin' Brands already ranks as a dessert purveyor. Its Baskin-Robbins ice-cream chain boasts 143 shops there, making it the No. 2 Western restaurant brand by number of stores behind the hamburger chain McDonald's Corp."[4] The strength of the company's ice cream brand is now enabling Dunkin' Brands to promote the donut chain as well.

As the opening case about Dunkin' Brands illustrates, local preferences, habits, values, and culture impact all aspects of doing business in a country. But what exactly do we mean by culture? Culture is different from personality. For our purposes here, let's define *personality* as a person's identity and unique physical, mental, emotional, and social characteristics.[5] No doubt one of the highest hurdles to cross-cultural understanding and effective relationships is our frequent inability to decipher the influence of culture from that of personality. Once we become culturally literate, we can more easily read individual personalities and their effect on our relationships.

So, What Is Culture, Anyway?

Culture in today's context is different from the traditional, more singular definition, used particularly in Western languages, where the word often implies refinement. Culture is the beliefs, values, mind-sets, and practices of a group of people. It includes the behavior pattern and norms of that group—the rules, the assumptions, the perceptions, and the logic and reasoning that are specific to a group. In essence, each of us is raised in a belief system that influences our individual perspectives to such a large degree that we can't always account for, or even comprehend, its influence. We're like other members of our culture—we've come to share a common idea of what's appropriate and inappropriate.

Culture is really the collective programming of our minds from birth. It's this collective programming that distinguishes one group of people from another. Much of the problem in any cross-cultural interaction stems from our expectations. The challenge is that whenever we deal with people from another culture—whether in our own country or globally—we expect people to behave as we do and for the same reasons. Culture awareness most commonly refers to having an understanding of another culture's values and perspective. This does not mean automatic acceptance; it simply means understanding another culture's mind-set and how its history, economy, and society have impacted what people think. Understanding so you can properly interpret someone's words and actions means you can effectively interact with them.

When talking about culture, it's important to understand that there really are no rights or wrongs. People's value systems and reasoning are based on the teachings and experiences of their culture. Rights and wrongs then really become perceptions. Cross-

cultural understanding requires that we reorient our mind-set and, most importantly, our expectations, in order to interpret the gestures, attitudes, and statements of the people we encounter. We reorient our mind-set, but we don't necessarily change it.

There are a number of factors that constitute a culture—manners, mind-set, rituals, laws, ideas, and language, to name a few. To truly understand culture, you need to go beyond the lists of dos and don'ts, although those are important too. You need to understand what makes people tick and how, as a group, they have been influenced over time by historical, political, and social issues. Understanding the "why" behind culture is essential.

When trying to understand how cultures evolve, we look at the factors that help determine cultures and their values. In general, a value is defined as something that we prefer over something else—whether it's a behavior or a tangible item. Values are usually acquired early in life and are often nonrational—although we may believe that ours are actually quite rational. Our values are the key building blocks of our cultural orientation.

Odds are that each of us has been raised with a considerably different set of values from those of our colleagues and counterparts around the world. Exposure to a new culture *may* take all you've ever learned about what's good and bad, just and unjust, and beautiful and ugly and stand it on its head.

Human nature is such that we see the world through our own cultural shades. Tucked in between the lines of our cultural laws is an unconscious bias that inhibits us from viewing other cultures objectively. Our judgments of people from other cultures will always be colored by the frame of reference we've been taught. As we look at our own habits and perceptions, we need to think about the experiences that have blended together to impact our cultural frame of reference.

In coming to terms with cultural differences, we tend to employ generalizations. This isn't necessarily bad. Generalizations can save us from sinking into what may be abstruse, esoteric aspects of a culture. However, recognize that cultures and values are not static entities. They're constantly evolving—merging, interacting, drawing apart, and reforming. Around the world, values and cultures are evolving from generation to generation as people are influenced by things outside their culture. In modern times, media and technology have probably single-handedly impacted cultures the most in the shortest time period—giving people around the world instant glimpses into other cultures, for better or for worse. Recognizing this fluidity will help you avoid getting caught in outdated generalizations. It will also enable you to interpret local cues and customs and to better understand local cultures.

Understanding what we mean by culture and what the components of culture are will help us better interpret the impact on business at both the macro and micro levels. Confucius had this to say about cultural crossings: "Human beings draw close to one another by their common nature, but habits and customs keep them apart."

What Kinds of Culture Are There?

Political, economic, and social philosophies all impact the way people's values are shaped. Our cultural base of reference—formed by our education, religion, or social structure—also impacts business interactions in critical ways. As we study cultures, it is very important to remember that all cultures are constantly evolving. When we say "cultural," we don't always just mean people from different countries. Every group of people has its own unique culture—that is, its own way of thinking, values, beliefs, and mind-sets. For our purposes in this chapter, we'll focus on national and ethnic cultures, although there are subcultures within a country or ethnic group.

Precisely where a culture begins and ends can be murky. Some cultures fall within geographic boundaries; others, of course, overlap. Cultures within one border can turn up within other geographic boundaries looking dramatically different or pretty much the same. For example, Indians in India or Americans in the United States may communicate and interact differently from their countrymen who have been living outside their respective home countries for a few years.

The countries of the Indian subcontinent, for example, have close similarities. And cultures within one political border can turn up within other political boundaries looking pretty much the same, such as the Chinese culture in China and the overseas Chinese culture in countries around the world. We often think that cultures are defined by the country or nation, but that can be misleading because there are different cultural groups (as depicted in the preceding figure). These groups include nationalities; subcultures (gender, ethnicities, religions, generations, and even socioeconomic class); and organizations, including the workplace.

Nationalities

A national culture is—as it sounds—defined by its geographic and political boundaries and includes even regional cultures within a nation as well as among several neighboring countries. What is important about nations is that boundaries have changed throughout history. These changes in what territory makes up a country and what the country is named impact the culture of each country.

In the past century alone, we have seen many changes as new nations emerged from the gradual dismantling of the British and Dutch empires at the turn of the 1900s. For example, today the physical territories that constitute the countries of India and Indonesia are far different than they were a hundred years ago. While it's easy to forget that the British ran India for two hundred years and that the Dutch ran Indonesia for more than one hundred and fifty years, what is clearer is the impact of the British and the Dutch on the respective bureaucracies and business environments. The British and the Dutch were well known for establishing large government bureaucracies in the countries they controlled. Unlike the British colonial rulers in India, the Dutch did little to develop Indonesia's infrastructure, civil service, or educational system. The British, on the other hand, tended to hire locals for administrative positions, thereby establishing a strong and well-educated Indian bureaucracy. Even though many businesspeople today complain that this Indian bureaucracy is too slow and focused on rules and regulations, the government infrastructure and English-language education system laid out by the British helped position India for its emergence as a strong high-tech economy.

Even within a national culture, there are often distinct regional cultures—the United States is a great example of diverse and distinct cultures all living within the same physical borders. In the United States, there's a national culture embodied in the symbolic concept of "all-American" values and traits, but there are also other cultures based on geographically different regions—the South, Southwest, West Coast, East Coast, Northeast, Mid-Atlantic, and Midwest.

Subcultures

Many groups are defined by ethnicity, gender, generation, religion, or other characteristics with cultures that are unique to them. For example, the ethnic Chinese business community has a distinctive culture even though it may include Chinese businesspeople in several countries. This is particularly evident throughout Asia, as many people often refer to Chinese businesses as making up a single business community. The overseas Chinese business community tends to support one another and forge business bonds whether they are from Indonesia, Malaysia, Singapore, or other ASEAN (Association of Southeast Asian Nations) countries. This group is perceived differently than Chinese from mainland China or Taiwan. Their common experience being a minority ethnic community with strong business interests has led to a shared understanding of how to quietly operate large businesses in countries. Just as in mainland China, *guanxi*, or "connections," are essential to admission into this overseas Chinese business network. But once in the network, the Chinese tend to prefer doing business with one another and offer preferential pricing and other business services.

Organizations

Every organization has its own workplace culture, referred to as the organizational culture. This defines simple aspects such as how people dress (casual or formal), how they perceive and value employees, or how they make decisions (as a group or by the manager alone). When we talk about an entrepreneurial culture in a company, it might imply that the company encourages people to think creatively and respond to new ideas fairly quickly without a long internal approval process. One of the issues managers often have to consider when operating with colleagues, employees, or customers in other countries is how the local country's culture will blend or contrast with the company's culture.

For example, Apple, Google, and Microsoft all have distinct business cultures that are influenced both by their industries and by the types of technology-savvy employees that they hire, as well as by the personalities of their founders. When these firms operate in a country, they have to assess how new employees will fit their respective corporate cultures, which usually emphasize creativity, innovation, teamwork balanced with individual accomplishment, and a keen sense of privacy. Their global employees may appear relaxed in casual work clothes, but underneath there is often a fierce competitiveness. So how do these companies effectively hire in countries like Japan, where teamwork and following rules are more important than seeking new ways of doing things? This is an ongoing challenge that human resources (HR) departments continually seek to address.

Key Takeaways

- Culture is the beliefs, values, mind-sets, and practices of a specific group of people. It includes the behavior pattern and norms of a specific group—the rules, the assumptions, the perceptions, and the logic and reasoning that are specific to a group. Culture is really the collective programming of our minds from birth. It's this collective programming that distinguishes one group of people from another. Cultural awareness most commonly refers to having an understanding of another culture's values and perspective.
- When trying to understand how cultures evolve, we look at the factors that help determine cultures and their values. In general, a *value*is defined as something that we prefer over something else—whether it's a behavior or a tangible item. Values are usually acquired early in life and are usually nonrational. Our values are the key building blocks of our cultural orientation.
- When we say cultural, we don't always just mean people from different countries. Cultures exist in all types of groups. There are even subcultures within a country or target ethnic group. Each person belongs to several kinds of cultures: national, subcultural (regional, gender, ethnic, religious, generational, and socioeconomic), and group or workplace (corporate culture).

References

1. Kevin Helliker, "Dunkin' Donuts Heads Back to Russia," *Wall Street Journal*, April 27, 2010, accessed February 15, 2011, http://online.wsj.com/article/SB10001424052748704464704575208320044839374.html.
2. David Jenkins (former director, International Operations Development, Allied-Domecq QSR International Ltd.), interview with the author, 2010.
3. Kevin Helliker, "Dunkin' Donuts Heads Back to Russia," Wall Street Journal, April 27, 2010, accessed February 15, 2011, http://online.wsj.com/article/SB10001424052748704464704575208320044839374.html.
4. Kevin Helliker, "Dunkin' Donuts Heads Back to Russia," *Wall Street Journal*, April 27, 2010, accessed February 15, 2011, http://online.wsj.com/article/SB1000...044839374.html.
5. Dictionary.com, s.v. "personality," accessed February 22, 2011, http://dictionary.reference.com/browse/personality.

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 3.5: What is Culture is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

3.6: Describing Culture

Learning Objectives

After reading this section, students should be able to …

1. Know several methods to describe cultures.
2. Define and apply Hofstede's and Hall's categories for cultural identification.
3. Identify and discuss additional determinants of culture.

The study of cross-cultural analysis incorporates the fields of anthropology, sociology, psychology, and communication. The combination of cross-cultural analysis and business is a new and evolving field; it's not a static understanding but changes as the world changes. Within cross-cultural analysis, two names dominate our understanding of culture—Geert Hofstede and Edward T. Hall. Although new ideas are continually presented, Hofstede remains the leading thinker on how we see cultures.

This section will review both the thinkers and the main components of how they define culture and the impact on communications and business. At first glance, it may seem irrelevant to daily business management to learn about these approaches. In reality, despite the evolution of cultures, these methods provide a comprehensive and enduring understanding of the key factors that shape a culture, which in turn impact every aspect of doing business globally. Additionally, these methods enable us to compare and contrast cultures more objectively. By understanding the key researchers, you'll be able to formulate your own analysis of the different cultures and the impact on international business.

Hofstede and Values

Geert Hofstede, sometimes called the father of modern cross-cultural science and thinking, is a social psychologist who focused on a comparison of nations using a statistical analysis of two unique databases. The first and largest database composed of answers that matched employee samples from forty different countries to the same survey questions focused on attitudes and beliefs. The second consisted of answers to some of the same questions by Hofstede's executive students who came from fifteen countries and from a variety of companies and industries. He developed a framework for understanding the systematic differences between nations in these two databases. This framework focused on value dimensions. Values, in this case, are *broad preferences for one state of affairs over others*, and they are mostly unconscious.

Most of us understand that values are our own culture's or society's ideas about what is good, bad, acceptable, or unacceptable. Hofstede developed a framework for understanding how these values underlie organizational behavior. Through his database research, he identified five key value dimensions that analyze and interpret the behaviors, values, and attitudes of a national culture:[1]

1. Power distance
2. Individualism
3. Masculinity
4. Uncertainty avoidance (UA)
5. Long-term orientation

Power distance refers to how openly a society or culture accepts or does not accept differences between people, as in hierarchies in the workplace, in politics, and so on. For example, *high power distance* cultures openly accept that a boss is "higher" and as such deserves a more formal respect and authority. Examples of these cultures include Japan, Mexico, and the Philippines. In Japan or Mexico, the senior person is almost a father figure and is automatically given respect and usually loyalty without questions.

In Southern Europe, Latin America, and much of Asia, power is an integral part of the social equation. People tend to accept relationships of servitude. An individual's status, age, and seniority command respect—they're what make it all right for the lower-ranked person to take orders. Subordinates expect to be told what to do and won't take initiative or speak their minds unless a manager explicitly asks for their opinion.

At the other end of the spectrum are *low power distance* cultures, in which superiors and subordinates are more likely to see each other as equal in power. Countries found at this end of the spectrum include Austria and Denmark. To be sure, not all cultures view

power in the same ways. In Sweden, Norway, and Israel, for example, respect for equality is a warranty of freedom. Subordinates and managers alike often have carte blanche to speak their minds.

Interestingly enough, research indicates that the United States tilts toward low power distance but is more in the middle of the scale than Germany and the United Kingdom.

Let's look at the culture of the United States in relation to these five dimensions. The United States actually ranks somewhat lower in power distance—under forty as noted in Figure 3.1 "The United States' Five Value Dimensions". The United States has a culture of promoting participation at the office while maintaining control in the hands of the manager. People in this type of culture tend to be relatively laid-back about status and social standing—but there's a firm understanding of who has the power. What's surprising for many people is that countries such as the United Kingdom and Australia actually rank lower on the power distance spectrum than the United States.

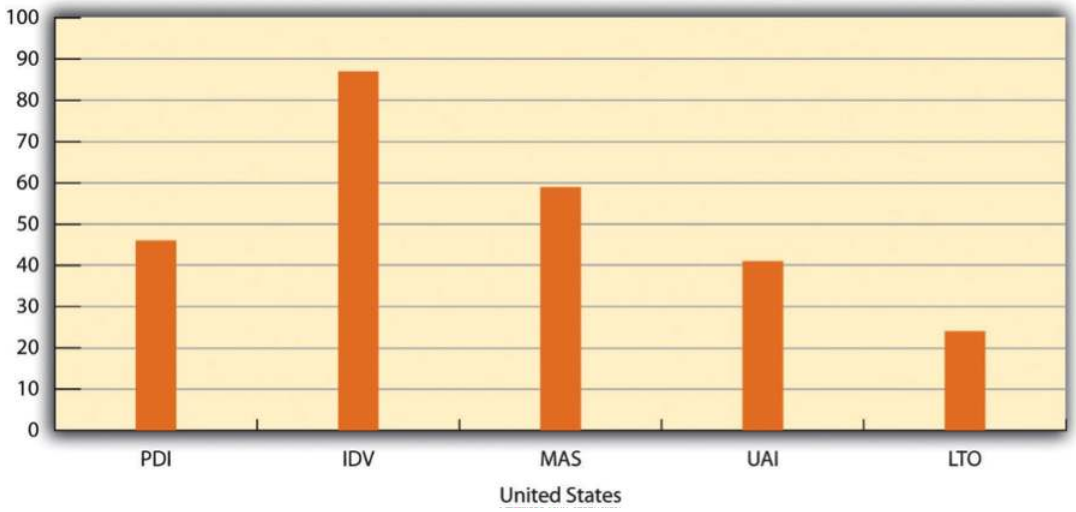


Figure 3.6.1: The United States' Five Value Dimensions Source: "Geert Hofstede™ Cultural Dimensions," Itim International, accessed June 3, 2011, http://www.geert-hofstede.com/hofste...d_states.shtml .

Individualism, noted as IDV in Figure 3.1 "The United States' Five Value Dimensions", is just what it sounds like. It refers to people's tendency to take care of themselves and their immediate circle of family and friends, perhaps at the expense of the overall society. In individualistic cultures, what counts most is self-realization. Initiating alone, sweating alone, achieving alone—not necessarily collective efforts—are what win applause. In individualistic cultures, competition is the fuel of success.

The United States and Northern European societies are often labeled as individualistic. In the United States, individualism is valued and promoted—from its political structure (individual rights and democracy) to entrepreneurial zeal (capitalism). Other examples of high-individualism cultures include Australia and the United Kingdom.

On the other hand, in collectivist societies, group goals take precedence over individuals' goals. Basically, individual members render loyalty to the group, and the group takes care of its individual members. Rather than giving priority to "me," the "us" identity predominates. Of paramount importance is pursuing the common goals, beliefs, and values of the group as a whole—so much so, in some cases, that it's nearly impossible for outsiders to enter the group. Cultures that prize collectivism and the group over the individual include Singapore, Korea, Mexico, and Arab nations. The protections offered by traditional Japanese companies come to mind as a distinctively group-oriented value.

The next dimension is masculinity, which may sound like an odd way to define a culture. When we talk about masculine or feminine cultures, we're not talking about diversity issues. It's about how a society views traits that are considered masculine or feminine.

This value dimension refers to how a culture ranks on traditionally perceived "masculine" values: assertiveness, materialism, and less concern for others. In masculine-oriented cultures, gender roles are usually crisply defined. Men tend to be more focused on performance, ambition, and material success. They cut tough and independent personas, while women cultivate modesty and quality of life. Cultures in Japan and Latin American are examples of masculine-oriented cultures.

Student Example

In the United States, we typically tend to land somewhere in the middle when evaluated based on masculinity, i.e., we emphasize both masculine values and feminine values. Our culture creates a society that is driven by both competition and achievement as well as also the quality of life or caring for others. In countries like Japan, however, they rank much higher on the masculinity scale. The fundamental issue is what motivates people. This is not male vs. female but rather what characteristics motivate the collective individuals who make up the society. There is still an emphasis on collectivism in Japan, but competition between groups can be fierce. From a young age, where children compete in sports teams, to the corporate world of business where competition can lead to rivalry amongst firms. As a result of this competition, material production and presentation are held to a high standard, further demonstrating how they are a masculine society. Understanding the differences between a masculine or feminine society can play an integral part in determining success in terms of international marketing as promotion efforts should represent masculinity in a way that is received well by the consumers.

Mitchel Mertins

Class of 2020

In contrast, feminine cultures are thought to emphasize “feminine” values: concern for all, an emphasis on the quality of life, and an emphasis on relationships. In feminine-oriented cultures, both genders swap roles, with the focus on quality of life, service, and independence. The Scandinavian cultures rank as feminine cultures, as do cultures in Switzerland and New Zealand. The United States is actually more moderate, and its score is ranked in the middle between masculine and feminine classifications. For all these factors, it’s important to remember that cultures don’t necessarily fall neatly into one camp or the other.

The next dimension is uncertainty avoidance (UA). This refers to how much uncertainty a society or culture is willing to accept. It can also be considered an indication of the risk propensity of people from a specific culture.

People who have high uncertainty avoidance generally prefer to steer clear of conflict and competition. They tend to appreciate very clear instructions. At the office, sharply defined rules and rituals are used to get tasks completed. Stability and what is known are preferred to instability and the unknown. Company cultures in these countries may show a preference for low-risk decisions, and employees in these companies are less willing to exhibit aggressiveness. Japan and France are often considered clear examples of such societies.

In countries with low uncertainty avoidance, people are more willing to take on risks, companies may appear less formal and structured, and “thinking outside the box” is valued. Examples of these cultures are Denmark, Singapore, Australia, and to a slightly lesser extent, the United States. Members of these cultures usually require less formal rules to interact.

The fifth dimension is long-term orientation, which refers to whether a culture has a long-term or short-term orientation. This dimension was added by Hofstede after the original four you just read about. It resulted in the effort to understand the difference in thinking between the East and the West. Certain values are associated with each orientation. The long-term orientation values persistence, perseverance, thriftiness, and having a sense of shame. These are evident in traditional Eastern cultures. Based on these values, it’s easy to see why a Japanese CEO is likely to apologize or take the blame for a faulty product or process.

The short-term orientation values tradition only to the extent of fulfilling social obligations or providing gifts or favors. These cultures are more likely to be focused on the immediate or short-term impact of an issue. Not surprisingly, the United Kingdom and the United States rank low on long-term orientation.

Long- and short-term orientation and the other value dimensions in the business arena are all evolving as many people earn business degrees and gain experience outside their home cultures and countries, thereby diluting the significance of a single cultural perspective. As a result, in practice, these five dimensions do not occur as single values but are really woven together and interdependent, creating very complex cultural interactions. Even though these five values are constantly shifting and not static, they help us begin to understand how and why people from different cultures may think and act as they do. Hofstede’s study demonstrates that there are national and regional cultural groupings that affect the behavior of societies and organizations and that these are persistent over time.

Edward T. Hall

Edward T. Hall was a respected anthropologist who applied his field to the understanding of cultures and intercultural communications. Hall is best noted for three principal categories that analyze and interpret how communications and interactions between cultures differ: context, space, and time.

Context: High-Context versus Low-Context Cultures

High and low context refers to how a message is communicated. In high-context cultures, such as those found in Latin America, Asia, and Africa, the physical context of the message carries a great deal of importance. People tend to be more indirect and to expect the person they are communicating with to decode the implicit part of their message. While the person sending the message takes painstaking care in crafting the message, the person receiving the message is expected to read it within context. The message may lack the verbal directness you would expect in a low-context culture. In high-context cultures, body language is as important and sometimes more important than the actual words spoken.

In contrast, in low-context cultures such as the United States and most Northern European countries, people tend to be explicit and direct in their communications. Satisfying individual needs is important. You're probably familiar with some well-known low-context mottos: "Say what you mean" and "Don't beat around the bush." The guiding principle is to minimize the margins of misunderstanding or doubt. Low-context communication aspires to get straight to the point.

Communication between people from high-context and low-context cultures can be confusing. In business interactions, people from low-context cultures tend to listen only to the words spoken; they tend not to be cognizant of body language. As a result, people often miss important clues that could tell them more about the specific issue.

Space

Space refers to the study of physical space and people. Hall called this the study of proxemics, which focuses on space and distance between people as they interact. *Space* refers to everything from how close people stand to one another to how people might mark their territory or boundaries in the workplace and in other settings. Stand too close to someone from the United States, which prefers a "safe" physical distance, and you are apt to make them uncomfortable. How close is too close depends on where you are from. Whether consciously or unconsciously, we all establish a comfort zone when interacting with others. Standing distances shrink and expand across cultures. Latins, Spaniards, and Filipinos (whose culture has been influenced by three centuries of Spanish colonization) stand rather close even in business encounters. In cultures that have a low need for territory, people not only tend to stand closer together but also are more willing to share their space—whether it be a workplace, an office, a seat on a train, or even ownership of a business project.

Attitudes toward Time: Polychronic versus Monochronic Cultures

Hall identified that time is another important concept greatly influenced by culture. In polychronic cultures—*polychronic* literally means "many times"—people can do several things at the same time. In monochronic cultures or "one-time" cultures, people tend to do one task at a time.

This isn't to suggest that people in polychronic cultures are better at multitasking. Rather, people in monochronic cultures, such as Northern Europe and North America, tend to schedule one event at a time. For them, an appointment that starts at 8 a.m. is an appointment that starts at 8 a.m.—or 8:05 at the latest. People are expected to arrive on time, whether for a board meeting or a family picnic. Time is a means of imposing order. Often the meeting has a firm end time as well, and even if the agenda is not finished, it's not unusual to end the meeting and finish the agenda at another scheduled meeting.

In polychronic cultures, by contrast, time is nice, but people and relationships matter more. Finishing a task may also matter more. If you've ever been to Latin America, the Mediterranean, or the Middle East, you know all about living with relaxed timetables. People might attend to three things at once and think nothing of it. Or they may cluster informally, rather than arrange themselves in a queue. In polychronic cultures, it's not considered an insult to walk into a meeting or a party well past the appointed hour.

In polychronic cultures, people regard work as part of a larger interaction with a community. If an agenda is not complete, people in polychronic cultures are less likely to simply end the meeting and are more likely to continue to finish the business at hand.

Those who prefer monochronic order may find polychronic order frustrating and hard to manage effectively. Those raised with a polychronic sensibility, on the other hand, might resent the "tyranny of the clock" and prefer to be focused on completing the tasks at hand.

What Else Determines a Culture?

The methods presented in the previous sections note how we look at the structures of cultures, values, and communications. They also provide a framework for a comparative analysis between cultures, which is particularly important for businesses trying to operate effectively in multiple countries and cultural environments.

Additionally, there are other external factors that also constitute a culture—manners, mindsets, values, rituals, religious beliefs, laws, arts, ideas, customs, beliefs, ceremonies, social institutions, myths, and legends, language, individual identity, and behaviors, to name a few. While these factors are less structured and do not provide a comparative framework, they are helpful in completing our understanding of what impacts a culture. When we look at these additional factors, we are seeking to understand how each culture views and incorporates each of them. For example, are there specific ceremonies or customs that impact the culture and for our purposes, its business culture? For example, in some Chinese businesses, feng shui—an ancient Chinese physical art and science—is implemented in the hopes of enhancing the physical business environment and success potential of the firm.

Of these additional factors, the single most important one is communication.

Communication

Verbal Language

Language is one of the more conspicuous expressions of culture. As Hall showed, understanding the context of how language is used is essential to accurately interpret the meaning. Aside from the obvious differences, vocabularies are actually often built on the cultural experiences of the users. For example, in the opening case with Dunkin' Donuts, we saw how the local culture complicated the company's ability to list its name in Chinese characters.

Similarly, it's interesting to note that Arabic speakers have only one word for ice, *telg*, which applies to ice, snow, hail, and so on. In contrast, Eskimo languages have different words for each type of snow—even specific descriptive words to indicate the amounts of snow.

Another example of how language impacts business is in written or e-mail communications, where you don't have the benefit of seeing someone's physical gestures or posture. For example, India is officially an English-speaking country, though its citizens speak the Queen's English. Yet many businesspeople experience miscommunications related to misunderstandings in the language, ranging from the comical to the frustrating. Take something as simple as multiplication and division. Indians will commonly say "6 into 12" and arrive at 72, whereas their American counterparts will divide to get an answer of 2. You'd certainly want to be very clear if math were an essential part of your communication, as it would be if you were creating a budget for a project.

Another example of nuances between Indian and American language communications is the use of the word *revert*. The word means "to go back to a previously existing condition." To Indians, though, the common and accepted use of the word is much more simplistic and means "to get back to someone."

To see how language impacts communications, look at a situation in which an American manager, in negotiating the terms of a project, began to get frustrated by the e-mails that said that the Indian company was going to "revert back." He took that to mean that they had not made any progress on some issues and that the Indians were going back to the original terms. Actually, the Indians simply meant that they were going to get back to him on the outstanding issues—again, a different connotation for the word because of cultural differences.

The all-encompassing "yes" is one of the hardest verbal cues to decipher. What does it really mean? Well, it depends on where you are. In a low-context country—the United States or Scandinavian countries, for example—"yes" is what it is: yes. In a high-context culture—Japan or the Philippines, for example—it can mean "yes," "maybe," "OK," or "I understand you,"—but it may not always signify agreement. The meaning is in the physical context, not the verbal.

Language or words become a code, and you need to understand the word and the context.

? Did You Know?

English Required in Japan

It's commonly accepted around the world that English is the primary global business language. In Japan, some companies have incorporated this reality into daily business practice. By 2012, employees at Rakuten, Japan's biggest online retailer by sales, will be "required to speak and correspond with one another in English, and executives have been told they will be fired if they aren't proficient in the language by then. Rakuten, which has made recent acquisitions in the U.S. and Europe, says the English-only policy is crucial to its goal of becoming a global company. It says it needed a common language to communicate with its new operations, and English, as the chief language of international business, was the obvious choice. It expects the change, among other things, to help it hire and retain talented non-Japanese workers."[2]

Rakuten is only one of many large and small Japanese companies pursuing English as part of its ongoing global strategy. English is key to the business culture and language at Sony, Nissan Motor, and Mitsubishi, to name a few Japanese businesses. English remains the leading global business language for most international companies seeking a standard common language with its employees, partners, and customers.

Body Language

How you gesture, twitch, or scrunch up your face represents a veritable legend to your emotions. Being able to suitably read—and broadcast—body language can significantly increase your chances of understanding and being understood. In many high-context cultures, it is essential to understand body language in order to accurately interpret a situation, comment, or gesture.

People may not understand your words, but they will certainly interpret your body language according to *their* accepted norms. Notice the word *their*. It is *their* perceptions that will count when you are trying to do business with them, and it's important to understand that those perceptions will be based on the teachings and experiences of their culture—not yours.

Another example of the "yes, I understand you" confusion in South Asia is the infamous head wobble. Indians will roll their head from side to side to signify an understanding or acknowledgement of a statement—but not necessarily an acceptance. Some have even expressed that they mistakenly thought the head wobble meant "no." If you didn't understand the context, then you are likely to misinterpret the gesture and the possible verbal cues as well.

? Did You Know?

OK or Not OK?

Various motions and postures can mean altogether divergent things in different cultures. Hand gestures are a classic example. The American sign for OK means "zero" in Tunisia and southern France, which far from signaling approval, is considered a threat. The same gesture, by the way, delivers an obscenity in Brazil, Germany, Greece, and Russia. If you want to tell your British colleagues that victory on a new deal is close at hand by making the V sign with your fingers, be sure your palm is facing outward; otherwise you'll be telling them where to stick it, and it's unlikely to win you any new friends.

Eye contact is also an important bit of unspoken vocabulary. People in Western cultures are taught to look into the eyes of their listeners. Likewise, it's a way the listener reciprocates interest. In contrast, in the East, looking into someone's eyes may come off as disrespectful, since focusing directly on someone who is senior to you implies disrespect. So when you're interacting with people from other cultures, be careful not to assume that a lack of eye contact means anything negative. There may be a cultural basis to their behavior.

? Amusing Anecdote

Kiss, Shake, Hug, or Bow

Additionally, touching is a tacit means of communication. In some cultures, shaking hands when greeting someone is a must. Where folks are big on contact, grown men might embrace each other in a giant bear hug, such as in Mexico or Russia.

Japan, by contrast, has traditionally favored bowing, thus ensuring a hands-off approach. When men and women interact for business, this interaction can be further complicated. If you're female interacting with a male, a kiss on the cheek may work in

Latin America, but in an Arab country, you may not even get a handshake. It can be hard not to take it personally, but you shouldn't. These interactions reflect centuries-old traditional cultural norms that will take time to evolve.

Ethnocentrism

A discussion of culture would not be complete without at least mentioning the concept of ethnocentrism. Ethnocentrism is the view that a person's own culture is central and other cultures are measured in relation to it. It's akin to a person thinking that their culture is the "sun" around which all other cultures revolve. In its worst form, it can create a false sense of superiority of one culture over others.

Human nature is such that we see the world through our own cultural shades. Tucked in between the lines of our cultural laws is an unconscious bias that inhibits us from viewing other cultures objectively. Our judgments of people from other cultures will always be colored by the frame of reference in which we have been raised.

The challenge occurs when we feel that our cultural habits, values, and perceptions are superior to other people's values. This can have a dramatic impact on our business relations. Your best defense against ethnocentric behavior is to make a point of seeing things from the perspective of the other person. Use what you have learned in this chapter to extend your understanding of the person's culture. As much as possible, leave your own frame of reference at home. Sort out what makes you and the other person different—*and* what makes you similar.

? Key Takeaways

- There are two key methods used to describe and analyze cultures. The first was developed by Geert Hofstede and focuses on five key dimensions that interpret behaviors, values, and attitudes: power distance, individualism, masculinity, uncertainty avoidance, and long-term orientation. The second method was developed by Edward T. Hall and focuses on three main categories for how communications and interactions between cultures differ: high-context versus low-context communications, space, and attitudes toward time.
- In addition to the main analytical methods for comparing and contrasting cultures, there are a number of other determinants of culture. These determinants include manners, mind-sets, values, rituals, religious beliefs, laws, arts, ideas, customs, beliefs, ceremonies, social institutions, myths and legends, language, individual identity, and behaviors. Language includes both verbal and physical languages.

References

1. "Dimensions of National Cultures," Geert Hofstede, accessed February 22, 2011, http://www.geerthofstede.nl/culture/...-cultures.aspx.
2. Daisuke Wakabayashi, "English Gets the Last Word in Japan," *Wall Street Journal*, August 6, 2010, accessed February 22, 2011, http://online.wsj.com/article/SB1000...407926080.html.

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 3.6: Describing Culture is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

3.7: Marketing Across Cultures

Learning Objectives

After reading this section, students should be able to …

1. understand the implications of host country research
2. appreciate the importance of cross-cultural training

While many similarities exist among businesses, there are dynamics that must be taken into consideration in an increasingly global environment, such as multicultural employees and varying experiences in countries outside that of the business. It is essential to take these differences seriously and not assume that individuals have similar values.

Host country research and cultural implications

Cultural issues can be divided into two categories, explicit and implicit. Explicit culture issues are related to characteristics that one can see or perceive. Implicit culture issues, on the other hand, are related to attitudes and values, symbolized in the figure below.

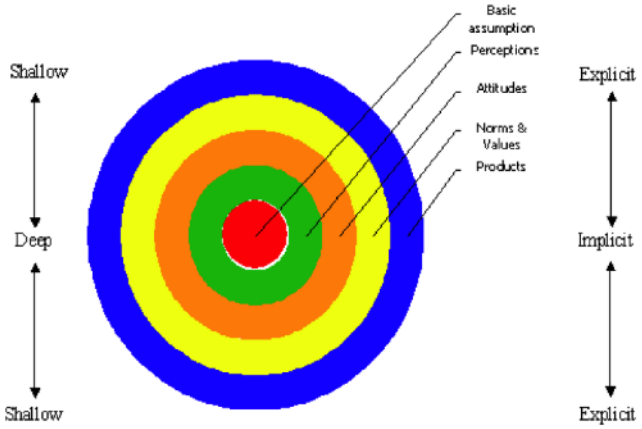


Figure 3.7.1: *The Onion Metaphor of Culture (Ulijn and Fayolle, 2004)*

Explicit culture exists on the outer layer and is the observable reality of the language, food, buildings, houses, monuments, agriculture, shrines, markets, fashions and art. These products are visible in people's behaviors, clothes, food, music and theater.

The middle layers include norms, values, and attitudes but are not directly visible. Norms are the mutual sense a group has of what is right and wrong that can develop on a formal level such as written law, or on an informal level such as social control. Values determine good from bad, and are closely related to the ideals shared by a group. A value in one culture may differ vastly from that of another, and therefore these differences must be studied and taken into consideration when doing business across cultures.

Cross-cultural Training

The creation of a stable and healthy workplace made up of people of varying cultural backgrounds is a matter of increasing importance in the global business environment. Employers must take into consideration the impact cultural diversity can have on both the homogeneity of the workplace and potential legal implications for improper discrimination.

The objective of training programs is to foster the four characteristics of preparedness, sensitivity, patience, and flexibility in managers and other personnel (Czinkota et al, 2005). Methods of training may range from factual preparation involving books and lectures to experiential training involving simulations and field experience. Some topics to be addressed in training might be, but are not limited to:

- comfort levels of trainees' with people of a different background
- impact of trainees' behaviors on others
- understanding stereotypes
- transforming knowledge into empathy

- embracing diversity as a source of strength
- learning a new language

Businesses with diverse cultural backgrounds must maintain an environment suited for every constituent so that the objectives of the business can be efficiently met. Installing cultural diversity training programs can help accomplish this by defining what cultural intelligence is, teaching employees to accept and work effectively with others from different cultural backgrounds, and taking advantage of advice from those who have a cross-cultural experience.

Cultural values determine the way people think and behave. International marketers must understand many subtle differences that may affect the way their marketing is made and perceived in foreign markets. One medium in which many such differences reside is language. Because language is a reflection of culture, some words cannot be cross-culturally translated, which implies that it is often better to have local copywriters write and translate marketing and advertising content to avoid cultural misunderstandings. Because of this phenomenon, global advertising, which is a main component of global marketing, often relies on symbol recognition to convey meaning in their ads, instead of words.

The approach to discussing culture, as it relates to global marketing, in most textbooks is a three-pronged approach. First, the concept of culture is defined, second, the various components of culture are identified, and third, vivid examples of cultural differences are provided. The dire consequences of firms not taking these differences into account are invariably described, as adherence to local culture is considered one of the most important, if not the most important, components of success in international marketing (Hofstede, 1996).

Ethical Considerations

Managers of businesses that conduct operations in an increasingly global environment face a dilemma when selecting and applying ethics to decisions in cross-cultural settings. Although ethical values may be similar across cultures in many cases, the application of those values to certain situations may vary. Ethics can be described as the science of human duty. It is upon the ethical standards of a person that judges whether or not an action is right or wrong.

Before a company does business across borders, it must first decide what its motivation is regarding ethical conduct, which will determine what kind of behavior is to be expected from employees.

Student Example

When we were analyzing the pros and cons of sweatshops in developing countries, Nike was brought up as an example of the dark side of sweatshops. As a quick recap: It was alleged that Nike cut jobs, stole money from workers, and created hazardous working conditions for sweatshop workers. Additionally, they allegedly turned away the Worker Rights Consortium (WRC) when the independent group came to review the factories. If these were true, ethics comes into play in two ways here. The first is that Nike would allow such terrible working conditions to persist, hurting hundreds if not thousands of workers. The ethical value of treating a human as a human should be cross-cultural, and the way a company treats workers shows the standards of the higher-management. Secondly, it is unethical to refuse a review by an independent sweatshop inspection organization. It essentially admits the guilt of treating workers so poorly that the company doesn't want it getting out into the public.

Lucio Chavarria

Class of 2020

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at Download for free at http://cnx.org/contents/65dfa6e7-819...dae5f033aece@4

This page titled 3.7: Marketing Across Cultures is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

4: The Economic and Political Environment

4.1: The Economic and Political Environment Summary

4.2: The Economic Environment

4.3: The Political Environment

4.4: Political Risk

4.5: Legal Risk

This page titled 4: The Economic and Political Environment is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

4.1: The Economic and Political Environment Summary

Summary

The economic environment is a major determinant of global market potential and opportunity. In today's global economy, capital movements are the driving force, production is uncoupled from employment, and capitalism has vanquished communism. Based on patterns of resource allocation and ownership, the world's economies can be categorized as market capitalism, centrally-planned capitalism, centrally-planned socialism, and market socialism. The final years of the twentieth century were marked by transitions toward market capitalism in many countries that had been centrally controlled. However, there still exists a great disparity among the nations of the world in terms of economic freedom.

The political environment of global marketing is the set of governmental institutions, political parties, and organizations that are the expression of the people in the nations of the world. In particular, anyone engaged in global marketing should have an overall understanding of the importance of sovereignty to national governments. The political environment varies from country to country, and political risk assessment is crucial. It is also important to understand a particular government's actions with respect to taxes and seizure of assets. Historically, the latter have taken the form of expropriation, confiscation, and nationalization.

When global managers explore how to expand, they start by looking at the world. Knowing the major markets and the stage of development for each allows managers to determine how best to enter and expand. The manager's goal is to hone in on a new country—hopefully, before their competitors and usually before the popular media does. China and India were expanding rapidly for several years before the financial press, such as the *Wall Street Journal*, elevated them to their current hot status.

It's common to find people interested in doing business with a country simply because they've read that it's the new "hot" economy. They may know little or nothing about the market or country—its history, evolution of thought, people, or how interactions are generally managed in a business or social context. Historically, many companies have only looked at new global markets once potential customers or partners have approached them. However, trade barriers are falling, and new opportunities are fast emerging in markets of the Middle East and Africa—further flattening the world for global firms. Companies are increasingly identifying these and other global markets for their products and services and incorporating them into their long-term growth strategies.

The legal environment consists of laws, courts, attorneys, legal customs, and practices. International law is comprised of the rules and principles that nation-states consider binding upon themselves. The countries of the world can be broadly categorized in terms of common-law legal systems or civil-law legal system. The United States and Canada and many former British colonies are common law countries; most other countries are civil-law. A third system, Islamic law, predominates in the Middle East. Some of the most important legal issues pertain to jurisdiction, antitrust, and licensing. In addition, bribery is pervasive in many parts of the world; the Foreign Corrupt Practice Act (FCPA) applies to American companies operating abroad. Intellectual property protection is another critical issue. Counterfeiting is a major problem in global marketing; it often involves infringement of a company's copyright or trademark ownership. When legal conflicts arise, companies can pursue the matter in court or use arbitration.

Savvy global managers realize that to be effective in a country, they need to know its recent political, economic, and legal history. This helps them evaluate not only the current business opportunity but also the risk of political, economic, and social changes that can impact their business.

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- "World Economies", chapter 4 from the book Challenges and Opportunities in International Business (v. 1.0)under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.
- The course note from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM). 'The Economic and Political environment' is Copyright (c) by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license.

This page titled 4.1: The Economic and Political Environment Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

4.2: The Economic Environment

Learning Objectives

After reading this section, students should be able to …

1. appreciate the importance of the economic environment
2. understand the implication of inflation, deflation and balance of payments

The economic environment is important because of the rapid integration of international economic markets. Increasingly, businesses, consumers, and governments realize that their lives are affected not only by what goes on in their own town, state, or country but also by what is happening around the world. Consumers can walk into their local shops today and buy goods and services from all over the world. Local businesses must compete with these foreign products. However, many of these same businesses also have new opportunities to expand their markets by selling to a multitude of consumers in other countries. The advance of telecommunications is also rapidly reducing the cost of providing services internationally, while the Internet will assuredly change the nature of many products and services as it expands markets even further.

A nation's economic situation represents its current and potential capacity to produce goods and services. The key to understanding market opportunities lies in the evaluation of the stage of a nation's economic growth. Economic growth is the increase in the amount of the goods and services produced by an economy over time. It is conventionally measured as a percentage change in the Gross Domestic Product (GDP) or Gross National Product (GNP). These two measures, which are calculated slightly differently, total the amounts paid for the goods and services that a country produced. As an example of measuring economic growth, a country that creates 9,000,000 in goods and services in 2010 and then creates 9,090,000 in 2011 has a nominal economic growth rate of 1% for 2011.

In order to compare per capita economic growth among countries, the total sales of the countries to be compared may be quoted in a single currency. This requires converting the value of currencies of various countries into a selected currency, for example, U.S. dollars. One way to do this conversion is to rely on exchange rates among the currencies, for example, how many Mexican pesos buy a single U.S. dollar? Another approach is to use the purchasing power parity method. This method is based on how much consumers must pay for the same "basket of goods" in each country.

Inflation or deflation can make it difficult to measure economic growth. If GDP, for example, goes up in a country by 1% in a year, was this due solely to rising prices (inflation) or because more goods and services were produced and saved? To express real growth rather than changes in prices for the same goods, statistics on economic growth are often adjusted for inflation or deflation.

For example, a table may show changes in GDP in the period 1990 to 2000, as expressed in 1990 U.S. dollars. This means that the single currency being used is the U.S. dollar, with the purchasing power it had in the U.S. in 1990. The table might mention whether the figures are "inflation-adjusted" or real. If no adjustments were made for inflation, the table might make no mention of inflation-adjustment or might mention that the prices are nominal.

A country's balance of payments is a record of its economic transactions with the rest of the world; this record shows whether a country has a trade surplus (value of exports exceeds the value of imports) or a trade deficit (value of imports exceeds the value of exports). Trade figures can be further divided into merchandise trade and services trade accounts; a country can run a surplus in both accounts, a deficit in both accounts, or a combination of the two. The U.S. merchandise trade deficit was $819 billion in 2007. However, the U.S.enjoys an annual service trade surplus. Overall, however, the United States is a debtor; Japan enjoys an overall trade surplus and serves as a creditor nation.

Student Example

The United States has been running on a trade deficit since 1976 because of high imports of consumer products and oil. It's very easy for an American citizen to go into any store and find a product that was not manufactured in the United States. When I go shopping for clothes, I always see tags stating, "Made in Vietnam/China/India/Taiwan/Indonesia." I don't think I have ever seen a clothing item with a tag stating, "Made in the U.S.A." The same could be said about other products, such as furniture, vehicles, and electronics. One of the main reasons why the United States is running on a trade deficit is because most

companies in the United States make their products abroad due to cheaper labor and import them into the United States to sell them. One of the biggest ways a trade deficit can affect the economy is through employment. If imports have a higher demand than exports, domestic jobs could be lost abroad, which could lead to increased unemployment rates.

Ivan Chavez

Class of 2020

Let's look at the growth of exports in the world during the past fifty or more years. 4.2.1: "World Exports, 1948–2008 (in Billions of U.S. Dollars)" shows the overall annual exports measured in billions of U.S. dollars from 1948 to 2008. Recognizing that one country's exports are another country's imports, one can see the exponential growth in outflows and inflows during the past fifty years.

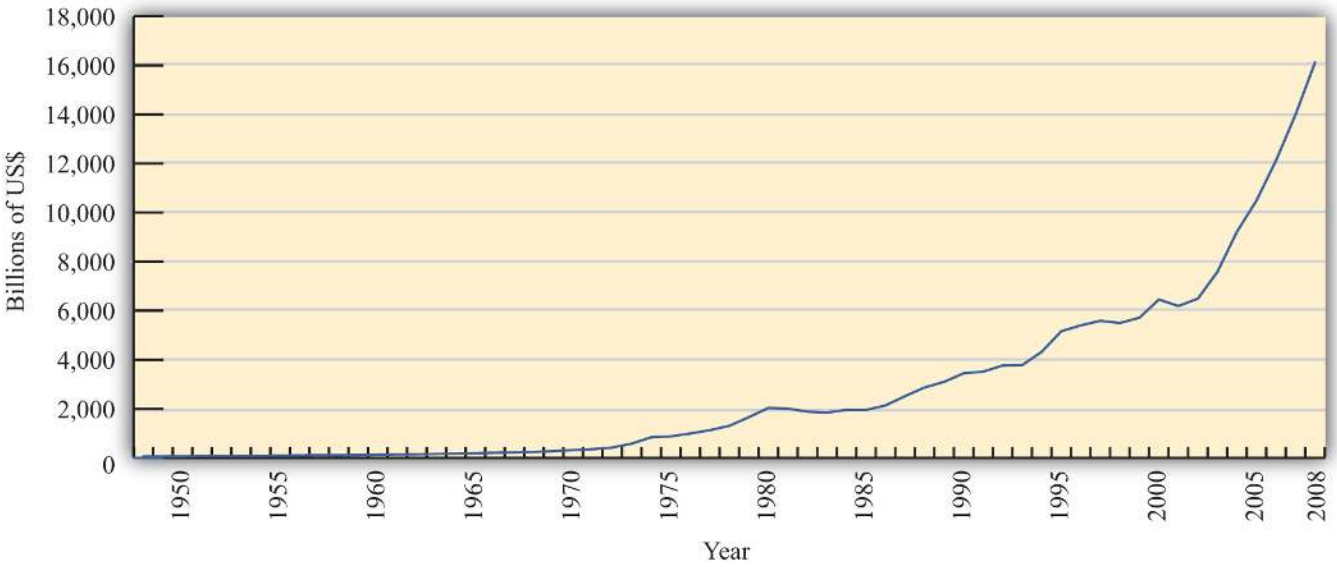


Figure 4.2.1: World Exports, 1948–2008 (in Billions of U.S. Dollars) Source: World Trade Organization, International trade and tariff data, http://www.wto.org/english/res_e/statis_e/statis_e.htm.

However, rapid growth in the value of exports does not necessarily indicate that trade is becoming more important. A better method is to look at the share of traded goods in relation to the size of the world economy. Figure 4.2.2: "World Exports, 1970–2008 (Percentage of World GDP)" shows world exports as a percentage of the world gross domestic product (GDP) for the years 1970 to 2008. It shows a steady increase in trade as a share of the size of the world economy. World exports grew from just over 10 percent of the GDP in 1970 to over 30 percent by 2008. Thus trade is not only rising rapidly in absolute terms; it is becoming relatively more important too.

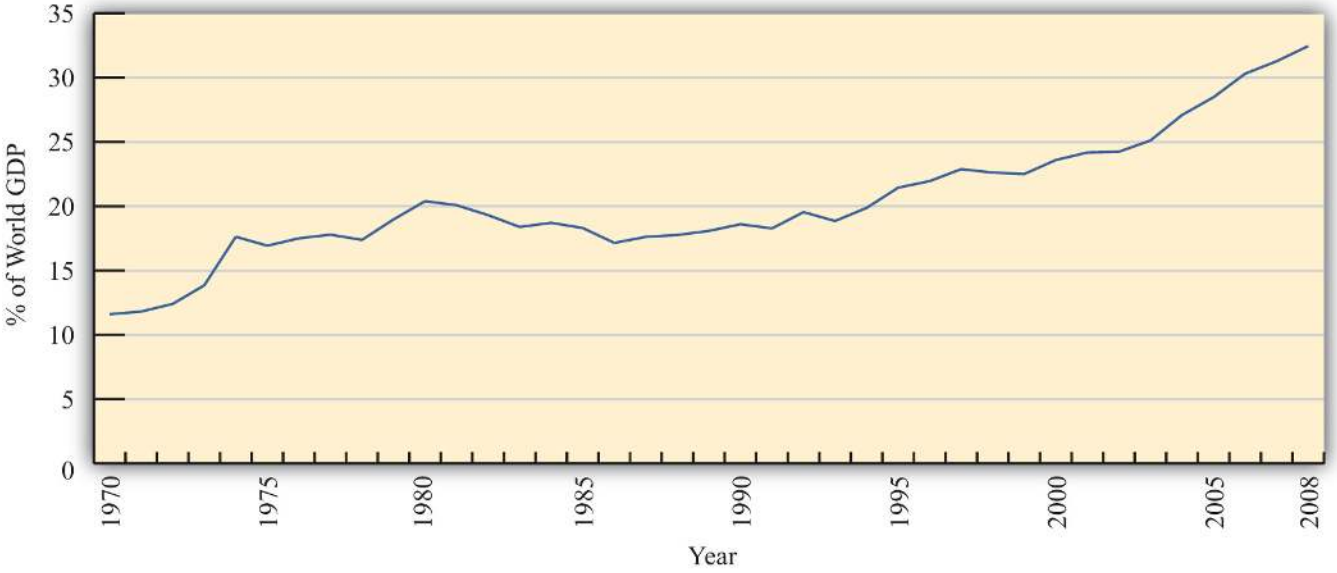


Figure 4.2.2: World Exports, 1970–2008 (Percentage of World GDP) Source: IMF World Economic Outlook Database, http://www.imf.org/external/pubs/ft/weo/2009/02/weodata/index.aspx.

One other indicator of world interconnectedness can be seen in changes in the amount of foreign direct investment (FDI). FDI is foreign ownership of productive activities and thus is another way in which foreign economic influence can affect a country. Figure 4.3 "World Inward FDI Stocks, 1980–2007 (Percentage of World GDP)" shows the stock, or the sum total value, of FDI around the world taken as a percentage of the world GDP between 1980 and 2007. It gives an indication of the importance of foreign ownership and influence around the world. As can be seen, the share of FDI has grown dramatically from around 5 percent of the world GDP in 1980 to over 25 percent of the GDP just twenty-five years later.

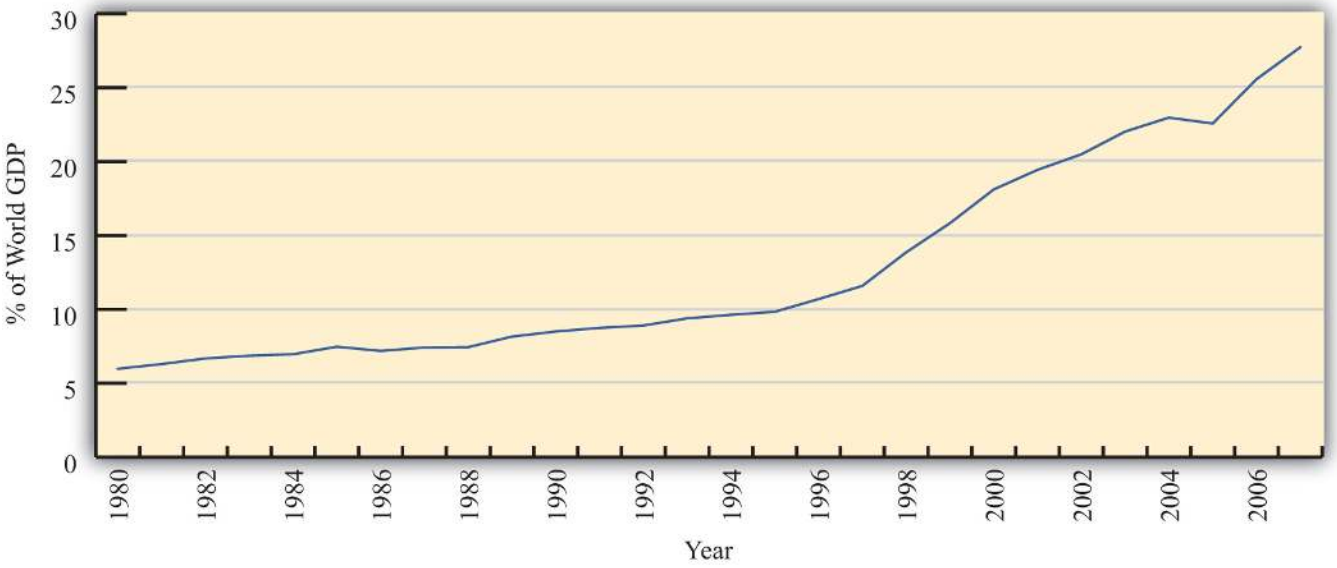


Figure 4.2.1: World Inward FDI Stocks, 1980–2007 (Percentage of World GDP) Source: IMF World Economic Outlook Database, http://www.imf.org/external/pubs/ft/weo/2009/02/weodata/index.aspx; UNCTAD, FDI Statistics: Division on Investment and Enterprise, http://www.unctad.org/Templates/Page.asp?intItemID=4979&lang=1.

The growth of international trade and investment has been stimulated partly by the steady decline of trade barriers since the Great Depression of the 1930s. In the post–World War II era, the General Agreement on Tariffs and Trade, or GATT, prompted regular negotiations among a growing body of members to reciprocally reduce tariffs (import taxes) on imported goods. During each of these regular negotiations (eight of these rounds was completed between 1948 and 1994), countries promised to reduce their tariffs on imports in exchange for concessions—that means tariffs reductions—by other GATT members. When the Uruguay Round, the most recently completed round, was finalized in 1994, the member countries succeeded in extending the agreement to include

liberalization promises in a much larger sphere of influence. Now countries not only would lower tariffs on goods trade but also would begin to liberalize the agriculture and services markets. They would eliminate the many quota systems—like the multifiber agreement in clothing—that had sprouted up in previous decades. And they would agree to adhere to certain minimum standards to protect intellectual property rights such as patents, trademarks, and copyrights. The World Trade Organization (WTO) was created to manage this system of new agreements, to provide a forum for regular discussion of trade matters, and to implement a well-defined process for settling trade disputes that might arise among countries.

Foreign exchange provides a means for settling accounts across borders. The dynamics of international finance can have a significant impact on a nation's economy as well as the fortunes of individual companies. Currencies can be subject to devaluation or revaluation as a result of actions taken by a country's central banker. Currency trading by international speculators can also lead to devaluation. When a country's economy is strong or when demand for its goods is high, its currency tends to appreciate in value. When currency values fluctuate, global firms face various types of economic exposure. Firms can manage exchange rate exposure by hedging.

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at Download for free at http://cnx.org/contents/65dfa6e7-819...dae5f033aece@4. The above content was also adapted from textbook content provided by: (i) CANDELA OPEN COURSES at https://courses.candelalearning.com/principlesmktg1x2kscope/chapter/the-global-environment-economic-growth/under a Creative Commons Attribution NonCommercial Attribution License: CC BY-NC-SA 3.0 US, and from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM). 'The Economic and Political environment' is Copyright (c) by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license; and (ii) form the book 'International Trade: Theory and Policy v. 1.0″ published by Saylor Academy (2012) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

CC licensed content, Shared previously Global Marketing. Provided by: Boundless. Located at: https://www.boundless.com/marketing/...l-marketing-7/?. License: CC BY-SA: Attribution-ShareAlike

---

This page titled 4.2: The Economic Environment is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

4.3: The Political Environment

Learning Objectives

After reading this section, students should be able to …

1. appreciate the importance of the political environment

The political environment abroad is quite different from that of the US. Most nations desire to become self-reliant and to raise their status in the eyes of the rest of the world. This is the essence of nationalism. The nationalistic spirit that exists in many nations has led them to engage in practices that have been very damaging to other countries' marketing organizations. For example, foreign governments can intervene in marketing programs in the following ways:

- contracts for the supply and delivery of goods and services
- the registration and enforcement of trademarks, brand names, and labeling
- patents
- marketing communications
- pricing
- product safety, acceptability, and environmental issues

Student Example

Recently I ordered a product from China, and I was to receive it in four weeks. The product cost and shipping seemed to be reasonable. However, in the second week, I received an email from the seller saying Chinese customs had detained my shipment. Apparently, a new governmental charge was imposed on the type of product I was ordering. Now I was faced with paying the new fee (close to the price of the product) or canceling my order and trying to get it from another seller/country. The seller was friendly and paid for half of the charge while I paid for the other half. Then the product released, but it arrived four weeks after paying the imposed fee.

Mari Carrillo De Olivares

Class of 2020

Political Stability

Business activity tends to grow and thrive when a nation is politically stable. When a nation is politically unstable, multinational firms can still conduct business profitably. Their strategies will be affected however. Most firms probably prefer to engage in the export business rather than invest considerable sums of money in investments in foreign subsidiaries. Inventories will be low and currency will be converted rapidly. The result is that consumers in the foreign nation pay high prices, get less satisfactory products, and have fewer jobs.

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at http://cnx.org/contents/d6db603c-cd3...9734673b90@4.3

This page titled 4.3: The Political Environment is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

4.4: Political Risk

Learning Objectives

After reading this section, students should be able to …

1. define political risk
2. the effect of government policy changes on international marketing

What is political risk?

Political risk is generally defined as the risk to business interests resulting from political instability or political change. Political risk exists in every country around the globe and varies in magnitude and type from country to country. Political risks may arise from policy changes by governments to change controls imposed on exchange rates and interest rates(Barlett et al, 2004). Moreover, political risk may be caused by actions of legitimate governments such as controls on prices, outputs, activities, and currency and remittance restrictions. Political risk may also result from events outside of government controls such as war, revolution, terrorism, labor strikes, and extortion.

Political risk can adversely affect all aspects of the international business from the right to export or import goods to the right to own or operate a business. AON (www.aon.com), for example, categorizes risk based on economic; exchange transfer; strike, riot, or civil commotion; war; terrorism; sovereign non-payment; legal and regulatory; political interference; and supply chain vulnerability.

Student Example

A business that operates abroad or that imports things from a certain country can be affected by the countries' political and economic environment. As most of us are aware, there have been constant riots in Venezuela in an effort to overthrow Nicolas Maduro. As one of the counties with the largest oil reserves, Venezuela is a great business source for U.S. based oil refineries. However, political instability has caused President Donald Trump to impose sanctions on Venezuelan oil. This has affected the U.S. refineries that purchase oil from that country. Additionally, Venezuela is currently facing hyperinflation rates that go above 2 million percent. This economic instability has led its citizens to live difficult lives. There has been news coverage on how individuals dig through garbage trucks to find scraps. Once more, President Donald Trump and other leaders have condemned Nicolas Maduro's regime on various occasions. One way this could affect an Oil Refinery business is that if they continue to conduct business with Venezuela, they might face challenges in importing the oil. They might also not be able to find other sources of business, which could lead to loss of jobs. These are just "what if" scenarios.

Silviano Espana Silva

Class of 2020

How to evaluate your level of political risk

Forms of investment and risk

For a firm considering a new foreign market, there are three broad categories of international business: trade, international licensing of technology and intellectual property, and foreign direct investment. A company developing a business plan may have different elements of all three categories depending on the type of product or service.

The choice of entry depends on the firm's experience, the nature of its product or services, capital resources, and the amount of risk it's willing to consider (Schaffer et al, 2005)

The risk between these three categories of market entry varies significantly with trade ranked the least risky if the company does not have offices overseas and does not keep inventories there. On the other side of the spectrum is direct foreign investment, which generally brings the greatest economic exposure and thus the greatest risk to the company.

Protection from political risk

Companies can reduce their exposure to political risk by careful planning and monitoring political developments. The company should have a deep understanding of domestic and international affairs for the country they are considering entering. The company should know how politically stable the country is, the strength of its institutions, the existence of any political or religious conflicts, ethnic composition, and minority rights. The country's standing in the international arena should also be part of the consideration; this includes its relations with neighbors, border disputes, membership in international organizations, and recognition of international law. If the company does not have the resources to conduct such research and analysis, it may find such information at their foreign embassies, international chambers of commerce, political risk consulting firms, insurance companies, and international businessmen familiar with a particular region. In some countries, governments will establish agencies to help private businesses grow overseas. Governments may also offer political risk insurance to promote exports or economic development. Private businesses may also purchase political risk insurance from insurance companies specialized in international business. Insurance companies offering political risk insurance will generally provide coverage against inconvertibility, expropriation, and political violence, including civil strife (US Small Business Administration). Careful planning and vigilance should be part of any company's preparation for developing an international presence.

Government policy changes and trade relations

A government makes changes in policies that have an impact on international business. Many reasons may cause governments to change their policies toward foreign enterprises. High unemployment, widespread poverty, nationalistic pressure, and political unrest are just a few of the reasons that can lead to changes in policy. Changes in policies can impose more restrictions on foreign companies to operate or limit their access to financing and trade. In some cases, changes in policy may be favorable to foreign businesses as well.

To solve domestic problems, governments often use trade relations. Trade as a political tool may cause an international business to be caught in a trade war or embargo (Schaffer et al, 2005). As a result, international businesses can experience frequent changes in regulations and policies, which can add additional costs of doing business overseas.

Student Example

This past year President Trump has imposed 25% tariffs on raw materials like steel and aluminum coming from China. In turn, China imposed a retaliatory tariff on American Agriculture. By doing this it American farmers have been hit the hardest by these tariffs. They are now seeing decreases in overseas purchasing of items like soybeans because other countries are reluctant to pay the tariffs. China was the number one market for American soybeans, and without their buying of soybeans, American farmers will have a hard time recovering from this financial loss. Farmers are also experiencing higher prices on farming equipment, because the material it is made of had tariffs placed on it. Large businesses like John Deere had to raise their prices on farm equipment since the metal that they used had tariffs imposed, thus making the prices higher. While for now, these tariffs seem to only be deeply affecting the American agricultural business, but there is fear that if metal tariffs increase, more industries like the car industry will be impacted.

Remy Plate

Class of 2020

A trade war is a situation where countries try to damage each other's trade. The most common way they do this is by imposing tariffs or quota restrictions. With the recent trade war the United States and China are having, there are a lot of American companies that are seeing an impact on their businesses and profits. One company seeing a negative impact is Apple. China is the third-largest market for Apple and since the market is currently unstable in-between the countries, Apple is skeptical about long-term outlooks. Analysts have stated that if the China market collapses, then Apple's global market is going to fail. Apple has already seen a 10% drop in their stock and a 3% drop in the Dow Jones industrial average.

Courtney Kent

Class of 2020

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at Download for free at http://cnx.org/contents/65dfa6e7-819...dae5f033aece@4

This page titled 4.4: Political Risk is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

4.5: Legal Risk

Learning Objectives

After reading this section, students should be able to …

1. define legal risk
2. appreciate the importance of the legal environment

What is legal risk?

Legal risk is the risk arising from failure to comply with statutory or regulatory obligations (http://www.ffiec.gov).

Generally, all laws in the host country will apply to an entrepreneur's local business operations. Examples include filing procedures, employment law, environmental law, tax law, and ownership requirements. The World Bank has a rather extensive country business law library which can be accessed from their website. This can be helpful in the initial phases of considering the legal ramifications of direct investment in a given country.

Student Example

In 2015, the German car manufacturer, Volkswagen was found guilty of making cars that were not meeting the emission standards of the U.S, through the years 2009-2015. Devices that were called "defeat devices" were made by engineers to detect when vehicles were being tested and produced fake results. Ultimately, Volkswagen faced a huge lawsuit and CEO Martin Winterkorn was charged with fraud and conspiracy in the U.S.

Lucio Chavarria

Class of 2020

Many countries limit foreign ownership of assets and legally force foreign companies into a joint venture with a local partner in order to do business there. Poland, for example, limits foreign ownership of farmland and will continue to do so for another decade under agreements with the EU (Dadak, 2004).

It is important to remember that while doing business outside of the home country certain home country laws will still apply. Applicable laws differ from country to country, but one common extension is employment law.

The extent of jurisdiction beyond national boundaries varies widely. In anti-trust for instance, the United States law covers only situations where the violation affects the US, (meaning that it does not matter where the act causing the violation took place), while the EU considers only where the antitrust offense was implemented (Shaffer et al., 2005, pgs 657-664).

In order to minimize exposure to legal risks arising from confusion and excess cost, a company should seek legal advice if possible. In making such arrangements, written contracts should be used. This can minimize confusion in case of litigation.

Source

The above content was adapted from textbook content produced by Global Text Project and is licensed under a Creative Commons Attribution License 3.0 license. Under this license, any user of the textbook contents herein must provide proper attribution as follows: The OpenStax name, OpenStax logo, OpenStax book covers, OpenStax CNX name, and OpenStax CNX logo are not subject to the creative commons license and may not be reproduced without the prior and express written consent of Rice University. For questions regarding this license, please contact support@openstax.org. The original content can be downloaded for free at Download for free at http://cnx.org/contents/65dfa6e7-819...dae5f033aece@4

This page titled 4.5: Legal Risk is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

5: Economic Development in the World

5.1: Chapter 5- Economic Development in the World
5.2: World Economies
5.3: Classifying World Economies
5.4: Understanding the Developed World
5.5: The Developing World
5.6: Emerging Markets

This page titled 5: Economic Development in the World is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

5.1: Chapter 5- Economic Development in the World

Summary

This chapter outlines how businesses and economists evaluate world economies. Then, the remaining sections review what developed and developing worlds are and how they differ, as well as explain how to evaluate the expanding set of emerging-market countries, which started with the BRIC countries (i.e., Brazil, Russia, India, and China) and has now expanded to include twenty-eight countries. Effective global managers need to be able to identify the markets that offer the best opportunities for their products and services. Additionally, managers need to monitor these emerging markets for new local companies that take advantage of business conditions to become global competitors.

Countries can be categorized in terms of their stage of economic development: low income, lower middle income, upper middle income, and high income. Gross domestic product (GDP) and gross national income (GNI) are commonly used measures of economic development. The 50 poorest countries in the low-income category are sometimes referred to as least-developed countries (LDCs). Upper middle-income countries with high growth are often called newly industrializing economies (NIEs). Several of the world's economies are notable for their fast growth; the BRIC nations include Brazil, Russia, India, and China. The Group of Seven (G7), Group of Eight (G-8), and Organization for Economic Cooperation and Development (OECD) represent efforts by high-income nations to promote democratic ideals and free-market policies throughout the rest of the world. Most of the world's income is located in the Triad, which is comprised of Japan, the United States, and Western Europe. Companies with global aspirations generally have operations in all three areas. Market potential for a product can be evaluated by determining product saturation levels in light of income levels.

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- "World Economies", chapter 4 from the book Challenges and Opportunities in International Business (v. 1.0)under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.
- The course note from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM). 'The Economic and Political environment' is Copyright (c) by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license.

This page titled 5.1: Chapter 5- Economic Development in the World is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

5.2: World Economies

Learning Objectives

After reading this section, students should be able to …

1. Understand the unique strengths as well as many similarities among the two major economies – China and India

When global marketing managers explore how to expand, they start by looking at the world. Knowing the major markets and the stage of development for each allows managers to determine how best to enter and expand. The manager's goal is to hone in on a new country—hopefully, before their competitors and usually before the popular media does. China and India were expanding rapidly for several years before the financial press, such as the *Wall Street Journal*, elevated them to their current hot status.

It's common to find people interested in doing business with a country simply because they've read that it's the new "hot" economy. They may know little or nothing about the market or country—its history, evolution of thought, people, or how interactions are generally managed in a business or social context. Historically, many companies have only looked at new global markets once potential customers or partners have approached them. However, trade barriers are falling, and new opportunities are fast emerging in markets of the Middle East and Africa—further flattening the world for global firms. Companies are increasingly identifying these and other global markets for their products and services and incorporating them into their long-term growth strategies.

Opening Case

China versus India: Who Will Win??

India and China are among the world's fastest-growing economies, contributing nearly 30 percent to global economic growth. Both China and India are not emerging economies—they're actually "re-emerging," having spent centuries at the center of trade throughout history: "These two Asian giants, which until 1800 used to make up half the world economy, are not, like Japan and Germany, mere nation states. In terms of size and population, each is a continent—and for all the glittering growth rates, a poor one."[1]

Both India and China are in fierce competition with each other as well as in their quest to catch up with the major economies in the developed world. Each have particular strengths and competitive advantages that have allowed each of them to weather the recent global financial crisis better than most countries. China's growth has been mainly investment and export driven, focusing on low-cost manufacturing, with domestic consumption as low as 36 percent of gross domestic product (GDP). On the other hand, India's growth has been derived mostly from a strong services sector and buoyant domestic consumption. India is also much less dependent on trade than China, relying on external trade for about 20 percent of its GDP versus 56 percent for China. The Chinese economy has doubled every eight years for the last three decades—the fastest rate for a major economy in recorded history. By 2011, China is the world's second largest economy in the world behind the United States.[2] A recent report by PricewaterhouseCoopers forecasts that China could overtake the US economy as early as 2020.[3]

China is also the first country in the world to have met the poverty-reduction target set in the UN Millennium Development Goals and has had remarkable success in lifting more than 400 million people out of poverty. This contrasts sharply with India, where 456 million people (i.e., 42 percent of the population) still live below the poverty line, as defined by the World Bank at $1.25 a day.[4]

China has made greater strides in improving the conditions for its people, as measured by the HDI. All of this contributes to the local business conditions by both developing the skill sets of the workforce as well as expanding the number of middle-class consumers and their disposable incomes.

India has emerged as the fourth-largest market in the world when its GDP is measured on the scale of purchasing power parity. Both economies are increasing their share of world GDP, attracting high levels of foreign investment, and are recovering faster from the global crisis than developed countries. "Each country has achieved this with distinctly different approaches—India with a 'grow first, build later' approach versus a 'top-down, supply driven' strategy in China."[5]

The Chinese economy historically outpaces India's by just about every measure. China's fast-acting government implements new policies with blinding speed, making India's fractured political system appear sluggish and chaotic. Beijing's shiny new airport and wide freeways are models of modern development, contrasting sharply with the sagging infrastructure of New Delhi and Mumbai. And as the global economy emerges from the Great Recession, India once again seems to be playing second fiddle. Pundits around the world laud China's leadership for its well-devised economic policies during the crisis, which were so effective in restarting economic growth that they helped lift the entire Asian region out of the downturn.[6]

As recently as the early 1990s, India was as rich, in terms of national income per head. China then hurtled so far ahead that it seemed India could never catch up. But India's long-term prospects now look stronger. While China is about to see its working-age population shrink, India is enjoying the sort of bulge in manpower which brought sustained booms elsewhere in Asia. It is no longer inconceivable that its growth could outpace China's for a considerable time. It has the advantage of democracy—at least as a pressure valve for discontent. And India's army is, in numbers, second only to China's and America's…And because India does not threaten the West, it has powerful friends both on its own merits and as a counterweight to China.[7]

India's domestic economy provides greater cushion from external shocks than China's. Private domestic consumption accounts for 57 percent of GDP in India compared with only 35 percent in China. India's confident consumer didn't let the economy down. Passenger car sales in India in December jumped 40 percent from a year earlier.[8]

Since 1978, China's economic growth and reform have dramatically improved the lives of hundreds of millions of Chinese, increased social mobility. The Chinese leadership has reduced the role of ideology in economic policy by adopting a more pragmatic perspective on many political and socioeconomic problems. China's ongoing economic transformation has had a profound impact not only on China but on the world. The market-oriented reforms China has implemented over the past two decades have unleashed individual initiative and entrepreneurship. The result has been the largest reduction of poverty and one of the fastest increases in income levels ever seen.

China used to be the third-largest economy in the world but has overtaken Japan to become the second-largest in August 2010. It has sustained average economic growth of over 9.5 percent for the past 26 years. In 2009 its $4.814 trillion economy was about one-third the size of the United States economy.[9] China leapfrogged over Japan and became the world's number two economy in the second quarter of 2010, as receding global growth sapped momentum and stunted a shaky recovery.

India's economic liberalization in 1991 opened gates to businesses worldwide. In the mid- to late 1980s, Rajiv Gandhi's government eased restrictions on capacity expansion, removed price controls, and reduced corporate taxes. While his government viewed liberalizing the economy as a positive step, political pressures slowed the implementation of policies. The early reforms increased the rate of growth but also led to high fiscal deficits and a worsening current account. India's major trading partner then, the Soviet Union, collapsed. In addition, the first Gulf War in 1991 caused oil prices to increase, which in turn led to a major balance-of-payments crisis for India. To be able to cope with these problems, the newly elected Prime Minister Narasimha Rao along with Finance Minister Manmohan Singh initiated a widespread economic liberalization in 1991 that is widely credited with what has led to the Indian economic engine of today. Focusing on the barriers for private sector investment and growth, the reforms enabled faster approvals and began to dismantle the *License Raj*, a term dating back to India's colonial historical administrative legacy from the British and referring to a complex system of regulations governing Indian businesses.[10]

Since 1990, India has been emerging as one of the wealthiest economies in the developing world. Its economic progress has been accompanied by increases in life expectancy, literacy rates, and food security. Goldman Sachs predicts that India's GDP in current prices will overtake France and Italy by 2020; Germany, the United Kingdom, and Russia by 2025; and Japan by 2035 to become the third-largest economy of the world after the United States and China. India was cruising at 9.4 percent growth rate until the financial crisis of 2008–9, which affected countries the world over.[11] Both India and China have several strengths and weaknesses that contribute to the competitive battleground between them.

China's Strengths

1. **Strong government control.** China's leadership has a development-oriented ideology, the ability to promote capable individuals, and a system of collaborative policy review. The strong central government control has enabled the country to experience consistent and managed economic success. The government directs economic policy and its implementation and

is less susceptible than democratic India to sudden changes resulting from political pressures.

2. **WTO and FDI.** China's entry into the World Trade Organization (WTO) and its foreign direct investment (FDI) in other global markets has been an important factor in the country's successful growth. Global businesses also find the consistency and predictability of the Chinese government a plus when evaluating direct investment.
3. **Cheap, abundant labor.** China's huge population offers large pools of skilled and unskilled workers, with fewer labor regulations than in India.
4. **Infrastructure.** The government has prioritized the development of the country's infrastructure including roads and highways, ports, airports, telecommunications networks, education, public health, law and order, mass transportation, and water and sewer treatment facilities.
5. **Effectiveness of two-pronged financial system.** "The first prong is a well-run directed-credit system that channels funds from bank and postal deposits to policy-determined public uses; the second is a profit-oriented and competitive system, albeit in early and inefficient stages of development. Both prongs continue to undergo rapid government-sponsored reforms to make them more effective."[12]

India's Strengths



Figure 5.2.1: *Infosys is one of India's new wave of world-class IT companies. Image courtesy of Infosys.*

Infosys is one of India's new wave of world-class IT companies.

Image courtesy of Infosys.

1. **Quality manpower.** India has a technologically competent, English-speaking workforce. As a major exporter of technical workers, India has prioritized the development of its technology and outsourcing sectors. India is the global leader in the business process outsourcing (BPO) and call-center services industries.
2. **Open democracy.** India's democratic traditions are ingrained in its social and cultural fabric. While the political process can at times be tumultuous, it is less likely than China to experience big uncertainties or sudden revolutionary changes as those recently witnessed in the Middle East in late 2010 and early 2011.
3. **Entrepreneurship.** India entrepreneurial culture has led to global leaders, such as the Infosys cofounder, Narayana Murthy. Utilizing the global network of Indians in business and Indian business school graduates, India has an additional advantage over China in terms of entrepreneurship-oriented bodies, such as the TiE network (The Indus Entrepreneurs) or the Wadhwani Foundation, which seek to promote entrepreneurship by, among other things, facilitating investments.[13]

4. **Reverse brain drain.** Historically many emerging and developing markets experienced what is known as brain drain—where its best young people, once educated, moved to developed countries to access better jobs, incomes, and prospects for career advancement. In the past decade, economists have observed that the fast-growing economies of China and India are experiencing the reverse. Young graduates are remaining in India and China to pursue dynamic domestic opportunities. In fact, older professionals are returning from developed countries to seek their fortunes and career advancements in the promising local economies—hence the term *reverse brain drain*. The average age of the Indian returnees is thirty years old, and these adults are well educated—66 percent hold a master's degree, while 12 percent hold PhDs. The majority of these degrees are in management, technology, and science. Indians returning home are encouraged by the increasing transparency in business and government as well as the political freedoms and the prospects for economic growth.[14]
5. **Indian domestic-market growth.** According to the *Trade and Development Report 2010*, for sustainable growth, policies "should be based on establishing a balanced mix of domestic and overseas demand."[15] Each country has embraced the trend toward urbanization differently. Global businesses are impacted in the way cities are run:

China is in much better shape than India is. While India has barely paid attention to its urban transformation, China has developed a set of internally consistent practices across every element of the urbanization operating model: funding, governance, planning, sectorial policies, and shape. India has underinvested in its cities; China has invested ahead of demand and given its cities the freedom to raise substantial investment resources by monetizing land assets and retaining a 25 percent share of value-added taxes. While India spends $17 per capita in capital investments in urban infrastructure annually, China spends $116. Indian cities have devolved little real power and accountability to its cities; but China's major cities enjoy the same status as provinces and have powerful and empowered political appointees as mayors. While India's urban planning system has failed to address competing demands for space, China has a mature urban planning regime that emphasizes the systematic development of run-down areas consistent with long-range plans for land use, housing, and transportation.[16]

Despite the urbanization challenges, India is likely to benefit in the future from its younger demographics: "By 2025, nearly 28 percent of China's population will be aged 55 or older compared with only 16 percent in India."[17] The trend toward urbanization is evident in both countries. By 2025, 64 percent of China's population will be living in urban areas, and 37 percent of India's people will be living in cities.[18] This historically unique trend offers global businesses exciting markets.

So what markets are likely to benefit the most from these trends? In India, by 2025, the largest markets will be transportation and communication, food, and health care followed by housing and utilities, recreation, and education. Even India's slower-growing spending categories will represent significant opportunities for businesses because these markets will still be growing rapidly in comparison with their counterparts in other parts of the world. In China's cities today, the fastest-growing categories are likely to be transportation and communication, housing and utilities, personal products, health care, and recreation and education. In addition, in both China and India, urban infrastructure markets will be massive.[19]

While both India and China have unique strengths as well as many similarities, it's clear that both countries will continue to grow in the coming decades offering global businesses exciting new domestic markets.[20]

References

1. "Contest of the Century," *Economist*, August 19, 2010, accessed January 3, 2011, http://www.economist.com/node/16846256.
2. Gopal Ethiraj, "China Edges Out Japan to Become World's No. 2 Economy," *Asian Tribune*, August 18, 2010, accessed January 7, 2011, http://www.asiantribune.com/news/201...s-no-2-economy.
3. Suzanne Rosselet, "Strengths of China and India to Take Them into League of Developing Countries," *Economic Times*, May 7, 2010, accessed January 3, 2011, http://economictimes.indiatimes.com/...ow/5900893.cms.
4. Suzanne Rosselet, "Strengths of China and India to Take Them into League of Developing Countries," *Economic Times*, May 7, 2010, accessed January 3, 2011, http://economictimes.indiatimes.com/...ow/5900893.cms.
5. Suzanne Rosselet, "Strengths of China and India to Take Them into League of Developing Countries," *Economic Times*, May 7, 2010, accessed January 3, 2011, http://economictimes.indiatimes.com/...ow/5900893.cms.
6. Michael Schuman, "India vs. China: Whose Economy Is Better?," *Time*, January 28, 2010, accessed January 3, 2011, http://www.time.com/time/world/artic...957281,00.html.
7. "Contest of the Century," *Economist*, August 19, 2010, accessed January 3, 2011, http://www.economist.com/node/16846256.

8. Michael Schuman, “India vs. China: Whose Economy Is Better?,” *Time*, January 28, 2010, accessed January 3, 2011, http://www.time.com/time/world/artic...957281,00.html.
9. “Background Note: China,” Bureau of East Asian and Pacific Affairs, US Department of State, August 5, 2010, accessed January 3, 2011, http://www.state.gov/r/pa/ei/bgn/18902.htm.
10. “Economic History of India,” History of India, accessed January 7, 2011, http://www.indohistory.com/economic_..._of_india.html.
14. Mamta Badkar, “Race of the Century: Is India or China the Next Economic Superpower?,” Business Insider, February 5, 2011, accessed May 18, 2011, http://www.businessinsider.com/are-y...ia-2011-1?op=1.
15. Albert Keidel, “E-Notes: Assessing China’s Economic Rise: Strengths, Weaknesses and Implications,” Foreign Policy Research Institute, July 2007, accessed January 3, 2011, http://www.fpri.org/enotes/200707.ke...singchina.html.
16. “Entrepreneurship: Riding Growth in India and China,” INSEAD, accessed January 3, 2011, http://knowledge.insead.edu/contents/Turner.cfm.
17. Vivek Wadhwa, “Beware the Reverse Brain Drain to India and China,” TechCrunch, October 17, 2009, accessed January 7, 2011, http://techcrunch.com/2009/10/17/bew...ndia-and-china.
18. Pioneer Edit Desk, “Expand Domestic Market,” The Pioneer, September 20, 2010, accessed January 7, 2011, http://dailypioneer.com/284197/Expan...ic-market.html. India has a good mix of both international and domestic markets.
19. Richard Dobbs and Shirish Sankhe, “Opinion: China vs. India,” *Financial Times*, May 18, 2010, reprinted on McKinsey Global Institute website, accessed January 3, 2011, http://www.mckinsey.com/mgi/mginews/...a_vs_india.asp.
20. Richard Dobbs and Shirish Sankhe, “Opinion: China vs. India,” *Financial Times*, May 18, 2010, reprinted on McKinsey Global Institute website, accessed January 3, 2011, http://www.mckinsey.com/mgi/mginews/...a_vs_india.asp.
21. Richard Dobbs and Shirish Sankhe, “Opinion: China vs. India,” *Financial Times*, May 18, 2010, reprinted on McKinsey Global Institute website, accessed January 3, 2011, http://www.mckinsey.com/mgi/mginews/...a_vs_india.asp.
22. Richard Dobbs and Shirish Sankhe, “Opinion: China vs. India,” *Financial Times*, May 18, 2010, reprinted on McKinsey Global Institute website, accessed January 3, 2011, http://www.mckinsey.com/mgi/mginews/...a_vs_india.asp.
23. See also “India’s Surprising Economic Miracle,” *Economist*, September 30, 2010, accessed January 3, 2011, http://www.economist.com/node/17147648; “A Bumpier but Freer Road,” *Economist*, September 3, 2010, accessed January 3, 2011, http://www.economist.com/node/17145035; Chris Monasterski, “Education: India vs. China,” *Private Sector Development Blog*, World Bank, April 25, 2007, accessed January 7, 2011, http://psdblog.worldbank.org/psdblog...ion_india.html; Shreyasi Singh, “India vs. China,” *The Diplomat*, August 27, 2010, accessed January 7, 2011, http://the-diplomat.com/indian-decad...india-vs-china; “The India vs. China Debate: One Up for India?,” *Benzinga*, January 29, 2010, accessed January 7, 2011, http://www.benzinga.com/global/10482...e-up-for-india; Steve Hamm, “India’s Advantages over China,” *Bloomberg Business*, March 6, 2007, accessed January 7, 2011, http://www.businessweek.com/globalbi..._advantag.html

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

This page titled 5.2: World Economies is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

5.3: Classifying World Economies

Learning Objectives

After reading this section, students should be able to …

1. Understand how economies are classified.
2. Evaluate the statistics used in classifications: GNP, GDP, PPP as well as HDI, HPI, GDI, and GEM.

Classification of Economies

Experts debate exactly how to define the level of economic development of a country—which criteria to use and, therefore, which countries are truly developed. This debate crosses political, economic, and social arguments.

When evaluating a country, a manager is assessing the country's income and the purchasing power of its people; the legal, regulatory, and commercial infrastructure, including communication, transportation, and energy; and the overall sophistication of the business environment.

Why does a country's stage of development matter? Well, if you're selling high-end luxury items, for example, you'll want to focus on the per capita income of the local citizens. Can they afford a $1,000 designer handbag, a luxury car, or cutting-edge, high-tech gadgets? If so, how *many* people can afford these expensive items (i.e., how large is the domestic market)? For example, in January 2011, the *Financial Times* quotes Jim O'Neill, a leading business economist, who states, "South Africa currently accounts for 0.6 percent of world GDP. South Africa can be successful, but it won't be big."[1] But clearly the size of the local market is an important key factor for businesspeople.

Even in developing countries, there are always wealthy people who want and can afford luxury items. But these consumers are just as likely to head to the developed world to make their purchase and have little concern about any duties or taxes they may have to pay when bringing the items back into their home country. This is one reason why companies pay special attention to understanding their global consumers as well as where and how these consumers purchase goods. Global managers also focus on understanding if a country's target market is growing and by what rate. Countries like China and India caught the attention of global companies, because they had large populations that were eager for foreign goods and services but couldn't afford them. As more people in each country acquired wealth, their buying appetites increased. The challenge is how to identify which consumers in which countries are likely to become new customers. Managers focus on globally standard statistics as one set of criteria to understand the stage of development of any country that they're exploring for business.[2]

Let's look more closely at some of these globally standard statistics and classifications that are commonly used to define the stage of a country's development.

Statistics Used in Classifications

Gross Domestic Product

Gross domestic product (GDP) is the value of all the goods and services produced by a country in a single year. Usually quoted in US dollars, the number is an official accounting of the country's output of goods and services. For example, if a country has a large black, or underground, market for transactions, it will not be included in the official GDP. Emerging-market countries, such as India and Russia, historically have had large black-market transactions for varying reasons, which often meant their GDP was underestimated.

Table 5.3.1: GDP for the largest 20 economies. (Public Domain, *US Central Intelligence Agency, accessed June 3, 2011,* *https://www.cia.gov/library/publicat.../2001rank.html*)

Rank	Countries	GDP (Purchasing Power Parity)
1	European Union	$14,430,000,000,000
2	United States	$14,140,000,000,000
3	China	$8,748,000,000,000
4	Japan	$4,150,000,000,000
5	India	$3,570,000,000,000
6	Germany	$2,810,000,000,000
7	United Kingdom	$2,128,000,000,000
8	Russia	$2,110,000,000,000
9	France	$2,097,000,000,000
10	Brazil	$2,013,000,000,000
11	Italy	$1,739,000,000,000
12	Mexico	$1,465,000,000,000
13	South Korea	$1,364,000,000,000
14	Spain	$1,362,000,000,000
15	Canada	$1,269,000,000,000
16	Indonesia	$962,500,000,000
17	Turkey	$874,500,000,000
18	Australia	$851,100,000,000
19	Iran	$827,100,000,000
20	Taiwan	$735,400,000,000

Table 5.3.1: shows the total size of the economy, but a company will want to know the income per person, which may be a better indicator of the strength of the local economy and the market opportunity for a new consumer product. GDP is often quoted on a per person basis. Per capita GDP is simply the GDP divided by the population of the country.

The per capita GDP can be misleading because actual costs in each country differ. As a result, more managers rely on the GDP per person adjusted for purchasing power to understand how much income local residents have. This number helps professionals evaluate what consumers in the local market can afford.

Companies selling expensive goods and services may be less interested in economies with low per capita GDP. Figure 5.3.2: "Per Capita GDP on a Purchasing Power Parity Basis" shows the income (GDP) on a per person basis. For space, the chart has been condensed by removing lower profile countries, but the ranks are valid. Surprisingly, some of the hottest emerging-market countries—China, India, Turkey, Brazil, South Africa, and Mexico—rank very low on the income per person charts. So, why are these markets so exciting? One reason might be that companies selling cheaper, daily-use items, such as soap, shampoos, and low-end cosmetics, have found success entering developing, but promising, markets.

Table 5.3.2: Per Capita GDP on a Purchasing Power Parity Basis (Public Domain, *US Central Intelligence Agency, "accessed June 3, 2011, https://www.cia.gov/library/publicat.../2004rank.html*)

Rank	Countries	GDP (Purchasing Power Parity) 2007 estimate
1	Lichtenstein	$122,100
2	Qatar	$119,500
3	Luxembourg	$79,600
4	Bermuda	$69,900
5	Norway	$57,400
6	Jersey	$57,000
7	Kuwait	$52,800
8	Singapore	$52,200
9	Brunei	$51,200
10	Faroe Islands	$48,200
11	United States	$46,000
15	Hong Kong	$42,800
17	Switzerland	$41,400
18	Ireland	$41,000
19	Australia	$40,000
20	Iceland	$39,600
21	Netherlands	$39,500
22	Austria	$39,200
23	United Arab Emirates	$38,900
24	Bahrain	$38,800
27	Canada	$38,200
29	Belgium	$36,800
30	Sweden	$36,600
31	Denmark	$36,000
32	Greenland	$35,900
35	United Kingdom	$34,800
36	Finland	$34,100
37	Germany	$34,100
38	Spain	$33,600
40	Japan	$32,700
41	France	$32,600
42	European Union	$32,500

Rank	Countries	GDP (Purchasing Power Parity) 2007 estimate
43	Taiwan	$32,000
44	Greece	$31,000
46	Italy	$29,900
48	Israel	$28,400
49	South Korea	$28,100
50	Slovenia	$27,700
51	New Zealand	$27,400
53	Czech Republic	$24,900
56	Portugal	$21,700
58	Slovakia	$21,100
59	Cyprus	$21,000
61	Saudi Arabia	$20,600
62	Hungary	$18,800
63	Estonia	$18,500
65	Poland	$17,900
68	Croatia	$17,500
69	Puerto Rico	$17,100
72	Russia	$15,100
74	Malaysia	$14,900
76	Chile	$14,600
80	Argentina	$13,400
83	Mexico	$13,200
85	Venezuela	$13,000
97	Turkey	$11,400
101	World Average	$10,400
104	South Africa	$10,300
107	Brazil	$10,100
119	Thailand	$8,200
128	China	$6,600
136	Egypt	$6,000
163	India	$3,100

Purchasing Power Parity

To compare production and income across countries, we need to look at more than just GDP. Economists seek to adjust this number to reflect the different costs of living in specific countries. Purchasing power parity (PPP) is, in essence, an economic theory that adjusts the exchange rate between countries to ensure that a good is purchased for the same price in the same currency. For example, a basic cup of coffee should cost the same in London as in New York.

A nation's GDP at purchasing power parity (PPP) exchange rates is the sum value of all goods and services produced in the country valued at prices prevailing in the United States. This is the measure most economists prefer when looking at per-capita welfare and when comparing living conditions or use of resources across countries. The measure is difficult to compute, as a US dollar value has to be assigned to all goods and services in the country regardless of whether these goods and services have a direct equivalent in the United States (for example, the value of an ox-cart or non-US military equipment); as a result, PPP estimates for some countries are based on a small and sometimes different set of goods and services. In addition, many countries do not formally participate in the World Bank's PPP project to calculate these measures, so the resulting GDP estimates for these countries may lack precision. For many developing countries, PPP-based GDP measures are multiples of the official exchange rate (OER) measure. The differences between the OER- and PPP-denominated GDP values for most of the wealthy industrialized countries are generally much smaller.[3]

In some countries, like Germany, the United Kingdom, or Japan, the cost of living is quite high and the per capita GDP (nominal) is higher than the GDP adjusted for purchasing power. Conversely, in countries like Mexico, Brazil, China, and India, the per capita GDP adjusted for purchasing power is higher than the nominal per capita GDP, implying that local consumers in each country can afford more with their incomes.

Figure 5.3.3: P*er Capita GDP (Nominal) versus Per Capita GDP (PPP) of Select Countries (2010)*. (Public Domain; *US Central Intelligence Agency*, *https://www.cia.gov/library/publicat.../2004rank.html*)

Country	Per Capita	GDP (Nominal) Per Capita GDP(PPP)
United States	47,100	47,400
Germany	40,500	35,900
United Kingdom	36,200	35,100
Japan	42,500	34,200
Mexico	8,900	13,800
Brazil	10,100	10,900
China	4,300	7,400
India	1,200	3,400

Human Development Index (HDI)

GDP and purchasing power provide indications of a country's level of economic development by using an income-focused statistic. However, in recent years, economists and business analysts have focused on indicators that measure whether people's needs are satisfied and whether the needs are equally met across the local population. One such indication is the human development index (HDI), which measures people's satisfaction in three key areas—long and healthy life in terms of life expectancy; access to quality education equally; and a decent, livable standard of living in the form of income.

Since 1990, the United Nations Development Program (UNDP) has produced an annual report listing the HDI for countries. The HDI is a summary composite index that measures a country's average achievements in three basic aspects of human development: health, knowledge, and a decent standard of living. Health is measured by *life expectancy* at birth; knowledge is measured by a combination of the adult *literacy* rate and the combined primary, secondary, and tertiary gross enrollment ratio; and standard of living by (*income as measured by*) GDP per capita (PPP US$).[4]

While the HDI is not a complete indicator of a country's level of development, it does help provide a more comprehensive picture than just looking at the GDP. The HDI, for example, does not reflect political participation or gender inequalities. The HDI and the other composite indices can only offer a broad proxy on some of the key the issues of human development, gender disparity, and human poverty.[5] Table 5.3.1: "Human Development Index (HDI)—2010 Rankings" shows the rankings of the world's countries for the HDI for 2010 rankings. Measures such as the HDI and its components allow global managers to more accurately gauge the local market.

Table 5.3.4: Human Development Index (HDI)—2010 Rankings

https://biz.libretexts.org/@go/page/84421

Very High Human Development	High Human Development	Medium Human Development	Low Human Development
1. Norway	43. Bahamas	86. Fiji	128. Kenya
2. Australia	44. Lithuania	87. Turkmenistan	129. Bangladesh
3. New Zealand	45. Chile	88. Dominican Republic	130. Ghana
4. United States	46. Argentina	89. China	131. Cameroon
5. Ireland	47. Kuwait	90. El Salvador	132. Myanmar
6. Liechtenstein	48. Latvia	91. Sri Lanka	133. Yemen
7. Netherlands	49. Montenegro	92. Thailand	134. Benin
8. Canada	50. Romania	93. Gabon	135. Madagascar
9. Sweden	51. Croatia	94. Suriname	136. Mauritania
10. Germany	52. Uruguay	95. Bolivia (Plurinational State of)	137. Papua New Guinea
11. Japan	53. Libyan Arab Jamahiriya	96. Paraguay	138. Nepal
12. Korea (Republic of)	54. Panama	97. The Philippines	139. Togo
13. Switzerland	55. Saudi Arabia	98. Botswana	140. Comoros
14. France	56. Mexico	99. Moldova (Republic of)	141. Lesotho
15. Israel	57. Malaysia	100. Mongolia	142. Nigeria
16. Finland	58. Bulgaria	101. Egypt	143. Uganda
17. Iceland	59. Trinidad and Tobago	102. Uzbekistan	144. Senegal
18. Belgium	60. Serbia	103. Micronesia (Federated States of)	145. Haiti

Very High Human Development	High Human Development	Medium Human Development	Low Human Development
19. Denmark	61. Belarus	104. Guyana	146. Angola
20. Spain	62. Costa Rica	105. Namibia	147. Djibouti
21. Hong Kong, China (SAR)	63. Peru	106. Honduras	148. Tanzania (United Republic of)
22. Greece	64. Albania	107. Maldives	149. Côte d'Ivoire
23. Italy	65. Russian Federation	108. Indonesia	150. Zambia
24. Luxembourg	66. Kazakhstan	109. Kyrgyzstan	151. Gambia
25. Austria	67. Azerbaijan	110. South Africa	152. Rwanda
26. United Kingdom	68. Bosnia and Herzegovina	111. Syrian Arab Republic	153. Malawi
27. Singapore	69. Ukraine	112. Tajikistan	154. Sudan
28. Czech Republic	70. Iran (Islamic Republic of)	113. Vietnam	155. Afghanistan
29. Slovenia	71. The former Yugoslav Republic of Macedonia	114. Morocco	156. Guinea
30. Andorra	72. Mauritius	115. Nicaragua	157. Ethiopia
31. Slovakia	73. Brazil	116. Guatemala	158. Sierra Leone
32. United Arab Emirates	74. Georgia	117. Equatorial Guinea	159. Central African Republic
33. Malta	75. Venezuela (Bolivarian Republic of)	118. Cape Verde	160. Mali
34. Estonia	76. Armenia	119. India	161. Burkina Faso
35. Cyprus	77. Ecuador	120. Timor-Leste	162. Liberia
36. Hungary	78. Belize	121. Swaziland	163. Chad

Very High Human Development	High Human Development	Medium Human Development	Low Human Development
37. Brunei Darussalam	79. Colombia	122. Lao People's Democratic Republic	164. Guinea-Bissau
38. Qatar	80. Jamaica	123. Solomon Islands	165. Mozambique
39. Bahrain	81. Tunisia	124. Cambodia	166. Burundi
40. Portugal	82. Jordan	125. Pakistan	167. Niger
41. Poland	83. Turkey	126. Congo	168. Congo (Democratic Republic of the)
42. Barbados	84. Algeria 85. Tonga	127. São Tomé and Príncipe	169. Zimbabwe

Source: UNDP, "Human Development Index (HDI)—2010 Rankings," Human Development Reports, accessed January 6, 2011, http://hdr.undp.org/en/statistics.

In 1995, the UNDP introduced two new measures of human development that highlight the status of women in each society.

The first, *gender-related development index (GDI)*, measures achievement in the same basic capabilities as the HDI does, but takes note of inequality in achievement between women and men. The methodology used imposes a penalty for inequality, such that the GDI falls when the achievement levels of both women and men in a country go down or when the disparity between their achievements increases. The greater the gender disparity in basic capabilities, the lower a country's GDI compared with its HDI. The GDI is simply the HDI discounted, or adjusted downwards, for gender inequality.

The second measure, *gender empowerment measure (GEM)*, is a measure of agency. It evaluates progress in advancing women's standing in political and economic forums. It examines the extent to which women and men are able to actively participate in economic and political life and take part in decision making. While the GDI focuses on expansion of capabilities, the GEM is concerned with the use of those capabilities to take advantage of the opportunities of life.[6]

In 1997, UNDP added a further measure—the human poverty index (HPI).

If human development is about enlarging choices, poverty means that opportunities and choices most basic to human development are denied. Thus a person is not free to lead a long, healthy, and creative life and is denied access to a decent standard of living, freedom, dignity, self-respect and the respect of others. From a human development perspective, poverty means more than the lack of what is necessary for material well-being.

For policy-makers, the poverty of choices and opportunities is often more relevant than the poverty of income. The poverty of choices focuses on the causes of poverty and leads directly to strategies of empowerment and other actions to enhance opportunities for everyone. Recognizing the poverty of choices and opportunities implies that poverty must be addressed in all its dimensions, not income alone.[7]

Rather than measure poverty by income, the HPI is a composite index that uses indicators of the most basic dimensions of deprivation: a short life (longevity), a lack of basic education (knowledge), and a lack of access to public and private resources (decent standard of living). There are two different HPIs—one for developing countries (HPI-1) and another for a group of select high-income OECD (Organization for Economic and Development) countries (HPI-2), which better reflects the socioeconomic differences between the two groups. HPI-2 also includes a fourth indicator that measures social exclusion as represented by the rate of long-term unemployment.[8]

Why Does All This Matter to Global Marketing?

So, the richest countries—like Liechtenstein, Qatar, and Luxembourg—may *not* always have big local markets or, in contrast, the poorest countries may *have* the largest local market as determined by the size of the local population. Savvy business managers need to compare and contrast a number of different classifications, statistics, and indicators before they can interpret the strength, depth, and extent of a local market opportunity for their particular industry and company.

? Advice to Students

The major classifications used by analysts are evolving. The primary criteria for determining the stage of development may change within a decade as demonstrated with the addition of the gender and poverty indices. In addition, with every global crisis or event, there's a tendency to add more acronyms and statistics into the mix. Savvy global managers have to sort through these to determine what's relevant to their industry and their business objectives in one or more countries. For example, in the fall of 2010, after two years of global financial crisis, global investors started using a new acronym to describe the changing economic fortunes among countries: HIICs, or heavily indebted industrialized countries. These countries include the United States, the United Kingdom, and Japan. "'Developed markets are basically behaving like emerging markets,' says HSBC's Richard Yetsenga. 'And emerging markets are quickly becoming more developed.'"[9] Investors are pulling money from the developed countries and into the BRIC countries (i.e., Brazil, Russia, India, and China), which are "'where the population growth is, where the raw materials are, and where the economic growth is,' says Michael Penn, global equity strategist at Bank of America Merrill Lynch."[10] *The key here is to understand that classifications—just like countries and international business—are constantly evolving.*

Rather than being overwhelmed by the evolving data, it's critical to understand *why* the changes are occurring, *what* attitudes and perceptions are shifting, and *if* they are supported by real, verifiable data. In the above example of HIICs, investors from the major economies are likely motivated by quick gains on stock prices and the prevailing perception that emerging markets offer companies the best growth prospects. But as a businessperson, the timeline for your company would be in years, not months; so it's important to evaluate information based on your company's goals rather than relying on the media, investment markets, or other singularly focused industry professionals.

To truly monitor the global business arena and select prospective countries, you need to follow the news, trends, and available information for a period of time. Over time, savvy global managers develop a geographic, industrial, or product expertise—or some combination. Those who become experts on a specific country spend a great deal of time in the country, sometimes learn the language, and almost always develop an understanding of the country's political, economic, and social history as well as its culture and evolution. They gain a deeper knowledge of more than just the country's current business environment. In the business world, these folks are affectionately called "old hands"—as in he is an "old China hand" or an "old Indonesia hand." This is a reflection of how seasoned or experienced a person is with a country.

? Key Takeaways

- There are some classifications that are commonly used to define a stage of a country's development. The GDP is the value of all the goods and services produced by a country in a single year. The income per person, a better indicator of the strength of the local economy and the market opportunity for a new consumer product, is the nominal per capita GDP—the GDP divided by the population of the country. Finally, to compare production and income across countries, economists adjust this number to reflect the different costs of living in specific countries. PPP adjusts the exchange rate between countries to ensure that a good is purchased for the same price in the same currency.
- The HDI measures people's satisfaction in three key areas: (1) long and healthy life in terms of life expectancy; (2) access to quality education equally; and (3) a decent standard of living in the form of income. Health is measured by *life expectancy*at birth; knowledge is measured by a combination of the adult *literacy* rate and the combined primary, secondary, and tertiary gross enrollment ratio; and standard of living by *(income as measured by)* per capita GDP.
- Standards are constantly evolving to meet changing global scenarios; for instance, in 1997, the UNDP added the HPI to factor in the denial of basic opportunities and choices to those who live in poverty. It's critical to understand *why*the changes are occurring, *what* attitudes and perceptions are shifting, and *if* they are supported by real, verifiable data.

References

1. Jennifer Hughes, "'Bric' Creator Adds Newcomers to List," *Financial Times*, January 16, 2010, accessed January 7, 2011, http://www.ft.com/cms/s/0/f717c8e8-2...#ixzz1MKbbO8ET.
2. "Global Economies," *CultureQuest Global Business Multimedia Series*(New York: Atma Global, 2010).
3. US Central Intelligence Agency, "Country Comparison:GDP (PPP)," *World Factbook*, accessed January 3, 2011, https://www.cia.gov/library/publications/the-world-factbook/rankorder/2001rank.html.
4. UNDP, "Frequently Asked Questions (FAQs) about the Human Development Index (HDI): What Is the HDI?," *Human Development Reports*, accessed May 15, 2011, http://hdr.undp.org/en/statistics/hdi.
5. UNDP, "Is the HDI Enough to Measure a Country's Level of Development?," *Human Development Reports*, accessed May 15, 2011, http://hdr.undp.org/en/statistics/hdi.
6. UNDP, "Measuring Inequality: Gender-related Development Index (GDI) and Gender Empowerment Measure (GEM)," *Human Development Reports*, accessed January 3, 2011, http://hdr.undp.org/en/statistics/indices/gdi_gem.
7. UNDP, "The Human Poverty Index (HPI)," *Human Development Reports*, accessed January 3, 2011, http://hdr.undp.org/en/statistics/indices/hpi.
8. UNDP, "The Human Poverty Index (HPI)," *Human Development Reports*, accessed January 3, 2011, http://hdr.undp.org/en/statistics/indices/hpi.
9. Kelly Evans, "'HIIC' Nations Are Acting Like Backwaters," *Wall Street Journal*, October 1, 2010, accessed January 3, 2011, http://online.wsj.com/article/SB1000...059410506.html.
10. Kelly Evans, "'HIIC' Nations Are Acting Like Backwaters," *Wall Street Journal*, October 1, 2010, accessed January 3, 2011, http://online.wsj.com/article/SB1000...059410506.html.

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 5.3: Classifying World Economies is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

5.4: Understanding the Developed World

Learning Objectives

After reading this section, students should be able to …

1. Understand what the developed world is.
2. Identify the major developed economies.

The Developed World

Many people are quick to focus on the developing economies and emerging markets as offering the brightest growth prospects. And indeed, this is often the case. However, you shouldn't overlook the developed economies; they too can offer growth opportunities, depending on the specific product or service. The key is to understand what developed economies are and to determine their suitability for a company's strategy.

In essence, developed economies, also known as advanced economies, are characterized as postindustrial countries—typically with a high per capita income, competitive industries, transparent legal and regulatory environments, and well-developed commercial infrastructure. Developed countries also tend to have high human development index (HDI) rankings—long life expectancies, high-quality health care, equal access to education, and high incomes. In addition, these countries often have democratically elected governments.

In general, the developed world encompasses Canada, the United States, Western Europe, Japan, South Korea, Australia, and New Zealand. While these economies have moved from a manufacturing focus to a service orientation, they still have a solid manufacturing base. However, just because an economy is developed doesn't mean that it's among the largest economies. And, conversely, some of the world's largest economies—while growing rapidly—don't have competitive industries or transparent legal and regulatory environments. The infrastructure in these countries, while improving, isn't yet consistent or substantial enough to handle the full base of business and consumer demand. Countries like Brazil, Russia, India, and China—also known as BRIC—are hot emerging markets but are not yet considered developed by most widely accepted definitions.

The following sections contain a sampling of the largest developed countries that focuses on the business culture, economic environment, and economic structure of each country.[1]

The United States

Geographically, the United States is the fourth-largest country in the world—after Russia, China, and Canada. It sits in the middle of North America, bordered to the north by Canada and to the south by Mexico. With a history steeped in democratic and capitalist institutions, values and entrepreneurship, the United States has been the driver of the global economy since World War II.

The US economy accounts for nearly 25 percent of the global gross domestic product (GDP). Recently, the severe economic crisis and recession have led to double-digit unemployment and record deficits. Nevertheless, the United States remains a global economic engine, with an economy that is about twice as large as that of the next single country, China. With an annual GDP of more than $14 trillion, only the entire European Union can match the US economy in size. An economist's proverb notes that when the US economy sneezes, the rest of the world catches a cold. Despite its massive wealth, 12 percent of the population lives below the poverty line.[2]



Figure 5.4.1: New York remains the financial capital of the world. (© *2003-2011, Atma Global, Inc. All Rights Reserved.*)

Throughout the cycles of growth and contractions, the US economy has a history of bouncing back relatively quickly. In recessions, the government and the business community tend to respond swiftly with measures to reduce costs and encourage growth. Americans often speak in terms of bull and bear markets. A bull market is one in which prices rise for a prolonged period of time, while a bear market is one in which prices steadily drop in a downward cycle.

The strength of the US economy is due in large part to its diversity. Today, the United States has a service-based economy. In 2009, industry accounted for 21.9 percent of the GDP; services (including finance, insurance, and real estate) for 76.9 percent; and agriculture for 1.2 percent.[3] Manufacturing is a smaller component of the economy; however, the United States remains a major global manufacturer. The largest manufacturing sectors are highly diversified and technologically advanced—petroleum, steel, motor vehicles, aerospace, telecommunications, chemicals, electronics, food processing, consumer goods, lumber, and mining.

The sectors that have grown the most in the past decades are financial services, car manufacturing, and, most important, information technology (IT), which has more than doubled its output in the past decade. It now accounts for nearly 10 percent of the country's GDP. As impressive as that figure is, it hardly takes into account the many ways in which IT has transformed the US economy. After all, improvements in information technology and telecommunications have increased the productivity of nearly every sector of the economy.

The United States is so big that its abundant natural resources account for only 4.3 percent of its GDP. Even so, it has the largest agricultural base in the world and is among the world's leading producers of petroleum and timber products. US farms produce about half the world's corn—though most of it is grown to feed beef and dairy cattle. The US imports about 30 percent of its oil, despite its own massive reserves. That's because Americans consume roughly a quarter of the world's total energy and more than half its oil, making them dependent on other oil-producing nations in some fairly troublesome ways.

The US retail and entertainment industries are very valuable to the economy. The country's media products, including movies and music, are the country's most visible exports. When it comes to business, the United States might well be called the "king of the jungle." Emboldened by a strong free-market economy, legions of US companies have achieved unparalleled success. One by-product of this competitive spirit is an abundance of secure, well-managed business partnerships at home and abroad. And although the majority of US companies aren't multinational giants, an emphasis on hard work and a sense of fair play pervade the business culture.

In a culture where entrepreneurialism is practically a national religion, the business landscape is broad and diverse. At one end are enduring multinationals, like Coca-Cola and General Electric, which were founded by visionary entrepreneurs and are now run by boards of directors and appointed managers who answer to shareholders. At the other end of the spectrum are small businesses—millions of them—many owned and operated by a single person.

Today, more companies than ever are "going global," fueled by an increased demand for varied products and services around the world. Expanding into new markets overseas—often through joint ventures and partnerships—is becoming a requirement for success in business.

Another trend that has gained much media attention is outsourcing—subcontracting work, sometimes to foreign companies. It's now quite common for companies of all sizes to pay outside firms to do their payroll, provide telecommunications support, and perform a range of operational services. This has led to a growth in small contractors, often operating out of their homes, who offer a variety of services, including advertising, public relations, and graphic design.[4]

European Union

Today, the European Union (EU) represents the monetary union of twenty-seven European countries. One of the primary purposes of the EU was to create a single market for business and workers accompanied by a single currency, the euro. Internally, the EU has made strides toward abolishing trade barriers, has adopted a common currency, and is striving toward convergence of living standards. Internationally, the EU aims to bolster Europe's trade position and its political and economic power. Because of the great differences in per capita income among member states (i.e., from $7,000 to $79,000) and historic national animosities, the EU faces difficulties in devising and enforcing common policies. The EU's strengths also come from the formidable strengths of some of its economic powerhouse members. Germany is the leading economy in the EU.

Spotlight on Germany

Germany has the fifth-largest economy in the world, after the United States, China, Japan, and India. With a heavily export-oriented economy, the country is a leading exporter of machinery, vehicles, chemicals, and household equipment and benefits from a highly skilled labor force. It remains the largest and strongest economy in Europe and the second most-populous country after Russia in Europe.

The country has a socially responsible market economy that encourages competition and free initiative for the individual and for business. The *Grundgesetz* (Basic Law) guarantees private enterprise and private property, but stipulates that these rights must be exercised in the welfare and interest of the public.

Germany's economic development has been shaped, in large part, by its lack of natural resources, making it highly dependent on other countries. This may explain why the country has repeatedly sought to expand its power, particularly on its eastern flank.

Since the end of World War II, successive governments have sought to retain the basic elements of Germany's complex economic system (the *Soziale Marktwirtschaft*). Notably, relationships between employer and employee and between private industry and government have remained stable. Over the years, the country has had few industrial disputes. Furthermore, active participation by all groups in the economic decision making process has ensured a level of cooperation unknown in many other Western countries. Nevertheless, high unemployment and high fiscal deficits are key issues.

Overall, living standards are high, and Germany is a prosperous nation. The majority of Germans live in comfortable housing with modern amenities. The choice of available food is broad and includes cuisine from around the world. Germans enjoy luxury cars, and technology and fashion are big industries. Under federal law, workers are guaranteed minimum income, vacation time, and other benefits. Recently, the government has focused on economic reforms, particularly in the labor market, and tax reduction.

Germany is home to some of the world's most important businesses and industries. Daimler, Volkswagen, and BMW are global forces in the automotive field. Germany remains the fourth-largest auto manufacturer behind China, Japan, and the United States. German BASF, Hoechst, and Bayer are giants in the chemical industry. Siemens, a world leader in electronics, is the country's largest employer, while Bertelsmann is the largest publishing group in the world. In the banking industry, Deutsche Bank is one of the world's largest. In addition to these international giants, Germany has many small- and medium-sized, highly specialized firms. These businesses make up a disproportionately large part of Germany's exports.

Services drive the economy, representing 72.3 percent (in 2009) of the total GDP. Industry accounts for 26.8 percent of the economy, and agriculture represents 0.9 percent. Despite the strong services sector, manufacturing remains one of the most important components of the Germany economy. Key German manufacturing industries are among the world's largest and most technologically advanced producers of iron, steel, coal, cement, chemicals, machinery, vehicles, machine tools, electronics, food and beverages, shipbuilding, and textiles. Manufacturing provides not only significant sources of revenue but also the know-how that Germany exports around the world.[5]

Japan

Located off the east coast of Asia, the Japanese archipelago consists of four large islands—Honshu, Hokkaido, Kyushu, and Shikoku—and about four thousand small islands, which when combined are equal to the size of California.

The American occupation of Japan following World War II laid the foundation for today's modern economic and political society. The occupation was intended to demilitarize Japan, to fully democratize the government, and to reform Japanese society and the economy. The Americans revised the then-existing constitution along the lines of the British parliamentary model. The Japanese adopted the new constitution in 1946 as an amendment to their original 1889 constitution. On the whole, American reforms rebuilt Japanese industry and were welcomed by the Japanese. The American occupation ended in 1952, when Japan was declared an independent state.

As Japan became an industrial superpower in the 1950s and 1960s, other countries in Asia and the global superpowers began to expect Japan to participate in international aid and defense programs and in regional industrial-development programs. By the late 1960s, Japan had the third-largest economy in the world. However, Japan was no longer free from foreign influences. In one century, the country had gone from being relatively isolated to being dependent on the rest of the world for its resources with an economy reliant on trade.

In the post–World War II period, Japanese politics have not been characterized by sharp divisions between liberal and conservative elements, which in turn have provided enormous support for big business. The Liberal Democratic Party (LDP), created in 1955 as the result of a merger of two of the country's biggest political parties, has been in power for most of the postwar period. The LDP, a major proponent of big business, generally supports the conservative viewpoint. The "Iron Triangle," as it is often called, refers to the tight relationship among Japanese politicians, bureaucrats, and big business leaders.

Until recently, the overwhelming success of the economy overshadowed other policy issues. This is particularly evident with the once powerful Ministry of International Trade and Industry (MITI). For much of Japan's modern history, MITI has been responsible for establishing, coordinating, and regulating specific industry policies and targets, as well as having control over foreign trade interests. In 2001, its role was assumed by the newly created METI, the Ministry of Economy, Trade and Industry.

Japan's post–World War II success has been the result of a well-crafted economic policy that is closely administered by the government in alliance with large businesses. Prior to World War II, giant corporate holding companies called *zaibatsu* worked in cooperation with the government to promote specific industries. At one time, the four largest zaibatsu organizations were Mitsui, Mitsubishi, Sumitomo, and Yasuda. Each of the four had significant holdings in the fields of banking, manufacturing, mining, shipping, and foreign marketing. Policies encouraged lifetime employment, employer paternalism, long-term relationships with suppliers, and minimal competition. Lifetime employment continues today, although it's coming under pressure in the ongoing recession. This policy is often credited as being one of the stabilizing forces enabling Japanese companies to become global powerhouses.[6]

The zaibatsus were dismantled after World War II, but some of them reemerged as modern-day *keiretsu*, and many of their policies continue to have an effect on Japan. Keiretsu refers to the intricate web of financial and nonfinancial relationships between companies that virtually links together in a pattern of formal and informal cross-ownership and mutual obligation. The keiretsu nature of Japanese business has made it difficult for foreign companies to penetrate the commercial sector. In response to recent global economic challenges, the government and private businesses have recognized the need to restructure and deregulate parts of the economy, particularly in the financial sector. However, they have been slow to take action, further aggravating a weakened economy.

Japan has very few mineral and energy resources and relies heavily on imports to bring in almost all of its oil, iron ore, lead, wool, and cotton. It's the world's largest importer of numerous raw materials including coal, copper, zinc, and lumber. Despite a shortage of arable land, Japan has gone to great lengths to minimize its dependency on imported agricultural products and foodstuffs, such as grains and beef. Agriculture represents 1.6 percent of the economy. The country's chief crops include rice and other grains, vegetables, and fruits. Japanese political and economic protectionist policies have ensured that the Japanese remain fully self-sufficient in rice production, which is their main staple.

As with other developed nations, services lead the economy, representing 76.5 percent of the national GDP.[7] Industry accounts for 21.9 percent of the country's output. Japan benefits from its highly skilled workforce. However, the high cost of labor combined

with the cost of importing raw materials has significantly affected the global competitiveness of its industries. Japan excels in high-tech industries, particularly electronics and computers. Other key industries include automobiles, machinery, and chemicals. The service industry is beginning to expand and provide high-quality computer-related services, advertising, financial services, and other advanced business services.[8]

Key Takeaways

- The developed economies, also known as advanced economies, are characterized as postindustrial countries—typically with a high per capita income, competitive industries, transparent legal and regulatory environments, and well-developed commercial infrastructure. Developed countries also tend to have high human development index (HDI) rankings (i.e., long life expectancies, high-quality health care, equal access to education, and high incomes). In addition, these countries often have democratically elected governments.
- The major developed economies include Canada, the United States, Western Europe, Japan, South Korea, Australia, and New Zealand.
- The United States is the fourth-largest country in the world—after Russia, China, and Canada. However, the United States is the world's largest single-country economy and accounts for nearly 25 percent of the global gross domestic product (GDP). The strength of the US economy is due in large part to its diversity. Today, the United States has a service-based economy. In 2009, industry accounted for 21.9 percent of the GDP; services (including finance, insurance, and real estate) for 76.9 percent; and agriculture for 1.2 percent.
- Germany, a member of the EU (European Union), has the fifth-largest economy in the world. The country is a leading exporter of machinery, vehicles, chemicals, and household equipment and benefits from a highly skilled labor force. It is the largest and strongest economy in Europe. Services drive the economy, representing 72.3 percent (in 2009) of the total GDP. Industry accounts for 26.8 percent of the economy, and agriculture represents 0.9 percent.
- Japan's post–World War II success has been the result of a well-crafted economic policy closely administered by the government in alliance with large businesses. It also benefits from its highly skilled workforce. Japan has very few mineral and energy resources and relies heavily on imports to bring in almost all of its oil, iron ore, lead, wool, and cotton. It is the world's largest importer of numerous raw materials including coal, copper, zinc, and lumber. As with other developed nations, services lead the economy, representing 76.5 percent of the national GDP, while industry accounts for 21.9 percent of the country's output.

References

1. The sections that follow are excerpted in part from two resources owned by author Sanjyot P. Dunung's firm, Atma Global: *CultureQuest Business Multimedia Series*and *bWise: Business Wisdom Worldwide*. The excerpts are reprinted with permission and attributed to the country-specific product when appropriate.
2. US Central Intelligence Agency, "North America: United States: Economy," World Factbook, accessed January 7, 2011, https://www.cia.gov/library/publicat...k/geos/us.html.
3. US Central Intelligence Agency, "North America: United States: Economy," World Factbook, accessed January 7, 2011, https://www.cia.gov/library/publicat...k/geos/us.html.
4. CultureQuest Business Multimedia Series: USA (New York: Atma Global, 2010); bWise: Business Wisdom Worldwide: USA(New York: Atma Global, 2011).
5. CultureQuest Business Multimedia Series: Germany (New York: Atma Global, 2010); bWise: Business Wisdom Worldwide: Germany (New York: Atma Global, 2011).
6. Sanjyot P. Dunung, Doing Business in Asia: The Complete Guide, 2nd ed. (New York: Jossey-Bass, 1998).
7. US Central Intelligence Agency, "East & Southeast Asia: Japan: Economy," World Factbook, accessed January 4, 2011, https://www.cia.gov/library/publicat...k/geos/ja.html.
8. CultureQuest Business Multimedia Series: Japan (New York: Atma Global, 2010); bWise: Business Wisdom Worldwide: Japan (New York: Atma Global, 2011)

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 5.4: Understanding the Developed World is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

5.5: The Developing World

Learning Objectives

After reading this section, students should be able to …

1. Understand what the developing world is.
2. Identify the major developing economies and regions.

The Developing World

The developing world refers to countries that rank lower on the various classifications. The residents of these economies tend to have lower discretionary income to spend on nonessential goods (i.e., goods beyond food, housing, clothing, and other necessities). Many people, particularly those in developing countries, often find the classifications limiting or judgmental. The intent here is to focus on understanding the information that a global business professional will need to determine whether a country, including a developing country, offers an interesting local market. Some countries may perceive the classification as a slight; others view it as a benefit. For example, in global trade, being a developing country sometimes provides preferences and extra time to meet any requirements dismantling trade barriers.

[In the World Trade Organization (WTO),] there are no WTO definitions of "developed" and "developing" countries. Members announce for themselves whether they are "developed" or "developing" countries. However, other members can challenge the decision of a member to make use of provisions available to developing countries.

Developing country status in the WTO brings certain rights. There are for example provisions in some WTO Agreements which provide developing countries with longer transition periods before they are required to fully implement the agreement and developing countries can receive technical assistance.

That a WTO member announces itself as a developing country does not automatically mean that it will benefit from the unilateral preference schemes of some of the developed country members such as the Generalized System of Preferences (GSP). In practice, it is the preference giving country which decides the list of developing countries that will benefit from the preferences.[1]

Developing countries sometimes find that their economies improve and gradually they become emerging markets. Many developing economies represent old cultures and rich histories. Focusing only on today's political, economic, and social conditions distorts the picture of what these countries have been and what they might become again. This category hosts the greatest number of countries around the world.

Did You Know?

It's important to understand that the term *developing countries* is different from Third-World countries, which was a traditional classification for countries along political and economic lines. It helps to understand how this terminology has evolved.

When people talk about the poorest countries of the world, they often refer to them with the general term Third World, and they think everybody knows what they are talking about. But when you ask them if there is a Third World, what about a Second or a First World, you almost always get an evasive answer…

The use of the terms First, the Second, and the Third World is a rough, and it's safe to say, outdated model of the geopolitical world from the time of the cold war.

There is no official definition of the first, second, and the third world. Below is OWNO's [One World—Nations Online] explanation of the terms…

After World War II the world split into two large geopolitical blocs and spheres of influence with contrary views on government and the politically correct society:

1. The bloc of democratic-industrial countries within the American influence sphere, the "First World."
2. The Eastern bloc of the communist-socialist states, the "Second World."

3. The remaining three-quarters of the world's population, states not aligned with either bloc were regarded as the "Third World."
4. The term "Fourth World," coined in the early 1970s by Shuswap Chief George Manuel, refers to widely unknown nations (cultural entities) of indigenous peoples, "First Nations" living within or across national state boundaries…

The term "First World" refers to so-called developed, *capitalist*, industrial countries, roughly, a bloc of countries aligned with the United States after World War II, with more or less common political and economic interests: North America, Western Europe, Japan and Australia.[2]

Developing economies typically have poor, inadequate, or unequal access to infrastructure. The low personal incomes result in a high degree of poverty, as measured by the human poverty index (HPI). These countries, unlike the developed economies, don't have mature and competitive industries. Rather, the economies usually rely heavily on one or more key industries—often related to commodities, like oil, minerals mining, or agriculture. Many of the developing countries today are in Africa, parts of Asia, the Middle East, parts of Latin America, and parts of Eastern Europe.

Developing countries can seem like an oxymoron in terms of technology. In daily life, high-tech capabilities in manufacturing coexist alongside antiquated methodologies. Technology has caused an evolution of change in just a decade or two. For example, twenty years ago, a passerby looking at the metal shanties on the sides of the streets of Mumbai, India, or Jakarta, Indonesia, would see abject poverty in terms of the living conditions; today, that same passerby peering inside the small huts would see the flicker of a computer screen and almost all the urban dwellers—in and around the shanties—sporting cell phones. Installing traditional telephone infrastructure was more costly and time-consuming for governments, and consumers opted for the faster and relatively cheaper option of cell phones.

? Did You Know?

Gillette's Innovative Razor Sales

Companies find innovative ways to sell to developing world markets. Procter & Gamble (P&G)'s latest innovation is a Gillette-brand eleven-cent blade. "Gillette commands about 70 percent of the world's razor and blade sales, but it lags behind rivals in India and other developing markets, mainly because those consumers can't afford to buy its flagship products."[3] The company has designed a basic blade, called the Gillette Guard, that isn't available in the United States or other richer economies. The blade is designed for the developing world, with the goal of bringing "'more consumers into Gillette,' says Alberto Carvalho, P&G's vice president of male grooming in emerging markets…Winning over low-income consumers in developing markets is crucial to the growth strategy….The need to grow in emerging markets is pushing P&G to change its product development strategy. In the past, P&G would sell basically the same premium Pampers diapers, Crest toothpaste, or Olay moisturizers in developing countries, where only the wealthiest consumers could afford them."[4] The company's approach now is to determine what the consumers can afford in each country and adjust the product features to meet the target price.

Global companies also recognize that in many developing countries, the local government is the buyer—particularly for higher value-added products and services, such as high-tech items, equipment, and infrastructure development. In addition, companies assess the political and economic environment in order to evaluate the risks and opportunities for business in managing key government relationships. In much of Africa and the Middle East, where the economies rely on one or two key industries, the governments remain heavily involved in sourcing and awarding key contracts. The lack of competitive domestic industry and local transparency has also made these economies ripe for graft.[5]

✔ Ethics in Action

Studies have shown that developing countries that are known to be rich in hydrocarbons [mainly oil] are plagued with corruption and environmental pollution. Paradoxically, most extractive resource-rich developing countries are found in the bottom third of the World Bank's composite governance indicator rankings. Again, on the Transparency International Corruption Perception Index (CPI), 2007—most of the countries found at the bottom of the table are rich in mineral resources. This is indicative of high prevalence of corruption in these countries.[6]

Major Developing Economies and Regions

The Middle East

The Middle East presents an interesting challenge and opportunity for global businesses. Thanks in large part to the oil-dependent economies, some of these countries are quite wealthy. Interestingly enough Qatar, Kuwait, United Arab Emirates (UAE), and Bahrain all rank in the top twenty-five. Only Saudi Arabia ranks much lower, due mainly to its larger population; however, it still has a per capita GDP (PPP) twice as high as the global average.

While the income level suggests a strong opportunity for global businesses, the inequality of access to goods and services, along with an inadequate and uncompetitive local economy, present both concerns and opportunities. Many of these countries are making efforts to shift from being an oil-dependent economy to a more service-based economy. Dubai, one of the seven emirates in the UAE, has sought to be the premier financial center for the Middle East. The financial crisis of 2008 has temporarily hampered, but not destroyed, these ambitions.

Spotlight on the UAE

Tucked into the southeastern edge of the Arabian Peninsula, the UAE borders Oman, Qatar, and Saudi Arabia. The UAE is a federation of seven states, called emirates because they are ruled by a local emir. The seven emirates are Abu Dhabi (capital), Dubai, Al-Shāriqah (or Sharjah), Ajmān, Umm al-Qaywayn, Ras'al-Khaymah, and Al-Fujayrah (or Fujairah). Dubai and Abu Dhabi have received the most global attention as commercial, financial, and cultural centers.

✔ Amusing Anecdote

Dubai, the Las Vegas of the Middle East

Dubai is sometimes called the Vegas of the Middle East in reference to its glitzy malls, buildings, and consumerism culture. Luxury brands and excessive wealth dominate the culture as oil wealth is displayed brashly. Among other things, Dubai is home to Mall of the Emirates and its indoor alpine ski resort.[7] Dubai also features aggressive architectural projects, including the spire-topped Burj Khalifa, which is the tallest skyscraper in the world, and the Palm Islands, which are man-made, palm-shaped, phased land-reclamation developments. Visionary proposals include the world's first underwater hotel, the Hydropolis. Dubai's tourism attracts visitors from its more religiously conservative neighbors such as Saudi Arabia as well as from countries in South Asia, primarily for its extensive shopping options. Dubai as well as other parts of the UAE hope to become major global-tourist destinations and have been building hotels, airports, attractions, shops, and infrastructure in order to facilitate this economic diversification goal.

The seven emirates merged in the early 1970s after more than a century of British control of their defense and military affairs. Thanks to its abundant oil reserves, the UAE has grown from an impoverished group of desert states to a wealthy regional commercial and financial center in just thirty years. Its oil reserves are ranked as the world's seventh-largest and the UAE possesses one of the most-developed economies in West Asia.[8] It is the twenty-second-largest economy at market exchange rates and has a high per capita gross domestic product, with a nominal per capita GDP of US$49,995 as per the International Monetary Fund (IMF).[9] It is the second-largest in purchasing power per capita and has a relatively high human development index (HDI) for the Asian continent, ranking thirty-second globally.[10] The UAE is classified as a high-income developing economy by the IMF.[11]

For more than three decades, oil and global finance drove the UAE's economy; however, in 2008–9, the confluence of falling oil prices, collapsing real estate prices, and the international banking crisis hit the UAE especially hard.[12]

Today, the country's main industries are petroleum and petrochemicals (which account for a sizeable 25 percent of total GDP), fishing, aluminum, cement, fertilizers, commercial ship repair, construction materials, some boat building, handicrafts, and textiles. With the UAE's intense investment in infrastructure and greening projects, the coastlines have been enhanced with large parks and gardens. Furthermore, the UAE has transformed offshore islands into agricultural projects that produce food.

A key issue for the UAE is the composition of its residents and workforce. The UAE is perhaps one of the few countries in the world where expatriates outnumber the local citizens, or nationals. In fact, of the total population of almost 5 million people, only 20 percent are citizens, and the workforce is composed of individuals from 202 different countries. As a result, the UAE is an incredible melting pot of cultural, linguistic, and religious groups. Migrant workers come mainly from the Indian subcontinent:

India, Pakistan, Bangladesh, and Sri Lanka as well as from Indonesia, Malaysia, the Philippines, and other Arab nations. A much smaller number of skilled managers come from Europe, Australia, and North America. While technically the diverse population results in a higher level of religious diversity than neighboring Arab countries, the UAE is an Islamic country.

The UAE actively encourages foreign companies to open branches in the country, so it is quite common and easy for foreign corporations to do so. Free-trade zones allow for 100 percent foreign ownership and no taxes. Nevertheless, it's common and in some industries required for many companies outside the free-trade zone to have an Emirati sponsor or partner.

While the UAE is generally open for global business, recently Research in Motion (RIM) found itself at odds with the UAE government, which wanted to block Blackberry access in the country. RIM uses a proprietary encryption technology to protect data and sends it to offshore servers in North America. For some countries, such as the UAE, this data encryption is perceived as a national security threat. Some governments want to be able to access the communications of people they consider high security threats. The UAE government and RIM were able to resolve this issue, and Blackberry service was not suspended.

Human rights concerns have forced the UAE government to address the rights of children, women, minorities, and guest workers with legal consistency, a process that is continuing to evolve. Today, the UAE is focused on reducing its dependence on oil and its reliance on foreign workers by diversifying its economy and creating more opportunities for nationals through improved education and increased private sector employment.[13]

Africa

For the past fifty years, Africa has been ignored in large part by most global businesses. Initial efforts that focused on access to minerals, commodities, and markets have given way to extensive local corruption, wars, and high political and economic risk.

When the emerging markets came into focus in the late 1980s, global business turned its attention to Asia. However, that's changing as companies look for the next growth opportunity. "A growing number of companies from the U.S., China, Japan, and Britain are eager to tap the potential growth of a continent with 1 billion people—especially given the weak outlook in many developed nations….Meanwhile, African governments are luring investments from Chinese companies seeking to tap the world's biggest deposits of platinum, chrome, and diamonds."[14]

Within the continent, local companies are starting to and expanding to compete with global companies. These homegrown firms have a sense of African solidarity.

Big obstacles for businesses remain. Weak infrastructure means higher energy costs and trouble moving goods between countries. Cumbersome trade tariffs deter investment in new African markets. And the majority of the people in African countries live well below the poverty line, limiting their spending power.

Yet many African companies are finding ways around these barriers. Nigerian fertilizer company, Notore Chemicals Ltd., for example, has gone straight to governments to pitch the benefits of improved regional trade, and recently established a distribution chain that the company hopes will stretch across the 20 nations of Francophone Africa.[15]

While the focus remains on South Africa, it's only a matter of time until businesses shift their attention to other African nations. Political unrest, poverty, and corruption remain persistent challenges for the entire continent. A key factor in the continent's success will be its ability to achieve political stability and calm the social unrest that has fueled regional civil conflicts.

✔ Google in Africa

Africa has some of the lowest Internet access in the world, and yet Google has been attracted to the continent by its growth potential. Africa with its one billion people is an exciting growth market for many companies.

"The Internet is not an integral part of everyday life for people in Africa," said Joe Mucheru of Google's Kenya office…

[Yet] Google executives say Africa represents one of the fastest growth rates for Internet use in the world. Nigeria already has about 24 million users and South Africa and Kenya aren't far behind, according to World Bank and research sites like Internet World Stats…

Other technology companies have also set their sights on the continent. Microsoft Corp., International Business Machines Corp. [IBM], Cisco Systems Inc., and Hewlett-Packard Co. have sales offices throughout Africa, selling laptops, printers and software to fast-growing companies and an emerging middle class.[16]

Infrastructure, oil, gas and technology firms are not the only businesses looking to Africa; the world of advertising has now set its sights on the continent, following their largest global corporate clients.

Advertising growth in Africa is soaring, driven by telecom companies, financial services firms and makers of consumer products…

"All of our major clients, as they are looking for geographical expansion opportunities, have Africa and the Middle East high up on their priority list, if not at the top," said Martin Sorrell, chief executive of WPP, the world's largest advertising company by revenue…

Nigeria, Angola, Kenya and Ghana have some of the highest growth potential, ad executives say….

And with so many languages and big cultural differences, crafting ads can be labor-intensive, marketing executives say. Ads in Nigeria, for example, need to be in five different languages to reach a large audience.

Africa and the Middle East together represent only about 2.9 percent, or around $14 billion, of the total $482.6 billion global ad market, according to market research firm, eMarketer.[17]

This small percentage indicates the potential for significant advertising growth and a huge opportunity for global advertising and marketing firms.

Spotlight on Nigeria

Located in West Africa, Nigeria shares borders with the Republic of Benin, Chad, Cameroon, and Niger. Its southern coast lies on the Atlantic Ocean. Nigeria is Africa's most populous country and its second largest economy. Goldman Sachs included Nigeria in its listing of the "Next Eleven" emerging economies after the BRIC countries (Brazil, Russia, India and China).[18]

Since its independence from the United Kingdom in 1960, Nigeria has seen civil war, ethnic tensions and violence, and military rule. Although recent elections have been marred by violence and accusations of voter fraud, Nigeria is technically experiencing its longest period of civilian government since its independence. However, Nigeria remains a fractious nation, divided along ethnic and religious lines.

As noted in the Ethics in Action sidebar in this section, developing country economies that are primarily dependent on oil have widespread government corruption. The Nigerian government continues to face the challenge of reforming a petroleum-based economy, whose revenues have been squandered through corruption and mismanagement, and institutionalizing the early efforts at democracy. "Oil-rich Nigeria, long hobbled by political instability, corruption, inadequate infrastructure, and poor macroeconomic management, has undertaken several reforms over the past decade. Nigeria's former military rulers failed to diversify the economy away from its overdependence on the capital-intensive oil sector, which provides 95 percent of foreign exchange earnings and about 80 percent of budgetary revenues."[19] The economy of Nigeria is one of the largest in the world, with GDP (PPP) at $341 billion. However on a per capita basis, the country ranks at a dismal 183rd in the world, with a per capita GDP (PPP) at just $2,300. Seventy percent of its population remains below the poverty line, and the country ranks at 142nd on the human development index (HDI) rankings for 2010. Despite the low quality of life rankings for the country, Nigeria's population of more than 152 million make it an interesting long-term prospect for global businesses, particularly as economic conditions enable more Nigerians to achieve middle-income status.[20]

Nigeria's economy is about evenly split between agriculture (which accounts for 32.5 percent), industry at 33.8 percent, and services at 33.7 percent. The country's main industries are crude oil, coal, tin, columbite, rubber products, wood, hides and skins, textiles, cement and other construction materials, food products, footwear, chemicals, fertilizer, printing, ceramics, and steel.[21]

Nigeria received IMF funding in 2000 but pulled out of the program in 2002, when it failed to meet the economic reform requirements, specifically failing to meet spending and exchange rate targets. In recent years, the Nigerian government has begun showing the political will to implement the market-oriented reforms urged by the IMF, such as to modernize the banking system, to curb inflation by blocking excessive wage demands, and to resolve regional disputes over the distribution of earnings from the oil industry. The country's main issues remain government corruption, poverty, inadequate infrastructure, and ethnic violence, mainly over the oil producing Niger Delta region. Nevertheless, with continued economic and political reforms, the expanding economy and large potential domestic market will continue to attract global business attention to Nigeria.[22]

How Do Developing Countries Become Emerging Markets?

However, it's important to remember that all of the emerging-market countries were once considered developing nations. What resulted in the transition? Are today's developing countries turning into tomorrow's emerging markets? These are the questions that not only global economists and development experts ask, but—more relevantly—global businesses as well.

Typically, the factors that result in the classification of many countries as developing economies are the same ones that—once addressed and corrected—enable these countries to become emerging markets. Countries that seek to implement transparency in the government as well as in the political and economic institutions help inspire business confidence in their countries. Developing the local commercial infrastructure and reducing trade barriers attract foreign businesses. Educating the population equally and creating a healthy domestic workforce that is both skilled and relatively cheap is another incentive for global business investment.

Unlike emerging markets, developing and underdeveloped countries still need special attention from international aid agencies to prevent starvation, mass disease and political instability. Developing countries need to improve their education systems and create a strategy to begin their transition to the global emerging market. Companies from developed and emerging markets should play an important role in this process. Companies from emerging markets are especially crucial, as they have a great deal of experience operating in conditions of non-developed economies.[23]

While developing countries comprise the largest category, it's important to remember that there are wide differences between the nations in this classification. If a company wants to stay ahead of the competition, it must be able to identify those countries ripe for development. Early entrance into these markets helps create first-mover advantage in terms of brand recognition, forging essential relationships with the government and the private sector, and harnessing any early-stage cost advantages. First-mover advantage refers the benefits that a company gains by entering into a market first or introducing a new product or service before its competitors.

? Did You Know?

Mongolia Is Becoming Hot!

For most people, the country of Mongolia conjures images of a remote place near China—a movie location. It hasn't been at the forefront of anyone's attention for almost two decades, and yet the "IMF says that Mongolia will be one of the fastest-growing economies over the next decade."[24] This is a remarkable turnaround for a country that lost its Soviet assistance—one-third of its economy—in 1990 with the fall of the Soviet Union. Traditionally an agriculture-based economy, Mongolia is landlocked by its borders with China and Russia and is the approximately the size of Western Europe, with a relatively small population. However, its tremendous untapped mineral resources, which include coal, copper, molybdenum, fluorspar, tin, tungsten, gold, and oil, are attracting foreign investment. The country is a major exporter to China—its large, relatively rich neighbor. The country is exploring new resources as well; according to Prime Minister Sukhbaatar Batbold, "Wind power could be a major opportunity for Mongolia and for export to China."[25]

? Key Takeaways

- The developing world refers to countries that rank lower on the various classifications. The residents of these economies tend to have lower discretionary income to spend on nonessential goods.
- The poorest countries of the world are often referred to as the Third World. However, the Third World is not synonymous with the developing world, instead it is part of an outdated model of the geopolitical world from the time of the Cold War. It encompasses three-quarters of the world's population and consists of the states that were not aligned with either the democratic-industrial bloc or the eastern, communist-socialist bloc.
- A developing country, in order to evolve into an emerging market, must (1) seek to implement transparency in its government as well as in its political and economic institutions to help inspire business confidence in its country, (2) develop the local commercial infrastructure and reduce trade barriers to attract foreign businesses, and (3) educate the population equally and create a healthy domestic workforce that's both skilled and relatively cheap.

References

1. “Who Are the Developing Countries in the WTO?,” World Trade Organization, accessed January 5, 2011, http://www.wto.org/english/tratop_e/devel_e/d1who_e.htm.
2. “Worlds within the World?,” One World—Nations Online, accessed January 5, 2011, http://www.nationsonline.org/oneworl..._countries.htm.
3. Ellen Byron, “Gillette’s Latest Innovation in Razors: The 11-Cent Blade,” Wall Street Journal, October 1, 2010, accessed January 5, 2011, http://online.wsj.com/article/SB1000...890970954.html.
4. Ellen Byron, “Gillette’s Latest Innovation in Razors: The 11-Cent Blade,” Wall Street Journal, October 1, 2010, accessed January 5, 2011, http://online.wsj.com/article/SB1000...890970954.html.
5. The sections that follow are excerpted in part from two resources owned by author Sanjyot P. Dunung’s firm, Atma Global: CultureQuest Business Multimedia Series and bWise: Business Wisdom Worldwide. The excerpts are reprinted with permission and attributed to the country-specific product when appropriate.
6. Gilbert Sam, “Ghana’s Oil Find: Benefits and Nightmares,” Daily Guide, April 30, 2009, reprinted on Modern Ghana website, accessed January 5, 2011, http://www.modernghana.com/news/2138...ightmares.html.
7. “About Mall of the Emirates,” Mall of the Emirates, accessed January 5, 2011, http://www.malloftheemirates.com/MOE...4/Default.aspx.
8. US Central Intelligence Agency, “Country Comparison: Oil—Proved Reserves,” World Factbook, accessed January 5, 2011, https://www.cia.gov/library/publicat.../2178rank.html.
9. “IMF Data Mapper,” International Monetary Fund, accessed January 5, 2011, http://www.imf.org/external/datamapper/index.php.
10. UNDP, “Human Development Index (HDI)—2010 Rankings,” Human Development Report 2010: The Real Wealth of Nations and Pathways to Human Development, November 4, 2010, accessed January 5, 2011, http://hdr.undp.org/en/statistics.
11. Wikipedia, s.v. “United Arab Emirates,” last modified February 15, 2011, accessed February 16, 2011, http://en.Wikipedia.org/wiki/United_Arab_Emirates.
12. US Central Intelligence Agency, “Middle East: United Arab Emirates,” World Factbook, accessed January 5, 2011, https://www.cia.gov/library/publications/the-world-factbook/geos/ae.html.
13. bWise: Business Wisdom Worldwide: U.A.E. (New York: Atma Global, 2011).
14. Renee Bonorchis, “Africa Is Looking Like a Dealmaker’s Paradise,” BusinessWeek, September 30, 2010, accessed January 5, 2011, http://www.businessweek.com/magazine/content/10_41/b4198020648051.htm.
15. Will Connors and Sarah Childress, “Africa’s Local Champions Begin to Spread Out,” Wall Street Journal, May 26, 2010, accessed January 5, 2011, http://online.wsj.com/article/SB10001424052748704912004575252593400609032.html.
16. Will Connors, “In Africa, Google Sows the Seeds for Future Growth,” Wall Street Journal, May 15, 2010, accessed January 5, 2011, http://online.wsj.com/article/SB1000...572630700.html.
17. Ruth Bender and Suzanne Vranica, “Global Ad Agencies Flocking to Africa,” Wall Street Journal, October 22, 2010, accessed January 5, 2011, http://online.wsj.com/article/SB1000...783950352.html.
18. Jim O’Neill and Anna Stupnytska, “Global Economics Paper No. 192: The Long-Term Outlook for the BRICs and N-11 Post Crisis,” accessed February 16, 2011, http://www2.goldmansachs.com/ideas/b...utlook-doc.pdf.
19. US Central Intelligence Agency, “Africa: Nigeria,” World Factbook, accessed January 5, 2011, https://www.cia.gov/library/publications/the-world-factbook/geos/ni.html.
20. US Central Intelligence Agency, “Africa: Nigeria,” World Factbook, accessed January 5, 2011, https://www.cia.gov/library/publicat...k/geos/ni.html; UNDP, “Nigeria,” International Human Development Indicators 2010, accessed January 5, 2011, http://hdrstats.undp.org/en/countrie...files/NGA.html.
21. US Central Intelligence Agency, “Africa: Nigeria,” World Factbook, accessed January 5, 2011, https://www.cia.gov/library/publicat...k/geos/ni.html.
22. US Central Intelligence Agency, “Africa: Nigeria,” World Factbook, accessed January 5, 2011, https://www.cia.gov/library/publications/the-world-factbook/geos/ni.html.
23. Vladimir Kvint, “Define Emerging Markets Now,” Forbes, January 28, 2008, accessed January 5, 3011, http://www.forbes.com/2008/01/28/kvi...0129kvint.html.

24. Charlie Rose, “Charlie Rose Talks to Mongolia’s Prime Minister,” BusinessWeek, September 30, 2010, accessed January 5, 2011, http://www.businessweek.com/magazine...8014855514.htm.
25. Charlie Rose, “Charlie Rose Talks to Mongolia’s Prime Minister,” BusinessWeek, September 30, 2010, accessed January 5, 2011, http://www.businessweek.com/magazine...8014855514.htm.

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

This page titled 5.5: The Developing World is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

5.6: Emerging Markets

Learning Objectives

After reading this section, students should be able to …

1. Understand what the emerging markets and BRIC countries are.
2. Identify key emerging markets.

What Exactly Is an Emerging Market?

On September 18, 2008, the *Economist* argued that the term *emerging market* is dated.

Is it time to retire the phrase "emerging markets"? Many of the people interviewed for this special report think so. Surely South Korea, with sophisticated companies such as Samsung, has fully emerged by now. And China already has the world's fourth-largest economy. [*Note:* As of summer 2010, China has the world's second-largest economy.]

The term "emerging markets" dates back to 1981, recalls the man who invented it, Antoine van Agtmael. He was trying to start a "Third-World Equity Fund" to invest in developing-country shares, but his efforts to attract money were constantly rebuffed. "Racking my brain, at last I came up with a term that sounded more positive and invigorating: emerging markets. 'Third world' suggested stagnation; 'emerging markets' suggested progress, uplift and dynamism."[1]

The 2008 article clearly articulates the challenge for global businesses, as well as analysts, who are trying to both define and understand the group of countries typically termed the emerging market. In a 2008 *Forbes* article, Vladimir Kvint, president of the International Academy of Emerging Markets, noted the following:

During the last 20 years, the global business world has gone through drastic, but mostly positive changes. In the 1980s, international business was essentially an exclusive club of the 20 richest countries. This changed as dictatorships and command economies collapsed throughout the world. Countries that once prohibited foreign investment from operating on their soil and were isolated from international cooperation are now part of the global marketplace.

I remember well when, in 1987, the first $80 million of foreign origin was allowed to be invested in the former Soviet Union. So-called "patriots" accused Mikhail Gorbachev of selling their motherland. Twenty years later, in 2007, Russia received about $43 billion of foreign direct investment, and emerging-market countries received about 40 percent of the $1.5 trillion FDI [foreign direct investment] worldwide.[2]

The definition of an emerging market is complex and inconsistent. There is a plethora of statistics and data available. The application and interpretation of this information varies depending on who is doing the analysis—a private sector business, the World Bank, the International Monetary Fund (IMF), the World Trade Organization (WTO), the United Nations (UN), or any number of global economic, political, and trade organizations. The varying statistics, in turn, produce a changing number of countries that "qualify" as emerging markets. For many businesspeople, the definition of an emerging market has been simply a country that was once a developing country but has achieved rapid economic growth, modernization, and industrialization. However, this approach can be limiting.

Knowing that there are wide inconsistencies, how do we define emerging markets consistently from the perspective of global businesses? First, understand that there are some common characteristics in terms of local population size, growth opportunities with changes in the local commercial infrastructure, regulatory and trade policies, efficiency improvements, and an overall investment in the education and well-being of the local population, which in turn is expected to increase local incomes and purchasing capabilities.

As a leading economic and strategic thinker in the area of emerging markets, Kvint concludes from his research that there are several major characteristics of emerging markets, which create "a comfortable and attractive environment for global business, foreign investment and international trade. Based on my study, an emerging market country can be defined as a society transitioning from a dictatorship to a free market-oriented economy, with increasing economic freedom, gradual integration within the global marketplace, an expanding middle class, improving standards of living and social stability and tolerance, as well as an increase in cooperation with multilateral institutions."[3]

In April 2010, the chief of HSBC, the largest bank in Europe, forecasted a change for the next ten years in which six new countries (the CIVETS: Colombia, Indonesia, Vietnam, Egypt, Turkey and South Africa) will replace the BRIC countries (Brazil, Russia, India and China) of the last decade:

"Each has a very bright future," HSBC CEO Michael Geoghegan said of the CIVETS, named after the cat-like animals found in some of the countries. "Each has large, young, growing population. Each has a diverse and dynamic economy. And each, in relative terms is politically stable."…

"Within three years, for the first time, the economic firepower of emerging markets will overtake the developed world, measured by purchasing power parity. It's a defining moment."

The size of the emerging market middle class will swell to 1.2 billion people by 2030, from 250 million in 2000, he said.

That bodes well for financial services, as households tend to open bank accounts and ask for other products when income reaches about $10,000, Geoghegan said.

"Many Chinese households are about to hit this level. They number about 33 million now. But they will quadruple to 155 million by 2014. In India, the change will also be dramatic," he said.[4]

In addition, to illustrate how experts debate the next group of emerging-market countries, the Goldman Sachs economist who created the term *BRIC* in 2001 in a report for the investment bank has added a new group, *MITSK*. A January article in the British *Financial Times* newspaper notes, "Jim O'Neill, who coined the term 'Bric', is about to redefine further emerging markets. The chairman of Goldman Sachs Asset Management (until end of 2010) plans to add Mexico, South Korea, Turkey and Indonesia into a new grouping with the Brics—Brazil, Russia, India and China—that he dubs 'growth markets. It's just pathetic to call these four "emerging markets."[5]

The *Financial Times* continues to note how the Brics have frequently been dismissed as a marketing ploy. However, the nine-year-old term has spawned government summits, investment funds, business strategies and a host of countries keen to join. Adding that Mr O'Neill himself stated that the term "emerging markets" was no longer helpful because it encompassed countries with too great a range of economic prospects. Mexico and South Korea account for 1.6 per cent each of global GDP in nominal terms. Turkey and Indonesia are worth 1.2 and 1.1 per cent respectively. China is the world's second-largest economy, at 9.3 per cent of global GDP (the US is worth 23.6 per cent), while Brazil, India and Russia combined provide a further 8 per cent. O'Neill offers a new approach that will involve looking at fresh ways to measure exposure to equity markets beyond market capitalisation—for example, looking at gross domestic product, corporate revenue growth and the volatility of asset returns.[6]

These opinions and analyses by different economists are highlighted in this chapter to illustrate that the category of emerging markets is complex, evolving, and subject to wide interpretation. So how then do savvy global professionals sort through all of this information? Managers focus on the criteria for emerging markets in an effort to take advantage of newly emerging ones. While there are differing opinions on which countries are emerging, it's clear that global businesses are focused on the groups of countries offering strong domestic markets. Many of these emerging-market countries are also home to companies that are taking advantage of the improved business conditions there. These companies are becoming world-class global competitors in their industries. Regardless of which definition or classification is used, the largest emerging markets remain lucrative and promising.[7]

Key Emerging Markets

Asia

Spotlight on China

Located below Russia on the western seaboard of the Pacific Ocean, China is about as large as the continent of Europe and slightly larger than the United States. It is the third-largest country in the world after Russia and Canada.

For more than fifty years, China has had a centrally planned economy in which the state controlled most of the commercial activity. Under Mao Zedong's over forty-year leadership, the Chinese government kept a firm grip on the country's economic activity. That grip has been loosening since the 1980s as a result of Deng Xiaoping's reforms, which introduced some strong capitalist characteristics into China's centrally planned economy. Since the early 1980s, the Chinese economy has been in transition away from central planning and toward a market-driven economy. In today's model, market forces work in conjunction with state ownership and intervention. This system is commonly referred to as "a socialist market economy with Chinese characteristics." The

government now realizes that it can't provide all the resources needed to fuel the economy by itself and that the private sector has a major role to play in providing investment—and jobs. Today, China's economy is caught between two opposing forces—a burgeoning market sector that is outgrowing government control and the inability of that market to function efficiently due to continued influence by the state on production and prices.

In 1979, China instituted economic reforms, established "special economic zones," and opened its economy to foreign investments and companies. This change in attitude brought remarkable changes to the socialist market economy, resulting in improved living standards and new social attitudes. As local provinces have benefited from foreign investment, particularly in the south, central economic control has weakened. Since 1978, industrial output has increased more than sixfold, in large part due to foreign manufacturers and investors who have established operations in China (usually as joint ventures with corporations owned or influenced by the Chinese government but also with some private-sector companies).

In many areas, China remains a predominantly agricultural society. Major crops include rice, barley, millet, tobacco, sweet potatoes, wheat, soybeans, cotton, tea, raw silk, rapeseed, corn, peanuts, watermelon, and sesame seed. Under the 1979 regulations, peasants were permitted to lease land for private farming and were allowed to sell for profit any surplus produce above the quota demanded by the state in the open market. There are still more collectives than family farms, but this is changing. Besides agriculture, the leading industries include textiles, machinery, cement, chemicals, communications and transportation equipment, building materials, and electronic machinery and equipment.

The results of these reforms have been spectacular—China's economy has grown an average of 9 percent per year over the last fifteen years and is now the second largest in the world. If it continues at this rate of expansion, some pundits predict China could eventually replace the United States in first place.

One of the most interesting facets of China's economic transition has been the rise of the middle class. Prior to the 1980s, there was only a small middle class, with most people occupying the lower echelons of the economic ladder. Now it's estimated that some 300 million Chinese have entered the middle-class cohort, fueling a huge increase in consumer spending.

In the 1990s, the seven-day workweek was progressively lowered to five days. With increased time off and longer national holidays, the average Chinese person now has more leisure time—and more time to spend money on consumer goods.

Take a look at some of China's major cities—particularly those along the eastern coast—and you'll see soaring skyscrapers, glitzy boutiques, luxury hotels, and expensive cars. There's a feeling of economic prosperity and high-powered consumerism. Apartment buildings aimed at the prosperous middle-class market are sprouting up all over China's major cities.

Travel just a few hundred miles from the cities, though, and you'll encounter farming scenes reminiscent of the early days of the twentieth century. The economic disparity between the urban rich and the rural poor and all its accompanying problems are likely to continue for the foreseeable future.

With a burgeoning market sector that's outgrowing government control, China is now at the crossroads of reform. Yet despite the high growth rates, enormous challenges remain, including marked regional inequality, an entrenched and at times inflexible bureaucracy, high unemployment, a large floating population, and environmental degradation. Most commentators agree that the country has recognized the complex issues facing its economic future and is now ready to address them.

The growth of China's telecommunications industry is outstripping expectations. The number of mobile-phone subscribers, for example, has grown from 1 million in 1994 to around 700 million in 2009.[8] But the industry's expansion hasn't automatically led to large profits. The growth has been fueled by an increase in competition, putting downward pressure on prices. In fact, a 2009 *China Daily* article claims that China's telecom market the biggest battlefield in the world.[9]

Internet use is also expanding rapidly, although its spread is hindered by the government's attempts to regulate the sector and control access as evidenced in the case between the government and Google in the spring of 2010. Keeping up with the newest technology in the areas of delivery networks, broadband access, payment procedures, and security has created enormous opportunities. The government has made extensive efforts to invest in infrastructure and emerging technologies.

In 2009, agriculture accounted for an estimated 10.6 percent of China's gross domestic product (GDP), industry represented 46.8 percent, and services totaled 42.6 percent. Apart from agriculture, China's leading industries include "mining and ore processing of iron, steel, aluminum, and other metals, coal; machine building; armaments; textiles and apparel; petroleum; cement; chemicals; fertilizers; consumer products, including footwear, toys, and electronics; food processing; transportation equipment, including

automobiles, rail cars and locomotives, ships, and aircraft; telecommunications equipment; commercial space launch vehicles; and satellites."[10] The production of consumer goods is now one of the fastest-growing sectors in the economy. Once a source of cheap consumer electronics for the West, China is now producing those items for its own rapidly expanding internal market.

Chinese economic statistics must still be regarded with a degree of skepticism. Often it's unclear where the numbers have originated or how they have been derived. Still, there's no doubt that phenomenal growth is taking place, and there are pressures for a more transparent economic reporting system.

In the past, China didn't see the environment as an issue in its race to industrialize. Now, there is an increasing sense of environmental awareness. "China is changing from the factory of the world to the clean-tech laboratory of the world. It has the unique ability to pit low-cost capital with large-scale experiments to find models that work."[11]

Government attention and foreign investment have been focused on further developing the country's inadequate infrastructure, including roads, railways, seaports, communications systems, and power generation. Industrial capability, in both light and heavy industries, has also improved. China is a vast country rich in natural resources, including coal, oil, gas, various metals, ores, and minerals.

The largest Chinese companies are those that have capitalized on China's natural strengths and have state backing or are state-run. For example, PetroChina is the country's largest oil and gas producer and distributor. PetroChina is the listed arm of state-owned China National Petroleum Corporation (CNPC). It is one of the world's largest oil producers and is the world's most valuable company by market value as of 2010, exceeding a trillion-dollar market capitalization. China's largest companies have benefited from this combination of government support through access to capital and markets along with private-sector efficiencies.

China joined the WTO in December 2001, and it will likely be drawn even more into the global economy as companies continue to vie for access to its 1.3 billion consumers and cheap and productive labor pool. Most companies expect that dealing with China will now become more straightforward, if not easier. Whatever the future brings, the Chinese economy continues to be a powerhouse of growth and opportunity.[12]

Spotlight on India

India is officially called the Republic of India and is also known as Hindustan or Bharat. As the seventh-largest country in the world, India spans 1.267 million square miles; it's about one-third the size of the United States. India shares borders in the northwest with Pakistan; in the north with China, Bhutan, and Nepal; and in the east with Bangladesh and Myanmar (Burma). The Indian territory also extends to the Andaman and Nicobar Islands in the Bay of Bengal as well as to Lakshadweep in the Arabian Sea.

Prior to the mid-1980s, the country pursued a policy of socialism with the state planning and controlling many sectors of the economy. Foreign investment had been discouraged except in the area of technology transfers. Since the early 1990s, India has embarked on an economic liberalization scheme that has proven beneficial to the country.

In 1991, India was on the brink of defaulting on its foreign debt. The government responded with a series of successful measures to initiate widespread economic reforms, including reducing export and import barriers, dismantling some of its swollen bureaucracy, making the currency partially convertible, and eliminating the black market for foreign currency and gold. Efforts were also made to privatize or increase the efficiencies of unprofitable state companies. Finance Minister Manmohan Singh (who later became prime minister) was successful in beginning to dismantle the "License Raj," an intricate system of government economic control through permits and quotas. Various policies initiated by the government provided a larger role for the private sector and encouraged foreign investment. As a result, investment increased, though at much lower levels than in other Asian countries.

Since the 1990s, central government intervention, licensing, and regulation have decreased, as have bureaucratic inefficiencies. India boasts an established free-market system; a sophisticated industrial and manufacturing base; and a huge pool of skilled, low-to-moderate-cost workers, including professional managers. Economic gains, particularly as a result of further integration into the global economy, have provided improved the standard of living for all communities. The country's 2.1 percent annual population growth ensures that its population will surpass China's within the next decade and remains a significant problem for the government, as limited resources threaten the distribution of economic reform benefits.

The country is rich in natural resources, such as rubber, timber, chromium, coal, iron, manganese, copper ore, petroleum, bauxite, titanium, mica salt, limestone, and gypsum. The country is one of the world's leading producers of iron ore, and coal accounts for

nearly 40 percent of all mined minerals. India also has reserves of natural gas and oil, but it remains a net importer of crude oil because its domestic generation is insufficient to meet demand. In addition, India has deposits of precious stones, including diamonds, emeralds, gold, and silver. Cut diamonds are one of India's biggest exports.

Agriculture remains an important economic sector, contributing roughly 17 percent of the country's GDP and employing almost 52 percent of the workforce. Major crops include rice, wheat, pulses, sugarcane, cotton, jute, oilseeds, tea, coffee, tobacco, onions, and potatoes. Other important agricultural interests include dairy products, sheep, goats, poultry, and fish.

Until the mid-1960s, India imported much of its food. The Green Revolution focused on improving farming techniques, increasing mechanization, and irrigating as well as introducing high-yielding seeds. All of these have increased agricultural production and made the country self-sufficient in food production. The government also provides incentives to farmers to expand production. Most of India's farms tend to be small and provide subsistence for the families that operate them. They aren't geared for commercial purposes. Northern fertile areas, such as those in the state of Punjab, account for much of the export production.

While India has more cattle than any other country, it isn't farmed for food consumption as Hindus are not supposed to eat beef. The animals are used for a variety of other purposes, including plowing land, producing milk for dairy products, and supplying leather.

The growth of Indian industry, which accounts for about 28.2 percent of its GDP and 14 percent of employment, has resulted in widespread improvements and diversity in the country's manufacturing base. The major manufacturing industries include cotton and jute textiles; iron, steel, and other basic metals; petrochemicals; electrical machinery and appliances; transport equipment; chemicals; cement; fertilizers; software; medicines and pharmaceuticals; and food products. The power, electronics, food processing, software, transportation equipment, and telecommunications industries are developing rapidly. The financial sector, including banking and insurance, is well developed, although efforts to modernize it are underway.

State-run entities continue to control some areas of telecommunications, banking, insurance, public utilities, and defense, as well as the production of minerals, steel, other metals, coal, natural gas, and petroleum. There have been some steps taken to shift more control to the private sector, although on a gradual and closely monitored scale.

Services account for 54.9 percent of the GDP, but employ only 34 percent of the workforce. The most dramatic change in the economy has come from the computer-programming industry, as companies around the world have turned to India for outsourcing. With its skilled, relatively cheap, and English-speaking professional workforce, India has received a much-needed boost in the form of investment and foreign earnings. This is expected to have continued significant impact on the economy, business environment, and the social values and expectations of the Indian population.

India's technology firms have gained global recognition. One of the best known is Infosys. Founded in 1981 by seven Indian entrepreneurs, Infosys today is a NASDAQ-listed global consulting and information technology services company—with $5.4 billion in revenues. Throughout twenty-nine years of growth, Infosys, in addition to other well-managed Indian companies, has been well positioned to take advantage of the Indian government's efforts at economic liberalization that began in the early 1990s. Under this program, the government has systematically reduced trade barriers and embraced globalization. These changes have led to India's emergence as the global destination for software services talent.[13]

Amusing Anecdote

India's Currency Gets a Visible Promotion



A clear sign of a currency's importance is its symbol. All of the major global economies' currencies (e.g., the dollar, pound , euro, and yen) have one. In July 2010, the Indian government announced that there was a new symbol for the rupee. Not yet available on keyboards or any electronic devices, the symbol will replace the often-used Rs. "The symbol is a matter of national pride, underscoring 'the robustness of the Indian economy,' said Ambika Soni, India's Information Minister" to the *New York Times*.[14]

Europe

Spotlight on Russia

Russia is the largest country in the world, stretching across two continents and eleven time zones. Eleven seas and two oceans wash the banks of this 6.6 million square mile territory. The south and southeast of the country are covered with mountains, and the central part is a plain, furrowed with rivers. Around 7,000 lakes spread over the western part of Russia. The border between Europe and Asia runs down the west side of the Ural Mountains, about 807 miles east of Moscow.

Anyone looking to do business in Russia today needs to comprehend the array of changes that have impacted the nation over the past three decades. Rising to power in the 1980s, General Secretary Mikhail Gorbachev was the first leader to end repressive political controls and to suffer nationalist movements in the constituent republics. Gorbachev set the forces in action that would overturn the Communist regime and seal his own expulsion. He relaxed government control on the media and the Russian culture, implementing a policy of *glasnost*, or openness and candor. Gorbachev also sought *perestroika* (i.e., restructuring) of the economy and political system that preserved some of the more positive elements of socialism. Gorbachev gained international fame as the head of the Soviet bloc who helped put an end to the Cold War. To reach a common understanding, Gorbachev met repeatedly with US Presidents Ronald Reagan and George Bush, helping broker arms-reduction agreements.

During Gorbachev's term, Communist regimes began to fall all over Eastern Europe. In an abrupt departure from previous Soviet policy, Gorbachev refused to intervene. The Berlin Wall fell in 1989, and Gorbachev did nothing to stop it. Sensing weakness, republic parliaments all over the Soviet bloc asserted their sovereignty; a few even went so far as to assert complete independence. In 1991, when Gorbachev attempted to negotiate with the republics, alarmed Soviet leaders attempted a coup. The coup failed, but Gorbachev had lost his political cache to rival Boris Yeltsin, who succeeded Gorbachev as the hero of the era. This changed political, economic, and military dynamics around the world.

While the changes Gorbachev implemented did little to develop the Soviet Union's struggling economy, he did overhaul Soviet elections by reintroducing multiparty elections in 1989. This essentially invited political dissidents and reform-minded leaders into the parliament. These individuals soon began to challenge Gorbachev's leadership, pushing him to implement more changes. In 1991, Gorbachev conceded to their demands and installed their leader, Boris Yeltsin, as the president of Russia.

The economic and political challenges the newly independent country faced were considerable. The inefficiency of the Soviet government had left its stamp on every area of the economy. Russia's industries had to update their technology, retrain their workers, and cut back their workforces. Russians were largely unfamiliar with Western ways of doing business and found it difficult to make the changes mandated by capitalism. Unemployment soared, and the plight of most Russians grew increasingly desperate.

In this climate of desperation, Yeltsin's government instituted a so-called shock therapy program intended to galvanize the economy by reducing barriers to free trade. These policies, while well intentioned, produced sweeping inflation that almost completely devalued Russian currency. Western newspapers were plastered with images of Russians waiting in long lines, carrying bags of devalued bills. In an attempt to address the crisis, the government introduced a privatization program, which resulted in rampant cronyism and theft of state property.

While the government encouraged the emergence of small businesses and the already-flourishing black-market trade was finally legitimatized, small businesses faced many obstacles inadvertently caused by the government's inefficiency. The tax system was so disorganized that the government couldn't obtain the funds necessary to sustain adequate police or military forces. Health care and other basic welfare systems collapsed, and organized crime forced small businesses to make regular payoffs.

As quality of life took a precipitous drop for the majority of the Russian population, the gap between the rich and poor broadened dramatically. But crime lords weren't the only ones profiting from the gap, the privatization of government assets enabled a few well-placed individuals to turn those assets into their private property. The nouveau riche, as this class of Russians was called,

tended to be ostentatious, and the construction of elaborate mansions at a time when ordinary Russians were suffering, outraged the citizens' sense of justice.

Since 1991, Russia has struggled to establish a market economy. The country "has undergone significant changes since the collapse of the Soviet Union, moving from a globally-isolated, centrally-planned economy to a more market-based and globally-integrated economy."[15] Today, Russia has shifted back to a more centralized, semi-authoritarian state. "Economic reforms in the 1990s privatized most industry, with notable exceptions in the energy and defense-related sectors. Nonetheless, the rapid privatization process, including a much criticized 'loans-for-shares' scheme that turned over major state-owned firms to politically-connected 'oligarchs', has left equity ownership highly concentrated."[16] Corruption remains a challenge for businesses operating in Russia. New business legislation, including a commercial code and the establishment of an arbitration court to resolve business disputes, has passed. However, the "protection of property rights is still weak and the private sector remains subject to heavy state interference."[17] However, the system continues to evolve. Additionally, global economic conditions have impacted the value of the ruble and the status of the country's international debts.[18]

Russian industry is primarily split between globally competitive commodity producers—in 2009 Russia was the world's largest exporter of natural gas, the second largest exporter of oil, and the third largest exporter of steel and primary aluminum—and other less competitive heavy industries that remain dependent on the Russian domestic market. This reliance on commodity exports makes Russia vulnerable to boom and bust cycles that follow the highly volatile swings in global commodity prices. The government since 2007 has embarked on an ambitious program to reduce this dependency and build up the country's high-technology sectors but with few results so far. A revival of Russian agriculture in recent years has led to Russia shifting from being a net grain importer to a net grain exporter. Russia has a highly industrialized and agrarian economy. Almost ten million people are engaged in the agriculture industry. Along with its vast spaces, Russia has always been known for its amazing resources. The country produces 30 percent of the world's nonferrous, rare, and noble metals; 17 percent of the world's crude oil; 30 percent of natural gas; and it holds 40 percent of the world's known natural gas deposits. Today, agriculture accounts for 4.7 percent of the economy, industry represents 34.8 percent, and services total 60.5 percent (based on a 2009 estimate).[19]

? Did You Know?

Russia, the Summer of 2010 Drought, and Wheat: Understanding the Domino Effect on Countries and Business

Think global business is all about leading-edge, high-tech gadgets, consumer products, or industrial manufacturing items? Think again. Since the early days of ancient trade, commodities, such as wheat, corn, spices, rice, and cotton, have been the primary objects of trade. Even today, wheat and corn, the most basic of foodstuffs across all cultures, can still make governments and economies—developed, developing, and emerging—quiver as a result of natural and unnatural disruptions to their marketplaces. Recently, in the summer of 2010, Russia experienced a crippling drought that led to a four-month ban on all grain exports. "Russia has become an increasingly important force in the global supply of grains and the move reignited fears that nervous governments would begin hoarding their own supplies, potentially causing a shortage….Countries such as Egypt, the world's number one importer of wheat, which had bought Russian wheat, now must consider other options."[20] Russia provided almost 15 percent of the world's wheat supply for global exports from the 2009–10 crop. As a result of the ban, many global packaged-foods companies, including Swiss giants, Migros-Genossenschafts-Bund and Coop Schweiz, and British-based Premier Foods, considered possible price increases as a result of the wheat ban.[21]

Like China, Russia's largest companies are either state-run or have state backing, providing the government with access to resources, capital, and markets. Business analysts and investors are eager for the government to privatize more of the largest firms. "The Economic Development Ministry said in July [of 2010] that the privatization list for 2011–2013 included oil pipeline monopoly Transneft, Russia's largest shipping company Sovcomflot, oil major Rosneft, the country's largest banks Sberbank and VTB, the Federal Grid Company of Unified Energy System, the Russian Agricultural Bank, hydropower holding company RusHydro and other assets."[22]

RUSAL is one of Russia's largest privately held companies. Headquartered in Moscow, RUSAL is the world's largest aluminum company and accounts for almost 11 percent of the world's primary aluminum output and 13 percent of the world's alumina production. The company has aggressively used a strategy of global mergers and acquisition to grow its operations, which now cover nineteen countries and five continents. To raise capital, the company listed on the Hong Kong Stock Exchange in 2010.[23]

Africa

Spotlight on South Africa

South Africa makes up the southern portion of the continent of Africa, from the Atlantic Ocean in the west to the Indian Ocean in the east. With a total land area of 750,000 miles, including the Prince Edward Islands, the country is the twenty-seventh largest in the world, or approximately the same size as France, Spain, and Portugal combined.

Initially a refueling station for Dutch sailors traveling to the East, South Africa gradually developed an agricultural sector, based on fruit, wine, and livestock production, along the coast of the Cape of Good Hope. All of this changed dramatically with the discovery of minerals in the late nineteenth century. Subsequently, the country emerged as the leading manufacturing and industrial economy on the African continent.

Surging prices for gold and the high demand for base metals and other mineral products propelled the country's economy after World War II. South Africa was fortunate to have this strong economic base when international sanctions were applied in the 1970s and 1980s.

Nonetheless, import substitution and sanction busting were necessary for economic survival, and the country as a whole became increasingly isolated. A handful of massive corporations controlled most of the country's wealth and provided the majority of goods and services. The national government controlled those sectors of the economy seen as critical to the national interest of the apartheid state, including transportation, telecommunications, and the media.

South Africa practiced legal racial segregation, under the apartheid system. In the 1970s, worldwide disapproval of apartheid led to economic sanctions against South Africa. An international oil embargo was imposed in 1974, and the country was suspended from participating in the United Nations. "Disinvestment (or divestment) from South Africa was first advocated in the 1960s, in protest of South Africa's system of Apartheid, but was not implemented on a significant scale until the mid-1980s. The disinvestment campaign…is credited as pressuring the South African Government to embark on negotiations ultimately leading to the dismantling of the apartheid system."[24]

During the 1980s, there was global political and economic isolation. Many global investment firms pulled out of South Africa as a result of the public outcry and investor pressures against apartheid. While global firms, such as PepsiCo, Coca-Cola, IBM, ExxonMobil, and others, didn't leave South Africa, they endured public boycotts and protests in their home countries. The moral arguments against apartheid eventually won. After F. W. de Klerk was elected president in 1989, change was immediate. Political prisoners were released, and a national debate was initiated on the future of the country. The ban was lifted on the African National Congress (ANC), and in February 1990, Nelson Mandela was released from prison after twenty-seven years behind bars. He was elected president in 1994, and to further unite the country, de Klerk agreed to serve as deputy president in his administration.

Following the 1994 election, South Africa's period as an international outcast came to a swift end. The country was readmitted into the United Nations, and sanctions were lifted. For the first time South Africans could travel freely, had a free press, and participated in truly democratic institutions. Global businesses could once again do business with South Africa without fear of investor or public backlash.

South Africa has emerged as a free-market economy with an active private sector. The country strives to develop a prosperous and balanced regional economy that can compete in global markets. As an emerging-market country, South Africa relies heavily on industrial imports and capital. Specialty minerals and metals, machinery, transport equipment, and chemicals are important import sectors.

Minerals and energy are central to South Africa's economic activity, and manufacturing, the country's largest industry, is still based to a large extent on mining. South Africa receives more foreign currency for its gold than for any other single item, although it exports other minerals including platinum, diamonds, coal, chrome, manganese, and iron ore. It is the world's largest producer of platinum, gold, and chromium. Agricultural products, such as fruit, wool, hides, corn, wheat, sugarcane, fruits, vegetables, beef, poultry, mutton, dairy products, and grains, account for 3 percent of its GDP.

Today, industry accounts for 31 percent of the country's GDP, focusing on mining and automobile assembly, metalworking, machinery, textiles, iron and steel, chemicals, fertilizer, foodstuffs, and commercial ship repair.

During the years of apartheid, the economy of South Africa stagnated and appeared directionless. That changed after the election of the Government of National Unity in 1994. The postapartheid government has clear priorities, including economic growth, job creation, and inequality reduction.

Under apartheid, large conglomerates achieved near-cartel status and stifled competition. In many instances, this occurred with tacit government approval, and many promising small companies were bought or forced out of the market by financial muscle. The overall effect was a blunting of innovation and growth throughout the country. Since the end of apartheid, the government has made significant strides in promoting small-business development, in part by offering large corporations incentives to donate funds to small companies.

With the growth of their international market, South African businesses are expanding their focus outward. Companies such as Anglo American and South African Breweries (SAB) are listed on the London Stock Exchange, and Sappi (formerly South African Pulp and Paper Industries), a giant paper concern, has invested in the US market.

As part of its effort to improve South Africa's business climate, the government has made a strong commitment to privatization. To date, it has sold parts of South African Airways and Telkom (the former telecommunications monopoly), as well as other companies. The government is also offering incentives to overseas companies to partner with disadvantaged community-owned South African enterprises and requires businesses with government contracts to make contributions to social programs.

Since the end of apartheid, corporate life in South Africa has changed dramatically, and the business scene is now evolving at a fast pace. The government is committed to liberalizing the country's economy in fundamental ways, and corporate culture is changing in response. Programs to encourage economic growth and globalization have attracted new companies from abroad and introduced new approaches to doing business. Companies have also experienced a boost in creative energy. Today, the hallmarks of the South African business culture are change and transformation.

Day to day, doing business in South Africa is relatively easy and becoming easier as regulations are modified to reflect international norms. At the same time, new policies, particularly in matters of employment and labor, are making business life more complex.

While South African society is officially color free, in practical terms there are many areas of business that are still segregated. Overseas companies looking to break into public-sector contract work would be wise to establish joint ventures with companies owned by blacks.

South Africa has one of the highest union-membership rates in the world—a total of 3.2 million workers, or 25 percent of the employed workforce. Although the labor movement has a reputation for militancy, strikes are virtually unheard of since the job market has become so tight, and labor relations have generally improved.

Because of the country's strong union culture, managers tend to be highly sensitive to union concerns in the workplace, and union issues are never far from the surface in decision making. In fact, unions used rolling mass action to disrupt the apartheid economy, and this weapon is still available.

Services now total 65 percent of the economy. South Africa has a well-developed financial services sector, and the South African Futures Exchange ranks among the top-ten international (i.e., non-US) stock exchanges. Trade with countries on the African continent has been increasing rapidly. Finished goods and prepared foodstuffs, as well as base metals and chemicals, are in particularly high demand.[25] Overall, the country has the most-sophisticated market economy on the African continent. Between its economic profile and its well-developed physical infrastructure, South Africa has become an attractive place to do business.[26]

"For much of the past decade, Asia has been the go-to continent for companies interested in tapping fast-growing economies. Now, Wal-Mart Stores' agreement on September 27, 2010 to buy South African retailer Massmart Holdings for $4.6 billion may signal a shift toward Africa as another deal-making destination for multinationals."[27] The deal was Walmart's largest in a decade, which indicates just how serious global businesses are taking the emerging opportunity in Africa. Other large representative acquisitions include HSBC's stake in Nedbank Group and Japan's Nippon Telephone & Telegraph (NTT) purchase of Dimension Data. While these acquisitions are South African companies, it's only a matter of time until the rest of Africa triggers global commercial interest as well.

Latin America

Spotlight on Brazil

With nearly 3.4 million square miles in area, Brazil is about the size of the continental United States and the fifth-largest country in the world. It covers nearly half of the South American continent, and, with the exception of Chile and Ecuador, it shares a border with every country in South America.

Brazil remains Latin America's largest market, the world's fifth-most-populous country, and the world's tenth-largest economy in GDP terms. Government policies for disinflation and income support programs for the poorest families have contributed to a significant reduction in poverty rates and income inequality in recent years. However, poverty remains a stubborn challenge for Brazil.

Brazil's economic history has progressed in cycles, each focused on a single export item. Soon after the arrival of the first Europeans, wood was the hot commodity. In the sixteenth and seventeenth centuries, the scramble was for sugar. Eighteenth-century traders lusted for gems, gold, and silver; and finally, in the nineteenth and twentieth centuries, coffee was king. Rubber had its day as well. Also of economic importance during these cycles were cattle and agriculture, though they mainly served the domestic market.

Brazil is best known as a leading world producer of coffee and sugar. These commodities, no doubt, enable the country to trade on the world's stage and remain critical to the Brazilian economy to this day. Brazil is also one of the largest producers and exporters of soybeans, orange juice, cocoa, and tropical fruits. A little known fact, however, is that today, nonagricultural products—namely, auto parts, aircraft, and machinery—bring in more money. Ironically, it's the oft-maligned industrial programs of the 1960s and 1970s that deserve much of the credit for these successes.

Industry came to Brazil in the mid-1800s. The depression of 1929 threw a wrench in development, but the setback was only temporary; during subsequent decades, expansion was steady. Growth was especially healthy between the 1960s and the oil crisis of 1979. It wasn't until the 1980s, when interest rates busted the charts, that the economy began its descent. The flow of foreign and domestic capital slowed to a trickle, devaluations played havoc with the national currency, and foreign companies initiated debilitating cutbacks or left the country altogether. Severely handicapped in its ability to invest, Brazil plunged into a period of runaway inflation and negative growth rates. To this day, the 1980s are referred to as "the lost decade."

In the 1990s, the government honed in on three economic goals: (1) trade reform, (2) stabilizing the economy, and (3) building the country's relationship with the global financial community. In 1994, Minister of Finance Fernando Henrique Cardoso (often called FHC), launched the Real Plan, which inspired the name for Brazil's currency (i.e., the real). The plan, with its emphasis on the need for a strong currency, high interest rates, strict limits on government spending, and an opening up of the economy, touched off a boom in Brazil. Foreign capital began pouring in. Brazil's economic wizards outwitted the forces that wracked Mexico in the mid-1990s as well as Southeast Asia in 1997 and 1998. Their main premise was a strong (i.e., increasingly overvalued) real and spiraling interest rates. However, this premise lost validity in January 1999, when the Central Bank stopped defending the real and let the currency float freely.

Economically, the remainder of the 1990s was a qualified success. In 2001 and 2002, Brazil managed to avoid the fate of its neighbor, Argentina. Nevertheless, the country's finances remained a disaster. Improved prudent economic policy led to early repayment of IMF loans in 2005 and stabilized the economy. Although Brazil has seen significant rates of economic growth in recent years, this growth hasn't benefited all sectors or all groups to the same extent. Simultaneously, the economy is undergoing major structural changes as large-scale privatization of formerly state-owned enterprises continues.[28]

Today, "characterized by large and well-developed agricultural, mining, manufacturing, and service sectors, Brazil's economy outweighs that of all other South American countries, and Brazil is expanding its presence in world markets."[29] Its industry accounts for 25.4 percent of the GDP and focuses on textiles, shoes, chemicals, cement, lumber, iron ore, tin, steel, aircraft, motor vehicles and parts, and other machinery and equipment. Agriculture, including coffee, soybeans, wheat, rice, corn, sugarcane, cocoa, citrus, and beef, accounts for 6.1 percent of the economy, while services total 68.5 percent.[30]

Since 2003, Brazil has steadily improved macroeconomic stability, building up foreign reserves, reducing its debt profile by shifting its debt burden toward real-denominated and domestically held instruments, adhering to an inflation target, and committing

to fiscal responsibility. Brazil has also experienced the global "recession, as global demand for Brazil's commodity-based exports dwindled and external credit dried up. However, Brazil was one of the first emerging markets to begin a recovery."[31]

Today, Brazil is home to several global firms. Embraer builds innovative small jets and has become the world's biggest producer of smaller jet aircraft. The Brazilian food processors, Sadia and Perdigao, exemplify the international entrepreneurship of modern Brazil. Each is a $2 billion enterprise and exports about half of its annual production. Brazil's abundant resources for producing pork, poultry, and grains and its ideal growing conditions for animal feed provide these companies with many advantages. Both Sadia and Perdigao also have world-class global distribution and supply-chain management systems for product categories in frozen foods, cereals, and ready-to-eat meals.

? Key Takeaways

- There are some common characteristics of emerging markets in terms of the size of the local population, the opportunity for growth with changes in the local commercial infrastructure, the regulatory and trade policies, improvements in efficiencies, and an overall investment in the education and well-being of the local population, which in turn is expected to increase local incomes and purchasing capabilities.
- A current definition of an emerging market is a country that can be defined as a society transitioning from a centrally managed economy to a free-market-oriented economy, with increasing economic freedom, gradual integration within the global marketplace, an expanding middle class, and improving standards of living, social stability, and tolerance, as well as an increase in cooperation with multilateral institutions.

References

1. "Ins and Outs: Acronyms BRIC Out All Over," *Economist*, September 18, 2008, accessed January 6, 2011, http://www.economist.com/node/12080703.
2. Vladimir Kvint, "Define Emerging Markets Now," *Forbes*, January 28, 2008, accessed January 5, 3011, http://www.forbes.com/2008/01/28/kvi...0129kvint.html.
3. Vladimir Kvint, "Define Emerging Markets Now," *Forbes*, January 28, 2008, accessed January 5, 3011, http://www.forbes.com/2008/01/28/kvi...0129kvint.html.
4. Steven Slater, "After BRICs, Look to CIVETS for Growth—HSBC CEO," *Reuters*, April 27, 2010, accessed January 6, 2011, http://www.reuters.com/article/idUSLDE63Q26Q20100427.
5. Jennifer Hughes, "'Bric' Creator Adds Newcomers to List," *Financial Times*, January 16, 2010, accessed January 5, 3011, http://www.ft.com/cms/s/0/f717c8e8-2...#ixzz1MKbbO8ET.
6. Jennifer Hughes, "'Bric' Creator Adds Newcomers to List," *Financial Times*, January 16, 2010, accessed January 5, 3011, http://www.ft.com/cms/s/0/f717c8e8-2...#ixzz1MKbbO8ET.
7. The sections that follow are excerpted in part from two resources owned by author Sanjyot P. Dunung's firm, Atma Global: *CultureQuest Business Multimedia Series*and *bWise: Business Wisdom Worldwide*. The excerpts are reprinted with permission and attributed to the country-specific product when appropriate. The discussion about Asia also draws heavily from the author's book *Doing Business in Asia: The Complete Guide*, 2nd ed. (New York: Jossey-Bass, 1998).
8. Wang Xing, "Battle Begins over 3G Market," *China Daily*, October 19, 2009, accessed May 17, 2011, http://www.chinadaily.com.cn/busines...nt_8808873.htm.
9. Wang Xing, "Battle Begins over 3G Market," *China Daily*, October 19, 2009, accessed May 17, 2011, http://www.chinadaily.com.cn/busines...nt_8808873.htm.
10. US Central Intelligence Agency, "East & Southeast Asia: China," *World Factbook*, accessed January 6, 2011, https://www.cia.gov/library/publicat...k/geos/ch.html.
11. Thomas L. Friedman, "World, Not U.S., Takes Lead with Green Technology," *Post-Bulletin*, September 21, 2010, accessed January 6, 2011, http://www.postbulletin.com/newsmana...?z=12&a=470550.
12. *CultureQuest Business Multimedia Series: China*(New York: Atma Global, 2010); *bWise: Business Wisdom Worldwide: China*(New York: Atma Global, 2011).
13. *CultureQuest Business Multimedia Series: India*(New York: Atma Global, 2010); *bWise: Business Wisdom Worldwide: India*(New York: Atma Global, 2011).

14. “The Rupee Gets Its Own Mark,” *New York Times*, July 18, 2010, accessed January 6, 2011, http://www.nytimes.com/2010/07/18/we.../18grist.html#.
15. US Central Intelligence Agency, “Central Asia: Russia,” *World Factbook*, accessed January 6, 2011, https://www.cia.gov/library/publicat...k/geos/rs.html.
16. US Central Intelligence Agency, “Central Asia: Russia,” *World Factbook*, accessed January 6, 2011, https://www.cia.gov/library/publicat...k/geos/rs.html.
17. US Central Intelligence Agency, “Central Asia: Russia,” *World Factbook*, accessed January 6, 2011, https://www.cia.gov/library/publicat...k/geos/rs.html.
18. *CultureQuest Business Multimedia Series: Russia*(New York: Atma Global, 2010); *bWise: Business Wisdom Worldwide: Russia*(New York: Atma Global, 2011).
19. US Central Intelligence Agency, “Central Asia: Russia,” *World Factbook*, accessed January 6, 2011, https://www.cia.gov/library/publicat...k/geos/rs.html.
20. Liam Pleven, Gregory Zuckerman, and Scott Kilman, “Russian Export Ban Raises Global Food Fears,” *Wall Street Journal*, August 6, 2010, accessed January 6, 2011, http://online.wsj.com/article/SB1000...617512592.html.
21. Liam Pleven, Gregory Zuckerman, and Scott Kilman, “Russian Export Ban Raises Global Food Fears,” *Wall Street Journal*, August 6, 2010, accessed January 6, 2011, http://online.wsj.com/article/SB1000...617512592.html.
22. “Russia Unlikely to Privatize Largest Companies in 2010,” RIA Novosti, August 30, 2010, accessed January 6, 2011, http://en.rian.ru/business/20100830/160394304.html.
23. “Who We Are,” RUSAL, accessed May 18, 2011, http://rusal.ru/en/about.aspx.
24. *Wikipedia*, s.v. “Disinvestment from South Africa,” last modified February 13, 2011, accessed February 16, 2011, http://en.Wikipedia.org/wiki/Disinve...m_South_Africa.
25. *bWise: Business Wisdom Worldwide: South Africa*(New York: Atma Global, 2011).
26. *CultureQuest Business Multimedia Series: South Africa*(New York: Atma Global, 2010).
27. Renee Bonorchis, “Africa Is Looking Like a Dealmaker’s Paradise,” *BusinessWeek*, September 30, 2010, accessed January 5, 2011, http://www.businessweek.com/magazine...8020648051.htm.
28. *CultureQuest Business Multimedia Series: Brazil*(New York: Atma Global, 2010); *bWise: Business Wisdom Worldwide: Brazil*(New York: Atma Global, 2011).
29. US Central Intelligence Agency, “Central America: Brazil,” *World Factbook*, accessed January 7, 2011, https://www.cia.gov/library/publicat...k/geos/br.html.
30. US Central Intelligence Agency, “Central America: Brazil,” *World Factbook*, accessed January 7, 2011, https://www.cia.gov/library/publicat...k/geos/br.html.
31. US Central Intelligence Agency, “Central America: Brazil,” *World Factbook*, accessed January 7, 2011, https://www.cia.gov/library/publicat...k/geos/br.html.

Source

The above content was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

This page titled 5.6: Emerging Markets is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

6: Global Market Planning

6.1: Global Market Planning Summary
6.2: Measuring Market Attractiveness
6.3: Global Market Opportunity Assessment – PESTEL Analysis
6.4: Global Market Opportunity Assessment – CAGE Analysis
6.5: Global Market Opportunity Assessment – Scenario Planning and Analysis
6.6: Selecting the Countries to Enter
6.7: Global Market Segmentation
6.8: Using Demographics to Guide Global Marketing Strategy
6.9: Target Market Selection
6.10: Global Positioning
6.11: Basics of Positioning

This page titled 6: Global Market Planning is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.1: Global Market Planning Summary

Summary

A wide variety of internationalization moves are available after choosing to expand. Moreover, some flatteners make global moves easier, while some make them more difficult. Indeed, even importing and outsourcing can be considered stealth, or at least early, steps in internationalization, because they involve doing business across borders. As companies look for growth in new areas of the world, they typically prioritize which countries to enter. Because many markets look appealing due to their market size or low-cost production, it is important for firms to prioritize which countries to enter first and to evaluate each country's relative merits. For example, some markets may be smaller in size, but their strategic complexity is lower, which may make them easier to enter and easier from an operations point of view. Sometimes there are even substantial regional differences within a given country, so careful investigation, research, and planning are important to do before entry.

Evaluating whether to enter a new market is like peeling an onion—there are many layers. For example, when evaluating whether to enter China, the advantage most people see immediately is its large market size. Further analysis shows that the majority of people in that market can't afford US products, however. But even deeper analysis shows that while many Chinese are poor, the number of people who can afford consumer products is increasing. [1]

Through global market segmentation, a company can identify and group customers or countries according to common needs and wants. Demographic segmentation can be based on country income and population, age, ethnic heritage, or other variables. Psychographic segmentation groups people according to attitudes, interests, opinions, and lifestyles. Behavioral segmentation utilizes user status and usage rate as segmentation variables. Benefits segmentation is based on the benefit buyers seek. Global teens and global elites are two examples of global market segments.

After marketers have identified segments, the next step is targeting: The identified groups are evaluated and compared, and one or more segments with the greatest potential is selected from them. The groups are evaluated on the basis of several factors, including segment size and growth potential, competition, and compatibility and feasibility. Target market assessment also entails a thorough understanding of the product-marketing question and determining marketing model drivers and enabling conditions in the countries under study. The timing of market entry should take into account whether a first-mover advantage is likely to be gained. After evaluating the identified segments, marketers must decide on an appropriate targeting strategy. The three basic categories of global target marketing strategies are standardized global marketing, niche marketing, and differentiated multi-segment marketing.

Positioning a product or brand to differentiate it in the minds of target customers can be accomplished in various ways: positioning by attribute or benefit, positioning by quality/price, positioning by use or user, and positioning by competition. In global marketing global consumer culture positioning (GCCP), foreign consumer culture positioning (FCCP), and local consumer culture positioning (LCCP) are additional strategic options.

References

1. Art Kleiner, "Getting China Right," *Strategy and Business*, March 22, 2010, accessed January 23, 2011, http://www.strategy-business.com/article/00026?pg=al.

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- "International Expansion and Global Market Opportunity Assessment", chapter 8 from the book Challenges and Opportunities in International Business (v. 1.0)under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.
- The course note from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM). 'The Economic and Political environment' is Copyright (c) by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license.

This page titled 6.1: Global Market Planning Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.2: Measuring Market Attractiveness

Learning Objectives

After reading this section, students should be able to …

1. understand the key factors in selecting global markets
2. appreciate the importance of cultural, administrative, geographic, and economic distance in estimating a market's attractiveness

Four key factors in selecting global markets are (a) a *market's size and growth rate*, (b) a particular country or region's *institutional contexts*, (c) a region's *competitive environment*, and (d) a market's *cultural*, *administrative*, *geographic*, and *economic distance* from other markets the company serves.

Market Size and Growth Rate

There is no shortage of country information for making market portfolio decisions. A wealth of country-level economic and demographic data are available from a variety of sources including governments, multinational organizations such as the United Nations or the World Bank, and consulting firms specializing in economic intelligence or risk assessment. However, while valuable from an overall investment perspective, such data often reveal little about the prospects for selling products or services in foreign markets to local partners and end users or about the challenges associated with overcoming other elements of distance. Yet many companies still use this information as their primary guide to market assessment simply because country market statistics are readily available, whereas real product market information is often difficult and costly to obtain.

What is more, a country or regional approach to market selection may not always be the best. Even though Theodore Levitt's vision of a global market for uniform products and services has not come to pass, and global strategies exclusively focused on the "economics of simplicity" and the selling of standardized products all over the world rarely pay off, research increasingly supports an alternative "global segmentation" approach to the issue of market selection, especially for branded products. In particular, surveys show that a growing number of consumers, especially in emerging markets, base their consumption decisions on attributes beyond direct product benefits, such as their perception of the global brands behind the offerings.

Specifically, research by John Quelch and others suggests that consumers increasingly evaluate global brands in "cultural" terms and factor three global brand attributes into their purchase decisions: (a) what a global brand signals about quality, (b) what a brand symbolizes in terms of cultural ideals, and (c) what a brand signals about a company's commitment to corporate social responsibility. This creates opportunities for global companies with the right values and the savvy to exploit them to define and develop target markets across geographical boundaries and create strategies for "global segments" of consumers. Specifically, consumers who perceive global brands in the same way appear to fall into one of four groups:

1. *Global citizens* rely on the global success of a company as a signal of quality and innovation. At the same time, they worry whether a company behaves responsibly on issues like consumer health, the environment, and worker rights.
2. *Global dreamers* are less discerning about, but more ardent in their admiration of, transnational companies. They view global brands as quality products and readily buy into the myths they portray. They also are less concerned with companies' social responsibilities than global citizens.
3. *Antiglobals* are skeptical that global companies deliver higher-quality goods. They particularly dislike brands that preach American values and often do not trust global companies to behave responsibly. Given a choice, they prefer to avoid doing business with global firms.
4. *Global agnostics* do not base purchase decisions on a brand's global attributes. Instead, they judge a global product by the same criteria they use for local brands (Quelch (2003, August); Holt, Quelch, and Taylor (2004, September)).

Companies that use a "global segment" approach to market selection, such as Coca-Cola, Sony, or Microsoft, to name a few, therefore must manage two dimensions for their brands. They must strive for superiority on basics like the brand's price, performance, features, and imagery, and, at the same time, they must learn to manage brands' global characteristics, which often separate winners from losers. A good example is provided by Samsung, the South Korean electronics maker. In the late 1990s, Samsung launched a global advertising campaign that showed the South Korean giant excelling, time after time, in engineering,

design, and aesthetics. By doing so, Samsung convinced consumers that it successfully competed directly with technology leaders across the world, such as Nokia and Sony. As a result, Samsung was able to change the perception that it was a down-market brand, and it became known as a global provider of leading-edge technologies. This brand strategy, in turn, allowed Samsung to use a global segmentation approach to making market selection and entry decisions.

Institutional Contexts Khanna, Palepu, and Sinha (2005)

Khanna and others developed a five-dimensional framework to map a particular country or region's institutional contexts. Specifically, they suggest careful analysis of a country's (a) *political and social systems*, (b) *openness*, (c) *product markets*, (d) *labor markets*, and (e) *capital markets*.

A country's political system affects its product, labor, and capital markets. In socialist societies like China, for instance, workers cannot form independent trade unions in the labor market, which affects wage levels. A country's social environment is also important. In South Africa, for example, the government's support for the transfer of assets to the historically disenfranchised native African community has affected the development of the capital market.

The more open a country's economy, the more likely it is that global intermediaries can freely operate there, which helps multinationals function more effectively. From a strategic perspective, however, openness can be a double-edged sword: a government that allows local companies to access the global capital market neutralizes one of the key advantages of foreign companies.

Even though developing countries have opened up their markets and grown rapidly during the past decade, multinational companies struggle to get reliable information about consumers. Market research and advertising are often less sophisticated and, because there are no well-developed consumer courts and advocacy groups in these countries, people can feel they are at the mercy of big companies.

Recruiting local managers and other skilled workers in developing countries can be difficult. The quality of local credentials can be hard to verify, there are relatively few search firms and recruiting agencies, and the high-quality firms that do exist focus on top-level searches, so companies scramble to identify middle-level managers, engineers, or floor supervisors.

Capital and financial markets in developing countries often lack sophistication. Reliable intermediaries like credit-rating agencies, investment analysts, merchant bankers, or venture capital firms may not exist, and multinationals cannot count on raising debt or equity capital locally to finance their operations.

Emerging economies present unique challenges. Capital markets are often relatively inefficient and dependable sources of information, scarce while the cost of capital is high and venture capital is virtually nonexistent. Because of a lack of high-quality educational institutions, labor markets may lack well-trained people requiring companies to fill the void. Because of an underdeveloped communications infrastructure, building a brand name can be difficult just when good brands are highly valued because of lower product quality of the alternatives. Finally, nurturing strong relationships with government officials often is necessary to succeed. Even then, contracts may not be well enforced by the legal system.

Competitive Environment

The number, size, and quality of competitive firms in a particular target market compose a second set of factors that affect a company's ability to successfully enter and compete profitably. While country-level economic and demographic data are widely available for most regions of the world, competitive data are much harder to come by, especially when the principal players are subsidiaries of multinational corporations. As a consequence, competitive analysis in foreign countries, especially in emerging markets, is difficult and costly to perform and its findings do not always provide the level of insight needed to make good decisions. Nevertheless, a comprehensive competitive analysis provides a useful framework for developing strategies for growth and for analyzing current and future primary competitors and their strengths and weaknesses.

✔ Mini Case: Which BRIC Countries? A Key Challenge for Carmakers Haddock and Jullens (2009)

Today, automobile manufacturers face a critical challenge: deciding which BRIC countries (Brazil, Russia, India, and China) to bet on. In each, as per capita income rises, so will per capita car ownership—not in a straight line but in classic "S-curve" fashion. Rates of vehicle ownership stay low during the first phases of economic growth, but as the GDP or purchasing power

of a country reaches a level of sustained broad prosperity, and as urbanization reshapes the work patterns of a country, vehicle sales take off. But that is about where the similarities end. Each of the four BRIC nations has a completely different set of market and industry dynamics that make decision choices about which countries to target, including making difficult decisions about which markets to avoid, extremely difficult.

For one thing, vehicle manufacturing is a high-profile industry that generates enormous revenue, employs millions of people, and is often a proxy for a nation's manufacturing prowess and economic influence. Governments are extensively involved in regulating or influencing virtually every aspect of the product and the way the industry operates—including setting emissions and safety standards, licensing distributors, and setting tariffs and rules about how much manufacturing must take place locally. This reality makes the job of understanding each market and appreciating the differences more vital. For example, a summary overview of the BRIC nations reveals the differences among these markets and the operating complexities in all of them.

Brazil, with Russia, is one of the smaller BRIC countries, with 188 million people (by comparison, China and India each have more than 1 billion, Russia has 142 million). Yet car usage is already relatively high: 104 cars in use per 1,000 people, nearly 10 times the rate of usage in India, according to the *Economist* Intelligence Unit. Because of this, growth projections for Brazil are relatively low—more in line with developed nations than with the other BRIC countries. Projections made by the industry research firm Global Insight show that sales will grow just 2% until 2013, underperforming even the U.S. market's projected growth rate.

On the plus side, Brazil is socioeconomically stable, with increasing wealth and a maturing finance system that is helping to propel growth among rural, first-time buyers who prefer compact cars. Few domestic brands exist, as the market is dominated by GM, Ford, Fiat, and Volkswagen. Prompted by generous government incentives, high import taxes, and exchange rate risks, foreign automakers have invested significantly in Brazil, which has thus become an unrivaled production hub for the rest of South America. Brazilian consumers live in a country with large rural areas and very rough terrain; they demand fairly large, SUV-like cars, made with economical small engines and flex-fuel power trains friendly to the country's biofuel industry. When a Latin American family buys its first automobile, chances are it was made in Brazil.

Russia, even though it is the smallest of the BRIC countries in population, has the highest auto adoption of the four: 213 cars in use per 1,000 people. (Western Europe, by comparison, has 518, according to the *Economist Intelligence Unit*.) Yet Global Insight expects future sales growth to average 6.5% from 2008 to 2013, far outpacing Brazil (2%), Western Europe (1.2%), and Japan and Korea (0.2%).

Given Russia's proximity to Europe, consumer preferences there are more akin to those of the developed markets than to those of China or India, and expensive, status-enhancing European models remain popular, although European safety features, interior components, and electronics are often stripped out to reduce costs. For vehicle manufacturers, the attractions of the Russian market include an absence of both local partnership requirements and significant local competitors. But there is high political risk. So far, the Russian government has permitted foreign carmakers to operate relatively freely, but the Kremlin's history of meddling in private enterprise and undercutting private ownership worries some executives. These concerns were heightened in November 2008, when Russia implemented tariffs against car imports in hopes of avoiding layoffs that might spark labor unrest among the country's 1.5 million car industry workers.

India has 1.1 billion people, but its level of car adoption is still low, with only 11 cars in use per 1,000 people. The upside is higher potential growth: among the BRIC countries, India is expected to have the fastest-growing auto sales, almost 15% per year until 2013, according to Global Insight. Sales of subcompact cars are strong, even during the global recession. The popularity of these small cars combines with India's energy shortages and the country's chronic pollution to provide foreign carmakers with an ideal opportunity to further develop electric power-train technologies there.

Until the early 1990s, foreign automobile manufacturers were mostly shut out of India. That has changed radically. Today, foreign automakers are welcomed and the government promotes foreign ownership and local manufacturing with tax breaks and strong intellectual property protection. And because foreign companies were shut out for a long period of time, India has capable manufacturers and suppliers for foreign vehicle manufacturers to partner with. Local competition is strong but is thus far concentrated among three players: Maruti Suzuki India, Ltd., Tata, and the Hyundai Corporation, which is well established in India.

China is almost as large as the other three combined in total auto sales and production. Its overall auto usage is just 18 cars per 1,000 households, but annual sales growth until 2013 is expected to be almost 10%. Its size and growth potential make China a dominant force in the industry going forward; new models and technologies developed there will almost certainly become available elsewhere.

But the Chinese government plays a central role in shaping the auto industry. Current ownership policies mandate that foreign vehicle manufacturers enter into 50-50 joint ventures with local automakers, and poor intellectual property rights enforcement puts the design and engineering innovations of foreign car companies at constant risk. At the same time, to cope with energy shortages and rampant pollution, the Chinese government is strongly encouraging research and development on alternative power trains, including electric cars and gasoline-electric hybrids. As a result, Chinese car companies may develop significant power-train capabilities ahead of their competitors.

Like their Indian counterparts, Chinese car companies have outpaced global automakers in developing cars specifically for emerging markets. A few Western companies, like Volkswagen AG, which has sold its Santana models in China through a joint venture (Shanghai Volkswagen Automotive Company) since 1985, are competitive. Some Chinese carmakers, like BYD Company, aspire to become global leaders in the industry. But many suffer from a talent shortage and inexperience in managing across borders. This may prompt them to acquire all or part of distressed Western automobile companies in the near future or to hire skilled auto executives from established companies and their suppliers.

In short, each of the four BRIC nations has a completely different set of market and industry dynamics. And the same is true for the other developing nations. Meanwhile, the number of autos in use in the developing world is projected to expand almost six-fold by 2018.

Cultural, Administrative, Geographic, and Economic Distance

Explicitly considering the four dimensions of *distance* can dramatically change a company's assessment of the relative attractiveness of foreign markets. In his book *The Mirage of Global Markets*, David Arnold describes the experience of Mary Kay Cosmetics (MKC) in entering Asian markets. MKC is a direct marketing company that distributes its products through independent "beauty consultants" who buy and resell cosmetics and toiletries to contacts either individually or at social gatherings. When considering market expansion in Asia, the company had to choose: enter Japan or China first? Country-level data showed Japan to be the most attractive option by far: it had the highest per capita level of spending on cosmetics and toiletries of any country in the world, disposable income was high, it already had a thriving direct marketing industry, and it had a high proportion of women who did not participate in the work force. MKC learned, however, after participating in both markets, that the market opportunity in China was far greater, mainly because of economic and cultural distance: Chinese women were far more motivated than their Japanese counterparts to boost their income by becoming beauty consultants. Thus, the entrepreneurial opportunity represented by what MKC describes as "the career" (i.e., becoming a beauty consultant) was a far better predictor of the true sales potential than high-level data on incomes and expenditures. As a result of this experience, MKC now employs an additional business-specific indicator of market potential within its market assessment framework: the average wage for a female secretary in a country (Arnold (2004), p. 34).

MKC's experience underscores the importance of analyzing distance. It also highlights the fact that different product markets have different success factors: some are brand-sensitive while pricing or intensive distribution are key to success in others. Country-level economic or demographic data do not provide much help in analyzing such issues; only locally gathered marketing intelligence can provide true indications of a market's potential size and growth rate and its key success factors.

✔ Mini Case: Tata Making Inroads Into China Chow (2008, April 28)

Not content with just India, Mumbai-based Tata Group, the maker of the $2,500 Nano small car, is developing a small car for China. The platform is being designed and developed by a joint Indian and Chinese team based in China. The alliance won a new project for the complete design and development of a vehicle platform for a leading original equipment manufacturer for a small car for the China's domestic market. The team is integrating components in automotive modules to radically improve manufacturability and bring down total cost.

Meanwhile, in 2009, Nanjing Tata AutoComp Systems began supplying automotive interior products to Shanghai General Motors and Changan Ford Automobile Company Products, including plastic vents, outlet parts, and cabin air-ventilation grilles. In the same year, Nanjing Tata began supplying General Motors Corporation in Europe. Eventually, the plant will supply global automakers in North America and Europe as well as emerging markets such as China.

Nanjing Auto is a wholly owned subsidiary of Tata AutoComp Systems, which is the automotive part manufacturing arm of India's Tata Motors. The company has 30 manufacturing facilities, mainly in India, and production capabilities in automotive plastics and engineering. It also has 15 joint ventures with Tier 1 supplier companies, mainly in India.

The company has almost completed construction of the 280,000-square-foot Nanjing plant at a cost of approximately $15 million. The first phase included capacity to make parts for air vents, handles, cupholders, ashtrays, glove boxes, and floor consoles. When completed, the plant will have double the current capacity and will also produce instrument panels, door panels, and larger parts. The plant is operated by local Chinese employees; only a few managers are Indian.

In its bid to become a $1 billion global automotive supplier by 2008, Tata AutoComp had to expand into China. Total passenger car sales in India in 2007 were slightly more than 1.4 million units; in China, the number was more than 5.2 million units, according to data from Automotive Resources Asia, a division of J.D. Power and Associates. Tata Motors sold 221,256 passenger cars in India in 2007. In the same year, Shanghai General Motors sold 495,405 cars. "We see huge potential in China. To us, China is not just a manufacturing base, but a window to the global market. Our investments are keeping this promising future in mind,'" says the Tata AutoComp's chief executive officer.

Source

The above content was adapted from "Measuring Market Attractiveness", section 5.2 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 6.2: Measuring Market Attractiveness is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.3: Global Market Opportunity Assessment – PESTEL Analysis

PESTEL, Globalization, and Importing

Learning Objectives

After reading this section, students should be able to …

1. Know the components of PESTEL analysis.
2. Recognize how PESTEL is related to the dimensions of globalization.
3. Understand why importing might be a stealth form of international entry.

Know the Components of PESTEL Analysis

PESTEL analysis is an important and widely used tool that helps show the big picture of a firm's external environment, particularly as related to foreign markets. PESTEL is an acronym for the political, economic, sociocultural, technological, environmental, and legal contexts in which a firm operates. A PESTEL analysis helps managers gain a better understanding of the opportunities and threats they face; consequently, the analysis aids in building a better vision of the future business landscape and how the firm might compete profitably. This useful tool analyzes for market growth or decline and, therefore, the position, potential, and direction for a business. When a firm is considering entry into new markets, these factors are of considerable importance. Moreover, PESTEL analysis provides insight into the status of key market *flatteners*, both in terms of their present state and future trends.

Firms need to understand the macroenvironment to ensure that their strategy is aligned with the powerful forces of change affecting their business landscape. When firms exploit a change in the environment—rather than simply survive or oppose the change—they are more likely to be successful. A solid understanding of PESTEL also helps managers avoid strategies that may be doomed to fail given the circumstances of the environment. JCPenney's failed entry into Chile is a case in point.

Finally, understanding PESTEL is critical prior to entry into a new country or region. The fact that a strategy is congruent with PESTEL in the home environment gives no assurance that it will also align in other countries. For example, when Lands' End, the online clothier, sought to expand its operations into Germany, it ran into local laws prohibiting it from offering unconditional guarantees on its products. In the United States, Lands' End had built a reputation for quality on its no-questions-asked money-back guarantee. However, this was considered illegal under Germany's regulations governing incentive offers and price discounts. The political skirmish between Lands' End and the German government finally ended when the regulations banning unconditional guarantees were abolished. While the restrictive regulations didn't put Lands' End out of business in Germany, they did inhibit its growth there until the laws were abolished.

There are three steps in the PESTEL analysis. First, consider the relevance of each of the PESTEL factors to your context. Next, identify and categorize the information that applies to these factors. Finally, analyze the data and draw conclusions. Common mistakes in this analysis include stopping at the second step or assuming that the initial analysis and conclusions are correct without testing the assumptions and investigating alternative scenarios.

The framework for PESTEL analysis is presented below. It's composed of six sections—one for each of the PESTEL headings.[1] The framework includes sample questions or prompts, the answers to which can help determine the nature of opportunities and threats in the macroenvironment. These questions are examples of the types of issues that can arise in a PESTEL analysis.

PESTEL Analysis

1. Political
    - How stable is the political environment in the prospective country?
    - What are the local taxation policies? How do these affect your business?
    - Is the government involved in trading agreements, such as the European Union (EU), the North American Free Trade Agreement (NAFTA), or the Association of Southeast Asian Nations (ASEAN)?
    - What are the country's foreign-trade regulations?

- o What are the country's social-welfare policies?

2. Economic

- o What are the current and forecast interest rates?
- o What is the current level of inflation in the prospective country? What is it forecast to be? How does this affect the possible growth of your market?
- o What are local employment levels per capita, and how are they changing?
- o What are the long-term prospects for the country's economy, gross domestic product (GDP) per capita, and other economic factors?
- o What are the current exchange rates between critical markets, and how will they affect production and distribution of your goods?

3. Sociocultural

- o What are the local lifestyle trends?
- o What are the country's current demographics, and how are they changing?
- o What is the level and distribution of education and income?
- o What are the dominant local religions, and what influence do they have on consumer attitudes and opinions?
- o What is the level of consumerism, and what are the popular attitudes toward it?
- o What pending legislation could affect corporate social policies (e.g., domestic-partner benefits or maternity and paternity leave)?
- o What are the attitudes toward work and leisure?

4. Technological

- o To what level do the local government and industry fund research, and are those levels changing?
- o What is the local government's and industry's level of interest and focus on technology?
- o How mature is the technology?
- o What is the status of intellectual property issues in the local environment?
- o Are potentially disruptive technologies in adjacent industries creeping in at the edges of the focal industry?

5. Environmental

- o What are the local environmental issues?
- o Are there any pending ecological or environmental issues relevant to your industry?
- o How do the activities of international activist groups (e.g., Greenpeace, Earth First!, and People for the Ethical Treatment of Animals [PETA]) affect your business?
- o Are there environmental-protection laws?
- o What are the regulations regarding waste disposal and energy consumption?

6. Legal

- o What are the local government's regulations regarding monopolies and private property?
- o Does intellectual property have legal protections?
- o Are there relevant consumer laws?
- o What is the status of employment, health and safety, and product safety laws?

Political Factors

The political environment can have a significant influence on businesses. In addition, political factors affect consumer confidence and consumer and business spending. For instance, how stable is the political environment? This is particularly important for companies entering new markets. Government policies on regulation and taxation can vary from state to state and across national boundaries. Political considerations also encompass trade treaties, such as NAFTA, ASEAN, and EU. Such treaties tend to favor trade among the member countries but impose penalties or less favorable trade terms on nonmembers.

Economic Factors

Managers also need to consider macroeconomic factors that will have near-term and long-term effects on the success of their strategy. Inflation rates, interest rates, tariffs, the growth of the local and foreign national economies, and exchange rates are critical. Unemployment, availability of critical labor, and the local cost of labor also have a strong bearing on strategy, particularly as related to the location of disparate business functions and facilities.

Sociocultural Factors

The social and cultural influences on business vary from country to country. Depending on the type of business, factors such as the local languages, the dominant religions, the cultural views toward leisure time, and the age and lifespan demographics may be critical. Local sociocultural characteristics also include attitudes toward consumerism, environmentalism, and the roles of men and women in society. For example, Coca-Cola and PepsiCo have grown in international markets due to the increasing level of consumerism outside the United States.

Making assumptions about local norms derived from experiences in your home market is a common cause for early failure when entering new markets. However, even home-market norms can change over time, often caused by shifting demographics due to immigration or aging populations.

Technological Factors

The critical role of technology is discussed in more detail later in this section. For now, suffice it to say that technological factors have a major bearing on the threats and opportunities firms encounter. For example, new technology may make it possible for products and services to be made more cheaply and to a better standard of quality. New technology may also provide the opportunity for more innovative products and services, such as online stock trading and remote working. Such changes have the potential to change the face of the business landscape.

Environmental Factors

The environment has long been a factor in firm strategy, primarily from the standpoint of access to raw materials. Increasingly, this factor is best viewed as both a direct and indirect cost for the firm.

Environmental factors are also evaluated on the footprint left by a firm on its respective surroundings. For consumer-product companies like PepsiCo, for instance, this can encompass the waste-management and organic-farming practices used in the countries where raw materials are obtained. Similarly, in consumer markets, it may refer to the degree to which packaging is biodegradable or recyclable.

Legal Factors

Finally, legal factors reflect the laws and regulations relevant to the region and the organization. Legal factors can include whether the rule of law is well established, how easily or quickly laws and regulations may change, and what the costs of regulatory compliance are. For example, Coca-Cola's market share in Europe is greater than 50 percent; as a result, regulators have asked that the company give shelf space in its coolers to competitive products in order to provide greater consumer choice.[2]

Many of the PESTEL factors are interrelated. For instance, the legal environment is often related to the political environment, where laws and regulations can only change when they're consistent with the political will.

PESTEL and Globalization

Over the past decade, new markets have been opened to foreign competitors, whole industries have been deregulated, and state-run enterprises have been privatized. So, globalization has become a fact of life in almost every industry.[3] This entails much more than

companies simply exporting products to another country. Some industries that aren't normally considered global do, in fact, have strictly domestic players. But these companies often compete alongside firms with operations in multiple countries; in many cases, both sets of firms are doing equally well. In contrast, in a truly global industry, the core product is standardized, the marketing approach is relatively uniform, and competitive strategies are integrated in different international markets.[4] In these industries, competitive advantage clearly belongs to the firms that can compete globally.

A number of factors reveal whether an industry has globalized or is in the process of globalizing. The sidebar below groups globalization factors into four categories: *markets*, *costs*, *governments*, and *competition*. These dimensions correspond well to Thomas Friedman's flatteners (as described in his book *The World Is Flat*), though they are not exhaustive.[5]

Factors Favoring Industry Globalization

1. Markets
    - o Homogeneous customer needs
    - o Global customer needs
    - o Global channels
    - o Transferable marketing approaches
2. Costs
    - o Large-scale and large-scope economies
    - o Learning and experience
    - o Sourcing efficiencies
    - o Favorable logistics
    - o Arbitrage opportunities
    - o High research-and-development (R&D) costs
3. Governments
    - o Favorable trade policies
    - o Common technological standards
    - o Common manufacturing and marketing regulations
4. Competition

o Interdependent countries

o Global competitors[6]

Markets

The more similar markets in different regions are, the greater the pressure for an industry to globalize. Coca-Cola and PepsiCo, for example, are fairly uniform around the world because the demand for soft drinks is largely the same in every country. The airframe-manufacturing industry, dominated by Boeing and Airbus, also has a highly uniform market for its products; airlines all over the world have the same needs when it comes to large commercial jets.

Costs

In both of these industries, costs favor globalization. Coca-Cola and PepsiCo realize economies of scope and scale because they make such huge investments in marketing and promotion. Since they're promoting coherent images and brands, they can leverage their marketing dollars around the world. Similarly, Boeing and Airbus can invest millions in new-product R&D only because the global market for their products is so large.

Governments and Competition

Obviously, favorable trade policies encourage the globalization of markets and industries. Governments, however, can also play a critical role in globalization by determining and regulating technological standards. Railroad gauge—the distance between the two steel tracks—would seem to favor a simple technological standard. In Spain, however, the gauge is wider than in France. Why? Because back in the 1850s, when Spain and neighboring France were hostile to one another, the Spanish government decided that making Spanish railways incompatible with French railways would hinder any French invasion.

These are a few key drivers of industry change. However, there are particular implications of technological and business-model breakthroughs for both the pace and extent of industry change. The *rate* of change may vary significantly from one industry to the next; for instance, the computing industry changes much faster than the steel industry. Nevertheless, change in both fields has prompted complete reconfigurations of industry structure and the competitive positions of various players. The idea that all industries change over time and that business environments are in a constant state of flux is relatively intuitive. As a strategic decision maker, you need to ask yourself this question: how accurately does current industry structure (which is relatively easy to identify) predict future industry conditions?

Importing as a Stealth Form of Internationalization

Ironically, the drivers of globalization have also given rise to a greater level of imports. Globalization in this sense is a very strong flattener. Importing involves the sale of products or services in one country that are sourced in another country. In many ways, importing is a stealth form of internationalization. Firms often claim that they have no international operations and yet—directly or indirectly—base their production or services on inputs obtained from outside their home country. Firms that engage in importing must learn about customs requirements, informed compliance with customs regulations, entry of goods, invoices, classification and value, determination and assessment of duty, special requirements, fraud, marketing, trade finance and insurance, and foreign trade zones. Importing can take many forms—from the sourcing of components, machinery, and raw materials to the purchase of finished goods for domestic resale and the outsourcing of production or services to nondomestic providers.

Outsourcing occurs when a company contracts with a third party to do some work on its behalf. The outsourcer may do the work within the same country or may take the work to another country (i.e., offshoring). Offshoring occurs when you take a function out of your country of residence to be performed in another country, generally at a lower cost. International outsourcing, or outsourcing work to a nondomestic third party, has become very visible in business and corporate strategy in recent years. But it's not a new phenomenon; for decades, Nike has been designing shoes and other apparel that are manufactured abroad. Similarly, Pacific Cycle doesn't make a single Schwinn or Mongoose bicycle in the United States but instead imports them entirely from manufacturers in Taiwan and China. It may seem as if international outsourcing is new because businesses are now more often outsourcing services, components, and raw materials from countries with developing economies (e.g., China, Brazil, and India).

In addition to factors of production, information technologies (IT)—such as telecommunications and the widespread diffusion of the Internet—have provided the impetus for outsourcing services. Business-process outsourcing (BPO) is the delegation of one or more IT-intensive business processes to an external provider that in turn owns, administers, and manages the selected process on the basis of defined and measurable performance criteria. The firms in service and IT-intensive industries—insurance, banking, pharmaceuticals, telecommunications, automotive, and airlines—are among the early adopters of BPO. Of these, insurance and banking are able to generate the bulk of the savings, purely because of the large proportion of processes that they can outsource (i.e., the processing of claims and loans and providing service through call centers). Among those countries housing BPO operations, India experienced the most dramatic growth in services where language skills and education were important. Research firm Gartner anticipates that the BPO market in India will reach $1.8 billion by 2013.[7]

Generally, foreign outsourcing locations tend to be defined by how automated a production process or service can be made and the transportation costs involved. When transportation costs and automation are both high, then the knowledge worker component of the location calculation becomes less important. You can see how you might employ the CAGE framework to evaluate potential outsourcing locations. In some cases, though, firms invest in both plant equipment and the training and development of the local workforce. This becomes important when the broader labor force needs to have a higher level of education to operate complex plant machinery or because a firm's specific technologies also have a cultural component. Brazil is one case in point; Ford, BMW, Daimler, and Cargill have all made significant investments in the educational infrastructure of this significant, emerging economy.[8]

Key Takeaways

- A PESTEL analysis examines a target market's political, economic, social, technological, environmental, and legal dimensions in terms of both its current state and possible trends.
- An understanding of the dimensions of PESTEL helps you better grasp the dimensions on which a target market or industry may be more global or local.
- Importing is a stealth form of international entry, because the factors that favor globalization can also lead to a higher level of imports, and inputs can be sourced from anywhere they have either the lowest cost, highest quality, or some combination of these characteristics.

References

1. Mason Carpenter, Talya Bauer, and Berrin Erdogan, Principles of Management(Nyack, NY: Unnamed Publisher, 2009), accessed January 5, 2011, http://www.gone.2012books.lardbucket.org/printed-book/127834.

2. "EU Curbs Coca-Cola Market Dominance," Food & Beverage Reporter, August 2005, accessed February 18, 2011, http://www.developtechnology.co.za/index.php?option=com_content&task=view&id=18464&Itemid=101.

3. George S. Yip, "Global Strategy in a World of Nations," Sloan Management Review 31, no. 1 (1989): 29–40.

4. a. Michael E. Porter, Competition in Global Industries (Boston: Harvard Business School Press, 1986

b. Yip, "Global Strategy in a World of Nations," Sloan Management Review 31, no. 1 (1989): 29–40.

5. Thomas L. Friedman, The World Is Flat (New York: Farrar, Straus and Giroux, 2005).

6. a. Michael E. Porter, Competition in Global Industries (Boston: Harvard Business School Press, 1986)

b. George S. Yip, "Global Strategy in a World of Nations," Sloan Management Review31, no. 1 (1989): 29–40.

7. "Indian BPO Market to Grow 25 percent in 2010," Times of India, March 29, 2010, accessed February 17, 2011, http://timesofindia.indiatimes.com/business/india-business/Indian-BPO-market-to-grow-25-in-2010/articleshow/5739043.cms.

8. a. Spencer E. Ante, "IBM Bets on Brazilian Innovation," *BusinessWeek* , August 17, 2009, accessed February 18, 2011, http://www.businessweek.com/technology/content/aug2009/tc20090817_998497.htm

b. "Cargill Annual Report 2006," Cargill website, accessed October 27, 2010, http://www.cargill.com.br/wcm/groups/public/@csf/@brazil/documents/document/br-2006-annual-rpt.pdf

c. "Ford to Raise Brazil Investments by $281 Million," Reuters, April 8, 2010, accessed February 18, 2011, http://www.reuters.com/article/2010/04/08/ford-brazil-idUSN0821323920100408

d. "Cargill Investing $210 Million in Brazilian Plant," Forbes, February 2, 2011, accessed February 18, 2011, http://www.forbes.com/feeds/ap/2011/02/02/business-food-retailers-amp-wholesalers-us-cargill-brazil_8289031.htm.

Source

This chapter was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License from the book 'International Business v. 1.0' published by Saylor Academy, the creator or licensor of this work.

This page titled 6.3: Global Market Opportunity Assessment – PESTEL Analysis is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.4: Global Market Opportunity Assessment – CAGE Analysis

Learning Objectives

After reading this section, students should be able to …

1. know the components of the CAGE analysis.
2. explain the three strategies for handling institutional voids

CAGE Analysis

Pankaj "Megawatt" Ghemawat is an international strategy guru who developed the CAGE framework to offer businesses a way to evaluate countries in terms of the "distance" between them.[1] In this case, distance is defined broadly to include not only the physical geographic distance between countries but also the cultural, administrative (currencies, trade agreements), and economic differences between them. As summarized in Table 6.4.1: "The CAGE Framework", the CAGE (cultural, administrative, geographic, and economic) framework offers a broader view of distance and provides another way of thinking about location and the opportunities and concomitant risks associated with global arbitrage.[2]

Table 6.4.1: The CAGE Framework

Cultural Distance	Administrative Distance	Geographic Distance	Economic Distance
Attributes Creating Distance			
Different languages	Absence of colonial ties	Physical remoteness	Differences in consumer incomes
Different ethnicities; lack of connective ethnic or social networks	Absence of shared monetary or political association	Lack of a common border	Differences in costs and quality of the following: • Natural resources • Financial resources • Human resources • Infrastructure • Intermediate inputs • Information or knowledge
Different religions	Political hostility	Lack of sea or river access	
Different social norms	Government policies	Size of country	
	Institutional weakness	Weak transportation or communication links	
		Differences in climates	
Industries or Products Affected by Distance			
Products have high-linguistic content (TV).	Government involvement is high in industries that are • producers of staple goods (electricity), • producers of other "entitlements" (drugs), • large employers (farming), • large suppliers to government (mass transportation), • national champions (aerospace), • vital to national security (telecommunications), • exploiters of natural resources (oil, mining), and • subject to high-sunk costs (infrastructure).	Products have a low value-of-weight or bulk ratio (cement).	Nature of demand varies with income level (cars).
Products affect cultural or national identity of consumers (foods).		Products are fragile or perishable (glass or fruit).	Economies of standardization or scale are important (mobile phones).
Product features vary in terms of size (cars), standards (electrical appliances), or packaging.		Communications and connectivity are important (financial services).	Labor and other factor cost differences are salient (garments).
Products carry country-specific quality associations (wines).		Local supervision and operational requirements are high (many services).	Distribution or business systems are different (insurance).

Cultural Distance	Administrative Distance	Geographic Distance	Economic Distance
			Companies need to be responsive and agile (home appliances).

Source: Recreated from Pankaj Ghemawat, "Distance Still Matters," Harvard Business Review 79, no. 8 (September 2001), accessed February 15, 2011, http://sabanet.unisabana.edu.co/post...%20matters.pdf.

To apply the CAGE framework, identify locations that offer low raw material costs, access to markets or consumers, or other key decision criteria. You might, for instance, determine that you're interested in markets with strong consumer buying power, so you would use per capita income as your first sorting criterion. As a result, you would likely end up with some type of ranking. Ghemawat provides an example for the fast-food industry, where he shows that on the basis of per capita income, countries like Germany and Japan would be the most attractive markets for the expansion of a North American fast-food company. However, when he adjusts this analysis for distance using the CAGE framework, he shows that Mexico ranks as the second most attractive market for international expansion, far ahead of Germany and Japan.[3] Recall though, that any international expansion strategy still needs to be supported by the specific resources and capabilities possessed by the firm, regardless of the picture presented by the CAGE analysis. To understand the usefulness of the CAGE framework, consider Dell and its efforts to compete effectively in China. The vehicles it used to enter China were just as important in its strategy as its choice of geographic arena. For Dell's corporate clients in China, the CAGE framework would likely have revealed relatively little distance on all four dimensions—even geographic—given the fact that many personal-computer components have been sourced from China. However, for the consumer segment, the distance was rather great, particularly on the dimensions of culture, administration, and economics. For example, Chinese consumers didn't buy over the Internet, which is the primary way Dell sells its products in the United States. One possible outcome could have been for Dell to avoid the Chinese consumer market altogether. However, Dell opted to choose a strategic alliance with distributors whose knowledge base and capabilities allowed Dell to better bridge the CAGE-framework distances. Thus the CAGE framework can be used to address the question of where (which arena) and how (by which entry vehicle) to expand internationally.

CAGE Analysis and Institutional Voids

While you can apply CAGE to consider some first-order distances (e.g., physical distance between a company's home market and the new foreign market) or cultural differences (e.g., the differences between home-market and foreign-market customer preferences), you can also apply it to identify institutional differences. Institutional differences include differences in political systems and in financial markets. The greater the distance, the harder it will be to operate in that country. Emerging markets in particular can have greater differences because these countries lack many of the specialized intermediaries that make institutions like financial markets work. Table 6.4.2: "Specialized Intermediaries within a Country or Other Geographic Arena" lists examples of specialized intermediaries for different institutions. If an institution lacks these specialized intermediaries, there is an institutional void. An institutional void refers to the absence of key specialized intermediaries found in the markets of finance, managerial talent, and products, which otherwise reduce transaction costs.

Table 6.4.2: Specialized Intermediaries within a Country or Other Geographic Arena

Institution	Specialized Intermediary
Financial markets	• Venture-capital firms • Private equity providers • Mutual funds • Banks • Auditors • Transparent corporate governance
Markets for managerial talent	• Management institute or business schools • Certification agencies • Headhunting firms • Relocation agencies
Markets for products	• Certification agencies • Consumer reports • Regulatory authorities (e.g., the Food and Drug Administration) • Extrajudicial dispute resolution services
All markets	• Legal and judiciary (for property rights protection and enforcement)

Three Strategies for Handling Institutional Voids

When a firm detects an institutional void, it has three choices for how to proceed in regard to the potential target market: (1) adapt its business model, (2) change the institutional context, or (3) stay away.

For example, when McDonald's tried to enter the Russian market, it found an institutional void: a lack of local suppliers to provide the food products it needs. Rather than abandoning market entry, McDonald's decided to adapt its business model. Instead of outsourcing supply-chain operations like it does in the United States, McDonald's worked with a joint-venture partner to fill the voids. It imported cattle from Holland and russet potatoes from the United States, brought in agricultural specialists from Canada and Europe to improve Russian farmers' management practices, and lent money to farmers so that they could invest in better seeds and equipment. As a result of establishing its own supply-chain and management systems, McDonald's controlled 80 percent of the Russian fast-food market by 2010. The process, however, took fifteen years and $250 million in investments."[4]

An example of the second approach to dealing with an institutional void—changing the institutional context—is that used by the "Big Four" audit firms (i.e., Ernst & Young, KPMG, Deloitte Touche Tohmatsu, and PricewaterhouseCoopers) when they entered Brazil. At the time, Brazil had a fledgling audit services market. When the four firms set up branches in Brazil, they raised financial reporting and auditing standards across the country, thus bringing a dramatic improvement to the local market.[5]

Finally, the firm can choose the strategy of staying away from a market with institutional voids. For example, The Home Depot's value proposition (i.e., low prices, great service, and good quality) requires institutions like reliable transportation networks (to minimize inventory costs) and the practice of employee stock ownership (which motivates workers to provide great service). The Home Depot has decided to avoid countries with weak logistics systems and poorly developed capital markets because the company would not be able to attain the low cost–great service combination that is its hallmark.[6]

✔ Ethics in Action

Nestlé's Nespresso division is one of the company's fastest-growing divisions. The division makes a single-cup espresso machine along with single-serving capsules of coffees from around the world. Nestlé is headquartered in Switzerland, but the coffee it needs to buy is primarily grown in rural Africa and Latin America. Nespresso set up local facilities in these regions that measure the quality of the coffee. Nespresso also helps local farmers improve the quality of their coffee, and then it pays more for coffee beans that are of higher quality. Nespresso has gone even further by advising farmers on farming practices that improve the yield of beans farmers get per hectare. The results have proven beneficial to all parties: farmers earn more money, Nespresso gets getter quality beans, and the negative environmental impact of the farms has diminished.[7]

Key Takeaways

- CAGE analysis asks you to compare a possible target market to a company's home market on the dimensions of culture, administration, geography, and economy.
- CAGE analysis yields insights in the key differences between home and target markets and allows companies to assess the desirability of that market.
- CAGE analysis can help you identify institutional voids, which might otherwise frustrate internationalization efforts. Institutional differences are important to the extent that the absence of specialized intermediaries can raise transaction costs just as their presence can reduce them.

References

1. Pankaj Ghemawat, "Distance Still Matters," Harvard Business Review 79, no. 8 (September 2001): 1–11.

2. Pankaj Ghemawat, "The Forgotten Strategy," Harvard Business Review 81, no. 11 (September 2003).

3. Pankaj Ghemawat, "Distance Still Matters," Harvard Business Review 79, no. 8 (September 2001): 1–11.

4. a. McDonald's in Russia: Accept or Attempt to Change Market Context?," Economic Times of India, April 30, 2010, accessed February 17, 2011, http://economictimes.indiatimes.com/features/corporate-dossier/McDonalds-in-Russia-Accept-or-attempt-to-change-market-context/articleshow/5874306.cms

b. Tarun Khanna and Krishna G. Palepu, Winning in Emerging Markets: A Road Map for Strategy (Cambridge, MA: Harvard Business School Press, 2010).

5. Tarun Khanna, Krishna G. Palepu, and Jayant Sinha, "Strategies That Fit Emerging Markets," Harvard Business Review 83, no. 6 (June 2005): 2–16.

6. Tarun Khanna, Krishna G. Palepu, and Jayant Sinha, "Strategies That Fit Emerging Markets," Harvard Business Review 83, no. 6 (June 2005): 2–16.

7. Michael E. Porter and Mark R. Kramer, "The Big Idea: Creating Shared Value," Harvard Business Review, January–February 2011, accessed January 23, 2011, http://hbr.org/2011/01/the-big-idea-creating-shared-value/ar/pr .

Source

This chapter was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License from the book 'International Business v. 1.0' published by Saylor Academy, the creator or licensor of this work.

This page titled 6.4: Global Market Opportunity Assessment – CAGE Analysis is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.5: Global Market Opportunity Assessment – Scenario Planning and Analysis

Scenario Planning and Analysis

Learning Objectives

After reading this section, students should be able to …

1. understand the history and role of scenario planning and analysis.
2. explain the six steps of scenario planning and analysis.
3. map scenarios in a two-by-two matrix.

The History and Role of Scenario Planning and Analysis

Strategic leaders use the information revealed by the application of PESTEL analysis, global dimensions, and CAGE analysis to uncover what the traditional SWOT framework calls opportunities and *threats*. A SWOT (strengths, weaknesses, opportunities, and threats) assessment is a strategic-management tool that helps you take stock of an organization's internal characteristics, or its strengths and weaknesses, such that any action plan builds on what it does well while overcoming or working around weaknesses; the SWOT assessment also helps a company assess external environmental conditions, or opportunities and threats, that favor or threaten an organization's strategy. In particular, you can use it to evaluate the implications of your industry analysis, both for your focal firm specifically and for the industry in general. However, a SWOT assessment works best with one situation or scenario and provides little direction when you're uncertain about potential changes to critical features of the scenario. Scenario planning can help in these cases.

Scenario Planning

Scenario planning helps leaders develop a detailed, internally consistent picture of a range of plausible outcomes as an industry evolves over time. You can also incorporate the results of scenario planning into your strategy formulation and implementation. Understanding the PESTEL conditions—as well as the level, pace, and drivers of industry globalization and the CAGE framework—will probably equip you with some insight into the outcomes of certain scenarios. The purpose of scenario planning, however, is to provide a bigger picture—one in which you can see specific trends and uncertainties. Developed in the 1950s at the global petroleum giant Shell, the technique is now regarded as a valuable tool for integrating changes and uncertainties in the external context into overall strategy.[1] Since September 11, 2001, the use of scenario planning has increased in businesses. Analysis of Bain & Company's *Management Tools and Trends Survey* shows that in the post-9/11 period, approximately 70 percent of 8,500 global executives reported that their firms used scenarios, in contrast to a usage rate of less than 50 percent in most of the 1990s.[2] In addition, scenarios ranked fifteenth in satisfaction levels among the twenty-five management tools that Bain examined in 1993, while it ranked eighth in 2006.[3]

Unlike forecasts, scenarios are not straight-line, one-factor projections from present to future. Rather, they are complex, dynamic, interactive stories told from a future perspective. To develop useful scenarios, executives need a rich understanding of their industry along with broad knowledge of the diverse PESTEL and global conditions that are most likely to affect them. The six basic steps in scenario planning are detailed below.

Six Basic Steps of Scenario Planning

- **Step 1.** Choose the target issue, scope and time frame that the scenario will explore. The scope will depend on your level of analysis (i.e., industry, subindustry, or strategic group), the stage of planning, and the nature and degree of uncertainty and the rate of change. Generally, four scenarios are developed and summarized in a grid. The four scenarios reflect the extremes of possible worlds. To fully capture critical possibilities and contingencies, it may be desirable to develop a series of scenario sets.
- **Step 2.** Brainstorm a set of key drivers and decision factors that influence the scenario. This could include social unrest, shifts in power, regulatory change, market or competitive change, and technology or infrastructure change. Other significant changes in external contexts, like natural disasters, might also be considered.
- **Step 3.** Define the two dimensions of greatest uncertainty. These two dimensions form the axes of the scenario framework. These axes should represent two dimensions that provide the greatest uncertainty for the industry. For instance, the example on

the global credit-union industry identifies changes in the playing field and technology as the two greatest areas of uncertainty up through the year 2005.

- **Step 4.** Detail the four quadrants of the scenarios with stories. Describe how the four worlds would look in each scenario. It's often useful to develop a catchy name for each world as a way to further develop its distinctive character. One of the worlds will likely represent a slightly future version of the status quo, while the others will be significant departures from it. As shown in the credit-union scenarios, *Chameleon* describes a world in which both the competitive playing field and technology undergo radical change, while *Wallet Wars* is an environment of intense competition but milder technological change. In contrast, in *Technocracy*, the radical changes are in technology, whereas in *Credit Union Power*, credit unions encounter only minor changes on either front.[4]
- **Step 5.** Identify indicators that could signal which scenario is unfolding. These can either be trigger points that signal the change is taking place or milestones that mean the change is more likely. An indicator may be a large industry supplier like Microsoft picking up a particular but little-known technological standard.
- **Step 6.** Assess the strategic implications of each scenario. Microscenarios may be developed to highlight and address business-unit-specific or industry-segment-specific issues. Consider needed variations in strategies, key success factors, and the development of a flexible, robust strategy that might work across several scenarios.

The process of developing scenarios and then conducting business according to the information that the scenarios reveal makes it easier to identify and challenge questionable assumptions. It also exposes areas of vulnerability (e.g., in a country, an industry, or a company), underscores the interplay of environmental factors and the impact of change, allows for robust planning and contingency preparation, and makes it possible to test and compare strategic options. Scenarios also help firms focus their attention on the trends and uncertainties that are likely to have the greatest potential impact on their future.

Once you've determined your target issue, scope, and time frame, you can draw up a list of driving forces that is as complete as possible and is organized into relevant categories (e.g., science-technology, political-economic, regulatory, consumer-social, or industry-market). As you proceed, be sure to identify *key* driving forces—the ones with the greatest potential to affect the industry, subindustry, or strategic group in which you're interested.

Trends and Uncertainties

Among the driving forces for change, be sure to distinguish between *trends* and *uncertainties*. Trends are forces for change whose direction—and sometimes timing—can be predicted. For example, experts can be reasonably confident in projecting the number of consumers in North America, Europe, and Japan who will be over sixty-five years old in the year 2020 because those people are alive now. If your firm targets these consumers, then the impact of this population growth will be significant to you; you may view it as a key trend. For other trends, you may know the direction but not the pace. China and India, for example, are experiencing a trend of economic growth, and many foreign investments depend on the course of infrastructure development and consumer-spending power in this enormous market. Unfortunately, the future pace of these changes is uncertain.

? Did You Know?

In his book *Africa Rising*, Vijay Mahajan documents how trends surrounding the 900 million African consumers may offer businesses more opportunities than they're currently taking advantage of:

Many tourists come to Africa every year to see the big game there—the elephants, lions, and rhinos. But I came for a different type of big game. I was seeking out the successful enterprises that are identifying and capitalizing on the market opportunities, and seeking lessons from those that are not so successful, too. In Nairobi, Maserame Mouyeme of The Coca-Cola Company told me how important it is 'to walk the market.' Then, in Harare, I first heard the term 'consumer safari' in a meeting with Unilever executives. This is what they call their initiatives to spend a day with consumers in their homes to understand how they use products. Years after I started on this journey, I now had a term to describe the quest I was on. I was on a consumer safari. The market landscape that is Africa is every bit as marvelous and surprising as its geographic landscape. It presents as big an opportunity as China and India.[5]

In contrast, uncertainties—forces for change whose direction and pace are largely unknown—are more important for your scenario. European consumers, for example, tend to distrust the biotechnology industry, and given the number of competing forces at work—

industries, academia, consumer groups, regulators, and so on—it is difficult to predict whether the consumers will be more or less receptive to biotechnology products in the future. Labeling regulations, for instance, may be either strengthened or relaxed in response to changing consumer opinion.

You might also want to consider the possibility of significant disruptions—that is, steep changes that have an important and unalterable impact on the business environment. A major disaster—such as the September 11 terrorist attacks—can spur regulatory and other legal reforms with major and lasting impact on certain technologies and competitive practices. Table 6.5.3: "Developing Scenarios for the Global Credit-Union Industry" provides sample scenarios created for the credit-union industry, providing an idea of how you would do this if asked to apply scenario analysis to another industry setting. As you can see, identifying the entry of new competitors and the impact of technology are the two primary sources of uncertainty about the future.

Table 6.5.3: Developing Scenarios for the Global Credit-Union Industry

CHANGES IN THE PLAYING FIELD

	Minor	**Major**	
TECHNOLOGICAL CHANGE	**Gradual**	**Credit Union Power:** Both technology and the playing field have changed at a moderate pace, making this the most stable scenario. Even with moderate change in these areas, however, the changing basis of competition, new business models, human resources challenges, and industry dynamics are different enough to pose significant challenges for many financial-services companies.	
	Radical	**Technocracy:** The wide-scale adoption of the Internet by US consumers has led to massive technological innovation for financial-services companies, increasing the range of distribution channels as well as the products, services, and geographic scope of financial-services organizations. Regulations and other changes in the playing field, however, have been slow to follow.	

Note: After considering a PESTEL analysis, experts in the credit-union industry would identify the two most significant macroeconomic factors as (1) regulatory factors affecting both the types of businesses that credit unions can compete in and the entry of new players and consolidation of existing ones, and (2) technological factors, or the speed with which new technologies related to banking are both developed and adopted by consumers. These two dimensions define the major areas of uncertainty facing credit union executives in the next decade. Considering those dimensions and following the six basic steps in scenario planning, you might then develop the following four scenarios.

Source: Adapted from "Scenarios for Credit Unions 2010: An Executive Report," Credit Union Executives Society, 2004, accessed May 10, 2011, http://www.dsicu.com/pdfs/2010_Scenarios.pdf.

Key Takeaways

- Scenario planning was developed in the 1950s by Shell as a tool for integrating changes and uncertainties in the external context into overall strategy. Today it ranks among the top ten management tools in the world in terms of usage. Scenarios are complex, dynamic, interactive stories told from a future perspective. To develop useful scenarios, you need a rich understanding of your industry along with broad knowledge of the diverse PESTEL and global conditions that are most likely to affect them.
- The six steps in formulating a scenario plan are the following: (1) choose the target issue, scope, and time frame that the scenario will explore; (2) brainstorm a set of key drivers and decision factors that influence the scenario; (3) define the two dimensions of greatest uncertainty; (4) detail the four quadrants of the scenarios with stories about that future; (5) identify indicators that could signal which scenario is unfolding; and (6) assess the strategic implications of each scenario.
- Considering the distillation of issues and drivers, select two dimensions of change that will serve as the two dimensions of your scenario-planning matrix. You must be able to describe the dimensions as high and low at each extreme.

References

1. a. Paul J. H. Schoemaker, “When and How to Use Scenario Planning: A Heuristic Approach with Illustration,” *Journal of Forecasting* 10, no. 6 (November 1991): 549–64

b. Paul J. H. Schoemaker and Cornelius A. J. M. van der Heijden, “Integrating Scenarios into Strategic Planning at Royal Dutch/Shell,” *Planning Review* 20, no. 3 (1992): 41–46

c. Paul J. H. Schoemaker, “Multiple Scenario Development: Its Conceptual and Behavioral Foundation,” *Strategic Management Journal* 14, no. 3 (March 1993): 193–213.

2. Darrell Rigby and Barbara Bilodeau, “A Growing Focus on Preparedness,” Harvard Business Review 85 (July–August 2007).

3. Darrell Rigby and Barbara Bilodeau, “A Growing Focus on Preparedness,” *Harvard Business Review* 85 (July–August 2007): 21–22.

4. Scenarios for Credit Unions 2010: An Executive Report,” Credit Union Executives Society, 2004, accessed May 10, 2011, http://www.dsicu.com/pdfs/2010_Scenarios.pdf.

5. Vijay Mahajan, *Africa Rising: How 900 Million African Consumers Offer More Than You Think* (Upper Saddle River, NJ: Pearson Prentice Hall, 2008), xii.

Source

This chapter was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License from the book ‘International Business v. 1.0’ published by Saylor Academy, the creator or licensor of this work.

This page titled 6.5: Global Market Opportunity Assessment – Scenario Planning and Analysis is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.6: Selecting the Countries to Enter

Learning Objectives

After reading this section, students should be able to …

1. conduct a preliminary screening to select countries to enter
2. conduct a Country Attractiveness Analysis to select countries to enter
3. make the final selection of countries to enter

In this section, we introduce a new tool, the 'Country Attractiveness Analysis (CAA)', which provides in-depth screening models for selecting and entering foreign markets. The process for evaluating foreign markets for potential entry typically consists of three stages – the Preliminary Screening stage, the in-depth screening page and the final selection.

Preliminary Screening

In the Preliminary Screening stage, potential countries are evaluated on macro-level indicators such as political stability, economic development, geographic distance, etc. The preliminary analysis can include one or more of the tools that were presented in the previous sections of this chapter – e.g., the PESTEL Analysis, the CAGE Analysis, and/or the Scenario Planning and Analysis.

Countries that pass through the preliminary screening process are then examined in more detail during the In-depth Screening stage. In the second stage, criteria specific to market success for the industry and product markets are identified, and countries are evaluated on them. The in-depth screening process is the core of country attractiveness analysis, since it brings to bear criteria that management feels are critical to business success. Because criteria must be relevant to industry and product market success factors, in-depth screening must be customized and updated.

Country Attractiveness Analysis

Step 1: The first step in conducting the CAA involves in identifying the criteria that are critical to business success. This will be different for different products. For example, the success factors for a toothpaste category would be Consumer Demand, Consumer Access to Supply, Competition, Distance, and Regulation. The specific criteria related to the 'Consumer Demand' of a toothpaste will be population, GDP per capita, GDP growth rate, inflation rate (the lower the better), toothpaste sales growth, toothpaste sales, etc. Similarly, the specific criteria related to the 'Supply' of a toothpaste will be sales-force expenses, average expenses (the lower the better), and distribution fixed costs (the lower the better). The specific criteria related to the 'Competition' factor for a toothpaste will be # of competitors, total marketing expenditures, # of MNCs, and largest competitor's share, the lower the better for all these criteria.

Another example: a company whose niche is luxury goods sold through wholesalers to retail stores and on to end users may identify two important factors: level of affluence and distribution network. Criteria used to assess affluence could be disposable income, income growth, and GDP.

Step 2: The next step is to weight the importance of each criterion. Weighting each criterion is necessary since not all criteria are equally important. Obviously, criteria are selected because they meet some minimum threshold level of importance. Yet some criteria are more important than others, and these differences need to be taken into account. A common approach is to allocate 100 points (or 100%) across all of the criteria, where more points (or a higher percentage) are awarded to criteria that are more important. An ideal way to do this is to first assign weights to the factors so that the sum of all weights adds up to 100%, and then divide the weight of each factor among their criteria.

Step 3: Third, each country needs to be rated on each criterion. The rating is designed to determine how well a country performs or is characterized on a particular criterion. A common rating scale ranges from one to ten, where 1 = very poor and 10 = very good.

Step 4: Finally, calculate the 'Assessment' score for each country by multiplying the weight of each criteria and its rating.

Table 6.6.1: Steps in the CAA

- Identify Factors and criteria
- Weight criteria (allocate 100 points or 100% across all criteria, where more points/percentage points are given to more important criteria) (Tip: Weight factors first)
- Use available data to rate each market opportunity on each criterion. A 10-point scale, where 10 = excellent and 1 = poor can be used.
- Multiply the criterion rating times the criterion weight to derive an assessment score for each criterion
- Sum the criterion assessment scores within each factor to derive factor assessments.
- Sum the factor (or criteria) assessment scores to derive an overall assessment for each market opportunity

Final Selection

Based on the assessment scores calculated for each country, one or more countries can be selected for market entry. The results of the in-depth screening illustrate the relative attractiveness of the countries investigated. Before making investment decisions, due diligence analyses will be performed to better forecast costs, revenues, capital (financial, human) requirements, cash flow, expected rate of return, etc. These forecasts will likely differ depending on entry mode. As due diligence analyses are very complex and time consuming, an important contribution of in-depth screening is to narrow down the number of markets for due diligence analysis.

Table 6.6.2: In-depth screening calculations

Factors/Criteria	Weight	Country 1	Country 2	Country 3	
Rating	Assessment	Rating	Assessment	Rating	Assessment
Factor #1					
Criteria 1.					
Criteria 2.					
Criteria 3.					
Factor #2					
Criteria 1.					
Criteria 2.					
Criteria 3.					
Factor #3	:				
Criteria 1.					
Criteria 2.					
Criteria 3.					
TOTAL	100%	-		-	

This page titled 6.6: Selecting the Countries to Enter is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.7: Global Market Segmentation

Learning Objectives

After reading this section, students should be able to …

1. outline the ways in which markets are segmented.
2. explain why marketers use some segmentation bases versus others.

Segmentation is an important strategic tool in international marketing because the main difference between calling a firm international and global is based on the scope and bases of segmentation. An international firm has different marketing strategies for different segments of countries, while a global firm views the whole world as a market, and then segments this whole world based on viable segmentation bases. Generally, there are three approaches to segmentation in international marketing: macro-segmentation, micro-segmentation and the hybrid approach.

Macro-segmentation:

Macro-segmentation or country-based segmentation identifies clusters of countries that demand similar products. Macro-segmentation uses geographic, demographic and socioeconomic variables such as location, GNP per capita, population size or family size to group countries intro market segments, and then selects one or more segments to create marketing strategies for each of the selected segments. This strategy enables a company to centralize its operations and save on production, sales, logistics and support functions. However, macro-segmentation doesn't take into consideration consumer differences within each country and among the country markets that are clustered together, and fails to acknowledge the existence of segments that go beyond the borders of a particular geographic region. Therefore, the company may be leaving money on the table, because the firm may be losing opportunities to solve the need of consumer segments across these country segments. Macro-segmentation leads to misleading national stereotyping, which results in neglect of within-country heterogeneity. Ignoring similarity in needs across country boundaries results in countries losing economies of scale benefits that can be achieved by serving the needs of a wider population across country (macro-segment) boundaries.

Table 6.7.1:: Macro-segmentation bases

Bases for segmentation	Segment(s) name	Segment description
GNP, GNP distribution, size	Country segments	Individual countries, represent separate segments
GNP. GNP, distribution, size.LDC technology level	Country grouping or clusters	Clusters with similar demographics, cultural patterns
	Import demand, segments	Two stage analysis of import data that includes factor scores and cluster analysis
Geographic proximity, economic integration, development levels	Regional segments	World regions (country groupings with similar characteristics for economies of scale
	Sourcing and purchasing of materials. components. technology	Survey of 135 firms based in 42 countries. Clustering based on sourcing strategics
Cross-cultural patterns	Cultural segments	Similar cultural values and attributes across countries
Levels of economic development and trade	Pro-trade segments	Attitudes toward imported products in developed and developing countries
Product adaptation. country variables	Specialty products and market segments	Product adaptation from one country segment to anothe

Source: Adapted from Hassan, Craft and Kortam (2003)

Micro-segmentation:

Micro-segmentation or consumer-based segmentation involves grouping consumers based on common characteristics using psychographic and/or behavioristic segmentation variables such as cultural preferences, values and attitudes, lifestyle choices. Table 6.7.2: "Micro-segmentation bases" and Table 6.7 "Common Ways of Segmenting Buyers" show some of the different types of buyer characteristics used for micro-segmentation. Notice that the characteristics fall into one of four segmentation categories: behavioral, demographic, geographic, or psychographic.

Table 6.7.2: "Micro-segmentation bases"

Bases for segmentation	Segments) name	Segment description
Lifestyle factors and product benefits	Across countries segmentation	Psychographic segmentation and benefits analysis
	Core value segment	A cross-cultural study of terminal values held by different demographic within country segments
Response* to marketing	Strategically equivalent segment*	Segmentation tag response to a specific marketing mix
	Convenience orientation segment*	A cross-cultural measure of convenience orientation is used to cluster segments based on time-saving orientation and comfort-orientation
	Affinity segment*	Segmentation-based on affinity for advertising
	Consumer-product segments	Segmentation-based on consumer-product relations
Cultural traits	Sensory segments	Divide consumers by the patterns of sensory characteristics that they like the most about a number of products
Attitudes	Attitude clusters	Similar consumer attitudes for specific products across countries
Hybrid factors (values, benefits, demographies, etc.)	Global segments	Profiling of global elites and teenagers
		Two-stage segmentation using environmental and behavioral indicators
Macro-level and micro-level diffusion parameters	Diffusion-based segments	Latent-structure method to accommodate the bass diffusion model

Source: Adapted from Hassan, Craft and Kortam (2003)

We'll discuss each of these categories in a moment. For now, you can get a rough idea of what the categories consist of by looking at them in terms of how marketing professionals might answer the following questions:

•**Behavioral segmentation:**What benefits do customers want, and how do they use our product?
•**Demographic segmentation:** How do the ages, races, and ethnic backgrounds of our customers affect what they buy?
•**Geographic segmentation:** Where are our customers located, and how can we reach them? What products do they buy based on their locations?
• **Psychographic segmentation:** What do our customers think about and value? How do they live their lives?

Table 6.7.3: Common Ways of Segmenting Buyers

By Behavior	By Demographics	By Geography	By Psychographics
• Benefits sought from the product • How often the product is used (usage rate) • Usage situation (daily use, holiday use, etc.) • Buyer's status and loyalty to product (nonuser, potential user, first-time users, regular user)	• Age/generation • Income • Gender • Family life cycle • Ethnicity • Family size • Occupation • Education • Nationality • Religion • Social class	• Region (continent, country, state, neighborhood) • Size of city or town • Population density • Climate	• Activities • Interests • Opinions • Values • Attitudes • Lifestyles

Segmenting by Behavior

Behavioral segmentation divides people and organization into groups according to how they behave with or act toward products. Benefits segmentation—segmenting buyers by the benefits they want from products—is very common. Take toothpaste, for example. Which benefit is most important to you when you buy a toothpaste: The toothpaste's price, ability to whiten your teeth, fight tooth decay, freshen your breath, or something else? Perhaps it's a combination of two or more benefits. If marketing professionals know what those benefits are, they can then tailor different toothpaste offerings to you (and other people like you).

Another way in which businesses segment buyers is by their usage rates—that is, how often, if ever, they use certain products. Companies are interested in frequent users because they want to reach other people like them. They are also keenly interested in nonusers and how they can be persuaded to use products. The way in which people use products can also be a basis for segmentation.

Segmenting by Demographics

Segmenting buyers by personal characteristics such as age, income, ethnicity and nationality, education, occupation, religion, social class, and family size is called demographic segmentation. Demographics are commonly utilized to segment markets because demographic information is publicly available in databases around the world.

Age

At this point in your life, you are probably more likely to buy a car than a funeral plot. Marketing professionals know this. That's why they try to segment consumers by their ages. You're probably familiar with some of the age groups most commonly segmented (see Table 6.7.4: "U.S. Generations and Characteristics") in the United States. Into which category do you fall?

Table 6.7.4: U.S. Generations and Characteristics

Generation	Also Known As	Birth Years	Characteristics
Seniors	"The Silent Generation," "Matures," "Veterans," and "Traditionalists"	1945 and prior	• Experienced very limited credit growing up • Tend to live within their means • Spend more on health care than any other age group • Internet usage rates increasing faster than any other group
Baby Boomers		1946–1964	• Second-largest generation in the United States • Grew up in prosperous times before the widespread use of credit • Account for 50 percent of U.S. consumer spending • Willing to use new technologies as they see fit
Generation X		1965–1979	• Comfortable but cautious about borrowing • Buying habits characterized by their life stages • Embrace technology and multitasking
Generation Y	"Millennials," "Echo Boomers," includes "Tweens" (preteens)	1980–2000	• Largest U.S. generation • Grew up with credit cards • Adept at multitasking; technology use is innate • Ignore irrelevant media
Note: Not all demographers agree on the cutoff dates between the generations.			

Today's college-age students (Generation Y) compose the largest generation. The baby boomer generation is the second largest, and over the course of the last thirty years or so, has been a very attractive market for sellers. Retro brands—old brands or products that companies "bring back" for a period of time—were aimed at baby boomers during the recent economic downturn. Pepsi Throwback and Mountain Dew Throwback, which are made with cane sugar—like they were "back in the good old days"—instead of corn syrup, are examples (Schlacter, 2009). Marketing professionals believe they appealed to baby boomers because they reminded them of better times—times when they didn't have to worry about being laid off, about losing their homes, or about their retirement funds and pensions drying up.

So which group or groups should your firm target? Although it's hard to be all things to all people, many companies try to broaden their customer bases by appealing to multiple generations so they don't lose market share when demographics change. Several companies have introduced lower-cost brands targeting Generation Xers, who have less spending power than boomers. For example, kitchenware and home-furnishings company Williams- Sonoma opened the Elm Street chain, a less-pricey version of the Pottery Barn franchise. The Starwood hotel chain's W hotels, which feature contemporary designs and hip bars, are aimed at Generation Xers (Miller, 2009).

The video game market is very proud of the fact that along with Generation X and Generation Y, many older Americans still play video games. (You probably know some baby boomers who own a Nintendo Wii.) Products and services in the spa market used to

be aimed squarely at adults, but not anymore. Parents are now paying for their tweens to get facials, pedicures, and other pampering in numbers no one in years past could have imagined.

As early as the 1970s, U.S. automakers found themselves in trouble because of changing demographic trends. Many of the companies' buyers were older Americans inclined to "buy American." These people hadn't forgotten that Japan bombed Pearl Harbor during World War II and weren't about to buy Japanese vehicles, but younger Americans were. Plus, Japanese cars had developed a better reputation. Despite the challenges U.S. automakers face today, they have taken great pains to cater to the "younger" generation—today's baby boomers who don't think of themselves as being old. If you are a car buff, you perhaps have noticed that the once-stodgy Cadillac now has a sportier look and stiffer suspension. Likewise, the Chrysler 300 looks more like a muscle car than the old Chrysler Fifth Avenue your great-grandpa might have driven.

Automakers have begun reaching out to Generations X and Y, too. General Motors (GM) has sought to revamp the century-old company by hiring a new younger group of managers—managers who understand how Generation X and Y consumers are wired and what they want. "If you're going to appeal to my daughter, you're going to have to be in the digital world," explained one GM vice president (Cox, 2009).

Income

Tweens might appear to be a very attractive market when you consider they will be buying products for years to come. But would you change your mind if you knew that baby boomers account for 50 percent of all consumer spending in the United States? Americans over sixty-five now control nearly three-quarters of the net worth of U.S. households; this group spends $200 billion a year on major "discretionary" (optional) purchases such as luxury cars, alcohol, vacations, and financial products (Reisenwitz, 2007).

Income is used as a segmentation variable because it indicates a group's buying power and may partially reflect their education levels, occupation, and social classes. Higher education levels usually result in higher paying jobs and greater social status. The makers of upscale products such as Rolexes and Lamborghinis aim their products at high-income groups. However, a growing number of firms today are aiming their products at lower-income consumers. The fastest-growing product in the financial services sector is prepaid debit cards, most of which are being bought and used by people who don't have bank accounts. Firms are finding that this group is a large, untapped pool of customers who tend to be more brand loyal than most. If you capture enough of them, you can earn a profit (von Hoffman, 2006). Based on the targeted market, businesses can determine the location and type of stores where they want to sell their products.

Gender

Gender is another way to segment consumers. Men and women have different needs and also shop differently. Consequently, the two groups are often, but not always, segmented and targeted differently. Marketing professionals don't stop there, though. For example, because women make many of the purchases for their households, market researchers sometimes try to further divide them into subsegments. (Men are also often subsegmented.) For women, those segments might include stay-at-home housewives, plan-to-work housewives, just-a-job working women, and career-oriented working women. Research has found that women who are solely homemakers tend to spend more money, perhaps because they have more time.

Family Life Cycle

Family life cycle refers to the stages families go through over time and how it affects people's buying behavior. For example, if you have no children, your demand for pediatric services (medical care for children) is likely to be slim to none, but if you have children, your demand might be very high because children frequently get sick. You may be part of the target market not only for pediatric services but also for a host of other products, such as diapers, daycare, children's clothing, entertainment services, and educational products. A secondary segment of interested consumers might be grandparents who are likely to spend less on day-to-day childcare items but more on special-occasion gifts for children. Many markets are segmented based on the special events in people's lives. Think about brides (and want-to-be brides) and all the products targeted at them, including Web sites and television shows such as Say Yes to the Dress, My Fair Wedding, Platinum Weddings, and Bridezillas.

Resorts also segment vacationers depending on where they are in their family life cycles. When you think of family vacations, you probably think of Disney resorts. Some vacation properties, such as Sandals, exclude children from some of their resorts. Perhaps

they do so because some studies show that the market segment with greatest financial potential is married couples without children (Hill, et. al., 1990).

Keep in mind that although you might be able to isolate a segment in the marketplace, including one based on family life cycle, you can't make assumptions about what the people in it will want. Just like people's demographics change, so do their tastes. For example, over the past few decades U.S. families have been getting smaller. Households with a single occupant are more commonplace than ever, but until recently, that hasn't stopped people from demanding bigger cars (and more of them) as well as larger houses, or what some people jokingly refer to as "McMansions."

The trends toward larger cars and larger houses appear to be reversing. High energy costs, the credit crunch, and concern for the environment are leading people to demand smaller houses. To attract people such as these, D. R. Horton, the nation's leading homebuilder, and other construction firms are now building smaller homes.

Ethnicity

People's ethnic backgrounds have a big impact on what they buy. If you've visited a grocery store that caters to a different ethnic group than your own, you were probably surprised to see the types of products sold there. It's no secret that the United States is becoming—and will continue to become—more diverse. Hispanic Americans are the largest and the fastest-growing minority in the United States. Companies are going to great lengths to court this once overlooked group. In California, the health care provider Kaiser Permanente runs television ads letting members of this segment know that they can request Spanish-speaking physicians and that Spanish-speaking nurses, telephone operators, and translators are available at all of its clinics (Berkowitz, 2006).

As you can guess, even within various ethnic groups there are many differences in terms of the goods and services buyers choose. Consequently, painting each group with a broad brush would leave you with an incomplete picture of your buyers. For example, although the common ancestral language among the Hispanic segment is Spanish, Hispanics trace their lineages to different countries. Nearly 70 percent of Hispanics in the United States trace their lineage to Mexico; others trace theirs to Central America, South America, and the Caribbean.

Segmenting by Geography

Suppose your great new product or service idea involves opening a local store. Before you open the store, you will probably want to do some research to determine which geographical areas have the best potential. For instance, if your business is a high-end restaurant, should it be located near the local college or country club? If you sell ski equipment, you probably will want to locate your shop somewhere in the vicinity of a mountain range where there is skiing. You might see a snowboard shop in the same area but probably not a surfboard shop. By contrast, a surfboard shop is likely to be located along the coast, but you probably would not find a snowboard shop on the beach.

Geographic segmentation divides the market into areas based on location and explains why the checkout clerks at stores sometimes ask for your zip code. It's also why businesses print codes on coupons that correspond to zip codes. When the coupons are redeemed, the store can find out where its customers are located—or not located. Geocoding is a process that takes data such as this and plots it on a map. Geocoding can help businesses see where prospective customers might be clustered and target them with various ad campaigns, including direct mail. One of the most popular geocoding software programs is PRIZM NE, which is produced by a company called Claritas. PRIZM NE uses zip codes and demographic information to classify the American population into segments. The idea behind PRIZM is that "you are where you live." Combining both demographic and geographic information is referred to as geodemographics or neighborhood geography. The idea is that housing areas in different zip codes typically attract certain types of buyers with certain income levels.

To see how geodemographics works, visit the following page on Claritas' Web site:
***http://www.claritas.com/MyBestSegments/Default.jsp?ID=20*.**

Type in your zip code, and you will see customer profiles of the types of buyers who live in your area. Table 6.7.5: "An Example of Geodemographic Segmentation for 76137 (Fort Worth, TX)" shows the profiles of buyers who can be found the zip code 76137—the "Brite Lites, Li'l City" bunch, and "Home Sweet Home" set. Click on the profiles on the Claritas site to see which one most resembles you.

Table 6.7.5: An Example of Geodemographic Segmentation for 76137 (Fort Worth, TX)

Number	Profile Name
12	Brite Lites, Li'l City
19	Home Sweet Home
24	Up-and-Comers
13	Upward Bound
34	White Picket Fences

The tourism bureau for the state of Michigan was able to identify and target different customer profiles using PRIZM. Michigan's biggest travel segment are Chicagoans in certain zip codes consisting of upper-middle-class households with children—or the "kids in cul-de-sacs" group, as Claritas puts it. The bureau was also able to identify segments significantly different from the Chicago segment, including blue-collar adults in the Cleveland area who vacation without their children. The organization then created significantly different marketing campaigns to appeal to each group.

In addition to figuring out where to locate stores and advertise to customers in that area, geographic segmentation helps firms tailor their products. Chances are you won't be able to find the same heavy winter coat you see at a Walmart in Montana at a Walmart in Florida because of the climate differences between the two places. Market researchers also look at migration patterns to evaluate opportunities. TexMex restaurants are more commonly found in the southwestern United States. However, northern states are now seeing more of them as more people of Hispanic descent move northward.

Segmenting by Psychographics

If your offering fulfills the needs of a specific demographic group, then the demographic can be an important basis for identifying groups of consumers interested in your product. What if your product crosses several market segments? For example, the group of potential consumers for cereal could be "almost" everyone although groups of people may have different needs with regard to their cereal. Some consumers might be interested in the fiber, some consumers (especially children) may be interested in the prize that comes in the box, other consumers may be interested in the added vitamins, and still other consumers may be interested in the type of grains. Associating these specific needs with consumers in a particular demographic group could be difficult. Marketing professionals want to know why consumers behave the way they do, what is of high priority to them, or how they rank the importance of specific buying criteria. Think about some of your friends who seem a lot like you. Have you ever gone to their homes and been shocked by their lifestyles and how vastly different they are from yours? Why are their families so much different from yours?

Psychographic segmentation can help fill in some of the blanks. Psychographic information is frequently gathered via extensive surveys that ask people about their activities, interests, opinion, attitudes, values, and lifestyles. One of the most well-known psychographic surveys is VALS (which originally stood for "Values, Attitudes, and Lifestyles") and was developed by a company called SRI International in the late 1980s. SRI asked thousands of Americans the extent to which they agreed or disagreed with questions similar to the following: "My idea of fun at a national park would be to stay at an expensive lodge and dress up for dinner" and "I could stand to skin a dead animal" (Donnelly, 2002).

Hybrid Segmentation

Hybrid or Universal segmentation looks for similarities across world markets. This strategy solves the disadvantages of using macro- and micro-segmentation bases to segment international markets, as they tend to ignore similarities and highlight only the differences. Certain segments identified in a micro-segmentation strategy may have the same characteristics present on a global scale. One such segment is the Global Teen segment – young people between the ages of 12 and 19. It is likely that a group of teenagers randomly chosen from different parts of the world share many of the same tastes. Another such global segment is the Global Elite segment, comprising affluent consumers who have the money to spend on prestigious products with an image of exclusivity. The global elite segment can be associated with older individuals who have accumulated wealth over the course of a long career, including movie stars, musicians, athletes, and people who have achieved financial success at a relatively young age.

Hybrid segmentation involves looking for similarities across micro–segments identified in the countries selected in the final step of the CAA procedure. Under this process, country borders are honorary, as the segmentation process considers the countries selected in the final step of the CAA procedure as one market and searches for similar segments across these countries.

Footnotes

(1) “Generation Y Lacking Savings,” Fort Worth Star-Telegram, September 13, 2009, 2D.

(2) “Telecommunications Marketing Opportunities to Ethnic Groups: Segmenting Consumer Markets by Ethnicity, Age, Income and Household Buying Patterns, 1998–2003,” The Insight Research Corporation, 2003, http://www.insight-corp.com/reports/ethnic.asp (accessed December 2, 2009).

(3) “Bluetooth Proximity Marketing,” April 24, 2007, http://bluetomorrow.com/bluetooth-ar...marketing.html (accessed December 2, 2009).

(4) “U.S. Framework and VALS™ Type,” Strategic Business Insights, http://www.strategicbusinessinsights.../ustypes.shtml (accessed December 2, 2009).

References

Barry, T., Mary Gilly, and Lindley Doran, “Advertising to Women with Different Career Orientations,” Journal of Advertising Research 25 (April–May 1985): 26–35.

Berkowitz, E. N., The Essentials of Health Care Marketing, 2nd ed. (Sudbury, MA: Jones & Bartlett Publishers, 2006), 13.

Cox, B., “GM Hopes Its New Managers Will Energize It,” Fort Worth Star-Telegram, August 29, 2009, 1C–4C.

Donnelly, J. H., preface to Marketing Management, 9th ed., by J. Paul Peter (New York: McGraw-Hill Professional, 2002), 79.

Harrison, M., Paul Hague, and Nick Hague, “Why Is Business-to-Business Marketing Special?”(whitepaper), B2B International, http://www.b2binternational.com/libr...tepapers04.php (accessed January 27, 2010).

Hill, B. J., Carey McDonald, and Muzzafer Uysal, “Resort Motivations for Different Family Life Cycle Stages,” Visions in Leisure and Business Number 8, no. 4 (1990): 18–27.

Miller R. K. and Kelli Washington, The 2009 Entertainment, Media & Advertising Market Research Handbook, 10th ed. (Loganville, GA: Richard K. Miller & Associates, 2009), 157–66.

Nee, E., “Due Diligence: The Customer Is Always Right,” CIO Insight, May 23, 2003.

Reisenwitz, T., Rajesh Iyer, David B. Kuhlmeier, and Jacqueline K. Eastman, “The Elderly’s Internet Usage: An Updated Look,” Journal of Consumer Marketing, 24, no. 7 (2007): 406–18.

Schlacter, B., “Sugar-Sweetened Soda Is Back in the Mainstream,” Fort Worth Star-Telegram, April 22, 2009, 1C, 5C.

Tornoe, J. G., “Hispanic Marketing Basics: Segmentation of the Hispanic Market,” January 18, 2008, http://learn.latpro.com/segmentation...spanic-market/ (accessed December 2, 2009).

von Hoffman, C., “For Some Marketers, Low Income Is Hot,” Brandweek, September 11, 2006, http://cfsinnovation.com/content/som...low-income-hot (accessed December 2, 2009).

Source

6.6 Global Market Segmentation is adapted from the chapter ‘Chapter 5: Market Segmenting, Targeting, and Positioning’ from the textbook ‘Principles of Marketing,’ authored by University of Minnesota Libraries Publishing edition, 2015 – this book was adapted from a work originally produced in 2010 by a publisher who has requested that it not receive attribution.

The following changes were made to the most recent edition: Created new title for Figure 6.3: Market segmentation; Created new title for Figure 6.4: Multiple uses; Created new title for Figure 6.5: Segmentation variables; Created new title for Figure 6.6: Marital-status as segmentation; Created new title for Figure 6.7: Family life cycle segmentation; Created new title for Figure 6.8: Proximity marketing; Added learning objectives.

This page titled 6.7: Global Market Segmentation is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.8: Using Demographics to Guide Global Marketing Strategy

Learning Objectives

After reading this section, students should be able to …

1. list the demographic variables to consider for global marketing
2. identify the problems in demographic profiling in global markets

Whether marketing to domestic or international markets, demographic information can provide important insights about a target market and how to address consumer needs. As discussed during this our discussion of consumer behavior, demographics refer to statistical information about the characteristics of a population.

Marketers typically combine several variables to create a demographic profile of a target market. A demographic profile (often shortened to a "demographic") is a term used in marketing and broadcasting to describe a demographic grouping or a market segment. Common demographic variables to consider for global and domestic marketing purposes include the following:

- **Age:** Age bands, such as 18–24, 25–34, etc., are great predictors of interest in some types of products. For example, few teenagers wish to purchase denture cream.
- **Social class:** Social-class bands such as wealthy, middle, and lower classes. The rich, for instance, may want different products than middle and lower classes, and may be willing to pay more.
- **Gender:** Males and females have different physical attributes that require different hygiene and clothing products. They also tend to have distinctive male/female mindsets and roles in the family and household decision making.
- **Religious affiliations:** Religion is linked to individual values as well as holiday celebrations, often tied to consumer preferences and spending patterns.
- **Income brackets:** Indicating level of wealth, disposable income, and quality of life.
- **Education:** Level of education is often tied to consumer preferences, as well as income.
- **Geography:** Area of residence, urban vs. rural, and population density can all be important inputs into marketing strategy and decisions about where and how to target advertising and other elements of the promotion mix.

Demographic research may include a variety of other characteristics used to separate a country's population into groups that fit a company's target customer profile. A demographic profile also provides enough information about the typical member of this group to create a mental picture of this hypothetical aggregate. For example, a marketer might speak of the single, female, middle-class, aged 18–24, college-educated demographic.

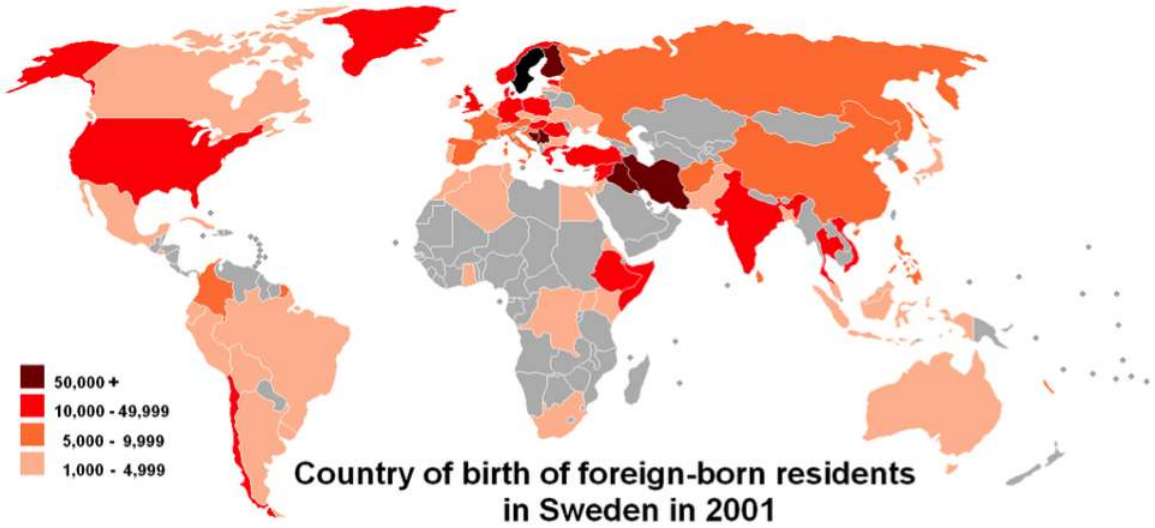


Figure 6.8.1: Country of birth of Swedes in 2001: Demographics can be measured in a variety of ways. The map shows an estimation of foreign-born residents in Sweden.

Researchers examining demographics typically have two objectives in mind: first, to segment the market by determining which subgroups exist in the overall population; and second, to create a clear and complete picture of the characteristics displayed by typical members of each segment. Once these profiles are constructed, marketers can use them to develop the targeting strategy and accompanying marketing strategy and marketing plan.

With demographic profiles about target segments in hand, marketers evaluate the marketing mix. They make recommendations about whether to change, decrease, or increase the goods or services offered. Based on demographic data, marketers may adjust product features, distribution strategy, or other factors in order to reach a market segment that has the most potential.

A demographic profile can be very useful in determining the promotional mix and how to achieve maximum results. Advertising is usually part of the promotional mix, especially when businesses are still in the early stages of entering a global market and launching products that are new to that market. Advertisers want to get the most results for their money, and so in global markets as in domestic markets, careful media research is conducted to match the demographic profile of the target market to the demographic profile of the advertising medium.

Cautions About Demographic Profiling in Global Markets

Demographic profiling is essentially an exercise in making generalizations about groups of people. As with all such generalizations, many individuals within these groups will not conform to the profile. Demographic information is aggregate and offers probabilistic data about groups—not specific individuals. Critics of demographic profiling argue that such broad-brush generalizations can only offer limited insight.

Marketers must also be careful to avoid interpreting demographic information using the the mindset of their own “home” cultures. For example, the generalizations that apply to “tweens” (9–12-year-olds) in the U.S. may not apply at all to children in this same age range in other geographies. Similarly, assumptions about how social class affects consumer preferences may be very different in a socially mobile society versus one with very rigid separation between groups from different social classes. Marketing research should seek to understand a complete picture of how demographic characteristics tend to influence consumer behavior in a given market, rather than simply applying stereotypes from elsewhere.

Source

The above content was adapted from textbook content provided by: Lumen Learning. License: CC BY-SA: Attribution-ShareAlike

CC LICENSED CONTENT, SHARED PREVIOUSLY

The Global Marketing Environment: Demographic Factors. Provided by: Lumen Learning. Located at: https://courses.candelalearning.com/...aphic-factors/. License: CC BY-SA: Attribution-ShareAlike

This page titled 6.8: Using Demographics to Guide Global Marketing Strategy is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.9: Target Market Selection

Learning Objectives

After reading this section, students should be able to …

1. explain the principles behind target market selection
2. list the options available for target selection in global markets

Few companies can afford to enter all markets open to them. Even the world's largest companies such as General Electric or Nestlé must exercise strategic discipline in choosing the markets they serve. They must also decide when to enter them and weigh the relative advantages of a direct or indirect presence in different regions of the world. Small and midsized companies are often constrained to an indirect presence; for them, the key to gaining a global competitive advantage is often creating a worldwide resource network through alliances with suppliers, customers, and, sometimes, competitors. What is a good strategy for one company, however, might have little chance of succeeding for another.

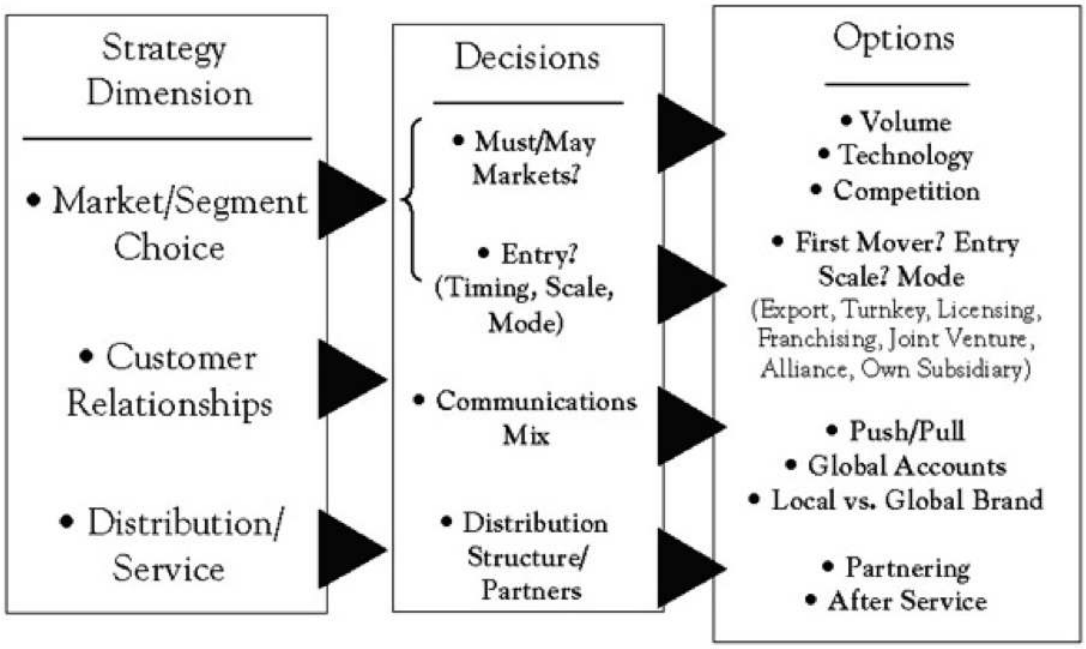


Figure 6.9.1: Market Participation.

The track record shows that picking the most attractive foreign markets, determining the best time to enter them, and selecting the right partners and level of investment has proven difficult for many companies, especially when it involves large emerging markets such as China. For example, it is now generally recognized that Western carmakers entered China far too early and overinvested, believing a "first-mover advantage" would produce superior returns. Reality was very different. Most companies lost large amounts of money, had trouble working with local partners, and saw their technological advantage erode due to "leakage." None achieved the sales volume needed to justify their investment.

Even highly successful global companies often first sustain substantial losses on their overseas ventures, and occasionally have to trim back their foreign operations or even abandon entire countries or regions in the face of ill-timed strategic moves or fast-changing competitive circumstances. Not all of Wal-Mart's global moves have been successful, for example—a continuing source of frustration to investors. In 1999, the company spent $10.8 billion to buy British grocery chain Asda. Not only was Asda healthy and profitable, but it was already positioned as "Wal-Mart lite." Today, Asda is lagging well behind its number-one rival, Tesco. Even though Wal-Mart's UK operations are profitable, sales growth has been down in recent years, and Asda has missed profit targets for several quarters running and is in danger of slipping further in the UK market.

This result comes on top of Wal-Mart's costly exit from the German market. In 2005, it sold its 85 stores there to rival Metro at a loss of $1 billion. Eight years after buying into the highly competitive German market, Wal-Mart executives, accustomed to using Wal-Mart's massive market muscle to squeeze suppliers, admitted they had been unable to attain the economies of scale it needed in Germany to beat rivals' prices, prompting an early and expensive exit.

What makes global market selection and entry so difficult? Research shows there is a pervasive the-grass-is-always-greener effect that infects global strategic decision making in many, especially globally inexperienced, companies and causes them to overestimate the attractiveness of foreign markets. Ghemawat (2001). "Distance," broadly defined, unless well-understood and compensated for, can be a major impediment to global success: cultural differences can lead companies to overestimate the appeal of their products or the strength of their brands; administrative differences can slow expansion plans, reduce the ability to attract the right talent, and increase the cost of doing business; geographic distance impacts the effectiveness of communication and coordination; and economic distance directly influences revenues and costs.

A related issue is that developing a global presence takes time and requires substantial resources. Ideally, the pace of international expansion is dictated by customer demand. Sometimes it is necessary, however, to expand ahead of direct opportunity in order to secure a long-term competitive advantage. But as many companies that entered China in anticipation of its membership in the World Trade Organization have learned, early commitment to even the most promising long-term market makes earning a satisfactory return on invested capital difficult. As a result, an increasing number of firms, particularly smaller and midsized ones, favor global expansion strategies that minimize direct investment. Strategic alliances have made vertical or horizontal integration less important to profitability and shareholder value in many industries. Alliances boost contribution to fixed cost while expanding a company's global reach. At the same time, they can be powerful windows on technology and greatly expand opportunities to create the core competencies needed to effectively compete on a worldwide basis.

Finally, a complicating factor is that a global evaluation of market opportunities requires a multidimensional perspective. In many industries, we can distinguish between "must" markets—markets in which a company must compete in order to realize its global ambitions—and "nice-to-be-in" markets—markets in which participation is desirable but not critical. "Must" markets include those that are critical from a *volume* perspective, markets that define *technological leadership*, and markets in which key *competitive* battles are played out. In the cell phone industry, for example, Motorola looks to Europe as a primary competitive battleground, but it derives much of its technology from Japan and sales volume from the United States.

Source

The above content was adapted from "Target Market Selection", section 5.1 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 6.9: Target Market Selection is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.10: Global Positioning

Learning Objectives

After reading this section, students should be able to …

1. identify the options for positioning in global markets
2. effectively approach the challenges in global posituioning

Johnson & Johnson (J&J) will not sacrifice premium pricing for its well-known brands. It believes that its popular Band-Aid adhesive bandages are superior to competitors' products, and a premium price is a way to signal that. But even in this dimension of its marketing strategy, J&J must allow for some improvisation as it expands around the world and pushes deeper into less-developed countries. Specifically, the company accepts lower margins in a developing market and sometimes delivers a smaller quantity of a product to make it more affordable. For instance, it might sell a four-pack of Band-Aids instead of the larger box it markets in the developed world or a sample-sized bottle of baby shampoo instead of a full-sized one.

Carefully adhering to a particular positioning is both aggregation and adaptation; this creates uniformity in different world markets, but it also serves to define target segments as the company enters new countries or regions. Consider the decision by Diageo, the British beer-and-spirits company, to stick to premium pricing wherever it does business, even when it enters a new market. By projecting a premium positioning for brands such as Johnnie Walker Black, Smirnoff vodka, Captain Morgan rum, Tanqueray gin, and Guinness stout, and foregoing price cutting to grow volume, it identifies loyal consumers who will pay for its well-known products. Rather than sell its products' functional benefits, Diageo successfully markets its drinks as either sophisticated, as it does with Tanqueray, or cool, as it does with Captain Morgan in its recent "Got a Little Captain in You?" ad campaign, Brand managers' high-wire act (2007, October 31).

Mini Case: Global Positioning of Master Card, http://www.leadingglobalbrands.com/

Back in 1997, the MasterCard "brand" did not stand for any one thing. The parent company—MasterCard International—had run through five different advertising campaigns in 10 years and was losing market share at home and abroad. Fixing the brand was a key element of the turnaround. Working with McCann-Erikson, the company developed the highly successful "priceless" campaign. The positioning created by "priceless" allowed MasterCard to integrate all its other campaigns and marketing practices within the United States, and this became a marketing platform that formed the basis for many globalization decisions.

Up until that time, every country used a different agency, a different campaign, and a different strategy. The success of "priceless" as a platform in the United States helped the company persuade other countries to adopt one, single approach, which, over time, produced a consistent global positioning. The "priceless" campaign now appears in more than 100 countries and more than 50 languages and informs all brand communications.

Starting with a locally developed positioning and then successfully expanding it globally is one way to approach the global branding and positioning challenge. More typically, companies start by identifying a unique consumer insight that is globally applicable in order to create a global positioning platform. No matter which route is selected, successful global branding and positioning requires (a) identifying a globally "robust" positioning platform—MasterCard's new positioning was readily accepted across all markets because of the quality of the insight and its instant recognition across cultural boundaries—and (b) clarity about roles and responsibilities for decision making locally and globally. There was a shared understanding of how the primary customer insight should be used at every stage in the process and which aspects of the branding platform were nonnegotiable; expectations for performance were clearly defined and communicated on a global basis; and a strategic partnership with a single advertising agency allowed for consistent, seamless execution around the world.

By providing a single, unifying consumer insight that "defines" the brand's positioning, MasterCard has created economies of scale and scope and, hence, benefited from aggregation principles. The company uses adaptation and arbitrage strategies in its approach to implementation. It empowers local teams by inviting them to create content for their own markets within a proven,

> globally robust positioning framework. Additional, ongoing research generates insights that allow local marketers to create a campaign that they truly feel has local resonance while at the same time maintaining the core brand positioning.

Source

The above content was adapted from “Global Branding Versus Global Positioning”, section 7.1 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

This page titled 6.10: Global Positioning is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

6.11: Basics of Positioning

Learning Objectives

After reading this section, students should be able to …

1. explain why positioning is an important element when it comes to targeting consumers.
2. describe how a product can be positioned and mapped.
3. explain what repositioning is designed is to do.

Why should buyers purchase your offering versus another? If your product faces competition, you will need to think about how to "position" it in the marketplace relative to competing products. After all you don't want the product to be just another "face in the crowd" in the minds of consumers. Positioning is how consumers perceive a product relative to the competition. Companies want to have a distinctive image and offering that stands out from the competition in the minds of consumers.

One way to position your product is to plot customer survey data on a perceptual map. A perceptual map is a two-dimensional graph that visually shows where your product stands, or should stand, relative to your competitors, based on criteria important to buyers. The criteria can involve any number of characteristics—price, quality, level of customer service associated with the product, and so on. An example of a perceptual map is shown in Figure 6.1 "An Example of a Perceptual Map". To avoid head-to-head competition with your competitors, you want to position your product somewhere on the map where your competitors aren't clustered.

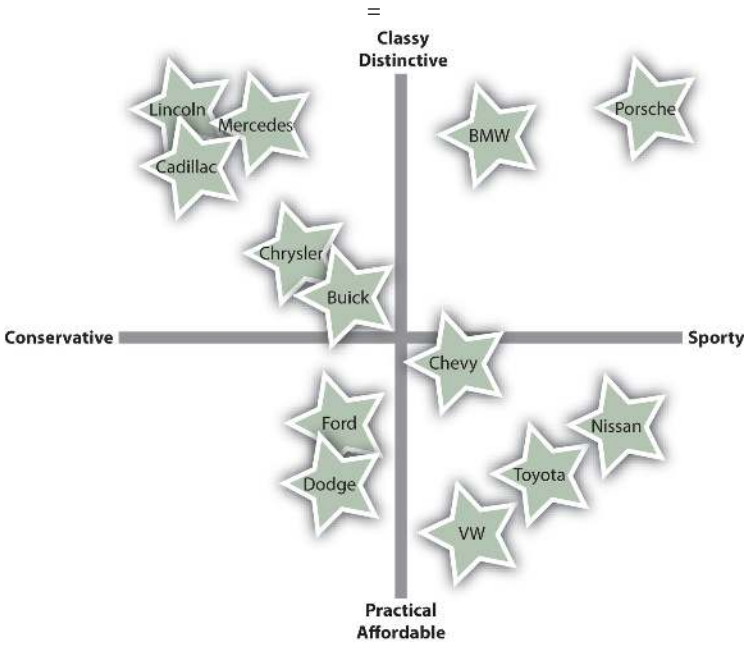


Figure 6.11.1: An Example of a Perceptual Map (Adapted from http://en.Wikipedia.org/wiki/Perceptual_mapping.)

Many companies use taglines in their advertising to try to position their products in the minds of the buyer—where they want them, of course. A tagline is a catchphrase designed to sum up the essence of a product. You perhaps have heard Wendy's tagline "It's better than fast food." The tagline is designed to set Wendy's apart from restaurants like McDonald's and Burger King—to plant the idea in consumers' heads that Wendy's offerings are less "fast foodish," given the bad rap fast food gets these days.

Sometimes firms find it advantageous to reposition their products—especially if they want the product to begin appealing to different market segments. Repositioning is an effort to "move" a product to a different place in the minds of consumers. The i-house, a prefab house built by Clayton Homes, a mobile home manufacturer, is an example. According to the magazine Popular Mechanics, the i-house "looks like a house you'd order from IKEA, sounds like something designed by Apple, and consists of amenities—solar panels, tankless water heaters and rainwater collectors—that one would expect to come from an offbeat green company out of California selling to a high-end market" (Schwartz, 2009). A Clayton Homes spokesperson says, "Are we

repositioning to go after a new market? I would think we are maintaining our value to our existing market and expanding the market to include other buyers that previously wouldn't have considered our housing product (1)."



Figure 6.11.1:*The Clayton i-house: "A Giant Leap from the Trailer Park" (Source: http://www.claytonihouse.com.)*

Recently, Porsche unveiled its new line of Panamera vehicles at a Shanghai car show. The car is a global model, but unlike Porsche's other cars, it's longer. Why? Because rich car buyers in China prefer to be driven by chauffeurs (Gapper, 2009). How do you think Porsche is trying to reposition itself for the future?

Audio Clip : Interview with Apurva Ghelani

Listen to Ghelani's advice to students interested in working in his area of marketing.

? Key Takeaway

- If a product faces competition, its producer will need to think about how to "position" it in the marketplace relative to competing products.
- Positioning is how consumers view a product relative to the competition.
- A perceptual map is a two-dimensional graph that visually shows where a product stands, or should stand, relative to its competitors, based on criteria important to buyers. Sometimes firms find it advantageous to reposition their products.
- Repositioning is an effort to "move" a product to a different place in the minds of consumers.

Footnotes

(1) "Clayton 'i-house' Is Giant Leap from Trailer Park," Knoxvillebiz.com, May 6, 2009, http://www.knoxnews.com/news/2009/may/06/clayton-i-house-giant-leap-trailer-park/ (accessed April 13, 2012).

References

Gapper, J., "Why Brands Now Rise in the East," Financial Times, April 23, 2009, 9.

Schwartz, A., "Clayton Homes' i-house Combines Energy Efficiency and Modular Affordability," Fast Company, May 4, 2009, http://www.fastcompany.com/blog/arie...icient-i-house (accessed December 9, 2009).

Source

Section 6.9 Basics of Positioning is adpated from the chapter 'Chapter 5: Market Segmenting, Targeting, and Positioning' from the textbook 'Principles of Marketing,' authored by University of Minnesota Libraries Publishing edition, 2015 – this book was adapted from a work originally produced in 2010 by a publisher who has requested that it not receive attribution.

The following changes were made to the most recent edition: Created new title for Figure 6.1: Mass marketing; Created new title for Figure 6.2: Targeted Marketing; Created new title for Figure 6.3: Market segmentation; Created new title for Figure 6.4: Multiple uses; Created new title for Figure 6.5: Segmentation variables; Created new title for Figure 6.6: Marital-status as segmentation; Created new title for Figure 6.7: Family life cycle segmentation; Created new title for Figure 6.8: Proximity marketing; Added learning objectives.

This page titled 6.11: Basics of Positioning is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

7: Global Market Entry Modes

7.1: Global Market Entry Modes Summary
7.2: International Entry Modes
7.3: 7.02- Exporting
7.4: Licensing
7.5: Franchising
7.6: Contract Manufacturing
7.7: Joint Ventures

This page titled 7: Global Market Entry Modes is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

7.1: Global Market Entry Modes Summary

Summary

Companies that wish to move beyond exporting and importing can avail themselves of a wide range of alternative market entry strategies. Each alternative has distinct advantages and disadvantages associated with it; the alternatives can be ranked on a continuum representing increasing levels of investment, commitment, and risk. Licensing can generate revenue flow with little new investment; it can be a good choice for a company that possesses advanced technology, a strong brand image, or valuable intellectual property. Contract manufacturing and franchising are two specialized forms of licensing that are widely used in global marketing.

A higher level of involvement outside the home country may involve foreign direct investment. This can take many forms. Joint ventures offer two or more companies the opportunity to share risk and combine value chain strengths. Companies considering joint ventures must plan carefully and communicate with partners to avoid “divorce.” Foreign direct investment can also be used to establish company operations outside the home country through greenfield investment, acquisition of a minority or majority equity stake in a foreign business, or taking full ownership of an existing business entity through merger or outright acquisition.

Cooperative alliances known as strategic alliances, strategic international alliances, and global strategic partnerships (GSPs) represent an important market entry strategy in the twenty-first century. GSPs are ambitious, reciprocal, cross-border alliances that may involve business partners in a number of different country markets. GSPs are particularly well suited to emerging markets in Central and Eastern Europe, Asia, and Latin America. Western businesspeople should also be aware of two special forms of cooperation found in Asia, namely Japan’s keiretsu and South Korea’s chaebol.

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- The course note from the ‘Global Marketing’ course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM). ‘The Economic and Political environment’ is Copyright (c) by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license.

This page titled 7.1: Global Market Entry Modes Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

7.2: International Entry Modes

Learning Objectives

After reading this section, students should be able to …

1. describe the five common international-expansion entry modes.
2. know the advantages and disadvantages of each entry mode.
3. understand the dynamics among the choice of different entry modes.

The Five Common International-Expansion Entry Modes

What is the best way to enter a new market? Should a company first establish an export base or license its products to gain experience in a newly targeted country or region? Or does the potential associated with first-mover status justify a bolder move such as entering an alliance, making an acquisition, or even starting a new subsidiary? Many companies move from exporting to licensing to a higher investment strategy, in effect treating these choices as a learning curve. Each has distinct advantages and disadvantages. In this section, we will explore the traditional international-expansion entry modes. Beyond importing, international expansion is achieved through exporting, licensing arrangements, partnering and strategic alliances, acquisitions, and establishing new, wholly owned subsidiaries, also known as greenfield ventures. These modes of entering international markets and their characteristics are shown in Table 7.2.1: "International-Expansion Entry Modes".[1] Each mode of market entry has advantages and disadvantages. Firms need to evaluate their options to choose the entry mode that best suits their strategy and goals.

Table 7.2.1: International-Expansion Entry Modes

Type of Entry	Advantages	Disadvantages
Exporting	Fast entry, low risk	Low control, low local knowledge, potential negative environmental impact of transportation
Licensing and Franchising	Fast entry, low cost, low risk	Less control, licensee may become a competitor, legal and regulatory environment (IP and contract law) must be sound
Partnering and Strategic Alliance	Shared costs reduce investment needed, reduced risk, seen as local entity	Higher cost than exporting, licensing, or franchising; integration problems between two corporate cultures
Acquisition	Fast entry; known, established operations	High cost, integration issues with home office
Greenfield Venture (Launch of a new, wholly owned subsidiary)	Gain local market knowledge; can be seen as insider who employs locals; maximum control	High cost, high risk due to unknowns, slow entry due to setup time

Exporting

Exporting is the marketing and direct sale of domestically produced goods in another country. Exporting is a traditional and well-established method of reaching foreign markets. Since it does not require that the goods be produced in the target country, no investment in foreign production facilities is required. Most of the costs associated with exporting take the form of marketing expenses.

While relatively low risk, exporting entails substantial costs and limited control. Exporters typically have little control over the marketing and distribution of their products, face high transportation charges and possible tariffs, and must pay distributors for a variety of services. What is more, exporting does not give a company firsthand experience in staking out a competitive position abroad, and it makes it difficult to customize products and services to local tastes and preferences.

Exporting is a typically the easiest way to enter an international market, and therefore most firms begin their international expansion using this model of entry. Exporting is the sale of products and services in foreign countries that are sourced from the home country. The advantage of this mode of entry is that firms avoid the expense of establishing operations in the new country. Firms must, however, have a way to distribute and market their products in the new country, which they typically do through contractual agreements with a local company or distributor. When exporting, the firm must give thought to labeling, packaging, and pricing the offering appropriately for the market. In terms of marketing and promotion, the firm will need to let potential buyers know of its offerings, be it through advertising, trade shows, or a local sales force.

? Amusing Anecdotes

One common factor in exporting is the need to translate something about a product or service into the language of the target country. This requirement may be driven by local regulations or by the company's wish to market the product or service in a locally friendly fashion. While this may seem to be a simple task, it's often a source of embarrassment for the company and humor for competitors. David Ricks's book on international business blunders relates the following anecdote for US companies doing business in the neighboring French-speaking Canadian province of Quebec. A company boasted of *lait frais usage*, which translates to "used fresh milk," when it meant to brag of *lait frais employé*, or "fresh milk used." The "terrific" pens sold by another company were instead promoted as *terrifiantes*, or terrifying. In another example, a company intending to say that its appliance could use "any kind of electrical current," actually stated that the appliance "wore out any kind of liquid." And imagine how one company felt when its product to "reduce heartburn" was advertised as one that reduced "the warmth of heart"![2]

Among the disadvantages of exporting are the costs of transporting goods to the country, which can be high and can have a negative impact on the environment. In addition, some countries impose tariffs on incoming goods, which will impact the firm's profits. In addition, firms that market and distribute products through a contractual agreement have less control over those operations and, naturally, must pay their distribution partner a fee for those services.

✔ Ethics in Action

Companies are starting to consider the environmental impact of where they locate their manufacturing facilities. For example, Olam International, a cashew producer, originally shipped nuts grown in Africa to Asia for processing. Now, however, Olam has opened processing plants in Tanzania, Mozambique, and Nigeria. These locations are close to where the nuts are grown. The result? Olam has lowered its processing and shipping costs by 25 percent while greatly reducing carbon emissions.[3]

Likewise, when Walmart enters a new market, it seeks to source produce for its food sections from local farms that are near its warehouses. Walmart has learned that the savings it gets from lower transportation costs and the benefit of being able to restock in smaller quantities more than offset the lower prices it was getting from industrial farms located farther away. This practice is also a win-win for locals, who have the opportunity to sell to Walmart, which can increase their profits and let them grow and hire more people and pay better wages. This, in turn, helps all the businesses in the local community.[4]

Firms export mostly to countries that are close to their facilities because of the lower transportation costs and the often greater similarity between geographic neighbors. For example, Mexico accounts for 40 percent of the goods exported from Texas.[5] The Internet has also made exporting easier. Even small firms can access critical information about foreign markets, examine a target market, research the competition, and create lists of potential customers. Even applying for export and import licenses is becoming easier as more governments use the Internet to facilitate these processes.

Because the cost of exporting is lower than that of the other entry modes, entrepreneurs and small businesses are most likely to use exporting as a way to get their products into markets around the globe. Even with exporting, firms still face the challenges of currency exchange rates. While larger firms have specialists that manage the exchange rates, small businesses rarely have this expertise. One factor that has helped reduce the number of currencies that firms must deal with was the formation of the European Union (EU) and the move to a single currency, the euro, for the first time. As of 2011, seventeen of the twenty-seven EU members use the euro, giving businesses access to 331 million people with that single currency.[6]

Licensing and Franchising

A company that wants to get into an international market quickly while taking only limited financial and legal risks might consider licensing agreements with foreign companies. An international licensing agreement allows a foreign company (the *licensee*) to sell the products of a producer (the *licensor*) or to use its intellectual property (such as patents, trademarks, copyrights) in exchange for royalty fees. Here's how it works: You own a company in the United States that sells coffee-flavored popcorn. You're sure that your product would be a big hit in Japan, but you don't have the resources to set up a factory or sales office in that country. You can't make the popcorn here and ship it to Japan because it would get stale. So you enter into a licensing agreement with a Japanese company that allows your licensee to manufacture coffee-flavored popcorn using your special process and to sell it in Japan under your brand name. In exchange, the Japanese licensee would pay you a royalty fee.

Licensing essentially permits a company in the target country to use the property of the licensor. Such property is usually intangible, such as trademarks, patents, and production techniques. The licensee pays a fee in exchange for the rights to use the intangible property and possibly for technical assistance as well.

Because little investment on the part of the licensor is required, licensing has the potential to provide a very large return on investment. However, because the licensee produces and markets the product, potential returns from manufacturing and marketing activities may be lost. Thus, licensing reduces cost and involves limited risk. However, it does not mitigate the substantial disadvantages associated with operating from a distance. As a rule, licensing strategies inhibit control and produce only moderate returns.

Another popular way to expand overseas is to sell franchises. Under an international franchise agreement, a company (the *franchiser*) grants a foreign company (the *franchisee*) the right to use its brand name and to sell its products or services. The franchisee is responsible for all operations but agrees to operate according to a business model established by the franchiser. In turn, the franchiser usually provides advertising, training, and new-product assistance. Franchising is a natural form of global expansion for companies that operate domestically according to a franchise model, including restaurant chains, such as McDonald's and Kentucky Fried Chicken, and hotel chains, such as Holiday Inn and Best Western.

Contract Manufacturing and Outsourcing

Because of high domestic labor costs, many U.S. companies manufacture their products in countries where labor costs are lower. This arrangement is called international contract manufacturing or outsourcing. A U.S. company might contract with a local company in a foreign country to manufacture one of its products. It will, however, retain control of product design and development and put its own label on the finished product. Contract manufacturing is quite common in the U.S. apparel business, with most American brands being made in a number of Asian countries, including China, Vietnam, Indonesia, and India.[4]

Thanks to twenty-first-century information technology, nonmanufacturing functions can also be outsourced to nations with lower labor costs. U.S. companies increasingly draw on a vast supply of relatively inexpensive skilled labor to perform various business services, such as software development, accounting, and claims processing. For years, American insurance companies have processed much of their claims-related paperwork in Ireland. With a large, well-educated population with English language skills, India has become a center for software development and customer-call centers for American companies. In the case of India, as you can see in Table 7.2.2: "Selected Hourly Wages, United States and India" , the attraction is not only a large pool of knowledge workers but also significantly lower wages.

Table 7.2.2: Selected Hourly Wages, United States and India

Occupation	U.S. Wage per Hour (per year)	Indian Wage per Hour (per year)
Middle-level manager	$29.40 per hour ($60,000 per year)	$6.30 per hour ($13,000 per year)
Information technology specialist	$35.10 per hour ($72,000 per year)	$7.50 per hour ($15,000 per year)
Manual worker	$13.00 per hour ($27,000 per year)	$2.20 per hour ($5,000 per year)

Source: Data obtained from "Huge Wage Gaps for the Same Work Between Countries – June 2011," WageIndicator.com, http://www.wageindicator.org/main/Wa...ries-June-2011 (Links to an external site.)Links to an external site.(accessed September 20, 2011).

Partnerships and Strategic Alliances

Another way to enter a new market is through a strategic alliance with a local partner. A strategic alliance involves a contractual agreement between two or more enterprises stipulating that the involved parties will cooperate in a certain way for a certain time to achieve a common purpose. To determine if the alliance approach is suitable for the firm, the firm must decide what value the partner could bring to the venture in terms of both tangible and intangible aspects. The advantages of partnering with a local firm are that the local firm likely understands the local culture, market, and ways of doing business better than an outside firm. Partners are especially valuable if they have a recognized, reputable brand name in the country or have existing relationships with customers that the firm might want to access. For example, Cisco formed a strategic alliance with Fujitsu to develop routers for Japan. In the alliance, Cisco decided to co-brand with the Fujitsu name so that it could leverage Fujitsu's reputation in Japan for IT equipment and solutions while still retaining the Cisco name to benefit from Cisco's global reputation for switches and routers.[7] Similarly, Xerox launched signed strategic alliances to grow sales in emerging markets such as Central and Eastern Europe, India, and Brazil.[8]

Strategic alliances and joint ventures have become increasingly popular in recent years. They allow companies to share the risks and resources required to enter international markets. And although returns also may have to be shared, they give a company a degree of flexibility not afforded by going it alone through direct investment.

There are several motivations for companies to consider a partnership as they expand globally, including (a) facilitating market entry, (b) risk and reward sharing, (c) technology sharing, (d) joint product development, and (e) conforming to government regulations. Other benefits include political connections and distribution channel access that may depend on relationships.

Such alliances often are favorable when (a) the partners' strategic goals converge while their competitive goals diverge; (b) the partners' size, market power, and resources are small compared to the industry leaders; and (c) partners are able to learn from one another while limiting access to their own proprietary skills.

What if a company wants to do business in a foreign country but lacks the expertise or resources? Or what if the target nation's government doesn't allow foreign companies to operate within its borders unless it has a local partner? In these cases, a firm might enter into a strategic alliance with a local company or even with the government itself. A strategic alliance is an agreement between two companies (or a company and a nation) to pool resources in order to achieve business goals that benefit both partners. For example, Viacom (a leading global media company) has a strategic alliance with Beijing Television to produce Chinese-language music and entertainment programming.[5]

An alliance can serve a number of purposes:

- Enhancing marketing efforts
- Building sales and market share
- Improving products
- Reducing production and distribution costs
- Sharing technology

Alliances range in scope from informal cooperative agreements to joint ventures—alliances in which the partners fund a separate entity (perhaps a partnership or a corporation) to manage their joint operation. Magazine publisher Hearst, for example, has joint ventures with companies in several countries. So, young women in Israel can read *Cosmo Israel* in Hebrew, and Russian women can pick up a Russian-language version of *Cosmo* that meets their needs. The U.S. edition serves as a starting point to which nationally appropriate material is added in each different nation. This approach allows Hearst to sell the magazine in more than fifty countries.[6]

Strategic alliances are also advantageous for small entrepreneurial firms that may be too small to make the needed investments to enter the new market themselves. In addition, some countries require foreign-owned companies to partner with a local firm if they want to enter the market. For example, in Saudi Arabia, non-Saudi companies looking to do business in the country are required by law to have a Saudi partner. This requirement is common in many Middle Eastern countries. Even without this type of regulation, a local partner often helps foreign firms bridge the differences that otherwise make doing business locally impossible. Walmart, for example, failed several times over nearly a decade to effectively grow its business in Mexico, until it found a strong domestic partner with similar business values.

The disadvantages of partnering, on the other hand, are lack of direct control and the possibility that the partner's goals differ from the firm's goals. David Ricks, who has written a book on blunders in international business, describes the case of a US company eager to enter the Indian market: "It quickly negotiated terms and completed arrangements with its local partners. Certain required documents, however, such as the industrial license, foreign collaboration agreements, capital issues permit, import licenses for machinery and equipment, etc., were slow in being issued. Trying to expedite governmental approval of these items, the US firm agreed to accept a lower royalty fee than originally stipulated. Despite all of this extra effort, the project was not greatly expedited, and the lower royalty fee reduced the firm's profit by approximately half a million dollars over the life of the agreement."[9] Failing to consider the values or reliability of a potential partner can be costly, if not disastrous.

To avoid these missteps, Cisco created one globally integrated team to oversee its alliances in emerging markets. Having a dedicated team allows Cisco to invest in training the managers how to manage the complex relationships involved in alliances. The team follows a consistent model, using and sharing best practices for the benefit of all its alliances.[10]

? Did You Know?

Partnerships in emerging markets can be used for social good as well. For example, pharmaceutical company Novartis crafted multiple partnerships with suppliers and manufacturers to develop, test, and produce antimalaria medicine on a nonprofit basis. The partners included several Chinese suppliers and manufacturing partners as well as a farm in Kenya that grows the medication's key raw ingredient. To date, the partnership, called the Novartis Malaria Initiative, has saved an estimated 750,000 lives through the delivery of 300 million doses of the medication.[11]

The key issues to consider in a joint venture are ownership, control, length of agreement, pricing, technology transfer, local firm capabilities and resources, and government intentions. Potential problems include (a) conflict over asymmetric new investments, (b) mistrust over proprietary knowledge, (c) performance ambiguity, that is, how to "split the pie," (d) lack of parent firm support, (e) cultural clashes, and (f) if, how, and when to terminate the relationship.

Ultimately, most companies will aim at building their own presence through company-owned facilities in important international markets. *Acquisitions* or greenfield start-ups represent this ultimate commitment. Acquisition is faster, but starting a new, wholly owned subsidiary might be the preferred option if no suitable acquisition candidates can be found.

Acquisitions

An acquisition is a transaction in which a firm gains control of another firm by purchasing its stock, exchanging the stock for its own, or, in the case of a private firm, paying the owners a purchase price. In our increasingly flat world, cross-border acquisitions have risen dramatically. In recent years, cross-border acquisitions have made up over 60 percent of all acquisitions completed worldwide. Acquisitions are appealing because they give the company quick, established access to a new market. However, they are expensive, which in the past had put them out of reach as a strategy for companies in the undeveloped world to pursue. What has changed over the years is the strength of different currencies. The higher interest rates in developing nations has strengthened their currencies relative to the dollar or euro. If the acquiring firm is in a country with a strong currency, the acquisition is comparatively cheaper to make. As Wharton professor Lawrence G. Hrebiniak explains, "Mergers fail because people pay too much of a premium. If your currency is strong, you can get a bargain."[12]

When deciding whether to pursue an acquisition strategy, firms examine the laws in the target country. China has many restrictions on foreign ownership, for example, but even a developed-world country like the United States has laws addressing acquisitions. For example, you must be an American citizen to own a TV station in the United States. Likewise, a foreign firm is not allowed to own more than 25 percent of a US airline.[13]

Acquisition is a good entry strategy to choose when scale is needed, which is particularly the case in certain industries (e.g., wireless telecommunications). Acquisition is also a good strategy when an industry is consolidating. Nonetheless, acquisitions are risky. Many studies have shown that between 40 percent and 60 percent of all acquisitions fail to increase the market value of the acquired company by more than the amount invested.[14]

Foreign Direct Investment and Subsidiaries

Many of the approaches to global expansion that we've discussed so far allow companies to participate in international markets without investing in foreign plants and facilities. As markets expand, however, a firm might decide to enhance its competitive advantage by making a direct investment in operations conducted in another country.

Also known as foreign direct investment (FDI), acquisitions and greenfield start-ups involve the direct ownership of facilities in the target country and, therefore, the transfer of resources including capital, technology, and personnel. Direct ownership provides a high degree of control in the operations and the ability to better know the consumers and competitive environment. However, it requires a high level of resources and a high degree of commitment.

Foreign direct investment refers to the formal establishment of business operations on foreign soil—the building of factories, sales offices, and distribution networks to serve local markets in a nation other than the company's home country. On the other hand offshoring occurs when the facilities set up in the foreign country replace U.S. manufacturing facilities and are used to produce goods that will be sent back to the United States for sale. Shifting production to low-wage countries is often criticized as it results in the loss of jobs for U.S. workers.[7]

FDI is generally the most expensive commitment that a firm can make to an overseas market, and it's typically driven by the size and attractiveness of the target market. For example, German and Japanese automakers, such as BMW, Mercedes, Toyota, and Honda, have made serious commitments to the U.S. market: most of the cars and trucks that they build in plants in the South and Midwest are destined for sale in the United States.

A common form of FDI is the foreign subsidiary: an independent company owned by a foreign firm (called the *parent*). This approach to going international not only gives the parent company full access to local markets but also exempts it from any laws or regulations that may hamper the activities of foreign firms. The parent company has tight control over the operations of a subsidiary, but while senior managers from the parent company often oversee operations, many managers and employees are citizens of the host country. Not surprisingly, most very large firms have foreign subsidiaries. IBM and Coca-Cola, for example, have both had success in the Japanese market through their foreign subsidiaries (IBM-Japan and Coca-Cola–Japan). FDI goes in the other direction, too, and many companies operating in the United States are in fact subsidiaries of foreign firms. Gerber Products, for example, is a subsidiary of the Swiss company Novartis, while Stop & Shop and Giant Food Stores belong to the Dutch company Royal Ahold.

Where does most FDI capital end up? Figure 7.2.1: "Where FDI Goes" provides an overview of amounts, destinations (developed or developing countries), and trends.

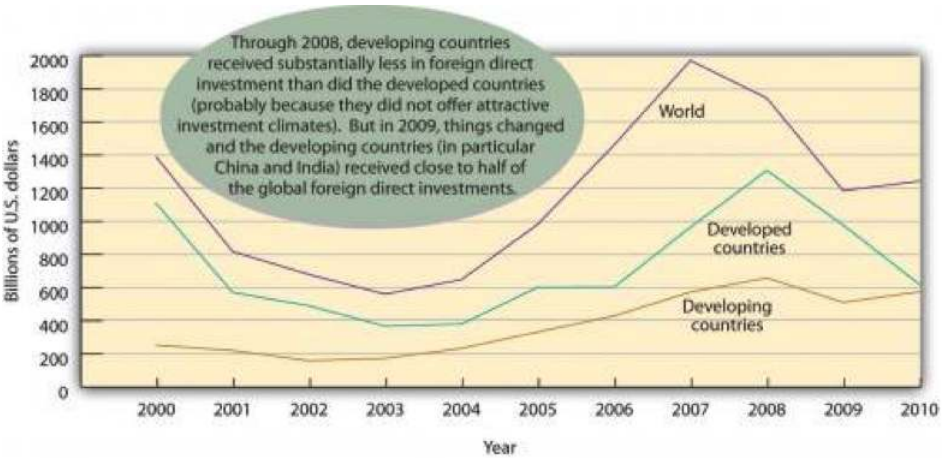


Figure 7.2.1: Where FDI Goes. (Copyright; author via source)

All these strategies have been successful in the arena of global business. But success in international business involves more than merely finding the best way to reach international markets. Doing global business is a complex, risky endeavor. As many companies have learned the hard way, people and organizations don't do things the same way abroad as they do at home. What differences make global business so tricky? That's the question that we'll turn to next.

Wholly Owned Subsidiaries

Firms may want to have a direct operating presence in the foreign country, completely under their control. To achieve this, the company can establish a new, wholly owned subsidiary (i.e., a greenfield venture) from scratch, or it can purchase an existing company in that country. Some companies purchase their resellers or early partners (as Vitrac Egypt did when it bought out the shares that its partner, Vitrac, owned in the equity joint venture). Other companies may purchase a local supplier for direct control of the supply. This is known as vertical integration.

Establishing or purchasing a wholly owned subsidiary requires the highest commitment on the part of the international firm, because the firm must assume all of the risk—financial, currency, economic, and political.

The process of establishing of a new, wholly owned subsidiary is often complex and potentially costly, but it affords the firm maximum control and has the most potential to provide above-average returns. The costs and risks are high given the costs of establishing a new business operation in a new country. The firm may have to acquire the knowledge and expertise of the existing market by hiring either host-country nationals—possibly from competitive firms—or costly consultants. An advantage is that the firm retains control of all its operations.

? Did You Know: McDonald's International

McDonald's has a plant in Italy that supplies all the buns for McDonald's restaurants in Italy, Greece, and Malta. International sales has accounted for as much as 60 percent of McDonald's annual revenue.[15]

Cautions When Purchasing an Existing Foreign Enterprise

As we've seen, some companies opt to purchase an existing company in the foreign country outright as a way to get into a foreign market quickly. When making an acquisition, due diligence is important—not only on the financial side but also on the side of the country's culture and business practices. The annual disposable income in Russia, for example, exceeds that of all the other BRIC countries (i.e., Brazil, India, and China). For many major companies, Russia is too big and too rich to ignore as a market. However, Russia also has a reputation for corruption and red tape that even its highest-ranking officials admit. In a *BusinessWeek* article, presidential economic advisor Arkady Dvorkovich (whose office in the Kremlin was once occupied by Soviet leader Leonid Brezhnev), for example, advises, "Investors should choose wisely" which regions of Russia they locate their business in, warning that some areas are more corrupt than others. Corruption makes the world less flat precisely because it undermines the viability of legal vehicles, such as licensing, which otherwise lead to a flatter world.

The culture of corruption is even embedded into some Russian company structures. In the 1990s, laws inadvertently encouraged Russian firms to establish legal headquarters in offshore tax havens, like Cyprus. A tax haven is a country that has very advantageous (low) corporate income taxes.

Businesses registered in these offshore tax havens to avoid certain Russian taxes. Even though companies could obtain a refund on these taxes from the Russian government, "the procedure is so complicated you never actually get a refund," said Andrey Pozdnyakov, cofounder of Siberian-based Elecard, in the same *BusinessWeek* article.

This offshore registration, unfortunately, is a danger sign to potential investors like Intel. "We can't invest in companies that have even a slight shadow," said Intel's Moscow-based regional director Dmitry Konash about the complex structure predicament. [16]

? Did You Know: Business Collaborations in China

Some foreign companies believe that owning their own operations in China is an easier option than having to deal with a Chinese partner. For example, many foreign companies still fear that their Chinese partners will learn too much from them and become competitors. However, in most cases, the Chinese partner knows the local culture—both that of the customers and workers—and is better equipped to deal with Chinese bureaucracy and regulations. In addition, even wholly owned subsidiaries can't be totally independent of Chinese firms, on whom they might have to rely for raw materials and shipping as well as maintenance of government contracts and distribution channels.

Collaborations offer different kinds of opportunities and challenges than self-handling Chinese operations. For most companies, the local nuances of the Chinese market make some form of collaboration desirable. The companies that opt to

self-handle their Chinese operations tend to be very large and/or have a proprietary technology base, such as high-tech or aerospace companies—for example, Boeing or Microsoft. Even then, these companies tend to hire senior Chinese managers and consultants to facilitate their market entry and then help manage their expansion. Nevertheless, navigating the local Chinese bureaucracy is tough, even for the most-experienced companies.

Let's take a deeper look at one company's entry path and its wholly owned subsidiary in China. Embraer is the largest aircraft maker in Brazil and one of the largest in the world. Embraer chose to enter China as its first foreign market, using the joint-venture entry mode. In 2003, Embraer and the Aviation Industry Corporation of China jointly started the Harbin Embraer Aircraft Industry. A year later, Harbin Embraer began manufacturing aircraft.



Figure 7.2.1:

In 2010, Embraer announced the opening of its first subsidiary in China. The subsidiary, called Embraer China Aircraft Technical Services Co. Ltd., will provide logistics and spare-parts sales, as well as consulting services regarding technical issues and flight operations, for Embraer aircraft in China (both for existing aircraft and those on order). Embraer will invest $18 million into the subsidiary with a goal of strengthening its local customer support, given the steady growth of its business in China.

Guan Dongyuan, president of Embraer China and CEO of the subsidiary, said the establishment of Embraer China Aircraft Technical Services demonstrates the company's "long-term commitment and confidence in the growing Chinese aviation market."[17]

Building Long-Term Relationships

Developing a good relationship with regulators in target countries helps with the long-term entry strategy. Building these relationships may include keeping people in the countries long enough to form good ties, since a deal negotiated with one person may fall apart if that person returns too quickly to headquarters.

? Did You Know: Guanxi

One of the most important cultural factors in China is *guanxi* (pronounced *guan shi*), which is loosely defined as a connection based on reciprocity. Even when just meeting a new company or potential partner, it's best to have an introduction from a common business partner, vendor, or supplier—someone the Chinese will respect. China is a relationship-based society. Relationships extend well beyond the personal side and can drive business as well. With guanxi, a person invests with relationships much like one would invest with capital. In a sense, it's akin to the Western phrase "You owe me one."

Guanxi can potentially be beneficial or harmful. At its best, it can help foster strong, harmonious relationships with corporate and government contacts. At its worst, it can encourage bribery and corruption. Whatever the case, companies without guanxi won't accomplish much in the Chinese market. Many companies address this need by entering into the Chinese market in a collaborative arrangement with a local Chinese company. This entry option has also been a useful way to circumvent

regulations governing bribery and corruption, but it can raise ethical questions, particularly for American and Western companies that have a different cultural perspective on gift giving and bribery.

Mini Case: Coca-Cola and Illy Caffé[18]

In March 2008, the Coca-Cola company and Illy Caffé Spa finalized a joint venture and launched a premium ready-to-drink espresso-based coffee beverage. The joint venture, Ilko Coffee International, was created to bring three ready-to-drink coffee products—Caffè, an Italian chilled espresso-based coffee; Cappuccino, an intense espresso, blended with milk and dark cacao; and Latte Macchiato, a smooth espresso, swirled with milk—to consumers in 10 European countries. The products will be available in stylish, premium cans (150 ml for Caffè and 200 ml for the milk variants). All three offerings will be available in 10 European Coca-Cola Hellenic markets including Austria, Croatia, Greece, and Ukraine. Additional countries in Europe, Asia, North America, Eurasia, and the Pacific were slated for expansion into 2009.

The Coca-Cola Company is the world's largest beverage company. Along with Coca-Cola, recognized as the world's most valuable brand, the company markets four of the world's top five nonalcoholic sparkling brands, including Diet Coke, Fanta, Sprite, and a wide range of other beverages, including diet and light beverages, waters, juices and juice drinks, teas, coffees, and energy and sports drinks. Through the world's largest beverage distribution system, consumers in more than 200 countries enjoy the company's beverages at a rate of 1.5 billion servings each day.

Based in Trieste, Italy, Illy Caffé produces and markets a unique blend of espresso coffee under a single brand leader in quality. Over 6 million cups of Illy espresso coffee are enjoyed every day. Illy is sold in over 140 countries around the world and is available in more than 50,000 of the best restaurants and coffee bars. Illy buys green coffee directly from the growers of the highest quality Arabica through partnerships based on the mutual creation of value. The Trieste-based company fosters long-term collaborations with the world's best coffee growers—in Brazil, Central America, India, and Africa—providing know-how and technology and offering above-market prices.

In summary, when deciding which mode of entry to choose, companies should ask themselves two key questions:

1. How much of our resources are we willing to commit? The fewer the resources (i.e., money, time, and expertise) the company wants (or can afford) to devote, the better it is for the company to enter the foreign market on a contractual basis—through licensing, franchising, management contracts, or turnkey projects.
2. How much control do we wish to retain? The more control a company wants, the better off it is establishing or buying a wholly owned subsidiary or, at least, entering via a joint venture with carefully delineated responsibilities and accountabilities between the partner companies.

Regardless of which entry strategy a company chooses, several factors are always important.

- **Cultural and linguistic differences.** These affect all relationships and interactions inside the company, with customers, and with the government. Understanding the local business culture is critical to success.
- **Quality and training of local contacts and/or employees.** Evaluating skill sets and then determining if the local staff is qualified is a key factor for success.
- **Political and economic issues.** Policy can change frequently, and companies need to determine what level of investment they're willing to make, what's required to make this investment, and how much of their earnings they can repatriate.
- **Experience of the partner company.** Assessing the experience of the partner company in the market—with the product and in dealing with foreign companies—is essential in selecting the right local partner.

Companies seeking to enter a foreign market need to do the following:

- Research the foreign market thoroughly and learn about the country and its culture.
- Understand the unique business and regulatory relationships that impact their industry.
- Use the Internet to identify and communicate with appropriate foreign trade corporations in the country or with their own government's embassy in that country. Each embassy has its own trade and commercial desk. For example, the US Embassy has a foreign commercial desk with officers who assist US companies on how best to enter the local market. These resources are best for smaller companies. Larger companies, with more money and resources, usually hire top consultants to do this for them.

They're also able to have a dedicated team assigned to the foreign country that can travel the country frequently for the later-stage entry strategies that involve investment.

Once a company has decided to enter the foreign market, it needs to spend some time learning about the local business culture and how to operate within it.

Entrepreneurship and Strategy

The Chinese have a "Why not me?" attitude. As Edward Tse, author of *The China Strategy: Harnessing the Power of the World's Fastest-Growing Economy*, explains, this means that "in all corners of China, there will be people asking, 'If Li Ka-shing [the chairman of Cheung Kong Holdings] can be so wealthy, if Bill Gates or Warren Buffett can be so successful, why not me?' This cuts across China's demographic profiles: from people in big cities to people in smaller cities or rural areas, from older to younger people. There is a huge dynamism among them."[19] Tse sees entrepreneurial China as "entrepreneurial people at the grassroots level who are very independent-minded. They're very quick on their feet. They're prone to fearless experimentation: imitating other companies here and there, trying new ideas, and then, if they fail, rapidly adapting and moving on." As a result, he sees China becoming not only a very large consumer market but also a strong innovator. Therefore, he advises US firms to enter China sooner rather than later so that they can take advantage of the opportunities there. Tse says, "Companies are coming to realize that they need to integrate more and more of their value chains into China and India. They need to be close to these markets, because of their size. They need the ability to understand the needs of their customers in emerging markets, and turn them into product and service offerings quickly."[20]

References

- [1]Fine Waters Media, "Bottled Water of France," http://www.finewaters.com/Bottled_Wa...ance/Evian.asp (Links to an external site.)Links to an external site. (accessed May 25, 2006).
- [2]H. Frederick Gale, "China's Growing Affluence: How Food Markets Are Responding" (U.S. Department of Agriculture, June 2003), http://www.ers.usda.gov/Amberwaves/J...gAffluence.htm (Links to an external site.)Links to an external site. (accessed May 25, 2006).
- [3]American Soybean Association, "ASA Testifies on Importance of China Market to U.S. Soybean Exports," June 22, 2010, http://www.soygrowers.com/newsroom/r...es/r062210.htm (Links to an external site.)Links to an external site. (accessed August 21, 2011).
- [4]Gary Gereffi and Stacey Frederick, "The Global Apparel Value Chain, Trade and the Crisis: Challenges and Opportunities for Developing Countries," The World Bank, Development Research Group, Trade and Integration Team, April 2010, http://www.iadb.org/intal/intalcdi/PE/2010/05413.pdf (Links to an external site.)Links to an external site. (accessed August 21, 2011).
- [5]Viacom International, "Viacom Announces a Strategic Alliance for Chinese Content Production with Beijing Television (BTV)," October 16, 2004, http://www.viacom.com/press.tin?ixPr...lease=80454169 (Links to an external site.)Links to an external site..
- [6]Liz Borod, "DA! To the Good Life," *Folio*, September 1, 2004, http://www.keepmedia.com/pubs/Folio/...ba=m&bi=1&bp=7 (Links to an external site.)Links to an external site. (accessed May 25, 2006); Jill Garbi, "Cosmo Girl Goes to Israel," *Folio*, November 1, 2003, http://www.keepmedia.com/pubs/Folio/...ba=m&bi=0&bp=7 (Links to an external site.)Links to an external site. (accessed May 25, 2006); Liz Borod, "A Passage to India," *Folio*, August 1, 2004, http://www.keepmedia.com/pubs/Forbes...ba=a&bi=1&bp=7 (Links to an external site.)Links to an external site. (accessed May 25, 2006); Jill Garbi, "A Sleeping Media Giant?" *Folio*, January 1, 2004, http://www.keepmedia.com/pubs/Folio/...ba=m&bi=0&bp=7 (Links to an external site.)Links to an external site. (accessed May 25, 2006).
- [7]Michael Mandel, "The Real Cost of Offshoring," *Bloomberg BusinessWeek*, June 28, 2007, http://www.businessweek.com/magazine...5/b4039001.htm (Links to an external site.)Links to an external site., (accessed August 21, 2011).
- [8]"Global 500," *Fortune* (CNNMoney), http://money.cnn.com/magazines/fortu...010/full_list/ (Links to an external site.)Links to an external site. (accessed August 21, 2011).
- [9]James C. Morgan and J. Jeffrey Morgan, *Cracking the Japanese Market* (New York: Free Press, 1991), 102.

- [10]“Glocalization Examples—Think Globally and Act Locally,” CaseStudyInc.com, http://www.casestudyinc.com/glocaliz...nd-act-locally (Links to an external site.)Links to an external site. (accessed August 21, 2011).
- [11]McDonald’s India, “Respect for Local Culture,” http://www.mcdonaldsindia.com/loccul.htm (Links to an external site.)Links to an external site. (accessed May 25, 2006).
- [12]McDonald’s Corp., “A Taste of McDonald’s Around the World,” *media.mcdonalds.com*, http://www.media.mcdonalds.com/secur.../international (Links to an external site.)Links to an external site. (accessed May 25, 2006).
- [13]“Glocalization Examples—Think Globally and Act Locally,” CaseStudyInc.com, http://www.casestudyinc.com/glocaliz...nd-act-locally (Links to an external site.)Links to an external site. (accessed August 21, 2011).
- [14]James C. Morgan and J. Jeffrey Morgan, *Cracking the Japanese Market* (New York: Free Press, 1991), 117.
- [15]Anne O. Krueger, “Supporting Globalization” (remarks, 2002 Eisenhower National Security Conference on “National Security for the 21st Century: Anticipating Challenges, Seizing Opportunities, Building Capabilities,” September 26, 2002), http://www.imf.org/external/np/speec...02/092602a.htm (Links to an external site.)Links to an external site. (accessed May 25, 2006).

1. Shaker A. Zahra, R. Duane Ireland, and Michael A. Hitt, “International Expansion by New Venture Firms: International Diversity, Mode of Market Entry, Technological Learning, and Performance,” *Academy of Management Journal* 43, no. 5 (October 2000): 925–50.

2. David A. Ricks, *Blunders in International Business* (Hoboken, NJ: Wiley-Blackwell, 1999), 101.

3. Michael E. Porter and Mark R. Kramer, “The Big Idea: Creating Shared Value,” *Harvard Business Review* , January–February 2011, accessed January 23, 2011, http://hbr.org/2011/01/the-big-idea-creating-shared-value/ar/pr.

4. Michael E. Porter and Mark R. Kramer, “The Big Idea: Creating Shared Value,” *Harvard Business Review* , January–February 2011, accessed January 23, 2011, http://hbr.org/2011/01/the-big-idea-creating-shared-value/ar/pr.

5. Andrew J. Cassey, “Analyzing the Export Flow from Texas to Mexico,” *StaffPAPERS: Federal Reserve Bank of Dallas* , No. 11, October 2010, accessed February 14, 2011, http://www.dallasfed.org/research/st.../staff1003.pdf.

6. “The Euro,” European Commission, accessed February 11, 2011, http://ec.europa.eu/euro/index_en.html.

7. Steve Steinhilber, *Strategic Alliances* (Cambridge, MA: Harvard Business School Press, 2008), 113.

8. “ASAP Releases Winners of 2010 Alliance Excellence Awards,” Association for Strategic Alliance Professionals, September 2, 2010, accessed February 12, 2011, http://newslife.us/technology/mobile/ASAP-Releases-Winners-of-2010-Alliance-Excellence-Awards.

9. David A. Ricks, *Blunders in International Business* (Hoboken, NJ: Wiley-Blackwell, 1999), 101.

10. Steve Steinhilber, *Strategic Alliances* (Cambridge, MA: Harvard Business School Press, 2008), 125.

11. “ASAP Releases Winners of 2010 Alliance Excellence Awards,” Association for Strategic Alliance Professionals, September 2, 2010, accessed September 20, 2010, http://newslife.us/technology/mobile/ASAP-Releases-Winners-of-2010-Alliance-Excellence-Awards.

12. “Playing on a Global Stage: Asian Firms See a New Strategy in Acquisitions Abroad and at Home,” Knowledge@Wharton, April 28, 2010, accessed January 15, 2011, http://knowledge.wharton.upenn.edu/article.cfm?articleid=2473.

13. “Playing on a Global Stage: Asian Firms See a New Strategy in Acquisitions Abroad and at Home,” Knowledge@Wharton, April 28, 2010, accessed January 15, 2011, http://knowledge.wharton.upenn.edu/article.cfm?articleid=2473.

14. “Playing on a Global Stage: Asian Firms See a New Strategy in Acquisitions Abroad and at Home,” *Knowledge@Wharton* , April 28, 2010, accessed January 15, 2011, http://knowledge.wharton.upenn.edu/article.cfm?articleid=2473.

15. Annual revenue in 2008 was $23.5 billion, of which 60 percent was international. Source: Suzanne Kapner, “Making Dough,” Fortune, August 17, 2009, 14.

16. *Source: Carol Matlack, "The Peril and Promise of Investing in Russia," BusinessWeek, October 5, 2009, 48–51.*

17. Source: United Press International, "Brazil's Embraer Expands Aircraft Business into China," July 7, 2010, accessed August 27, 2010, http://www.upi.com/Business_News/2010/07/07/Brazils-Embraer-expands-aircraft-business-into-China/UPI-10511278532701.

18. http://www.thecoca-colacompany.com/; http://www.illy.com/

19. Art Kleiner, "Getting China Right," *Strategy and Business* , March 22, 2010, accessed January 23, 2011, http://www.strategy-business.com/article/00026?pg=al.

20. Art Kleiner, "Getting China Right," Strategy and Business, March 22, 2010, accessed January 23, 2011, http://www.strategy-business.com/article/00026?pg=al.

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- Original content contributed by Lumen Learning
- Content(Links to an external site.)Links to an external site. created by Anonymous under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site.)Links to an external site.
- International Business. **Authored by**: anonymous. **Provided by**: Lardbucket. **Located at**: **License**: **CC BY-NC-SA: Attribution-NonCommercial-ShareAlike**
- International Business v. 1.0' published by Saylor Academy, the creator or licensor of this work.
- "Entry Strategies: Modes of Entry", section 5.3 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.
- 'Fundamentals of Global Strategy v. 1.0' under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.
- Image of Embraer190. **Authored by**: Antonio Milena. **Located at**: **http://en.Wikipedia.org/wiki/Embraer...mbraer_190.jpg**. **License**: **CC BY: Attribution**

This page titled 7.2: International Entry Modes is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

7.3: 7.02- Exporting

Learning Objectives

After reading this section, students should be able to …

1. explain why companies export products
2. state the benefits of exporting
3. state the risks of exporting

Exporting is defined as the sale of products and services in foreign countries that are sourced or made in the home country. Importing is the flipside of exporting. Importing refers to buying goods and services from foreign sources and bringing them back into the home country. Importing is also known as global sourcing.

An Entrepreneur's Import Success Story

Selena Cuffe started her wine import company, Heritage Link Brands, in 2005. Importing wine isn't new, but Cuffe did it with a twist: she focused on importing wine produced by black South Africans. Cuffe got the idea after attending a wine festival in Soweto, where she saw more than five hundred wines from eighty-six producers showcased. Cuffe did some market research and learned of the $3 billion wine industry in Africa. She also saw a gap in the existing market related to wine produced by indigenous African vintners and decided to fill it. She started her company with $70,000, financed through her savings and credit cards. In the first year, sales were only $100,000 but then jumped to $1 million in the second year, when Cuffe sold to more than one thousand restaurants, retailers, and grocery stores. Even better, American Airlines began carrying Cuffe's imported wines on flights, thus providing a steady flow of business amid the more uncertain restaurant market. Cuffe has attributed her success to passion as well as to patience for meeting the multiple regulations required when running an import business.

Exporting is an effective entry strategy for companies that are just beginning to enter a new foreign market. It's a low-cost, low-risk option compared to the other strategies. These same reasons make exporting a good strategy for small and midsize companies that can't or won't make significant financial investment in the international market.

Companies can sell into a foreign country either through a local distributor or through their own salespeople. Many government export-trade offices can help a company find a local distributor. Increasingly, the Internet has provided a more efficient way for foreign companies to find local distributors and enter into commercial transactions.

Distributors are export intermediaries who represent the company in the foreign market. Often, distributors represent many companies, acting as the "face" of the company in that country, selling products, providing customer service, and receiving payments. In many cases, the distributors take title to the goods and then resell them. Companies use distributors because distributors know the local market and are a cost-effective way to enter that market.

However, using distributors to help with export can have its own challenges. For example, some companies find that if they have a dedicated salesperson who travels frequently to the country, they're likely to get more sales than by relying solely on the distributor. Often, that's because distributors sell multiple products and sometimes even competing ones. Making sure that the distributor favors one firm's product over another product can be hard to monitor. In countries like China, some companies find that —culturally—Chinese consumers may be more likely to buy a product from a foreign company than from a local distributor, particularly in the case of a complicated, high-tech product. Simply put, the Chinese are more likely to trust that the overseas salesperson knows their product better.

Why Do Companies Export?

Companies export because it's the easiest way to participate in global trade, it's a less costly investment than the other entry strategies, and it's much easier to simply stop exporting than it is to extricate oneself from the other entry modes. An export partner in the form of either a distributor or an export management company can facilitate this process. An export management company (EMC) is an independent company that performs the duties that a firm's own export department would execute. The EMC handles the necessary documentation, finds buyers for the export, and takes title of the goods for direct export. In return, the EMC charges a

fee or commission for its services. Because an EMC performs all the functions that a firm's export department would, the firm doesn't have to develop these internal capabilities. Most of all, exporting gives a company quick access to new markets.

Benefits of Exporting: Vitrac

Egyptian company Vitrac was founded by Mounir Fakhry Abdel Nour to take advantage of Egypt's surplus fruit products. At its inception, Vitrac sourced local fruit, made it into jam, and exported it worldwide. Vitrac has acquired money, market, and manufacturing advantages from exporting.

- **Market.**The company has access to a new market, which has brought added revenues.
- **Money.**Not only has Vitrac earned more revenue, but it has also gained access to foreign currency, which benefits companies located in certain regions of the world, such as in Vitrac's home country of Egypt.
- **Manufacturing.**The cost to manufacture a given unit decreased because Vitrac has been able to manufacture at higher volumes and buy source materials in higher volumes, thus benefitting from volume discounts.

Risks of Exporting

There are risks in relying on the export option. If you merely export to a country, the distributor or buyer might switch to or at least threaten to switch to a cheaper supplier in order to get a better price. Or someone might start making the product locally and take the market from you. Also, local buyers sometimes believe that a company which only exports to them isn't very committed to providing long-term service and support once a sale is complete. Thus, they may prefer to buy from someone who's producing directly within the country. At this point, many companies begin to reconsider having a local presence, which moves them toward one of the other entry options.

✔ Ethics in Action: Different Countries, Different Food and Drug Rules

Particular products, especially foods and drugs, are often subject to local laws regarding safety, purity, packaging, labeling, and so on. Companies that want to make a product that can be sold in multiple countries must comply with the highest common denominator of all the laws of all the target markets. Complying with the highest standard could increase the overall cost of the product. As a result, some companies opt to stay out of markets where compliance with the regulation would be more costly. Is it ethical to be selling a product in one country that another country deems substandard?

Exporting is a easy way to enter an international market. In addition to exporting, companies can choose to pursue more specialized modes of entry—namely, contracutal modes or investment modes. Contractual modes involve the use of contracts rather than investment. Let's look at the two main contractual entry modes, licensing and franchising.

Source

The above content was adapted from International Business. Authored by: anonymous. Provided by: Lardbucket. Located at: . License: *CC BY-NC-SA: Attribution-NonCommercial-ShareAlike*

This page titled 7.3: 7.02- Exporting is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

7.4: Licensing

Learning Objectives

After reading this section, students should be able to …

1. define licensing
2. explain the advantages and disadvantages of international licensing

Licensing gives a licensee certain rights or resources to manufacture and/or market a certain product in a host country.

Licensing

Licensing is a business arrangement in which one company gives another company permission to manufacture its product for a specified payment. Licensing is defined as the granting of permission by the licenser to the licensee to use intellectual property rights, such as trademarks, patents, brand names, or technology, under defined conditions. The possibility of licensing makes for a flatter world, because it creates a legal vehicle for taking a product or service delivered in one country and providing a nearly identical version of that product or service in another country. Under a licensing agreement, the multinational firm grants rights on its intangible property to a foreign company for a specified period of time. The licenser is normally paid a royalty on each unit produced and sold. Although the multinational firm usually has no ownership interests, it often provides ongoing support and advice. Most companies consider this market-entry option of licensing to be a low-risk option because there's typically no up-front investment.

For a multinational firm, the advantage of licensing is that the company's products will be manufactured and made available for sale in the foreign country (or countries) where the product or service is licensed. The multinational firm doesn't have to expend its own resources to manufacture, market, or distribute the goods. This low cost, of course, is coupled with lower potential returns, because the revenues are shared between the parties.

Licensing generally involves allowing another company to use patents, trademarks, copyrights, designs, and other intellectual in exchange for a percentage of revenue or a fee. It's a fast way to generate income and grow a business, as there is no manufacturing or sales involved. Instead, licensing usually means taking advantage of an existing company's pipeline and infrastructure in exchange for a small percentage of revenue.

An international licensing agreement allows foreign firms, either exclusively or non-exclusively, to manufacture a proprietor's product for a fixed term in a specific market.

To summarize, in this foreign market entry mode, a licensor in the home country makes limited rights or resources available to the licensee in the host country. The rights or resources may include patents, trademarks, managerial skills, technology, and others that can make it possible for the licensee to manufacture and sell in the host country a similar product to the one the licensor has already been producing and selling in the home country without requiring the licensor to open a new operation overseas. The licensor's earnings usually take the form of one-time payments, technical fees, and royalty payments, usually calculated as a percentage of sales.



Figure 7.4.1: Batman (Copyright; author via source)

Batman

The Batman character has been licensed to many companies, such as Lego.

As in this mode of entry the transference of knowledge between the parental company and the licensee is strongly present, the decision of making an international license agreement depend on the respect the host government shows for intellectual property and on the ability of the licensor to choose the right partners and avoid having them compete in each other's market. Licensing is a relatively flexible work agreement that can be customized to fit the needs and interests of both licensor and licensee. The following are the main advantages and reasons to use international licensing for expanding internationally:

- Obtain extra income for technical know-how and services.
- Reach new markets not accessible by export from existing facilities.
- Quickly expand without much risk and large capital investment.
- Pave the way for future investments in the market.
- Retain established markets closed by trade restrictions.
- Political risk is minimized as the licensee is usually 100% locally owned.

This is highly attractive for companies that are new in international business. On the other hand, international licensing is a foreign market entry mode that presents some disadvantages and reasons why companies should not use it because there is:

- Lower income than in other entry modes
- Loss of control of the licensee manufacture and marketing operations and practices leading to loss of quality
- Risk of having the trademark and reputation ruined by an incompetent partner
- The foreign partner also can become a competitor by selling its products in places where the parental company has a presence

KEY POINTS

- Licensing is a business agreement involving two companies: one gives the other special permissions, such as using patents or copyrights, in exchange for payment.
- An international business licensing agreement involves two firms from different countries, with the licensee receiving the rights or resources to manufacture in the foreign country.
- Rights or resources may include patents, copyrights, technology, managerial skills, or other factors necessary to manufacture the good.
- Advantages of expanding internationally using international licensing include: the ability to reach new markets that may be closed by trade restrictions and the ability to expand without too much risk or capital investment.
- Disadvantages include the risk of an incompetent foreign partner firm and lower income compared to other modes of international expansion.

Terms

- *Licensing*: A business arrangement in which one company gives another company permission to manufacture its product for a specified payment.
- *License*: The legal terms under which a person is allowed to use a product.

Examples

- Suppose Company A, a manufacturer and seller of Baubles, was based in the US and wanted to expand to the Chinese market with an international business license. They can enter the agreement with a Chinese firm, allowing them to use their product patent and giving other resources, in return for a payment. The Chinese firm can then manufacture and sell Baubles in China.

Source

The above content was adapted from Boundless Business. Authored by: Boundless. Provided by: Boundless. Located at: https://www.boundless.com/business/. License: CC BY-SA: Attribution-ShareAlike under a Creative Commons Attribution-NonCommercial-ShareAlike License and from International Business. Authored by: anonymous. Provided by: Lardbucket. Located at: . License: CC BY-NC-SA: Attribution-NonCommercial-ShareAlike

Image of Lego Batman. Authored by: Vanessa Oshiro. Located at: https://www.flickr.com/photos/vosh/2...-iPxU5r-bjpvre. License: CC BY-NC-SA: Attribution-NonCommercial-ShareAlike

This page titled 7.4: Licensing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

7.5: Franchising

Learning Objectives

After reading this section, students should be able to …

1. define franchising
2. explain the advantages and disadvantages of international franchising

Franchising is the practice of licensing another firm's business model as an operator.

Franchising is the practice of using another firm's successful business model. For the franchiser, the franchise is an alternative to building "chain stores" to distribute goods that avoids the investments and liability of a chain. The franchiser's success depends on the success of the franchisees. The franchisee is said to have a greater incentive than a direct employee because he or she has a direct stake in the business. Essentially, and in terms of distribution, the franchiser is a supplier who allows an operator, or a franchisee, to use the supplier's trademark and distribute the supplier's goods. In return, the operator pays the supplier a fee.

Similar to a licensing agreement, under a franchising agreement, the multinational firm grants rights on its intangible property, like technology or a brand name, to a foreign company for a specified period of time and receives a royalty in return. The difference is that the franchiser provides a bundle of services and products to the franchisee. For example, McDonald's expands overseas through franchises. Each franchise pays McDonald's a franchisee fee and a percentage of its sales and is required to purchase certain products from the franchiser. In return, the franchisee gets access to all of McDonald's products, systems, services, and management expertise.

In short, in terms of distribution, the franchiser is a supplier who allows an operator, or a franchisee, to use the supplier's trademark and distribute the supplier's goods. In return, the operator pays the supplier a fee.

Each party to a franchise has several interests to protect. The franchiser is involved in securing protection for the trademark, controlling the business concept, and securing know how. The franchisee is obligated to carry out the services for which the trademark has been made prominent or famous. There is a great deal of standardization required. The place of service has to bear the franchiser's signs, logos, and trademark in a prominent place. The uniforms worn by the staff of the franchisee have to be of a particular design and color. The service has to be in accordance with the pattern followed by the franchiser in the successful franchise operations. Thus, franchisees are not in full control of the business, as they would be in retailing.

A service can be successful if equipment and supplies are purchased at a fair price from the franchiser or sources recommended by the franchiser. A coffee brew, for example, can be readily identified by the trademark if its raw materials come from a particular supplier. If the franchiser requires purchase from his stores, it may come under anti-trust legislation or equivalent laws of other countries. So too the purchase of uniforms of personnel, signs, etc., as well as the franchise sites, if they are owned or controlled by the franchiser.

Franchise agreements carry no guarantees or warranties, and the franchisee has little or no recourse to legal intervention in the event of a dispute. Franchise contracts tend to be unilateral contracts in favor of the franchiser, who is generally protected from lawsuits from their franchisees because of the non-negotiable contracts that require franchisees to acknowledge, in effect, that they are buying the franchise knowing that there is risk, and that they have not been promised success or profits by the franchiser. Contracts are renewable at the sole option of the franchiser. Most franchisers require franchisees to sign agreements that mandate where and under what law any dispute would be litigated.

KEY POINTS

- Essentially, and in terms of distribution, the franchiser is a supplier who allows an operator, or a franchisee, to use the supplier's trademark and distribute the supplier's goods. In return, the operator pays the supplier a fee.
- Thirty three countries, including the United States, China, and Australia, have laws that explicitly regulate franchising, with the majority of all other countries having laws which have a direct or indirect impact on franchising.
- Franchise agreements carry no guarantees or warranties, and the franchisee has little or no recourse to legal intervention in the event of a dispute.

Terms

- *Franchisee*: A holder of a franchise; a person who is granted a franchise.
- *Franchising*: The establishment, granting, or use of a franchise.
- *Franchise:* The authorization granted by a company to sell or distribute its goods or services in a certain area.
- *Franchiser:* A franchisor, a company which or person who grants franchises.

Source

The above content was adapted from Boundless Business. Authored by: Boundless. Provided by: Boundless. Located at: https://www.boundless.com/business/. License: CC BY-SA: Attribution-ShareAlike under a Creative Commons Attribution-NonCommercial-ShareAlike License and from International Business. **Authored by**: anonymous. **Provided by**: Lardbucket. **Located at**: . **License**: **CC BY-NC-SA: Attribution-NonCommercial-ShareAlike**

Image of Subway in Russia. **Authored by**: Dgbouma. **Located at**: **http://en.Wikipedia.org/wiki/Subway_...Russia2011.JPG**. **License**: **CC BY-SA: Attribution-ShareAlike**

This page titled 7.5: Franchising is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

7.6: Contract Manufacturing

Learning Objectives

After reading this section, students should be able to …

1. define contract manufacturing
2. explain the advantages and disadvantages of contract manufacturing

In contract manufacturing, a hiring firm makes an agreement with the contract manufacturer to produce and ship the hiring firm's goods.

A contract manufacturer ("CM") is a manufacturer that enters into a contract with a firm to produce components or products for that firm . It is a form of outsourcing. In a contract manufacturing business model, the hiring firm approaches the contract manufacturer with a design or formula. The contract manufacturer will quote the parts based on processes, labor, tooling, and material costs. Typically a hiring firm will request quotes from multiple CMs. After the bidding process is complete, the hiring firm will select a source, and then, for the agreed-upon price, the CM acts as the hiring firm's factory, producing and shipping units of the design on behalf of the hiring firm.

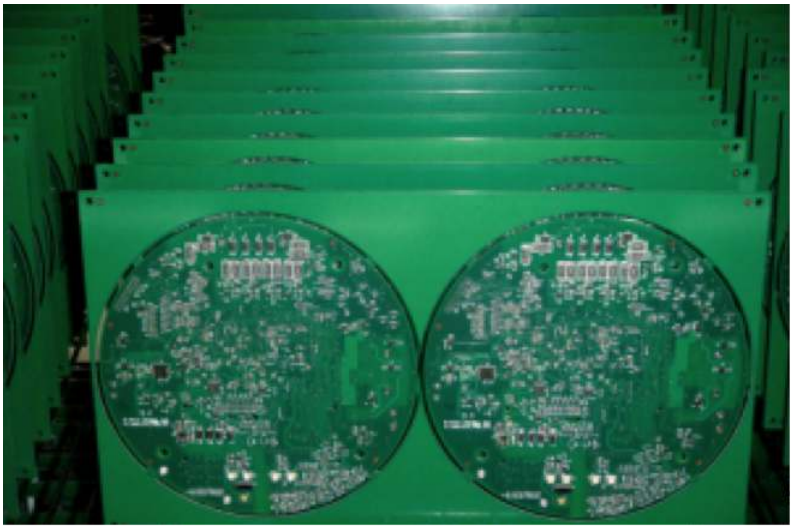


Figure 7.6.1: Printed circuit boards. (CC BY-SA: JayHand: https://en.Wikipedia.org/wiki/Electr...cuit_Board.jpg.

Benefits

Contract manufacturing offers a number of benefits:

- **Cost Savings:** Companies save on their capital costs because they do not have to pay for a facility and the equipment needed for production. They can also save on labor costs such as wages, training, and benefits. Some companies may look to contract manufacture in low-cost countries, such as China, to benefit from the low cost of labor.
- **Mutual Benefit to Contract Site:** A contract between the manufacturer and the company it is producing for may last several years. The manufacturer will know that it will have a steady flow of business at least until that contract expires.
- **Advanced Skills:** Companies can take advantage of skills that they may not possess, but the contract manufacturer does. The contract manufacturer is likely to have relationships formed with raw material suppliers or methods of efficiency within their production.
- **Quality:** Contract Manufacturers are likely to have their own methods of quality control in place that help them to detect counterfeit or damaged materials early.
- **Focus:** Companies can focus on their core competencies better if they can hand off base production to an outside company.
- **Economies of Scale:** Contract Manufacturers have multiple customers that they produce for. Because they are servicing multiple customers, they can offer reduced costs in acquiring raw materials by benefiting from economies of scale. The more units there are in one shipment, the less expensive the price per unit will be.

Risks

Balanced against the above benefits of contract manufacturing are a number of risks:

- **Lack of Control:** When a company signs the contract allowing another company to produce their product, they lose a significant amount of control over that product. They can only suggest strategies to the contract manufacturer; they cannot force them to implement those strategies.
- **Relationships:** It is imperative that the company forms a good relationship with its contract manufacturer. The company must keep in mind that the manufacturer has other customers. They cannot force them to produce their product before a competitor's. Most companies mitigate this risk by working cohesively with the manufacturer and awarding good performance with additional business.
- **Quality:** When entering into a contract, companies must make sure that the manufacturer's standards are congruent with their own. They should evaluate the methods in which they test products to make sure they are of good quality. The company has to ensure the contract manufacturer has suppliers that also meet these standards.
- **Intellectual Property Loss:** When entering into a contract, a company is divulging their formulas or technologies. This is why it is important that a company not give out any of its core competencies to contract manufacturers. It is very easy for an employee to download such information from a computer and steal it. The recent increase in intellectual property loss has corporate and government officials struggling to improve security. Usually, it comes down to the integrity of the employees.
- **Outsourcing Risks:** Although outsourcing to low-cost countries has become very popular, it does bring along risks such as language barriers, cultural differences, and long lead times. This could make the management of contract manufacturers more difficult, expensive, and time-consuming.
- **Capacity Constraints:** If a company does not make up a large portion of the contract manufacturer's business, they may find that they are de-prioritized over other companies during high production periods. Thus, they may not obtain the product they need when they need it.
- **Loss of Flexibility and Responsiveness:** Without direct control over the manufacturing facility, the company will lose some of its ability to respond to disruptions in the supply chain. It may also hurt their ability to respond to demand fluctuations, risking their customer service levels.

? KEY POINTS

- A hiring firm may enter a contract with a contract manufacturer (CM) to produce components or final products on behalf of the hiring firm for some agreed-upon price.
- There are many benefits to contract manufacturing, and companies are finding many reasons why they should be outsourcing their production to other companies.
- Production outside of the company does come with many risks attached. Companies must first identify their core competencies before deciding about contract manufacture.

Terms

- *Contract manufacturing:* Business model in which a firm hires a contract manufacturer to produce components or final products based on the hiring firm's design. A business model where a firm hires another firm to produce components or products.

Source

The above content was adapted from Boundless Business. Authored by: Boundless. Provided by: Boundless. Located at: https://www.boundless.com/business/. License: CC BY-SA: Attribution-ShareAlike under a Creative Commons Attribution-NonCommercial-ShareAlike License.

Image of Circuit Boards. **Authored by**: JayHand. **Located at**: **https://en.Wikipedia.org/wiki/Electr...cuit_Board.jpg**. **License**: **CC BY-SA: Attribution-ShareAlike**

This page titled 7.6: Contract Manufacturing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

7.7: Joint Ventures

Learning Objectives

After reading this section, students should be able to …

1. define joint ventures
2. explain the advantages and disadvantages of joint ventures

In a joint venture business model, two or more parties agree to invest time, equity, and effort for the development of a new shared project.

Joint Ventures

A joint venture is a business agreement in which parties agree to develop a new entity and new assets by contributing equity. They exercise control over the enterprise and consequently share revenues, expenses and assets.

When two or more persons come together to form a partnership for the purpose of carrying out a project, this is called a joint venture. In this scenario, both parties are equally invested in the project in terms of money, time and effort to build on the original concept. While joint ventures are generally small projects, major corporations use this method to diversify. A joint venture can ensure the success of smaller projects for those that are just starting in the business world or for established corporations. Since the cost of starting new projects is generally high, a joint venture allows both parties to share the burden of the project as well as the resulting profits. Since money is involved in a joint venture, it is necessary to have a strategic plan in place. In short, both parties must be committed to focusing on the future of the partnership rather than just the immediate returns. Ultimately, short term and long term successes are both important. To achieve this success, honesty, integrity and communication within the joint venture are necessary.

A consortium JV (also known as a cooperative agreement) is formed when one party seeks technological expertise, franchise and brand-use agreements, management contracts, and rental agreements for one-time contracts. The JV is dissolved when that goal is reached. Some major joint ventures include Dow Corning, Miller Coors, Sony Ericsson, Penske Truck Leasing, Norampac, and Owens-Corning.

An equity joint venture is a contractual, strategic partnership between two or more separate business entities to pursue a business opportunity together. The partners in an equity joint venture each contribute capital and resources in exchange for an equity stake and share in any resulting profits. (In a nonentity joint venture, there is no contribution of capital to form a new entity.)

To see how an equity joint venture works, let's return to the example of Egyptian company, Vitrac. Mounir Fakhry Abdel Nour founded his jam company to take advantage of Egypt's surplus fruit products. Abdel Nour initially approached the French jam company, Vitrac, to enter into a joint venture with his newly founded company, VitracEgypt. Abdel Nour supplied the fruit and the markets, while his French partner supplied the technology and know-how for producing jams.

In addition to exporting to Australia, the United States, and the Middle East, Vitrac began exporting to Japan. Sales results from Japan indicated a high demand for blueberry jam. To meet this demand—in an interesting twist, given Vitrac's origin—Vitrac had to import blueberries from Canada. Vitrac thus was importing blueberries from Canada, manufacturing the jam in Egypt, and exporting it to Japan.[1]

Using French Vitrac's manufacturing know-how, Abdel Nour had found a new supply and the opportunity to enter new markets with it, thus expanding his partner's reach. The partnership fit was good. The two companies' joint venture continued for three years, until the French company sold its shares to Abdel Nour, making Vitrac a 100 percent owned and operated Egyptian company. Abdel Nour's company reached $22 million in sales and was the Egyptian jam-market leader before being bought by a larger Swiss company, Hero.

Risks of Joint Ventures

Equity joint ventures pose both opportunities and challenges for the companies involved. First and foremost is the challenge of finding the right partner—not just in terms of business focus but also in terms of compatible cultural perspectives and management

practices.

Second, the local partner may gain the know-how to produce its own competitive product or service to rival the multinational firm. This is what's currently happening in China. To manufacture cars in China, non-Chinese companies must set up joint ventures with Chinese automakers and share technology with them. Once the contract ends, however, the local company may take the knowledge it gained from the joint venture to compete with its former partner. For example, Shanghai Automotive Industry (Group) Corporation, which worked with General Motors (GM) to build Chevrolets, has pursued plans to increase sales of its own vehicles tenfold to 300,000 in five years and to compete directly with its former partner.[2]

? Did You Know: Joint Ventures in China

In the past, joint ventures were the only relationship foreign companies could form with Chinese companies. In fact, prior to 1986, foreign companies could not wholly own a local subsidiary. The Chinese government began to allow equity joint ventures in 1979, which marked the beginning of the Open Door Policy, an economic liberalization initiative. The Chinese government strongly encouraged equity joint ventures as a way to gain access to the technology, capital, equipment, and know-how of foreign companies. The risk to the foreign company was that if the venture soured, the Chinese company could end up keeping all of these assets. Often, Chinese companies only contributed things like land or tax concessions that foreign companies couldn't keep if the venture ended. As of 2010, equity joint ventures between a Chinese company and a foreign partner require a minimum equity investment by the foreign partner of at least 33 to 70 percent of the equity, but there's no minimum investment set for the Chinese partner.

? KEY TAKEAWAYS

- Joint business ventures involve two parties contributing their own equity and resources to develop a new project. The enterprise, revenues, expenses and assets are shared by the involved parties.
- Since money is involved in a joint venture, it is necessary to have a strategic plan in place.
- As the cost of starting new projects is generally high, a joint venture allows both parties to share the burden of the project as well as the resulting profits.

Term

- *Joint venture*: A cooperative partnership between two individuals or businesses in which profits and risks are shared.

Example

- Sony Ericsson is a joint venture between Swedish telecom corporation Ericsson and Japanese electronics manufacturer Sony

References

1. Source: Japan External Trade Organization, "Big in Japan," case study, accessed August 27, 2010, **http://www.jetro.go.jp/en/reports/**.

2. Source: Ian Rowley, "Chinese Carmakers Are Gaining at Home," BusinessWeek, June 8, 2009, 30–31.

Source

The above content was adapted from Boundless Business. Authored by: Boundless. Provided by: Boundless. Located at: https://www.boundless.com/business/. License: CC BY-SA: Attribution-ShareAlike under a Creative Commons Attribution-NonCommercial-ShareAlike License and from International Business. **Authored by**: anonymous. **Provided by**: Lardbucket. **Located at**: . **License**: **CC BY-NC-SA: Attribution-NonCommercial-ShareAlike**

Image of Sony-Ericsson. **Authored by**: mroach. **Located at**: **http://commons.wikimedia.org/wiki/Fi...csson_sign.jpg**. **License**: **CC BY-SA: Attribution-ShareAlike**

This page titled 7.7: Joint Ventures is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

8: Global Products

8.1: Global Products Summary
8.2: Global Product Development
8.3: Global Products and Services
8.4: Product Adaptation Decisions
8.5: Global Innovation
8.6: Global Innovation at the BOP

This page titled 8: Global Products is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

8.1: Global Products Summary

Summary

The product is the most important element of a company's marketing program. Global marketers face the challenge of formulating coherent product and brand strategies on a worldwide basis. A product can be viewed as a collection of tangible and intangible attributes that collectively provide benefits to a buyer or user. A brand is a complex bundle of images and experiences in the mind of the customer. In most countries, local brands compete with international brands and global brands. A local product is available in a single country; a global product meets the wants and needs of a global market.

Product and communications strategies can be viewed within a framework that allows for combinations of three strategies: extension strategy, adaptation strategy, and creation strategy. Five strategic alternatives are open to companies pursuing geographic expansion: product-communication extension; product extension-communication adaptation; product adaptation-communication extension; product-communication adaptation; and product invention (innovation). The strategic alternative(s) that a particular company chooses will depend on the product and the need it serves, customer preferences and purchasing power, and the costs of adaptation versus standardization. Product transformation occurs when a product that has been introduced into new country markets serves a different function or is used differently than originally intended. When choosing a strategy, management should consciously strive to avoid the "not invented here" syndrome.

Global competition has put pressure on companies to excel at developing standardized product platforms that can serve as a foundation for cost-efficient adaptation. New products can be classified as discontinuous, dynamically continuous, or continuous innovations. A successful product launch requires an understanding of how markets develop: sequentially over time or simultaneously. Today, many new products are launched in multiple national markets as product development cycles shorten and product development costs soar.

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- The course note from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM). 'The Economic and Political environment' is Copyright (c) by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license.

This page titled 8.1: Global Products Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

8.2: Global Product Development

Learning Objectives

After reading this section, students should be able to …

1. appreciate the fundamentals of global product development

Globalization pressures have changed the practice of product development (PD) in many industries in recent years. Eppinger and Chitkara (2006). Rather than using a centralized or local cross-functional model, companies are moving to a mode of global collaboration in which skilled development teams dispersed around the world collaborate to develop new products. Today, a majority of global corporations have engineering and development operations outside of their home region. China and India offer particularly attractive opportunities: Microsoft, Cisco, and Intel all have made major investments there.

The old model was based on the premise that colocation of cross-functional teams to facilitate close collaboration among engineering, marketing, manufacturing, and supply-chain functions was critical to effective product development. Colocated PD teams were thought to be more effective at concurrently executing the full range of activities involved, from understanding market and customer needs through conceptual and detailed design, testing, analysis, prototyping, manufacturing engineering, and technical product support and engineering. Such colocated concurrent practices were thought to result in better product designs, faster time to market, and lower-cost production. They were generally located in corporate research and development centers, which maintained linkages to manufacturing sites and sales offices around the world.

Today, best practice emphasizes a highly distributed, networked, and digitally supported development process. The resulting global product development process combines centralized functions with regionally distributed engineering and other development functions. It often involves outsourced engineering work as well as captive offshore engineering. The benefits of this distributed model include greater engineering efficiency (through utilization of *lower-cost* resources), *access to technical expertise* internationally, more *global input to product design*, and greater *strategic flexibility*.

Source

The above content was adapted from “Combining Adaptation and Arbitrage: Global Product Development”, section 6.4 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

This page titled 8.2: Global Product Development is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

8.3: Global Products and Services

Learning Objectives

After reading this section, students should be able to …

1. outline the trade-offs between standardized versus customized products.
2. know the influence of the country-of-origin effect.
3. comprehend the benefits of reverse innovation.

Straight Product Extension

Companies deciding to market their products in different countries typically have a choice of three common strategies to pursue. The first is the straight product extension. This means taking the company's current products and selling them in other countries without making changes to the product. The advantages of this strategy are that the company doesn't need to invest in new research, development, or manufacturing. Changes may be made in packaging and labeling, but these are driven by local regulatory requirements. The disadvantages, however, are that its products may not be well suited to local needs and that the products may be more costly due to higher manufacturing and labor costs in the United States.

Product Adaptation

The second strategy is product adaptation and refers to modifying the company's existing product in a way that makes it fit better with local needs. For example, when Procter & Gamble (P&G) introduced Tide laundry detergent in emerging markets like India, it changed the formulation to remove softeners. The reformulated Tide cost less than the original Tide. This change was important because price was an important factor in India where income levels were lower. Indian consumers were more able to afford the reformulated Tide.

Another way to localize a product is through packaging. Locally appropriate packaging doesn't just mean using the country's language. It also means creating packaging sizes that suit the country. For example, a company wanting to make its products more economical to less-wealthy countries may be tempted to sell larger, economy-sized packaging. But emerging-market consumers often prefer smaller package sizes, even if that increases the cost-per-use. They tend to buy sachets of shampoo rather than economy-size bottles. These smaller sizes are also easier to transport to local villages or to store in smaller-sized homes.

Mobile-phone maker Nokia went a step further in localizing its phones to different markets. The company uses local designers to create mobile-phone handset models that are specifically appropriate for each country. For example, the handsets designed in India are dust resistant and have a built-in flashlight. The models designed in China have a touchscreen, stylus, and Chinese character recognition.

Local designers are more likely to understand the needs of the local population than headquarters-located designers do.

The examples of Tide and Nokia show how companies can create a version of their existing product tailored to specific countries.

Product Invention: P&G Diapers

The third strategy, product invention, is creating an entirely new product for the target market. In this strategy, companies go back to the drawing board and rethink how best to design a product for that country.

The first step in inventing a product for a new country market is to understand the key product characteristics needed to succeed in that market. For example, when P&G wanted to sell diapers in BRIC countries (i.e., Brazil, Russia, India, and China), it started from square one. Rather than merely modifying the existing design, P&G engaged local knowledge and reconsidered all the key features of the design in the context of the needs of the emerging markets.

A major issue was price. To make the diaper affordable, P&G settled on an aggressive price target—each diaper should cost as much as one egg. But the company also wanted a diaper that could uphold the P&G brand name. At first, the designers thought that the lower-cost product needed to do everything that the current developed-world product did. But further discussions refined and narrowed the definition so that P&G could meet the cost target without damaging the brand.

P&G designers debated features such as absorbency, color, fit, and packaging to find a design that was acceptable on cost targets, acceptable to emerging-market consumers, and acceptable as a P&G-branded product. The designers considered materials and how they could avoid using high-paid, specialized suppliers. Some characteristics, such as packaging, could be adjusted to meet local cost standards. In other cases, a characteristic was nonnegotiable—such as corporate social-responsibility issues. For example, P&G wanted to ensure that none of the suppliers to its diaper business used child labor. In the end, P&G succeeded by understanding both the critical elements of the brand and the emerging-market customers' expectations.

Nuances of Product Extension, Adaptation, and Invention

The product-adaptation strategy is easier for firms to execute than product invention. Nonetheless, even product adaptation requires understanding the local market well. Consider Ford Motor Company's missteps in adapting its midpriced car model to the Indian market. Ford realized that it needed to lower the cost of its car to make it more affordable to Indian consumers. Ford brought a team of designers together in Detroit and tasked them with figuring out how to reduce the cost of the car. The designers looked at removing nonessential elements. The first feature to go was air conditioning. Next, the team decided to remove power windows in the back, keeping them only in the front. These and other such tweaks brought the total cost of the car down from $20,000 to $15,000. Reducing the cost by 25 percent is notable, but unfortunately the design team lacked vital local knowledge about India. First, even though the price of the car was lower, the $15,000 price point in India is still way above what the middle class can afford. The Indians who can afford a $15,000 car are the very rich. Second, the very rich in India who can afford to pay $15,000 for a car can also afford (and will have) a chauffeur. Remember the clever idea of removing the air conditioning and the power windows in the back? The consequence is that the chauffeur is the only one who gets a breeze. Given the sweltering summer temperatures and traffic congestion in Indian cities, you can guess that the Ford car didn't sell well.[1]

Country-of-Origin Effect

The country-of-origin effect refers to consumers using the country where the product was made as a barometer for evaluating the product. Their perceptions of the country influence whether they will perceive the product favorably or unfavorably. That perception influences consumers' purchasing decisions. For example, France is known for its wines and luxury goods. Wines from Chile may be just as good and more affordably priced, but consumers may perceive French wines to be better due to the country-of-origin effect. In the 1960s, "Made in Japan" was a signal of low quality, but over time Japan has changed that perception through a dedicated focus on high quality. Specifically, Japan adopted Total Quality Management (TQM) which is a set of management practices initially introduced to Japan by W. Edwards Deming. The focus of TQM is increasing quality and reducing errors in production or service delivery. TQM consists of systematic processes, planning, measurement, continuous improvement, and customer satisfaction. These days, "made in Japan" is viewed positively, but "made in China" faces more of a stigma. Likewise, consumers in Colombia don't want products that are made in Colombia. A similar problem happens with Mercedes-Benz—Mercedes-Benz cars assembled in Egypt have much lower resale value than those assembled in Germany. In these cases, local assembly in Egypt might be taken as a sign of inferior quality.

Reverse Innovation: How Designing for Emerging Economies Brings Benefits Back Home

Increasingly, marketing and innovation are directly linked. Reverse innovation means designing a product for a developing country and bringing that innovation back to the home country. Creating new products and services for developing countries requires radical innovation and opens new opportunities in developed-world markets as well. For example, GE Healthcare sells sophisticated medical-imaging devices around the world. Historically, GE has sold these high-end machines in emerging economies like India. But only 10 percent of Indian hospitals can afford a $10,000 electrocardiogram (ECG) machine. Reaching the other 90 percent of the market takes more than simply cutting a few costs. It requires radical innovation and an in-depth understanding of local conditions.

One important local fact to know is that most Indians live in rural areas. That means they don't have a local hospital to visit. Therefore, medical equipment needs to go to them, and no rural health care clinic is going to lug a $10,000 ECG machine into the field even if it *could* afford the device. Achieving the goal of a lightweight, reliable, simple-to-use ECG device took radical rethinking. GE built such a device that could fit in a shoulder bag or backpack. The device has a built-in replaceable printer and costs only $500. In addition, because the device would be used in rural locations with scant access to electricity, GE designed a battery that could do 500 ECGs on one charge. To make it easy to use, GE designed the device to have only three buttons. Finally,

just because the device is inexpensive doesn't mean it's dumb. GE installed professional-level analysis software to aid rural doctors.

With its new portable ECG device, GE has unlocked a whole new market in developing countries. Beyond that, GE has also opened up new opportunities back home—and that's the reverse innovation side of the story. How? The portable ECG machine with a $500 price tag is ideal for use in ambulances, saving lives of accident victims in developed countries as well. Cheap, portable, and easy-to-use devices are desirable in any country.[2]

? Key Takeaways

- There are three strategies for introducing a company's product to a new international market: (1) straight product extension, (2) product adaptation, and (3) product invention.
- A straight product extension involves taking the company's current product and selling it in other countries without making changes to the product. The advantages of this strategy are that the company doesn't need to invest in new research and development or manufacturing. The disadvantages, however, are that its products may not be well suited to local needs and that the products may be more costly due to higher US manufacturing and labor costs.
- Product adaptation refers to modifying the company's existing product in a way that makes it fit better with local needs, as Nokia did by making its mobile phones for India dust-resistant.
- Product invention means creating an entirely new product for the target market, as P&G did by designing a diaper for emerging markets that cost the same as a single egg. Such a price would make the diaper affordable in emerging-market countries.
- When adapting or inventing a product for a new market, it's important to have local knowledge, as the missteps of Ford's car for India have shown. In addition, the country-of-origin effect influences consumers' purchasing decisions. If consumers perceive one country more favorably than another, they're more apt to buy products from that country.
- Inventing a new product for an international country can bring benefits back to the home market. GE Healthcare completely reinvented a $10,000 medical-imaging device to create a $500 portable, imaging device for the Indian market. In the process, GE realized it had created a new product for its home market as well.

References

1. Vijay Govindarajan, "Ten Rules for Strategic Innovators" (presentation, World Innovation Forum, New York, NY, May 5–6, 2009).

2. a. Vijay Govindarajan, "Reverse Innovation: A New Strategy for Creating the Future" (webinar, HSM Global, March 18, 2010), accessed November 23, 2010, http://us.hsmglobal.com/contenidos/hsm-webinars-vijay.html.,

b. "An ECG for Less Than Rs 10? New, Made-in-India, GE Device, Does IT," *India Tech Online* , November 25, 2009, accessed August 1, 2010, http://www.indiatechonline.com/ge-mac-i-ecg-168.php.

Source

This chapter was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License from the book 'International Business v. 1.0' published by Saylor Academy, the creator or licensor of this work.

This page titled 8.3: Global Products and Services is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

8.4: Product Adaptation Decisions

Learning Objectives

After reading this section, students should be able to …

1. appreciate when product adaptation are warranted
2. list the dimensions of value proposition adaptation
3. list the major drivers behind value proposition adaptation

Value proposition adaptation deals with a whole range of issues, ranging from the quality and appearance of products to materials, processing, production equipment, packaging, and style. A product may have to be adapted to meet the physical, social, or mandatory requirements of a new market. It may have to be modified to conform to government regulations or to operate effectively in country-specific geographic and climatic conditions. Or it may be redesigned or repackaged to meet the diverse buyer preferences or standard-of-living conditions. A product's size and packaging may also have to be modified to facilitate shipment or to conform to possible differences in engineering or design standards in a country or in regional markets. Other dimensions of value proposition adaptation include changes in brand name, color, size, taste, design, style, features, materials, warranties, after-sale service, technological sophistication, and performance.

The need for some changes, such as accommodating different electricity requirements, will be obvious. Others may require in-depth analysis of societal customs and cultures, the local economy, technological sophistication of people living in the country, customers' purchasing power, and purchasing behavior. Legal, economic, political, technological, and climatic requirements of a country market may all dictate some level of localization or adaptation.

As tariff barriers (tariffs, duties, and quotas) are gradually reduced around the world in accordance with World Trade Organization (WTO) rules, other *nontariff barriers*, such as *product standards*, are proliferating. For example, consider regulations for food additives. Many of the United States' "generally recognized as safe" (GRAS) additives are banned today in foreign countries. In marketing abroad, documentation is important not only for the amount of additive but also for its source, and often additives must be listed on the label of ingredients. As a result, product labeling and packaging must often be adapted to comply with another country's legal and environmental requirements.

Many kinds of equipment must be engineered in the metric system for integration with other pieces of equipment or for compliance with the standards of a given country. The United States is virtually alone in its adherence to a nonmetric system, and U.S. firms that compete successfully in the global market have found metric measurement to be an important detail in selling to overseas customers. Even instruction or maintenance manuals, for example, should be made available in centimeters, weights in grams or kilos, and temperatures in degrees Celsius.

Many products must be adapted to local *geographic and climatic* conditions. Factors such as topography, humidity, and energy costs can affect the performance of a product or even define its use in a foreign market. The cost of petroleum products, along with a country's infrastructure, for example, may mandate the need to develop products with a greater level of energy efficiency. Hot, dusty climates of countries in the Middle East and other emerging markets may force automakers to adapt automobiles with different types of filters and clutch systems than those used in North America, Japan, and European countries. Even shampoo and cosmetic product makers have to chemically reformulate their products to make them more suited for people living in hot, humid climates.

The availability, performance, and level of sophistication of a *commercial infrastructure* will also warrant a need for adaptation or localization of products. For example, a company may decide not to market its line of frozen food items in countries where retailers do not have adequate freezer space. Instead, it may choose to develop dehydrated products for such markets. Size of packaging, material used in packaging, before- and after-sale service, and warranties may have to be adapted in view of the scope and level of service provided by the distribution structure in the country markets targeted. In the event that postsale servicing facilities are conspicuous by their absence, companies may need to offer simpler, more robust products in overseas markets to reduce the need for maintenance and repairs.

Differences in *buyer preferences* are also major drivers behind value proposition adaptation. Local customs, such as religion or the use of leisure time, may affect market acceptance. The sensory impact of a product, such as taste or its visual impression, may also be a critical factor. The Japanese consumer's desire for beautiful packaging, for example, has led many U.S. companies to redesign cartons and packages specifically for this market. At the same time, to make purchasing mass-marketed consumer products more affordable in lesser developed countries, makers of products such as razor blades, cigarettes, chewing gum, ball-point pens, and candy bars repackage them in small, single units rather than multiple units prevalent in the developed and more advanced economies.

Expectations about *product guarantees* may also vary from country to country depending on the level of development, competitive practices, and degree of activism by consumer groups; local standards of production quality; and prevalent product usage patterns. Strong warranties may be required to break into a new market, especially if the company is an unknown supplier. In other cases, warranties similar to those in the home country market may not be expected.

As a general rule, *packaging design* should be based on customer needs. For industrial products, packaging is primarily functional and should reflect needs for storage, transportation, protection, preservation, reuse, and so on. For consumer products, packaging has additional functionality and should be protective, informative, appealing, conform to legal requirements, and reflect buying habits (e.g., Americans tend to shop less frequently than Europeans, so larger sizes are more popular in the United States).

In analyzing adaptation requirements, careful attention to *cultural differences* between the target customers in the home country (country of origin) and those in the host country is extremely important. The greater the cultural differences between the two target markets, the greater the need for adaptation. Cultural considerations and customs may influence branding, labeling, and package considerations. Certain colors used on labels and packages may be found unattractive or offensive. Red, for example, stands for good luck and fortune in China and parts of Africa; aggression, danger, or warning in Europe, America, Australia, and New Zealand; masculinity in parts of Europe; mourning (dark red) in the Ivory Coast; and death in Turkey. Blue denotes immortality in Iran, while purple denotes mourning in Brazil and is a symbol of expense in some Asian cultures. Green is associated with high tech in Japan, luck in the Middle East, connotes death in South America and countries with dense jungle areas, and is a forbidden color in Indonesia. Yellow is associated with femininity in the United States and many other countries but denotes mourning in Mexico and strength and reliability in Saudi Arabia. Finally, black is used to signal mourning, as well as style and elegance, in most Western nations, but it stands for trust and quality in China, while white—the symbol for cleanliness and purity in the West—denotes mourning in Japan and some other Far Eastern nations.

A country's *standard of living* and the *target market's purchasing power* can also determine whether a company needs to modify its value proposition. The level of income, the level of education, and the availability of energy are all factors that help predict the acceptance of a product in a foreign market. In countries with a lower level of purchasing power, a manufacturer may find a market for less-sophisticated product models or products that are obsolete in developed nations. Certain high-technology products are inappropriate in some countries, not only because of their cost but also because of their function. For example, a computerized, industrial washing machine might replace workers in a country where employment is a high priority. In addition, these products may need a level of servicing that is unavailable in some countries.

When potential customers have limited purchasing power, companies may need to develop an entirely new product designed to address the market opportunity at a price point that is within the reach of a potential target market. Conversely, companies in lesser-developed countries that have achieved local success may find it necessary to adopt an "up-market strategy" whereby the product may have to be designed to meet world-class standards.

✔ Mini Case: Kraft Reformulates Oreo Cookies in China, Jargon (2008, May 1)

Kraft's Oreo has long been the top-selling cookie in the U.S. market, but the company had to reinvent it to make it sell in China. Unlike their American counterparts, Oreo cookies sold in China are long, thin, four-layered, and coated in chocolate.

Oreos were first introduced in 1912 in the United States, but it was not until 1996 that Kraft introduced Oreos to Chinese consumers. After more than 5 years of flat sales, the company embarked on a complete makeover. Research had shown, among other findings, that traditional Oreos were too sweet for Chinese tastes and that packages of 14 Oreos priced at 72 cents were too expensive. In response, Kraft developed and tested 20 prototypes of reduced-sugar Oreos with Chinese consumers before settling on a new formula; it also introduced packages containing fewer Oreos for just 29 cents.

But Kraft did not stop there. The research team had also picked up on China's growing thirst for milk, which Kraft had not considered before. It noted that increased milk demand in China and other developing markets was a contributing factor to higher milk prices around the world. This put pressure on food manufacturers like Kraft, whose biggest business is cheese, but it also spelled opportunity.

Kraft began a grassroots marketing campaign to educate Chinese consumers about the American tradition of pairing milk with cookies. The company created an Oreo apprentice program at 30 Chinese universities that drew 6,000 student applications. Three hundred were accepted and trained as Oreo-brand ambassadors. Some of them rode around Beijing on bicycles, outfitted with wheel covers resembling Oreos, and handed out cookies to more than 300,000 consumers. Others organized Oreo-themed basketball games to reinforce the idea of dunking cookies in milk. Television commercials showed kids twisting apart Oreo cookies, licking the cream center, and dipping the chocolate cookie halves into glasses of milk.

Still, Kraft realized it needed to do more than just tweak its recipe to capture a bigger share of the Chinese biscuit market. China's cookie-wafer segment was growing faster than the traditional biscuit-like cookie segment, and Kraft needed to catch up to rival Nestlé SA, the world's largest food company, which had introduced chocolate-covered wafers there in 1998.

So Kraft decided this market opportunity was big enough to justify a complete remake of the Oreo itself and, departing from longstanding corporate policy for the first time, created an Oreo that looked almost nothing like the original. The new Chinese Oreo consisted of four layers of crispy wafer filled with vanilla and chocolate cream, coated in chocolate. To ensure that the chocolate product could be shipped across the country, could withstand the cold climate in the north and the hot, humid weather in the south, and would still melt in the mouth, the company had to develop a new proprietary handling process.

Kraft's adaptation efforts paid off. In 2006, Oreo wafer sticks became the best-selling biscuit in China, outpacing HaoChiDian, a biscuit brand made by the Chinese company Dali. The new Oreos also outsell traditional (round) Oreos in China. They also have created opportunities for further aggregation and product innovation. Kraft now sells the wafers elsewhere in Asia, as well as in Australia and Canada, and the company has introduced another new product in China: wafer rolls, a tube-shaped wafer lined with cream. The hollow cookie can be used as a straw through which to drink milk.

This success encouraged Kraft to empower managers in other businesses around the globe. For example, to take advantage of the European preference for dark chocolate, Kraft introduced dark chocolate in Germany under its Milka brand. Research showed that Russian consumers like premium instant coffee, so Kraft positioned its Carte Noire freeze-dried coffee as an upscale brand. And in the Philippines, where iced tea is popular, Kraft launched iced-tea-flavored Tang.

As Kraft's experience shows, successful global marketing and branding is rooted in a careful blend of aggregation, adaptation, and arbitrage strategies that is tailored to the specific needs and preferences of a particular region or country.

Source

The above content was adapted from "Value Proposition Adaptation Decisions", section 6.1 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 8.4: Product Adaptation Decisions is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

8.5: Global Innovation

Learning Objectives

After reading this section, students should be able to …

1. illustrate the significant advantages of a global innovation strategy
2. explain the relationship between geography and knowledge diversity
3. list the steps in the global innovation strategy of a firm

Many companies now have global supply chains and product development processes, but few have developed effective global innovation capabilities. Santos, Doz, and Williamson (2004, Summer).Increasingly, however, technology access and innovation are becoming key global strategic drivers. This move from cost to growth and innovation is likely to continue as the center of gravity of economic activity shifts further to the East.

To illustrate the significant advantages of a truly global innovation strategy, Santos and others cite the battle between Motorola, Inc. and Nokia Corporation in the cellular phone industry. Motorola was a pioneer in the technology, building on initial path-breaking research from Bell Laboratories. But by focusing primarily on U.S. customers and U.S. solutions, it missed the market shift toward digital mobile technology and the global system for mobile (GSM) communication, which became the standard in Europe. The company also failed to appreciate that consumers were rapidly developing different use patterns and preferences about product design, thereby rendering a one-size-fits-all strategy obsolete.

A core competency in global innovation—the ability to leverage new ideas all around the world—has become a major source of global competitive advantage, as companies such as Nokia, Airbus, SAP, and Starbucks demonstrate. They realize that the principal constraint on innovation "performance" is knowledge. Accessing a diverse set of sources of knowledge is, therefore, a key challenge and is critical to successful differentiation. Companies whose knowledge pool is the same as that of its competitors will likely develop uninspired "me, too" products; access to a diversity of knowledge allows a company to move beyond incremental innovation to attention-grabbing designs and breakthrough solutions.

There is an interesting relationship between *geography* and *knowledge* diversity. In Finland, for example, the high cost of installing and maintaining fixed telephone lines in isolated places has spurred advances in radio telephony. In Germany, cultural and political factors have encouraged the growth of a strong "green movement," which in turn has generated a distinctive market and technical knowledge in recycling and renewable energy. Just-in-time production systems were pioneered in part because of high land costs there. Recognition of the role played by geography in innovation has prompted many companies to globalize their perspective on the innovation process. For example, pharmaceutical companies such as Novartis AG and GlaxoSmithKline plc now realize that the knowledge they need extends far beyond traditional chemistry and therapeutics to include biotechnology and genetics. What is more, much of this new knowledge comes from sources other than the companies' traditional R&D labs in Basel, Bristol, and in New Jersey, from places such as California, Tel Aviv, Cuba, or Singapore. For these companies, globalization of innovation processes is no longer optional—it has become imperative.

Companies that globalize their supply chains by accessing raw materials, components, or services from around the world are typically able to reduce the overall costs of their operations. Similarly, a side benefit of global innovation is cost reduction. Consider, for example, how companies are now leveraging software programmers in Bangalore, India, aerospace technologists in Russia, or chipset designers in China to cut the costs of their innovation processes.

To reap the benefits of global innovation, companies must do three things:

1. *Prospect* (find the relevant pockets of knowledge from around the world)
2. *Assess* (decide on the optimal "footprint" for a particular innovation)
3. *Mobilize* (use cost-effective mechanisms to move distant knowledge without degrading Santos, Doz, and Williamson (2004, Summer).

Prospecting—that is, finding valuable new pockets of knowledge to spur innovation—may well be the most challenging task. The process involves knowing what to look for, where to look for it, and how to tap into a promising source. Santos and colleagues cite the efforts of the cosmetics maker Shiseido Co., Ltd., in entering the market for fragrance products. Based in Japan, a country with

a very limited tradition of perfume use, Shiseido was initially unsure of the precise knowledge it needed to enter the fragrance business. But the company did know where to look for it. So it bought two exclusive beauty boutique chains in Paris, mainly as a way to experience, firsthand, the personal care demands of the most sophisticated customers of such products. It also hired the marketing manager of Yves Saint Laurent Parfums and built a plant in Gien, a town located in the French perfume "cluster." France's leadership in that industry made the *where* fairly obvious to Shiseido. The *how*had also become painfully clear because the company had previously flopped in its efforts to develop perfumes in Japan. Those failures convinced Shiseido executives that to access such complex knowledge—deeply rooted in local culture and combining customer information, aesthetics, and technology—the company had to immerse itself in the French environment and learn by doing. Having figured out the *where* and *how*, Shiseido would gradually learn *what* knowledge it needed to succeed in the perfume business.

Assessing new sources of innovation, that is, incorporating new knowledge into and optimizing an existing innovation network, is the second important challenge companies face. If a semiconductor manufacturer is developing a new chipset for mobile phones, for example, should it access technical and market knowledge from Silicon Valley, Austin, Hinschu, Seoul, Bangalore, Haifa, Helsinki, and Grenoble? Or should it restrict itself to just some of those sites? At first glance, determining the best footprint for innovation does not seem fundamentally different from the trade-offs companies face in optimizing their global supply chains: adding a new source might reduce the price or improve the quality of a required component, but more locations may also mean additional complexity and cost. Similarly, every time a company adds a source of knowledge to the innovation process, it might improve its chances of developing a novel product, but it also increases costs. Determining an optimal innovation footprint is more complicated, however, because the direct and indirect cost relationships are far more imprecise.

Mobilizing the footprint, that is, integrating knowledge from different sources into a virtual melting pot from which new products or technologies can emerge, is the third challenge. To accomplish this, companies must bring the various pieces of (technical) knowledge that are scattered around the world together and provide a suitable organizational form for innovation efforts to flourish. More importantly, they would have to add the more complex, contextual (market) knowledge to integrate the different pieces into an overall innovation blueprint.

✔ Mini CaseP&G's Success in Trickle-Up Innovation: Vicks Cough Syrup With Honey, Jana (2009, March 31)

A new over-the-counter medicine from Vicks that has recently become popular in Switzerland is not as new as it seems. The product, Vicks Cough Syrup with Honey, is really just the latest incarnation of a product that Vicks parent company, Procter & Gamble (P&G), initially created for lower-income consumers in Mexico and then "trickled up" to more affluent markets.

The term "trickle up" refers to a strategy of creating products for consumers in emerging markets and then repackaging them for developed-world customers. Until recently, affluent consumers in the United States and Western Europe could afford the latest and greatest in everything. Now, with purchasing power dramatically reduced because of the global recession, budget items once again make up a growing portion of total sales in many product categories.

P&G is not the only multinational company using this strategy. Other practitioners of trickle-up innovation include General Electric (GE), Nestlé, and Nokia. In early 2008, GE Healthcare launched the MAC 400, GE's first portable Electrocardiograph (ECG) that was designed in India for the fast-growing local market there. The company simplified elements of its earlier, 65-lb devices made for U.S. hospitals by shrinking its case to the size of a fax machine and removing features such as the keyboard and screen. The smaller MAC 400 costs only $1,500, versus $15,000 for its U.S. predecessor. This trickle-down innovation trickled back up again when GE Healthcare decided to sell the unit in Germany as well.

Nestlé offers inexpensive instant noodles in India and Pakistan under its Maggi brand. The line includes dried noodles that are engineered to taste as if they were fried, while they have a whole-wheat flavor that is popular in South Asia. And Nokia researches how people in emerging nations share phones, such as the best-selling 1100 series of devices created for developing-world consumers. The company then uses the information as inspiration for new features for developed-world users.

But what is unique about P&G's Honey Cough, as it is also called, is that it has moved around the globe in more than one direction. Honey Cough originated in 2003 in P&G's labs in Caracas, Venezuela, which creates products for all of Latin America. Market research revealed that Latin American shoppers tended to prefer homeopathic remedies for coughs and colds,

so P&G set out to create a medicine using natural honey rather than the artificial flavors typically used. The company first introduced the syrup in Mexico, under the label VickMiel, and then in other Latin American markets, including Brazil.

P&G deduced that the product would appeal to parts of the United States that have large Hispanic populations. In 2005, the company rebranded it as Vicks Casero for sale in California and Texas, at a price slightly less than Vicks' mainstay product, Vicks Formula 44. Within the first year of its release, the company boosted distribution to 27% more outlets.

Figuring that natural ingredients could appeal to even wider groups, P&G took the product to other markets where research indicated that homeopathic cold medicines are popular. In the past 2 years, the company has been marketing the product in Britain, France, Germany, and Italy, as well as Switzerland, and plans to add other Western European countries to the roster.

And Western Europe is not the last destination for iterations of Honey Cough. If P&G's current market research in the greater United States shows that mainstream American shoppers will buy Honey Cough, P&G will repackage it and market it nationwide, not just as Vicks Casero in Latino markets.

Developing and marketing a new product for each nation or ethnic group can take half a decade. Trickle-up innovation can reduce this time by several years, which explains its appeal. In each rollout, P&G has needed to do little more than make adjustments for each nation's health regulations.

At a time when companies are looking to speed product offerings while dealing with shrinking budgets and cash-strapped consumers, P&G's experience with its Honey Cough line shows how an international product portfolio can be tapped quickly and cheaply—that is, if American companies learn how to go against the flow.

Source

The above content was adapted from 'Fundamentals of Global Strategy v. 1.0' under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 8.5: Global Innovation is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

8.6: Global Innovation at the BOP

Innovation for the Bottom of the Pyramid

Learning Objectives

After reading this section, students should be able to …

1. outline the nature and size of BOP markets.
2. know examples of firms pursuing BOP strategies.
3. be conversant with the twelve principles of BOP innovation.

Contemporary View of BOP

In 1998, Professors C. K. Prahalad and Stuart L. Hart defined the bottom of the pyramid (BOP)as the billions of people living on less than $2 per day. Both men expanded this definition of BOP in their subsequent writing[1].The BOP is estimated to comprise between four billion and five billion people.

Too Good to Be True?

Professor Aneel Karnani at the University of Michigan argues that the BOP proposition is indeed too good to be true. "It is seductively appealing, but it is riddled with fallacies. There is neither glory nor fortune at the bottom of the pyramid—it is all a mirage."[2] He argues that the BOP proposition is logically flawed and is not supported by empirical evidence. He proposes an alternative approach for the private sector to alleviate poverty by viewing the poor as producers, not consumers. This shift in view, Karnani argues, is the way to alleviate poverty by raising the incomes of the poor.

In Prahalad and Hart's view, companies that understand the potential for commercial consumption at the BOP can open a new, potentially lucrative market that benefits the business as well as BOP consumers. By innovating to meet the needs of BOP customers, a company treats them with dignity and respect that previously was afforded only to the wealthy, Prahalad and Hart say.

Twelve Principles of BOP Innovation

Addressing the bottom of the pyramid requires a fresh managerial mind-set, summarized below in Prahalad's "12 Principles of BOP Innovation"—which are innovations themselves.[3] In developed markets, Prahalad suggests that one may take the availability of electricity, telephones, credit, refrigeration, and other such amenities for granted. At the BOP, the infrastructure is much spottier and more hostile. Consumers may have to cope with frequent electric-power blackouts and brownouts. Credit may be extremely costly. Refrigeration may be unavailable. Products marketed to the bottom of the pyramid must be able to withstand such an environment.

Below are Prahalad's "12 Principles of BOP Innovation," along with examples of each.

1. **Focus on value and on delivering performance for the price.** The BOP consumer isn't interested merely in cheap prices but in getting the greatest possible performance for the price paid. It's extraordinary how low a price can be and still be highly profitable, if the seller is organized to deliver value. For example, doctors at India's Aravind Eye Care System, the world's largest eye-care business, perform hundreds of thousands of cataract surgeries each year. The prices range from $50 to $300 per surgery, including the hospital stay. Aravind is quite profitable, although 60 percent of its patients pay nothing.
2. **Innovate.** Old technologies can't solve the problems of BOP consumers, and products aimed at the BOP market can't simply be watered-down versions of developed-world products. Instead, products must be rethought to bring radically lower cost while at the same time having features that meet the BOP's highest needs. For example, Hindustan Unilever Limited (HUL), a Unilever subsidiary, developed a new molecular encapsulation technology to prevent iodized salt from losing its iodine before consumption. To test the efficacy of the technology, the researchers used radioactive tracing techniques pioneered by the Indian Atomic Energy Commission.
3. **Make the solution scalable.** When delivering high performance at affordable prices, profits must be generated through volume sales. The product itself must be low cost, but with four billion to five billion BOP customers across the world, scaling the

operation is what will make the venture sustainable. Solutions should be scalable across borders.

4. **Aim to conserve resources.** BOP consumers cannot afford to waste resources. Per capita water consumption in the United States is almost 2,000 cubic meters per year, compared to less than 500 in China and less than 700 in India. The developed world's high standard of living is a water- and waste-intensive lifestyle. Innovations should emphasize conserving resources, recycling materials, and eliminating waste. Creating products for five billion people means designing the products in ways that can be environmentally sustainable. China's focus on electric cars rather than gasoline-powered cars reflects the reality that it's unlikely China could obtain the oil it would need for that many cars and that its extremely polluted cities could handle the additional exhaust fumes.
5. **Identify functionality.** BOP customers likely require different functionality than high-end consumers. For example, prosthetic legs developed for India's BOP consumers needed to meet some special requirements: consumers needed to be able to squat, sit cross-legged, and walk on rough ground. Dr. Pramod Karan Sethi and Ram Chandra developed the Jaipur Foot prosthetic for this purpose. The charity Bhagwan Mahaveer Viklang Sahayata Samiti, which is based in Jaipur, India, made them available for less than $30.[4]
6. **Think in terms of process innovations.** One way to bring costs down dramatically is to standardize processes. That's how Aravind is able to bring down the costs of cataract surgery so dramatically. Aravind made the process highly standardized and trained young village women to prepare patients and handle postoperative care. Thus doctors focus exclusively on surgery and perform only cataract surgery—nothing else. This focused process lets one doctor and two technicians perform fifty surgeries per day.
7. **Reduce the skills required to do the job.** Design products and services suitable to people without skills. Voxiva, a Peruvian start-up, developed a system enabling health-care workers to diagnose illnesses such as smallpox by comparing a patient's lesions to a picture of a similar lesion. With this simplified diagnostic process, health-care workers don't require great skills to know when to call a doctor.
8. **Educate consumers in the use of products.** This may require collaborating with nongovernmental organizations (NGOs), governments, and others. HUL launched a program in some of India's village schools to promote the washing of hands with soap as a way to prevent the childhood diarrhea that kills two million children per year. HUL educated the children, who in turn educated their parents.
9. **Design products and services to operate in very tough infrastructure environments.**For example, when Indian conglomerate ITC built a network connecting Indian villages, it had to provide personal computers that could handle wide voltage fluctuations. ITC included surge suppressors and solar panels to give the system adequate, reliable electricity.
10. **Make the interface simple and the learning curve short.** In Mexico, the chain retailer Elektra uses automated teller machines (ATMs) with a fingerprint identification system so BOP consumers don't have to remember lengthy identification codes.
11. **Innovate in distribution.** Avon has built a Brazilian direct-sales business that delivers revenues of $1.7 billion annually.
12. **Challenge assumptions.** The Jaipur Foot and Aravind Eye Care System hospitals defy conventional wisdom about how (and at what price) it's possible to deliver health care to the poor.

✔ Ethics in Action

NextBillion.net began as an initiative of the World Resources Institute's Markets and Enterprise Program. The name refers to the next billion people to rise from the bottom of the pyramid into the middle class and connotes the next billion in profits that companies can make serving this market. The purpose of the site is to provide a source for news, analysis, research and discussion on development through enterprise and BOP ideas. In addition, the NextBillion.net website has a career center that posts jobs (consulting projects as well as full-time jobs and academic appointments). As the site states, its mission is to "highlight the development and implementation of business strategies that open opportunities and improve the lives of the world's approximately 4 billion low-income producers and consumers."[5]

? Key Takeaways

- The BOP (or bottom-of-the-pyramid) market refers to the four billion to five billion people living on less than $2 per day.
- When businesses get involved in BOP economies, they can stimulate the creation of new services and products. Though there is some debate as to whether the goal should be to innovate and sell to the BOP or to engage the BOP markets as the source of innovation, all parties agree that engagement with BOP economies is desired and productive.

References

1. Prahalad's The Fortune at the Bottom of the Pyramid in 2004 and Hart's Capitalism at the Crossroads in 2005).C. K. Prahalad, The Fortune at the Bottom of the Pyramid (Upper Saddle River, NJ: Wharton School Publishing, 2004); Stuart L. Hart, Capitalism at the Crossroads (Upper Saddle River, NJ: Wharton School Publishing, 2005

2. Aneel Karnani, "Fortune at the Bottom of the Pyramid: A Mirage," Ross School of Business Working Paper Series, Working Paper No. 1035, July 2006, accessed February 12, 2011,http://deepblue.lib.umich.edu/bitstr.../1035-Karnani_ OLD.pdf.

3. C. K. Prahalad, The Fortune at the Bottom of the Pyramid (Upper Saddle River, NJ: Wharton School Publishing, 2004), 25–27.

4. Tim McGirk, "The $28 Foot," Time, accessed May 11, 2011, http://www.time.com/time/reports/heroes/foot.html .

5. "About NextBillion," NextBillion, accessed May 11, 2011, http://www.nextbillion.net/about .

Source

This chapter was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License from the book 'International Business v. 1.0' published by Saylor Academy, the creator or licensor of this work.

This page titled 8.6: Global Innovation at the BOP is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

9: Global Branding

9.1: Global Branding Summary
9.2: Formulating a Global Brand Strategy
9.3: Global Branding
9.4: Global Brand Structures
9.5: Determinants of Global Brand Structure
9.6: Managing Key Strategic Brands

This page titled 9: Global Branding is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

9.1: Global Branding Summary

Summary

A global brand has the same name and a similar image and positioning in most parts of the world. Many global companies leverage favorable brand images and high brand equity by employing combination (tiered) branding, cobranding, and brand extension strategies. Companies can create strong brands in all markets through global brand leadership. Maslow's hierarchy is a needs-based framework that offers a way of understanding opportunities to develop local and global products in different parts of the world. Some products and brands benefit from the country-of-origin effect. Product decisions must also address packaging issues such as labeling and aesthetics. Also, express warranty policies must be appropriate for each country market.

Companies invest a lot in building their brand recognition and reputation because a brand name signals trust. "Trust is what drives profit margin and share price," says Larry Light, CEO of Arcature brand consultancy and a veteran of McDonald's and BBDO Worldwide and Bates Worldwide advertising agencies. "It is what consumers are looking for and what they share with one another."[1]

Many emerging markets call for lower-cost goods. But how low can a company go on quality and performance without damaging the company's brand? The challenge is to balance maintaining a global reputation for quality while serving local markets at lower cost points.

One way to resolve the challenge is to offer the product at quality levels that are the best in that country even though they would be somewhat below developed-country standards. This is the tactic Walmart has successfully used in Mexico. Walmart's flooring, lighting, and air conditioning make its Mexican stores better than any other local stores even if they might seem Spartan to US consumers.

References

1. David Kiley and Burt Helm, "The Great Trust Offensive," *BusinessWeek*, September 17, 2009, accessed November 4, 2010, http://www.businessweek.com/magazine...8038492933.htm

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- The book 'International Business v. 1.0' published by Saylor Academy, the creator or licensor of this work.
- The course note from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM). 'The Economic and Political environment' is Copyright (c) by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license.

This page titled 9.1: Global Branding Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

9.2: Formulating a Global Brand Strategy

Learning Objectives

After reading this section, students should be able to …

1. outline the elements of brand architecture
2. explain the value of a corporate brand endorsement

To create an effective global brand structure capable of spanning operations in different countries and product lines, companies must clearly define the importance and role of each level of branding (corporate, product division, or product brand level), as well as the interrelation or overlap of branding at each level. They should also determine the appropriate geographic scope for each level relative to the firm's current organizational structure. To be effective, such "architecture" should satisfy three key principles: parsimony, consistency, and connectivity.

Parsimony requires that the brand architecture should incorporate all existing brands, whether developed internally or acquired, and provide a framework for consolidation to reduce the number of brands and strengthen the role of individual brands. Brands that are acquired need to be melded into the existing structure, especially when these brands occupy similar market positions to those of existing brands. When the same or similar products are sold under different brand names or are positioned differently in each country, ways to harmonize these should be examined.

Student Example

PVH Corp. is one of the largest fashion apparel companies in the world. In addition to owning Tommy Hilfiger and Calvin Klein, they also own Heritage Brands. Heritage Brands is the umbrella for the other existing clothing lines like Van Heusen, IZOD, ARROW, Speedo, and more. This allows PVH Corp. to consolidate its additional clothing lines under one main brand, allowing for the individuality of each line as well as a centralized management team. Each line has its own market, but they are all clothing lines and owned by the same company.

Zach Harper

Class of 2020

A second important element of brand architecture is its consistency relative to the number and diversity of products and product lines within the company. A balance needs to be struck between the extent to which brand names differentiate product lines or establish a common identity across different products. The development of strong and distinctive brand images for different product lines helps establish their separate identities. Conversely, the use of a common brand name consolidates effort and can produce synergies.

The value of corporate brand endorsement across different products and product lines and at lower levels of the brand hierarchy—a brand's connectivity—also needs to be assessed. The use of corporate brand endorsement as either a name identifier or logo connects the different product brands to the company and helps provide reassurance to customers, distributors, and other value-chain partners. Implemented well, a corporate brand endorsement can integrate and unify different brand identities across national boundaries. At the same time, corporate endorsement of a highly diverse range of product lines can result in dilution of the image. Worse, if one product brand is "damaged," corporate endorsement can spread the resulting negative effects or associations to other brands in the portfolio and create lasting effects across multiple product lines. Thus, both aspects need to be weighed in determining the role of corporate brand endorsement in brand architecture.

Source

The above content was adapted from "Formulating a Global Brand Strategy", section 7.4 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 9.2: Formulating a Global Brand Strategy is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

9.3: Global Branding

Learning Objectives

After reading this section, students should be able to …

1. outline the advantages and disadvantages of global branding.
2. know the trade-offs of centralized versus decentralized marketing decision making.
3. identify the special challenges of branding decisions in emerging markets.

Global Branding

A global brand is the brand name of a product that has worldwide recognition. Indeed, the world does become flatter to the extent a brand is recognized, accepted, and trusted across borders. Some of the most-recognized brands in the world include Coca-Cola, IBM, Microsoft, GE, Nokia, McDonald's, Google, Toyota, Intel, and Disney.[1]

Student Example

Apple's success in establishing a global brand with a strong identity exemplifies the concept discussed above. Apple is one company out of many that have succeeded in creating a big global brand so it can sell its products the same way everywhere. Their one-size-fits-all approach involves using a standardized design and features across all countries. One of Apple's largest strengths is its brand equity. Everyone around the world knows Apple and what products they sell. Having a global brand like Apple is beneficial because they do not have to modify their products to sell them in other regions. Not all companies that have created a global brand can sell its products the same way everywhere like Apple. One-way Apple achieved this was by opening stores in every country they served and matching the building with the culture there, which caught the attention of consumers. For example, the Apple store in Paris is housed in a Haussmann-type building that satisfies the architectural tastes of the people there.

Ivan Chavez

Class of 2020

The advantages of creating a global brand are economies of scale in production and packaging, which lower marketing costs while leveraging power and scope. The disadvantages, however, are that consumer needs differ across countries, as do legal and competitive environments. So while global branding, and consumer acceptance of such, is a flattener, significant country differences remain even when a firm has a strong global brand. Companies may decide to follow a global-brand strategy but also make adjustments to their communications strategy and marketing mix locally based on local needs.

The decision companies face is whether they should market one single brand around the world or multiple brands. Coca-Cola uses the Coke name on its cola products around the world but markets its water under the Dasani brand. Nestlé uses a local branding strategy for its 7,000 brands but also promotes the Nestlé corporate brand globally.

Acer's Multiple-Brand Strategy

PC maker Acer sells its personal computers under four different brands. Using a multi-brand strategy is a good choice when a country has a strong, positive association with a particular brand. For example, when Taiwan-based Acer bought US PC-maker Gateway, Acer kept the Gateway brand to use in the United States for midtier PCs. In Europe, however, Acer uses the Packard Bell brand. Acer also has two other brands, which are segmented by price. Acer's eMachines brand is for the lower-end consumer who is most focused on price, whereas the Acer brand is reserved for the highest-quality products aimed at technophiles. This multi-brand strategy also helps Acer's distribution. As Acer's chief marketing officer, Gianpiero Morello, says, "It's difficult to get a retailer to place 50 percent of his space with one brand. It's easier to split that same space with three brands."[2]

Student Example

Starbucks owns multiple brands other than its eponymous coffee. The firm also owns Seattle's Best, Tazo, and Ethos water, among other beverage brands. This allows Starbucks to capture parts of the market that are inaccessible to their Starbucks brand, for instance, those who refuse to pay Starbucks' coffee's premium price tag would be more likely to buy Seattle's Best. On the other hand, those who only drink tea would be more likely to purchase Tazo, both at Starbucks stores or in the grocery store. In this way too, retailers can dedicate space to a variety of brands, rather than just Starbucks.

David Brown

Class of 2020

Global Brand Web Strategy

Companies that are promoting their global brands successfully on the web include Google, Philips, Skype, Ericsson, Hewlett-Packard, and Cisco Systems. These companies are mindful of the cultural and language differences across countries. They have created websites in local languages and are using images and content specific to each country. At the same time, however, each country website has the same look and feel of the main corporate website to preserve the overall brand.[3]

Planning a Brand Strategy for Emerging Markets

Entering an emerging market with a developed-country brand poses an extra challenge. Income levels in emerging markets are lower, so companies tend to price their products as inexpensively as possible. This low-cost strategy may have consequences for the company's brand, however. For example, if a company introduces its brand as a "premium" product despite having a lower price, how will it introduce and differentiate its true "premium" brand later as consumers' incomes rise?

Centralized versus Decentralized Marketing Decisions

Who has the authority to make marketing decisions? In a centralized-marketing organizational structure, the home-country headquarters retains decision-making power. In a decentralized-marketing organizational structure, the regions are able to make decisions without headquarters' approval. The advantage of the centralized structure is speed, consistency, and economies of scale that can save costs (such as through global-marketing campaigns). The disadvantages are that the marketing isn't tied to local knowledge and doesn't reflect local tastes, so sales aren't optimized to appeal to regional differences.

Student Example

Ford Motor Company (FoMoCo) is a great example of this concept. Ford sells its vehicles in many countries, both developed and developing. For instance, we have a U.S. based Ford division that primarily targets its marketing efforts towards U.S. based customers. There is also a Ford Germany division that focuses its marketing efforts on the German market. These are just two countries where FoMoCo has shown its responsiveness to local needs. For instance, Ford does not sell full-size pick-ups in Germany. I believe the closest to the truck they do provide in that market is the Ford Ranger. However, they heavily market their F-150 trucks in the United States. By allowing each division to make their own calls, Ford can increase sales because they can focus on what local markets need rather than what Ford thinks they need.

Silviano Espana Silva

Class of 2020

Key Takeaways

- One of the key decisions that must be made when marketing internationally is how to set up the structure of the marketing organization in the company—centralized or decentralized. In a centralized structure, the home-country headquarters makes the decisions, which can save costs and bring consistency to marketing campaigns. In a decentralized organizational structure, the regions are able to make decisions autonomously, which enables regions to tailor their marketing to local sensibilities.

- Another decision concerns whether to pursue a single global-brand strategy or a multiple-brand strategy. A global brand is the brand name of a product that has worldwide recognition, such as Coca-Cola or IBM. Global brands bring economies of scale and marketing power. Multiple brands, however, may resonate more with specific markets, especially if a company merges with or acquires a local brand that is well respected in that region. The purpose of brands is to signal trust. In some cases, consumers may trust a familiar local brand more than a foreign global brand.
- Finally, companies need to plan a brand strategy for emerging markets, where products have to be sold at lower price points, which could hurt a premium brand reputation.

References

1. "Best Global Brands Report 2010," Interbrand, accessed October 22, 2010, http://issuu.com/interbrand/docs/bgb...rsion?mode=a_p.
2. Bruce Einhorn and Tim Culpan, "With Dell in the Dust, Acer Chases HP," BusinessWeek, March 8, 2010, 58–59.
3. Chanin Ballance, "Speaking Their Language: How to Localize Your Message for Global Customers," Marketing Profs, March 24, 2009, accessed November 4, 2010, http://www.marketingprofs.com/9/spea...s-ballance.asp.

Source

This chapter was adapted under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License from the book 'International Business v. 1.0' published by Saylor Academy, the creator or licensor of this work.

This page titled 9.3: Global Branding is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

9.4: Global Brand Structures

Learning Objectives

After reading this section, students should be able to …

1. outline the brand structures in multinational companies
2. outline the principles guiding brands in the global market

Multinational companies typically operate with one of three brand structures: (a) a corporate-dominant, (b) a product-dominant, or (c) a hybrid structure. A corporate-dominant brand structure is most common among firms with relatively limited product or market diversity, such as Shell, Toyota, or Nike. Product-dominant structures, in contrast, are often used by (mostly industrial) companies, such as Akzo Nobel, that have multiple national or local brands or by firms such as Procter & Gamble (P&G) that have expanded internationally by leveraging their "power" brands. The most commonly used structure is a hybrid (think of Toyota Corolla cars or Cadbury Dairy Milk chocolate) consisting of a mix of global (corporate), regional, and national product-level brands or different structures for different product divisions.

Student Example

An example of a company with a corporate-dominant brand structure is Duracell. While Duracell might sell various products such as LED light bulbs and flashlights, they are primarily known for their strong and trusted batteries. Even though Duracell has a wide range of batteries, such as AAA and car batteries, their customers do not distinguish between or identify brand differences between those batteries, or the different products Duracell sells. Rather, their customers recognize the Duracell name and brand as one that creates and sells reliable batteries. When someone hears the Duracell name, they will most likely immediately think of batteries.

Emily Ternes

Class of 2020

One example of a Hybrid brand is the Nintendo Switch gaming console. In their marketing, Nintendo emphasizes both its corporate brand name and the unique Switch branding and logo. By using both the company and brand name Nintendo can draw on the strong reputation of their other products while also promoting the unique product attributes of the Switch.

Ridge Peterson

Class of 2020

In many companies, "global" branding evolves as the company enters new countries or expands product offerings within an existing country. Typically, expansion decisions are made incrementally, and often on a country-by-country, product-division, or product-line basis, without considering their implications on the overall balance or coherence of the global brand portfolio. As their global market presence evolves and becomes more closely interlinked, however, companies must pay closer attention to the coherence of their branding decisions across national markets and formulate an effective global brand strategy that transcends national boundaries. In addition, they must decide how to manage brands that span different geographic markets and product lines, who should have custody of international brands and who is responsible for coordinating their positioning in different national or regional markets, as well as making decisions about use of a given brand name on other products or services.

To make such decisions, companies must formulate a coherent set of principles to guide the effective use of brands in the global marketplace. These principles must define the company's "brand architecture," that is, provide a guide for deciding which brands should be emphasized at what levels in the organization, how brands are used and extended across product lines and countries, and the extent of brand coordination across national boundaries.

Mini Case: Henkel's "Fox" Brands: An Example of a Hybrid Strategy, Arnold (2007); Schroiff and Arnold (2004)

Like many European companies, Henkel, the German consumer-brands corporation, has globalized mostly via acquisitions, and, consequently, it has a portfolio of localized brands with a national heritage and good local market shares. As the portfolio grew, escalating media costs, increased communication and stronger linkages across markets, and the globalization of distribution created pressures for parsimony in the number of the firm's brands and the consolidation of architecture across countries and markets. Henkel executives understood very well that a focus on a limited number of global strategic brands can yield cost economies and potential synergies. At the same time, they also knew that they needed to develop procedures for managing the custody of these brands, and that these should be clearly understood and shared throughout all levels of the organization, thus promoting a culture focused on global growth. They knew that failing to do so would likely trigger territorial power struggles between corporate and local teams for control of the marketing agenda.

While many companies would have focused on deciding between sacrificing local brand equity to develop "global power brands" (aggregation) or continuing to sacrifice global marketing economies of scale by investing separately in its portfolio of local brands (adaptation), Henkel chose an ingenious middle path. Henkel's choice serves as a model for globalization of marketing concepts without loss of local brand equity through the grouping of all its "value-for-money" brands under the umbrella "Fox" brand. In each country, Henkel retained the local brand name but identifies it with the Fox umbrella brand. (In most cultures, the fox is seen as clever, selfish, and cunning—the sort of character who would buy a value-for-money brand but not a brand so cheap that its quality might be compromised.)

By using a fox to represent smart and cunning shoppers, Henkel has created a "global power brand concept" that can travel to almost any culture to enrich a local brand—especially local brands that individually could not have been globalized. But the scale economies Henkel gains from this program are more managerial than economic in nature. Programs and ideas to promote the Fox brands, and the concept of value-for-money detergents, are managed centrally and offered as a menu to all local markets in which these brands participate. Thus, a manager experienced in managing one of the Fox families of brands in one market can be transferred to another market and rapidly reach effective levels of performance. Because each brand still requires local investment, financial economies of scale are more modest.

Compare Henkel's success to the failures of its major competitors as they tried to fully globalize their brand portfolios. Years ago, P&G, for example, attempted to globalize its European laundry detergent operations. In 2000, the company renamed its popular "Fairy" laundry detergent in Germany "Dawn" to position the latter as a global brand. There was no change in the product's formulation. But by the end of 2001, P&G's market share of Dawn in Germany had fallen drastically. While Fairy had represented a familiar and trusted brand persona to German consumers, Dawn meant nothing. With the renaming, the bond between consumers and the brand was broken; not even changing the brand's name back to Fairy could restore it.

This experience suggests that attempting to achieve global brand positioning by deleting local brands can be problematic. In fact, a strategy of acquisition, and the subsequent shedding, of local brands by multinationals may actually create fragmentation in consumer demand rather than be a globalizing force. Such a scenario is particularly plausible if one or more of the local brands have reached "icon" status. Icon brands do not necessarily have distinctive features, deliver good service, or represent innovative technology. Rather, they resonate deeply with consumers because they possess cultural brand equity. Most of these brands fall into lifestyle categories: food, apparel, alcohol, and automobiles.

Source

The above content was adapted from "Global Brand Structures", section 7.2 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 9.4: Global Brand Structures is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

9.5: Determinants of Global Brand Structure

Learning Objectives

After reading this section, students should be able to …

1. outline the factors shaping a company's international brand structure
2. explain the role of firm-based, product-market, and market dynamic characteristics in global branding

The kinds of issues a company must resolve as it tries to shape a coherent global branding strategy reflect its globalization history—how it has expanded internationally and how it has organized its international operations. At any given point, the structure of a brand portfolio reflects a company's past management decisions as well as the competitive realities the brand faces in the marketplace. Some companies, such as P&G and Coca-Cola, expanded primarily by taking domestic "power" brands to international markets. As they seek to expand further, they must decide whether to further extend their power brands or to develop brands geared to specific regional or national preferences and how to integrate the latter into their overall brand strategy. Others, such as Nestlé and Unilever, grew primarily by acquisition. As a consequence, they relied mainly on country-centered strategies, building or acquiring a mix of national and international brands. Such companies must decide how far to move toward greater harmonization of brands across countries and how to do so. This issue is particularly relevant in markets outside the United States, which often are fragmented, have small-scale distribution, and lack the potential or size to warrant the use of heavy mass-media advertising needed to develop strong brands.

Specifically, a company's international brand structure is shaped by three sets of factors: (a) firm-based characteristics, (b) product-market characteristics, and (c) underlying market dynamics (Douglas, Craig, and Nijssen (2001).

Firm-Based Characteristics

Firm-based characteristics reflect the full array of past management decisions. First, a company's administrative heritage—in particular, its organizational structure—defines the template for its brand structure. Second, a firm's international expansion strategy—acquisition or organic growth—affects how its brand structure evolves over time. What is more, the use of strategic alliances to broaden the geographic scope of the firm's operations often results in a "melding" of the brand strategies of the partners. Third and fourth, the importance of corporate identity and the diversity of the firm's product lines and product divisions also determine the range and number of brands.

An appreciation of a company's administrative heritage is critical to understanding its global brand structure.Bartlett and Ghoshal (1989). A firm that has historically operated on a highly decentralized basis, in which country managers have substantial autonomy and control over strategy as well as day-to-day operations, is likely to have a substantial number of local brands. In some cases, the same product may be sold under different brand names in different countries. In others, a product may be sold under the same brand name but have a different positioning or formulation in different countries.

Firms with a centralized organizational structure and global product divisions, such as Panasonic or Siemens, are more likely to have global brands. Both adopted a corporate branding strategy that emphasizes quality and reliability. Product lines are typically standardized worldwide, with minor variations in styling and features for local country markets.

Firms that expand internationally by acquiring local companies, even when the primary goal is to gain access to distribution channels, often acquire local brands. If these brands have high local recognition or a strong customer or distributor franchise, the company will normally retain the brand. This is particularly likely if the brand does not occupy a similar positioning to that of another brand currently owned by the firm. Nestlé and Unilever are examples of companies following this type of expansion strategy.

Expansion is often accompanied by diversification. Between 1960 and 1990, Nestlé expanded by acquiring a number of companies in a range of different product-markets, mostly in the food and beverage segment. These acquisitions included well-known global brands such as Perrier and San Pellegrino (mineral water), confectionery companies such as Rowntree and Perugina, pet food companies and brands such as Spillers and Alpo, and grocery companies such as Buitoni, Crosse & Blackwell, and Herta. The

resulting proliferation of brands created the need to consolidate and integrate company-branding structures (Douglas, Craig, and Nijssen (2001), p. 101).

Firms that have expanded predominantly by extending strong domestic, so-called power brands into international markets primarily use product-level brand strategies. P&G, for instance, has rolled out several of its personal products brands, such as Camay and Pampers, into international markets. This strategy appears most effective when customer interests and desired product attributes are similar worldwide and brand image is an important cue for the consumer.

The relative importance placed by the firm on its corporate identity also influences brand structure. Companies such as General Electric (GE) and Apple place considerable emphasis on corporate identity in the communications strategies. In the case of GE, "Imagination at Work" is associated with a corporate reputation dedicated to turning innovative ideas into leading products and services that help alleviate some of the world's toughest problems. Equally, Apple uses its apple logo to project the image of a vibrant innovator in the personal computer market. Increasingly, companies use their corporate identity as a means of reassuring customers and distributors that the company is reliable and stands behind its products. As a result, even companies with highly diverse product lines—such as Samsung—rely on the corporate brand name (and its logo) to project an image of reliability.

A fourth determinant of a company's brand structure is the diversity, or, conversely, the interrelatedness of the product businesses in which the firm is involved. Firms that are involved in closely related product lines or businesses that share a common technology or rely on similar core competencies often emphasize corporate brands. 3M Corporation, for example, is involved in a wide array of product businesses worldwide, ranging from displays and optics to health care products to cleaners to abrasives and adhesives. All rely heavily on engineering skills and have a reputation of being cutting-edge. The use of the 3M brand provides reassurance and reinforces the firm's reputation for competency and reliable products worldwide.

✔ Mini Case: Pharmaceutical Companies Try Global Branding

In Paris, stomach ulcers are treated with Mopral; in Chicago, it is called Prilosec. These two products are, in fact, exactly the same drug. Prilosec is the U.S. brand of AstraZeneca's omeprazole; Mopral is its French counterpart. Unlike manufacturers of consumer goods, the pharmaceutical industry traditionally has been wary of creating big, international brands. But that is about to change. Take a look at pharmacists' shelves. Viagra is there. So are Celebrex for arthritis pain, the antidiabetic agent Avandia, and the anticoagulant Plavix.

It is perhaps surprising that companies did not consider global branding sooner because a drug works for everybody in the same way in every country. While the industry has become global from a technological and geopolitical perspective, few companies have mastered globally integrated marketing practices. But change is coming—and fast. As more people travel internationally and the Internet makes information—including drug advice—readily available for doctors and patients, companies want to avoid any brand inconsistencies while maximizing exposure. Another globalizing force is growing standardization of the regulatory environment. With the establishment of the European Medical Evaluations Agency, for example, which approves drugs for all the members of the European Union, the borders are coming down. Japan has also adapted its approval system to facilitate the entry of Western products.

And then there is direct-to-consumer (DTC) advertising. While doctors and health care professionals remained the targets for pharmaceutical marketing, consumer-style branding was unnecessary. But companies are preparing for the spread of DTC beyond the shores of the United States. The introduction of global branding anticipates the transition to a more consumer-driven market.

Pressure to cut or contain costs is perhaps the most powerful driver behind the industry's move to global branding. Mega mergers were a way to contain the costs of research and development and find pipeline products, yet the big companies still need about five new blockbuster products each year to return the promised growth. Global branding promises reduced marketing costs and much faster and higher product rollout.

Local market conditions, such as reimbursement policies, however, may still override the benefits of global strategies and therefore inhibit the globalization of brands. Local flexibility will be key to success. Significant cost savings may therefore be slow in coming. Even with a centralized, global brand, most companies will still likely use local agencies for their marketing campaigns.

Product-Market Factors

Three product-market factors play an important role in brand architecture: the nature and scope of the target market, the product's cultural associations, and the competitive market structure (Douglas, Craig, and Nijssen (2001), p. 103).

When companies target a global market segment with relatively homogeneous needs and preferences worldwide, global brands provide an effective means of establishing a distinctive global identity. Luxury brands such as Godiva, Moet and Chandon, and Louis Vuitton, as well as brands such as deBeers, Benetton, and L'Oreal are all targeted to the same market segment worldwide and benefit from the cachet provided by their appeal to a global consumer group. Sometimes it is more effective to segment international markets by region and target regional segments with similar interests and purchase behavior, such as Euro-consumers. This provides cost efficiencies when such segments are readily accessible through targeted regional media and distribution channels.

A critical factor influencing brand structure is the extent to which the product is associated with a particular culture, that is, the extent to which there are strong and deeply ingrained local preferences for specific products or product variants (think of beer) or the products are an integral part of a culture (think of bratwurst, soccer teams). The stronger the cultural association, the less likely it is that global product brands will thrive; instead, local branding may be called for.

✔ Student Example

In almost all of Mexico, global brands tend to struggle due to the price being a bit more than the products developed in their country. Many Mexican consumers tend to be loyal to one brand because of its price and because they already know the quality of the product. An example of this can be seen in baked goods. Mexico has a well-known brand called BIMBO, which they manufacture a variety of pastries and snacks. They are the Mexican version of the Hostess brand from the US. BIMBO is very popular among Mexican consumers and in any store, you'll see BIMBO products. There are some stores in Mexico that sell pastries from other parts of the world, but they are usually priced higher and available in small quantities. Most Mexicans tend to stick to pastries that BIMBO makes, such as Mantecadas, Bimbunelos, Rebanadas, among many others. Since BIMBO is a Mexican company, they know the Mexican people better than any outside organization ever could.

Lucio Chavarria

Class of 2020

A third product-market driver of a company's brand structure is the product's competitive market structure, defined as the relative strength of local (national) versus global competitors in a given product market. If markets are fully integrated and the same competitors compete in these markets worldwide, as in aerospace, the use of global brands helps provide competitive differentiation on a global basis. If strong local, national, or regional competitors, as well as global competitors, are present in a given national or regional market, the use of a multitier branding structure, including global corporate or product brands as well as local brands, is desirable. Coca-Cola, for example, beyond promoting its power brands, has introduced several local and regional brands that cater to specific market tastes around the world.

✔ Mini Case: Use of Country of Origin Effects in Global Branding, Silverstein (2008, November 24)

Whether you prefer obscure imports or something mainstream, most beer brands like to invoke their country of origin. Guinness comes from Ireland, Corona is Mexican, Heineken and Amstel are Dutch, and Budweiser is a truly American brand.

The use of "country of origin effects" is an essential part of beer branding. Using the country of origin as part of the brand equity is free, so companies can avoid having to build an image from scratch over decades. For a long time, Foster's used a kangaroo in its advertisements, while Lapin Kulta, from Lapland in Finland, relies heavily on its unusual provenance in its marketing. Images of Finland's stark landscapes adorn communications material and bottle labels.

Swiss watchmakers certainly know the value of their "Swiss made" brand. The Federation of the Swiss Watch Industry actively polices all uses of the term and has strict guidelines on how it may be used on clocks and watches. In a similar vein, the French leverage their reputation for good wine, cooking, and fashion and the Italians view themselves as the masters of style.

German companies have been particularly effective in leveraging country effects. Of Interbrand's Top 100 Global Brands in 2008, 10 were German brands—five automobile brands (BMW, Porche, Mercedes-Benz, Volkswagen, and Audi), while brands in technology (SAP and Siemens), clothing (Adidas), financial services (Allianz), and cosmetics (Nivea) were also represented. Together, this group of German brands is valued at over $98 billion. Germany was second only to the United States in the number of brands making the Top 100 list.

It should come as no surprise, then, that Germany itself was ranked the best overall "country brand" in the 2008 Anholt-GfK Roper Nation Brands Index, which measures the world's perception of each nation as if it were a public brand. Fifty nations were measured in the study. The United States, the world's leading branding powerhouse, ranked seventh. So what is it about German brands, and the country that produces them, that is so special? Two words might be all the explanation that's required: discipline and quality.

German companies are highly disciplined in their approach to creating, introducing, and selling brands. They have the ability to consistently produce exceptional-quality products that are of lasting value. "German engineering" is a term closely associated with the country's automobile industry, which has seen a level of global success second only to the Japanese automakers. In fact, between 1990 and 2000, Mercedes-Benz and BMW more than doubled their sales in the United States alone.

Why do customers like German brands? German companies are widely admired for their intense focus on product quality and service, thought to be less interested in competing on price and strict about adhering to safety and other government standards.

BMW, a maker of premium automobiles, is one such revered brand. Founded in 1917 in Munich, Germany, as "Bavarian Motor Works," BMW produced aircraft engines during World War I, then built motorcycles in 1923 and went on to make cars in 1928. In recent years, BMW has been recognized as much for its innovative, quality marketing as for its high-performance cars.

But Germany's branding power extends well beyond automobiles. NIVEA, whose name comes from the Latin for "snow white," was created in late 1911. From its origins as a simple cream, NIVEA has now grown into a global manufacturer of a broad range of cosmetic and personal care products. NIVEA was voted the most trusted skin-care brand in 15 countries in the Reader's Digest survey of European Trusted Brands 2007.

Adidas, named after its founder Adolf (Adi) Dassler (Das), is an 80-year-old company that today is a global leader in sports footwear, apparel, and accessories. In 1996, Adidas equipped 6,000 Olympic athletes from 33 countries with its athletic gear. "Adidas athletes" won 220 medals, including 70 gold, and apparel sales increased 50%.

SAP, founded in 1972, is the world's largest business software company and the third-largest software supplier overall. The company employs almost 52,000 people and serves more than 76,000 customers in over 120 countries.

Other well-known global brands, from Bayer (pharmaceuticals) to Becks (beer) to Boss (clothing) to Braun (consumer products), are a testament to the fact that Germany is, and will continue to be, a prolific producer of some of the world's finest products. It is Germany's disciplined approach to quality that inspires consumer loyalty to German brands.

Market Dynamics

Finally, while the firm's history and the product markets in which it operates shape its brand structure, market dynamics—including ongoing political and economic integration, the emergence of a global market infrastructure, and consumer mobility—shape and continually change the context in which this evolves (Douglas, Craig, and Nijssen (2001), p. 104).

Increasing political and economic integration in many parts of the world has been a key factor behind the growth of international branding. As governments remove tariff and nontariff barriers to business transactions and trade with other countries, and as people and information move easily across borders, the business climate has become more favorable to the marketing of international brands. Firms are less frequently required to modify products to meet local requirements or to develop specific variants for local markets and increasingly can market standardized products with the same brand name in multiple country markets. In many cases, harmonization of product regulation across borders has further facilitated this trend.

The growth of a global market infrastructure is also a major catalyst to the spread of international brands. Global and regional media provide economical and effective vehicles for advertising international brands. At the same time, global media help lay the

groundwork for consumer acceptance of, and interest in, international brands by developing awareness of these brands and the lifestyles with which they are associated in other countries. In many cases, this stimulates a desire for the brands that consumers perceive as symbolic of a coveted lifestyle.

The globalization of retailing has further facilitated and stimulated the development of international manufacturer brands. As retailers move across borders, they provide an effective channel for international brands and, at the same time, increase their power. This forces manufacturers to develop strong brands with an international appeal so that they can negotiate their shelf position more effectively and ensure placement of new products.

A final factor shaping the context for international branding is increased consumer mobility. While global media provide passive exposure to brands, increasing international travel and movement of customers across national boundaries provides active exposure to brands in different countries. Awareness of the availability and high visibility of an international brand in multiple countries enhances its value to consumers and provides reassurance of its strength and reliability. Increased exposure to, and familiarity with, new and diverse products and the lifestyles and cultures in which they are embedded also generate greater receptivity to products of foreign origin or those perceived as international rather than domestic. All these factors help create a climate more favorable to international brands.

Source

The above content was adapted from “Determinants of Global Brand Structure”, section 7.3 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

This page titled 9.5: Determinants of Global Brand Structure is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

9.6: Managing Key Strategic Brands

Learning Objectives

After reading this section, students should be able to …

1. list the approaches to globally manage and monitor strategic brands
2. state the benefits of corporate branding

Companies must also think about how to globally manage and monitor key strategic brands to ensure that they build and retain their integrity, visibility, and value. This entails assigning brand custody or appointing a brand champion responsible for approving brand extensions and monitoring brand positioning.

One option is to negotiate the harmonization of specific brand positions between corporate headquarters and country managers. This is appropriate for firms with strong country management that operate in product markets where brands were historically tailored to local market characteristics.

A more proactive and increasingly popular solution is to appoint a brand champion responsibility for building and managing a brand worldwide. This includes monitoring the consistency of the brand positioning in international markets as well as authorizing use of the brand (brand extensions) on other products or other product businesses. The brand champion can be a senior manager at corporate headquarters, a country manager, or a product development group. It is critical that the brand champion report directly to top management and have clear authority to sanction or refuse brand extensions to other product lines and product businesses so as to maintain the integrity of the brand and avoid brand dilution.

A third option is to centralize control of brands within a global product division. This approach is likely to be most effective when the business is targeted to a specific global market segment, with new products or brands, when there is greater consistency in market characteristics across countries, and when the company's administrative heritage has only a limited history of strong country management.

Benefits of Corporate Branding

Corporations around the world are increasingly becoming aware of the enhanced value that corporate branding strategies can provide. Holt, Quelch, and Taylor (2004, September). A strong corporate branding strategy can add significant value in terms of helping the entire corporation and the management team with implementing its long-term vision, creating unique positions in the marketplace for the company and its brands, and signaling a commitment to a broader set of stakeholder issues. An effective corporate branding strategy therefore enables the company to leverage its tangible and nontangible assets and promote excellence throughout the corporation. To be effective and meet such objectives, corporate branding requires a high level of personal attention and commitment from the CEO and the senior management. Examples of effective corporate brands include Microsoft, Intel, Singapore Airlines, Disney, CNN, Samsung, and Mercedes. In recent years, the global financial powerhouses HSBC and Citibank have both acquired a vast number of companies across the globe and have fully adopted them under their international corporate brands with great success and within a relatively short time frame. All these companies understand that a well-executed corporate branding strategy can confer significant benefits.

Corporate Brand as the "Face of the Company"

A strong corporate brand acts as the face of the company, portraying what it wants to do and what it wants to be known for in the marketplace. In other words, the corporate brand is the umbrella for the corporation's activities and encapsulates its vision, values, personality, positioning, and image, among many other dimensions. Think of HSBC. It employs the same slogan—"The world's local bank"—around the world. This creative platform enables the corporation to portray itself as a bridge between cultures.

Simplicity

An effective corporate branding strategy creates simplicity by making the top of the brand portfolio the ultimate identifier of the corporation. P&G is widely known for its multibrand strategy. Yet, the corporate name P&G encapsulates all of its activities. Depending on the business strategy and the potential need for multiple brands, a corporate brand can assist management focus on

the company's core vision and values. Once established, it facilitates revisiting the definition of other brands in the corporations' portfolio and the creation of new brand identities.

Cost Savings

A corporate branding strategy is often more cost-efficient than a multibrand architecture. Specifically, corporate branding produces efficiencies in terms of marketing and advertising spending as the corporate brand replaces budgets for individual product marketing efforts. Even a combined corporate and product branding strategy can often enable management to reduce costs and exploit synergies from a new and more focused brand architecture. The Apple brand has established a very strong position of being a design-driven and innovative company offering many types of products and services. Their corporate brand encapsulates the body and soul of the company, and the main messages from the company use the corporate Apple brand. Various sub-brands then help to identify the individual product lines.

Corporate Brands as Assets

In recent years, corporate brands themselves have become valuable assets on the company balance sheet, with market values very often much beyond book value.

✔ Mini Case: The Best Global Brands, http://www.Interbrand.com/(2009)

Interbrand, a leading international brand consultancy specializing in brand services and activities, has developed a method for valuing (global) brands. It examines brands through the lens of financial strength, the importance of the brand in driving consumer selection, and the likelihood of ongoing revenue generated by the brand.

Each year, Interbrand compiles a list of global brands for analysis based on five criteria:

1. There must be substantial publicly available financial data for the brand.
2. One-third of the brand's revenues must come from outside its country of origin.
3. The brand must be positioned to play a significant role in the consumers' purchase decision.
4. The Economic Value Added (EVA) must be positive, showing that there is revenue above the company's operating and financing costs.
5. The brand must have a broad public profile and awareness.

The use of these criteria excludes a number of brands one might expect to be included. The Mars and BBC brands, for example, are privately held and do not have financial data publicly available. Wal-Mart, although it does business in international markets, does not do so under the Wal-Mart brand and is therefore not sufficiently global. Certain industry sectors are also not included in Interbrand's study. An example is provided by telecommunication brands, which tend to have strong national roots and have faced awareness challenges due to numerous mergers and acquisitions. The major pharmaceutical companies, while very valuable businesses, are also excluded since their consumers tend to build a relationship with the product brands rather than the corporate brand.

For brands that meet the Interbrand criteria, the company next looks at the current financial health of the business and brand, the brand's role in creating demand, and the future strength of the brand as an asset to the business.

Financial Analysis

Interbrand's model first forecasts the current and future revenue specifically attributable to the branded products. It subtracts operating costs from this revenue to calculate branded operating profit. Next, a charge is applied to the branded profit that is based on the capital a business spends versus the money it makes. This yields an estimate of a business's economic earnings. All financial analysis is based on publicly available company information.

Role of Brand Analysis

Brand analysis involves a measurement of how a brand influences customer demand at the point of purchase. It is applied to the economic earnings in order to arrive at the revenue that the brand alone generates (branded earnings). Interbrand uses in-house market research to establish individual brand scores against industry benchmarks to define the role a brand plays within the

category. For example, *role of brand* is traditionally much higher in the luxury category than in the energy and utilities sector. The brand, not the business, is the principal reason consumers choose these goods and services.

Brand Strength Score

As brands are assets, valuing them requires an assessment of their ability to secure future earnings on behalf of the businesses that own them. Brand strength is a measure of the brand's ability to secure demand, and therefore earnings, over time. Securing customer demand typically means achieving loyalty, advocacy, and favorable levels of customer trial, as well as maintaining a price premium. Interbrand's methodology generates a discount factor that adjusts the forecasted brand earnings for their riskiness based on the level of demand the brand is able to secure. Brand strength is calculated by assessing the brand's performance against a set of seven critical factors, including measures of relevance, leadership, market position, customer franchise, diversification, and brand support.

Brand Value

A brand's value is a financial representation of a business's earnings due to the superior demand created for its products and services through the strength of its brand. Brand value is the absolute financial worth of the brand as it stands today. Accordingly, the brand's value can be compared to the total value of the business as it would be assessed on the stock exchange.

The winner and number 1 global brand on Interbrand's 2009 list, once again, is *Coca-Cola*, which has topped the list for more than 20 years. *IBM* is number 2, *Microsoft* ranks third, *GE* comes in fourth, and *Nokia* has moved up to fifth position. Rounding out the top 10 are *McDonald's* (6), *Google* (7), *Toyota* (8), *Intel* (9), and *Disney* (10).

Interestingly, not one of the 100 Best Global Brands emanates from the developing world, at least for now. But Interbrand's research suggests this may soon change. With their huge populations, there is a decided shift in economic power to countries like China, India, Russia, Brazil, and Africa, and former global giants are making way for new leaders from fast developing markets.

The following brands are strong leaders in their home markets and already show some early signs of globalization:

- China: *Lenovo* (PCs), *Haier* (refrigerators, *Tsingtao* (beer)
- India: *Tata* (communications and information technology, engineering, materials, services, energy, consumer products, and chemicals), *Reliance* (energy and materials), *ArcelorMittal*(steel)
- Russia: *Kaspersky Lab* (information security to computer users, *Aeroflot* (airline), *Gazprom*(gas)
- South Africa: *MTN* (communications), *Anglo American* (mining), *SABMiller* (beer and soft drinks).
- Brazil: *Banco Itaú* (finance), *Vale* (mining), *Natura Cosmético* (cosmetics)

Source

The above content was adapted from "Managing Key Strategic Brands", section 7.5 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 9.6: Managing Key Strategic Brands is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

10: Global Channels and Supply Chains

10.1: Global Channels and Supply Chains Summary

10.2: Basics of Distribution Channels

10.3: Global Supply Chains

10.4: Global Sourcing and Distribution

10.5: Organizing The Channel

This page titled 10: Global Channels and Supply Chains is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

10.1: Global Channels and Supply Chains Summary

Summary

In today's global competitive environment, individual companies no longer compete as autonomous entities but as supply-chain networks. Instead of brand versus brand or company versus company, then network is increasingly suppliers-brand-company versus suppliers-brand-company.

Top-performing supply chains have three distinct qualities. First, they are agile enough to react readily to sudden changes in demand or supply. Second, they adapt over time as market structures and environmental conditions change. And third, they align the interests of all members of the supply-chain network in order to optimize performance.

Driven by e-commerce's capabilities to empower clients, most companies have moved from the traditional "push" business model —where manufacturers, suppliers, distributors, and marketers have most of the power—to a customer-driven "pull" model.

Supply-chain management (SCM) has three principal components: (a) creating the supply-chain network structure, (b) developing supply-chain business processes, and (c) managing the supply-chain activities. The supply-chain network structure consists of the member firms and the links between these firms. Business processes are the activities that produce a specific output of value to the customer. The management function integrates the business processes across the supply chain.

The best companies create supply chains that can respond to sudden and unexpected changes in markets. Agility—the ability to respond quickly and cost-effectively to unexpected change—is critical because in most industries, both demand and supply fluctuate more rapidly and widely than they used to. Key to increasing agility and resilience is building flexibility into the supply-chain structure, processes, and management.

Global companies must be able to adapt their supply networks when markets or strategies change. Companies that compete primarily on the basis of operational effectiveness typically focus on creating supply chains that deliver goods and services to consumers as quickly and inexpensively as possible. They invest in state-of-the-art technologies and employ metrics and reward systems aimed at boosting supply-chain performance. For companies competing on the basis of customer intimacy or product leadership, a focus on efficiency is not enough; agility is a key factor. Customer-intimate companies must be able to add and delete products and services as customer needs change; product leadership companies must be able to adapt their supply chains to changes in technology and to capitalize on new ideas.

Leading companies take care to align the interests of all the firms in their supply chain with their own. This is important because every supply-chain partner firm—whether a supplier, an assembler, a distributor, or a retailer—will focus on its own interests. If any company's interests differ from those of the other organizations in the supply chain, its actions will not maximize the chain's performance.

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- "Points to Remember", section 9.6 from the book Global Strategy(v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.
- Section 10.1 Basics of Distribution Channels and Section 10.4 Organizing the channel are edited versions of the chapter '10. Channel concepts: distributing the product' from the textbook 'Introducing Marketing, First Edition, 2011' authored by John Burnett – this book was published under The Global Text Project, funded by the Jacobs Foundation, Zurich, Switzerland.
- The following changes were made to the most recent edition: Divided 'Chapter 10. Channel concepts: distributing the product'' into three sections; Removed Created new title for Figure featuring Anderson ad.; Removed box titled 'In Practice' from wsj.com; Removed case application at the end of chapter; Added learning objectives for sections 10.1, and 10.4.

This page titled 10.1: Global Channels and Supply Chains Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

10.2: Basics of Distribution Channels

Learning Objectives

After reading this section, students should be able to …

- outline the role of distribution channels
- explain flows in channels
- list the participants in the marketing channel
- state their capabilities and limitations

In this chapter, we will look at the basics of channels of distribution. We shall see that several basic functions have emerged that are typically the responsibility of a channel member. Also, it will become clear that channel selection is not a static, once-and-for-all choice, but that it is a dynamic part of marketing planning. As was true for the product, the channel must be managed in order to work. Unlike the product, the channel is composed of individuals and groups that exhibit unique traits that might be in conflict, and that have a constant need to be motivated. These issues will also be addressed. Finally, the institutions or members of the channel will be introduced and discussed.

The dual functions of channels

Just as with the other elements of the firm's marketing program, distribution activities are undertaken to facilitate the exchange between marketers and consumers. There are two basic functions performed between the manufacturer and the ultimate consumer. The first called the exchange function, involves sales of the product to the various members of the channel of distribution. The second, the physical distribution function, moves products through the exchange channel, simultaneously with title and ownership. Decisions concerning both of these sets of activities are made in conjunction with the firm's overall marketing plan and are designed so that the firm can best serve its customers in the market place. In actuality, without a channel of distribution the exchange process would be far more difficult and ineffective.

The key role that distribution plays is satisfying a firm's customer and achieving a profit for the firm. From a distribution perspective, customer satisfaction involves maximizing time and place utility to: the organization's suppliers, intermediate customers, and final customers. In short, organizations attempt to get their products to their customers in the most effective ways. Further, as households find their needs satisfied by an increased quantity and variety of goods, the mechanism of exchange—i.e. the channel—increases in importance.

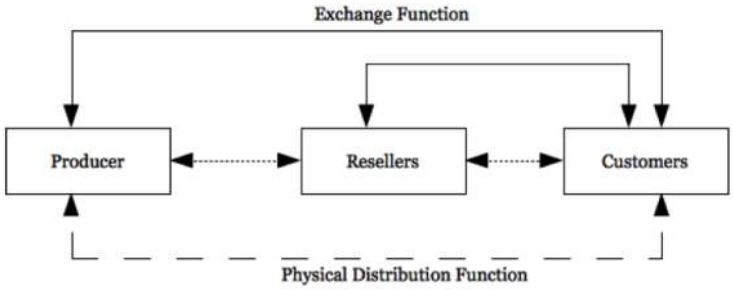


Figure 10.2.1: Dual-flow system in marketing channels.

As consumers, we have clearly taken for granted that when we go to a supermarket the shelves will be filled with products we want; when we are thirsty there will be a Coke machine 0r bar around the corner; and, when we do not have time to shop, we can pick-up the telephone and order from the J.C. Penney catalog or through the Internet. Of course, if we give it some thought, we realize that this magic is not a given, and that hundreds of thousands of people plan, organize, and labor long hours so that this modern convenience is available to you, the consumer. It has not always been this way, and it is still not this way in many other countries. Perhaps a little anthropological discussion will help our understanding.

The channel structure in a primitive culture is virtually nonexistent. The family or tribal group is almost entirely self-sufficient. The group is composed of individuals who are both communal producers and consumers of whatever goods and services can be made

available. As economies evolve, people begin to specialize in some aspect of economic activity. They engage in farming, hunting, or fishing, or some other basic craft. Eventually this specialized skill produces excess products, which they exchange or trade for needed goods that have been produced by others. This exchange process or barter marks the beginning of formal channels of distribution. These early channels involve a series of exchanges between two parties who are producers of one product and consumers of the other.

With the growth of specialization, particularly industrial specialization, and with improvements in methods of transportation and communication, channels of distribution become longer and more complex. Thus, corn grown in Illinois may be processed into corn chips in West Texas, which are then distributed throughout the United States. Or, turkeys raised in Virginia are sent to New York so that they can be shipped to supermarkets in Virginia. Channels do not always make sense.

The channel mechanism also operates for service products. In the case of medical care, the channel mechanism may consist of a local physician, specialists, hospitals, ambulances, laboratories, insurance companies, physical therapists, home care professionals, and so forth. All of these individuals are interdependent, and could not operate successfully without the cooperation and capabilities of all the others.

Based on this relationship, we define a marketing channel as sets of interdependent organizations involved in the process of making a product or service available for use or consumption, as well as providing a payment mechanism for the provider.

This definition implies several important characteristics of the channel. First, the channel consists of institutions, some under the control of the producer and some outside the producer's control. Yet all must be recognized, selected, and integrated into an efficient channel arrangement.

Second, the channel management process is continuous and requires continuous monitoring and reappraisal. The channel operates 24 hours a day and exists in an environment where change is the norm.

Finally, channels should have certain distribution objectives guiding their activities. The structure and management of the marketing channel is thus in part a function of a firm's distribution objective. It is also a part of the marketing objectives, especially the need to make an acceptable profit. Channels usually represent the largest costs in marketing a product.

Flows in marketing channels

One traditional framework that has been used to express the channel mechanism is the concept of flow. These flows reflect the many linkages that tie channel members and other agencies together in the distribution of goods and services. From the perspective of the channel manager, there are five important flows.

- Product flow
- Negotiation flow
- Ownership flow
- Information flow
- Promotion flow

These flows are illustrated for Perrier Water in Figure Figure 10.2.2:

The product flow refers to the movement of the physical product from the manufacturer through all the parties who take physical possession of the product until it reaches the ultimate consumer. The negotiation flow encompasses the institutions that are associated with the actual exchange processes. The ownership flow shows the movement of title through the channel. Information flow identifies the individuals who participate in the flow of information either up or down the channel. Finally, the promotion flow refers to the flow of persuasive communication in the form of advertising, personal selling, sales promotion, and public relations.

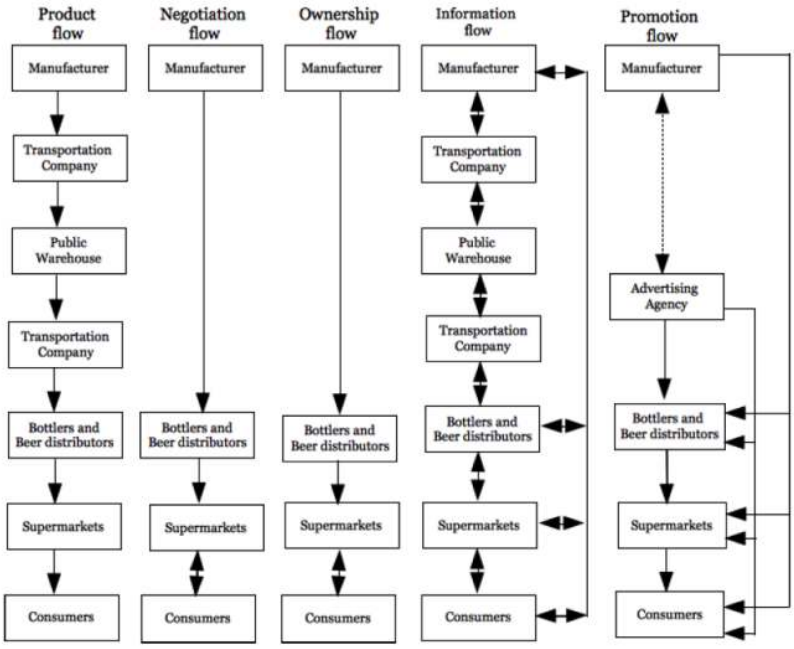


Figure 10.2.2: Five flows in the marketing channel for Perrier Water. *(Source: Bert Rosenbloom, Marketing Channels: A Management View, Dryden Press, Chicago, 1983, p.11.)*

Functions of the channel

The primary purpose of any channel of distribution is to bridge the gap between the producer of a product and the user of it, whether the parties are located in the same community or in different countries thousands of miles apart. The channel is composed of different institutions that facilitate the transaction and the physical exchange. Institutions in channels fall into three categories: (a) the producer of the product–a craftsman, manufacturer, farmer, or other extractive industry producer; (b) the user of the product–an individual, household, business buyer, institution, or government; and (c) certain middlemen at the wholesale and/or retail level. Not all channel members perform the same function.

Heskett (2) suggests that a channel performs three important functions:

- Transactional functions: buying, selling, and risk assumption
- Logistical functions: assembly, storage, sorting, and transportation
- Facilitating functions: post-purchase service and maintenance, financing, information dissemination, and channel coordination or leadership

These functions are necessary for the effective flow of product and title to the customer and payment back to the producer. Certain characteristics are implied in every channel. First, although you can eliminate or substitute channel institutions, the functions that these institutions perform cannot be eliminated. Typically, if a wholesaler or a retailer is removed from the channel, the function they perform will be either shifted forward to a retailer or the consumer, or shifted backward to a wholesaler or the manufacturer. For example, a producer of custom hunting knives might decide to sell through direct mail instead of retail outlets. The producer absorbs the sorting, storage, and risk functions; the post office absorbs the transportation function; and the consumer assumes more risk in not being able to touch or try the product before purchase.

Second, all channel institutional members are part of many channel transactions at any given point in time. As a result, the complexity may be quite overwhelming. Consider for the moment how many different products you purchase in a single year, and the vast number of channel mechanisms you use.

Third, the fact that you are able to complete all these transactions to your satisfaction, as well as to the satisfaction of the other channel members, is due to the routinization benefits provided through the channel. Routinization means that the right products are most always found in places (catalogues or stores) where the consumer expects to find them, comparisons are possible, prices are marked, and methods of payment are available. Routinization aids the producer as well as the consumer, in that the producer knows what to make, when to make it, and how many units to make.

Fourth, there are instances when the best channel arrangement is direct, from the producer to the ultimate user. This is particularly true when available middlemen are incompetent, unavailable, or the producer feels he can perform the tasks better. Similarly, it may be important for the producer to maintain direct contact with customers so that quick and accurate adjustments can be made. Direct-to-user channels are common in industrial settings, as are door-to-door selling and catalogue sales. Indirect channels are more typical and result, for the most part, because producers are not able to perform the tasks provided by middlemen.

=

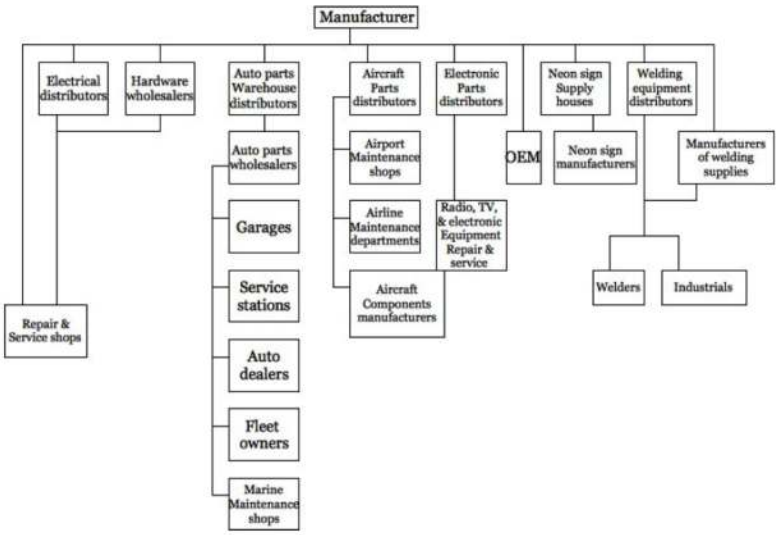


Figure 10.2.3: Marketing channels of a manufacturer of electrical wire and cable. (*Source: Edwin H. Lewis, Marketing Electrical Apparatus and Supplies,McGraw-Hill, Inc., 1961, p. 215.)*

Finally, although the notion of a channel of distribution may sound unlikely for a service product, such as health care or air travel, service marketers also face the problem of delivering their product in the form, at the place and time their customer demands. Banks have responded by developing bank-by-mail, Automatic Teller Machines (ATMs), and other distribution systems. The medical community provides emergency medical vehicles, out patient clinics, 24-hour clinics, and home-care providers. As noted in Figure 10.3 even performing arts employ distribution channels. In all three cases, the industries are attempting to meet the special needs of their target markets while differentiating their product from that of their competition. A channel strategy is evident.

Channel institutions: capabilities and limitations

There are several different types of parties participating in the marketing channel. Some are members, while others are nonmembers. The former perform negotiation functions and participate in negotiation and/or ownership while the latter participants do not.

Producer and manufacturer

These firms extract, grow, or make products. A wide array of products is included, and firms vary in size from a one-person operation to those that employ several thousand people and generate billions in sales. Despite these differences, all are in business to satisfy the needs of markets. In order to do this, these firms must be assured that their products are distributed to their intended markets. Most producing and manufacturing firms are not in a favorable position to perform all the tasks that would be necessary to distribute their products directly to their final user markets. A computer manufacturer may know everything about designing the finest personal computer, but know absolutely nothing about making sure the customer has access to the product.

In many instances, it is the expertise and availability of other channel institutions that make it possible for a producer or manufacturer to even participate in a particular market. Imagine the leverage that a company like Frito-Lay has with various supermarket chains. Suppose you developed a super-tasting new snack chip. What are your chances of taking shelf-facings away from Frito-Lay? Zero. Thankfully, a specialty catalog retailer is able to include your product for a prescribed fee. Likewise, other channel members can be useful to the producer in designing the product, packaging it, pricing it, promoting it, and distributing it through the most effective channels. It is rare that a manufacturer has the expertise found with other channel institutions.

Retailing

Retailing involves all activities required to market consumer goods and services to ultimate consumers who are motivated to buy in order to satisfy individual 0r family needs in contrast to business, institutional, or industrial use. Thus, when an individual buys a computer at Circuit City, groceries at Safeway, or a purse at Ebags.com, a retail sale has been made.

We typically think of a store when we think of a retail sale. However, retail sales are made in ways other than through stores. For example, retail sales are made by door-to-door salespeople, such as an Avon representative, by mail order through a company such as: L.L. Bean, by automatic vending machines, and by hotels and motels. Nevertheless, most retail sales are still made in brick-and-mortar stores.

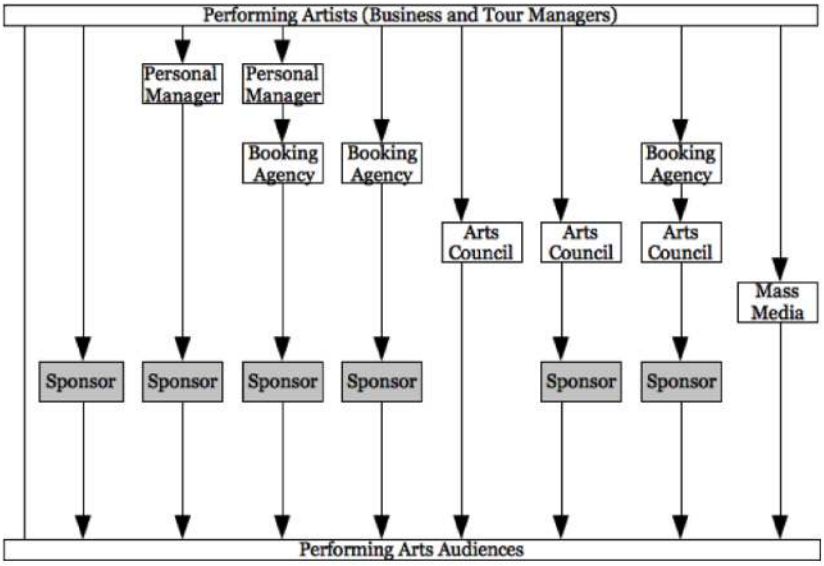


Figure 10.2.4: The marketing channels for the performing arts. *(Sources: John R. Nevin, "An Empirical Analysis of Marketing Channels for the Performing Arts," in Michael P. Mokwa, William M. Dawson, and E. Arthur Prieve (eds.). Marketing the Arts, New York: Praeger Publishers, 1980, p. 204.)*

The structure of retailing

Stores vary in size, in the kinds of services that are provided, in the assortment of merchandise they carry and in many other respects. Most stores are small and have weekly sales of only a few hundred dollars. A few are extremely large, having sales of USD 500,000 or more on a single day. In fact, on special sale days, some stores have exceeded USD 1 million in sales.

Department stores

Department stores are characterized by their very wide product mixes. That is, they carry many different types of merchandise that may include hardware, clothing, and appliances. Each type of merchandise is typically displayed in a different section or department within the store. The depth of the product mix depends on the store.

Chain stores

The 1920s saw the evolution of the chain store movement. Because chains were so large, they were able to buy a wide variety of merchandise in large quantity discounts. The discounts substantially lowered their cost compared to costs of single unit retailers. As a result, they could set retail prices that were lower than those of their small competitors and thereby increase their share of the market. Furthermore, chains were able to attract many customers because of their convenient locations, made possible by their financial resources and expertise in selecting locations.

Supermarkets

Supermarkets evolved in the 192os and 1930s. For example, Piggly Wiggly Food Stores, founded by Clarence Saunders around 1920, introduced self-service and customer checkout counters. Supermarkets are large, selfservice stores with central checkout facilities, they carry an extensive line of food items and often nonfood products.

Supermarkets were among the first to experiment with such innovations as mass merchandising and low-cost distributed on methods. Their entire approach to the distribution of food and household cleaning and maintenance products was to make available to the public large assortments of a variety of such goods at each store at a minimal price.

Discount houses

Cut-rate retailers have existed for a long time. However, since the end of World War II, the growth of discount houses as a legitimate and extremely competitive retailer has assured this type of outlet a permanent place among retail institutions. It essentially followed the growth of the suburbs.

Discount houses are characterized by an emphasis on price as their main sales appeal. Merchandise assortments are generally broad including both hard and soft goods, but assortments are typically limited to the most popular items, colors, and sizes. Such stores are usually large, self-service operations with long hours, free parking, and relatively simple fixtures.

Warehouse retailing

Warehouse retailing is a relatively new type of retail institution that experienced considerable growth in the 1970s. Catalog showrooms are the largest type of warehouse retailer, at least in terms of the number of stores operated. Retail sales for catalog showrooms grew from USD 1 billion dollars in 1970 to over USD 12 billion today. Their growth rate has slowed recently, but is still substantial.

Franchises

Over the years, particularly since the 1930s, large chain store retailers have posed a serious competitive threat to small storeowners. One of the responses to this threat has been the rapid growth of franchising. Franchising is not a new development. The major oil companies such as Mobil have long enfranchised its dealers, who only sell the products of the franchiser (the oil companies). Automobile manufacturers also enfranchise their dealers, who sell a stipulated make of car (e.g. Chevrolet) and operate their business to some extent as the manufacturer wishes.

Student Example

I used to work at McDonald's and every time I get the opportunity to talk about a franchise I choose their example. They started out with two brothers who streamlined ways to make food quickly. A milkshake machine salesman named Ray Kroc was so amazed at their restaurant that he worked with them to franchise the restaurant and later bought them out. Today, people can own a franchise of McDonald's which means that they pay McDonald's to use their business. New owners usually need to pay an upfront payment (e.g., $500,000) to get started and then pay a small percentage of profits to the McDonald's corporation.

Cade Timmons

Class of 2020

Planned shopping centers/malls

After World War II, the United States underwent many changes. Among those most influential on retailing were the growth of the population and of the economy. New highway construction enabled people to leave the congested central cities and move to newly developed suburban residential communities. This movement to the suburbs established the need for new centers of retailing to serve the exploding populations. By 1960 there were 4,500 such centers with both chains and nonchains vying for locations.

Such regional shopping centers are successful because they provide customers with a wide assortment of products. If you want to buy a suit or a dress, a regional shopping center pr0vides many alternatives in one location. Regional centers are those larger centers that typically have one or more department stores as major tenants. Community centers are moderately sized with perhaps a junior department store; while neighborhood centers are small, with the key store usually a supermarket. Local clusters are shopping districts that have simply grown over time around key intersections, courthouses, and the like. String street locations are along major traffic routes, while isolated locations are freestanding sites not necessarily in heavy traffic areas. Stores in isolated locations must use promotion or some other aspect of their marketing mix to attract shoppers. Still, as indicated in the next Newsline, malls are facing serious problems.

Newsline: The mall: a thing of the past?

She was born into retail royalty, a double-decker shrine to capitalism that seduced cool customers and wild-eyed shopaholics alike to roam her exhausting mix of 200 stores. Her funky, W-shaped design was pure 1960s, as if dreamed up by that era's noted architectural whiz, Mike Brady. When her doors opened the first morning, a brass band serenaded the arriving mob.

Cinderella City, once the biggest covered malls on the planet, was a very big deal–for about six years, until the next gleaming mall came along in 1974. That's when the music stopped at Cinderella City. Soon the patrons grew scarce, the concrete began crumbling and graffiti stained some of the walls. It's not pretty, but that's the cold law of the consumer jungle. One minute you're luring shoppers from miles around to chug an Orange Julius or grab a snack at the Pretzel Hut; a few years go by, and they're planting you in the dreaded mall graveyard.

Back then, people made a day out of wandering the massive concourses and lunching in the food courts. Today, with less free time available for many people, shopping is seen as a necessity. Spending time with your family and at home is more important than spending time in a store.

The newest malls reflect the modern need for shopping speed. Covered shopping centers now come equipped with dozens of doors to the outside instead of two main entrances that usher crowds in and out through the anchor department store. That same trend paved the way for the flurry of freestanding Home Depots and TJ Maxx stores as well as discount giants like Wal-Mart. All are sapping customers from mid-market malls, already struggling. In addition to the fresh success of freestanding discount stores, the Internet is drawing off even more customers who seek to buy books or music online.

For the mall to survive, they'll have to be something different–a high-quality environment for the delivery of high touch, high experience, high margin retail goods and services: a place you go for the entertainment shopping experience. (37)

Nonstore retailing

Nonstore retailing describes sales made to ultimate consumers outside of a traditional retail store setting. In total, nonstore retailing accounts for a relatively small percentage of total retail sales, but it is growing and very important with certain types of merchandise, such as life insurance, cigarettes, magazines, books, CDs, and clothing.

Student Example

Many businesses had found non-store retailing as a successful model of selling their products. Some non-store retailing businesses heavily rely on personal connections between the seller and the buyer. In the life insurance business, many individuals own life insurance policies through group policy through their employers. However, some individuals also purchase their individual policies through agents or brokers. Many agents and brokers have their office but they often meet their clients at a public location or the clients' house. I had experience with being an insurance broker for a few years, my clients are referred by friends and clients. I did presentations to the clients at the café, library, or their home. My life insurance license not only allows me to sell life insurance products but also other types of fixed financial products, such as a fixed annuity. I was able to help the clients to review their financial situation and offer the most suitable products for the clients.

Anthony Chen

Class of 2020

One type of nonstore retailing used by such companies as Avon, Electrolux, and many insurance agencies is inhome selling. Such sales calls may be made to preselected prospects or in some cases on a cold call basis. A variation of door-to-door selling is the demonstration party. Here one customer acts as a host and invites friends. Tupperware has been very successful with this approach.

Vending machines are another type of nonstore retailing. Automated vending uses coin-operated, self-service machines to make a wide variety of products and services available to shoppers in convenient locations. Cigarettes, soft drinks, hosiery, and banking transactions are but a few of the items distributed in this way. This method of retailing is an efficient way to provide continuous; service. It is particularly useful with convenience goods.

Mail order is a form of nonstore retailing that relies on product description to sell merchandise. The communication with the customer can be by flyer or catalog. Magazines, CDs, clothing, and assorted household items are often sold in this fashion. As with

vending machines, mail order offers convenience but limited service. It is an efficient way to cover a very large geographical area when shoppers are not concentrated in one location. Many retailers are moving toward the use of newer communications and computer technology in catalog shopping.

Online marketing has emerged during the last decade; it requires that both the retailer and the consumer have computer and modem. A modem connects the computer to a telephone line so that the computer user can reach various online information services. There are two types of online channels: (a) commercial online channels— various companies have set up online information and marketing services that can be assessed by those who have signed up and paid a monthly fee, and (b) Internet—a global web of some 45,000 computer networks that is making instantaneous and decentralized global communication possible. Users can send e-mail, exchange views, shop for products, and access real-time news.

✔ Student Example

Steam is an online marketplace that sells video games directly from developers to PC users. Steam either completely manages the digital rights management of the games that it sells, or sells license keys for games which then are launched through other digital rights management platforms. For a very long time, Steam was the only retail platform available for the digital distribution of video games on PC. In fact, the physical distribution of PC games is rapidly becoming a thing of the past.

David Brown

Class of 2020

Marketers can carry on online marketing in four ways: (a) using e-mail; (b) participating in forums, newsgroups, and bulletin boards; (c) placing ads online; and (d) creating an electronic storefront. The last two options represent alternative forms of retailing. Today, more than 40,000 businesses have established a home page on the Internet, many of which serve as electronic storefronts. One can order clothing from Lands' End or J.C. Penney, books from B. Dalton or Amazon.com, or flowers from Lehrer's Flowers to be sent anywhere in the world. Essentially, a company can open its own store on the Internet.

Companies and individuals can place ads on commercial online services in three different ways. First, the major commercial online services offer an ad section for listing classified ads; the ads are listed according to when they arrived, with the latest ones heading the list. Second, ads can be placed in certain online newsgroups that are basically set up for commercial purposes. Finally, ads can also be put on online billboards; they pop up while subscribers are using the service, even though they did not request an ad.

Catalog marketing occurs when companies mail one or more product catalogs to selected addresses that have a high likelihood of placing an order. Catalogs are sent by huge general-merchandise retailers–J.C. Penney's, Spiegel–that carry a full line of merchandise. Specialty department stores such as Neiman-Marcus and Saks Fifth Avenue send catalogs to cultivate an upper-middle class market for high-priced, sometimes exotic merchandise.

Integrated marketing

The death of retailing greatly exaggerated

Recently, the MIT economist Lester Thurow suggested that e-commerce could mean the end of 5,000 years of conventional retailing if online stores can combine price advantages with a pleasant virtual shopping experience. Let's face it: the growth of malls and megastores have shown that people want selection, convenience, and low prices, and that's about it. Sure, people say they would rather shop from the mom-and-pop on Main Street. But if the junk chain store out on the highway has those curling irons for a dollar less, guess where people go?

So a few years into the e-commerce revolution, here are a few observations and predictions:

- Online stores need to become easier to use as well as completely trustworthy.
- If people can go online and get exactly what they get from retail stores for less money, that is precisely what they will do.
- Some stores will have a kind of invulnerability to online competition; i.e. stores that sell last minute items or specialty items that you have to see.
- Retail stores may improve their chances by becoming more multidimensional; i.e. they have to be fun to visit.
- Still, not everything is rosy for e-tailers. Research provides the following insights:

- For net upstarts, the cost per new customer is USD 82, compared to USD 31 for traditional retailers.
- E-tailers customer satisfaction levels were: 41 per cent for customer service; 51 per cent for easy returns; 57 per cent for better product information; 66 per cent for product selection; 70 per cent for price, and 74 per cent for ease of use.
- Repeat buyers for e-tailers was 21 per cent compared to 34 per cent for traditional retailers.

Suggstions to improve the plight of e-tailers include the following :

- Keep it simple.
- Think like your customer.
- Engage in creative marketing
- Don't blow everything on advertising.
- Don't undercut prices.

While all this advice is good, the recent roller coaster ride of high-tech stocks and its disappointing results for e-tailers has completely changed the future of e-tailing. While e-tailers have spent about USD 2 billion industry-wide on advertising campaigns, they often devote far less attention and capital to the quality of services their prospective customers receive once they arrive on site. Etailers are learning what brick and mortar retailers have known all along, that success is less about building market share than about satisfying and retaining customers who can generate substantial profits. (38)

Several major corporations have also acquired or developed mail-order divisions via catalogs. Using catalogs, Avon sells women's apparel, W.R. Grace sells cheese, and General Mills sells sport shirts.

Some companies have designed "customer-order placing machines", i.e. kiosks (in contrast to vending machines, which dispense actual products), and placed them in stores, airports, and other locations. For example, the Florsheim Shoe Company includes a machine in several of its stores in which the customer indicates the type of shoe he wants (e.g. dress, sport), and the color and size. Pictures of Florsheim shoes that meet his criteria appear on the screen.

Wholesaling

Another important channel member in many distribution systems is the wholesaler. Wholesaling includes all activities required to market goods and services to businesses, institutions, or industrial users who are motivated to buy for resale or to produce and market other products and services. When a bank buys a new computer for data processing, a school buys audio-visual equipment for classroom use, or a dress shop buys dresses for resale, a wholesale transaction has taken place.

The vast majority of all goods produced in an advanced economy have wholesaling involved in their marketing. This includes manufacturers. who operate sales offices to perform wholesale functions, and retailers, who operate warehouses or otherwise engage in wholesale activities. Even the centrally planned socialist economy needs a structure to handle the movement of goods from the point of production to other product activities or to retailers who distribute to ultimate consumers. Note that many establishments that perform wholesale functions also engage in manufacturing or retailing. This makes it very difficult to produce accurate measures of the extent of wholesale activity. For purposes of keeping statistics, the Bureau of the Census of the United States Department of Commerce defines wholesaling in terms of the per cent of business done by establishments who are primary wholesalers. It is estimated that only about 60 per cent of all wholesale activity is accounted for in this way.

Today there are approximately 600,000 wholesale establishments in the United States, compared to just fewer than 3 million retailers. These 600,000 wholesalers generate a total volume of over USD 1.3 trillion annually; this is approximately 75 per cent greater than the total volume of all retailers. Wholesale volume is greater because it includes sales to industrial users as well as merchandise sold to retailers for resale.

Functions of the wholesaler

- Wholesalers perform a number of useful functions within the channel of distributions. These may include all or some combination of the following:
- Warehousing–the receiving, storage, packaging, and the like necessary to maintain a stock of goods for the customers they service.
- Inventory control and order processing–keeping track of the physical inventory, managing its composition and level, and processing transactions to insure a smooth flow of merchandise from producers to buyers and payment back to the producers.
- Transportation–arranging the physical movement of merchandise.

- Information–supplying information about markets to producers and information about products and suppliers to buyers.
- Selling–personal contact with buyers to sell products and service.

In addition, the wholesaler must perform all the activities necessary for the operation of any other business such as planning, financing, and developing a marketing mix. The five functions listed previously emphasize the nature of wholesaling as a link between the producer and the organizational buyer.

By providing this linkage, wholesales assist both the producer and the buyer. From the buyer's perspective, the wholesaler typically brings together a wide assortment of products and lessens the need to deal directly with a large number of producers. This makes the buying task much more convenient. A hardware store with thousands of items from hundreds of different producers may find it more efficient to deal with a small number of wholesalers. The wholesaler may also have an inventory in the local market, thus speeding delivery and improving service. The wholesaler assists the producer by making products more accessible to buyers. They provide the producer with wide market coverage information about local market trends in an efficient manner. Wholesalers may also help with the promotion of a producer's products to a local or regional market via advertising or a sales force to call on organizational buyers.

Types of wholesalers

There are many different types of wholesalers. Some are independent; others are part of a vertical marketing system. Some provide a full range of services; others offer very specialized services. Different wants and needs on the part of both buyers and producers have led to a wide variety of modern wholesalers. Table 10.2.1 provides a summary of general types. Wholesaling activities cannot be eliminated, but they can be assumed by manufacturers and retailers. Those merchant wholesalers who have remained viable have done so by providing improved service to suppliers and buyers. To do this at low cost, modern technologies must be increasingly integrated into the wholesale operation.

Table 10.2.1: Types of modern wholesalers

Type	Definition	Subcategories
Full-service merchandise wholesaler	*Take title* to the merchandise and assume the risk involved in an independent operation; buy and resell products; offer a complete range of services.	General Limited-line
Limited-service merchant wholesalers	*Take title* to the merchandise and assume the risk involved in an independent operation; buy and resell products; offer a limited range of services.	Cash and carry Rack jobbers Drop shippers Mail orders
Agents and brokers	*Do not take title* to the merchandise; bring buyers and sellers together and negotiate the terms of the transaction: agents merchants represent either the buyer or seller, usually on a permanent basis; brokers bring parties together on a temporary basis.	Agents Buying agents Selling agents Commission merchants Manufacturers' agents Brokers Real estate Food Other products
Manufacturer's sales	*Owned directly* by the manufacturers; performs wholesaling functions for the manufacturer.	
Facilitator	Perform some *specialized functions* such as finance or warehousing; to facilitate the wholesale transactions; may be independent or owned by producer or buyer.	Warehouses Finance companies Transportation companies Trade marts

Physical distribution

In a society such as ours, the task of physically moving, handling and storing products has become the responsibility of marketing. In fact, to an individual firm operating in a high level economy, these logistical activities are critical. They often represent the only cost saving area open to the firm. Likewise, in markets where product distinctiveness has been reduced greatly, the ability to excel in physical distribution activities may provide a true competitive advantage. Ultimately, physical distribution activities provide the bridge between the production activities and the markets that are spatially and temporally separated.

Physical distribution management may be defined as the process of strategically managing the movement and storage of materials, parts, and finished inventory from suppliers, between enterprise facilities, and to customers. Physical distribution activities include those undertaken to move finished products from the end of the production line to the final consumer. They also include the movement of raw materials from a source of supply to the beginning of the production line, and the movement of parts, etc. to maintain the existing product. Finally, it may include a network for moving the product back to the producer or reseller, as in the case of recalls or repair.

Before discussing physical distribution, it is important to recognize that physical distribution and the channel of distribution are not independent decision areas. They must be considered together in order to achieve the organization's goal of satisfied customers. Several relationships exist between physical distribution and channels, including the following:

- Defining the physical distribution standards that channel members want.
- Making sure the proposed physical distribution program designed by an organization meets the standards of channel members.
- Selling channel members on physical distribution programs.
- Monitoring the results of the physical distribution program once it has been implemented.

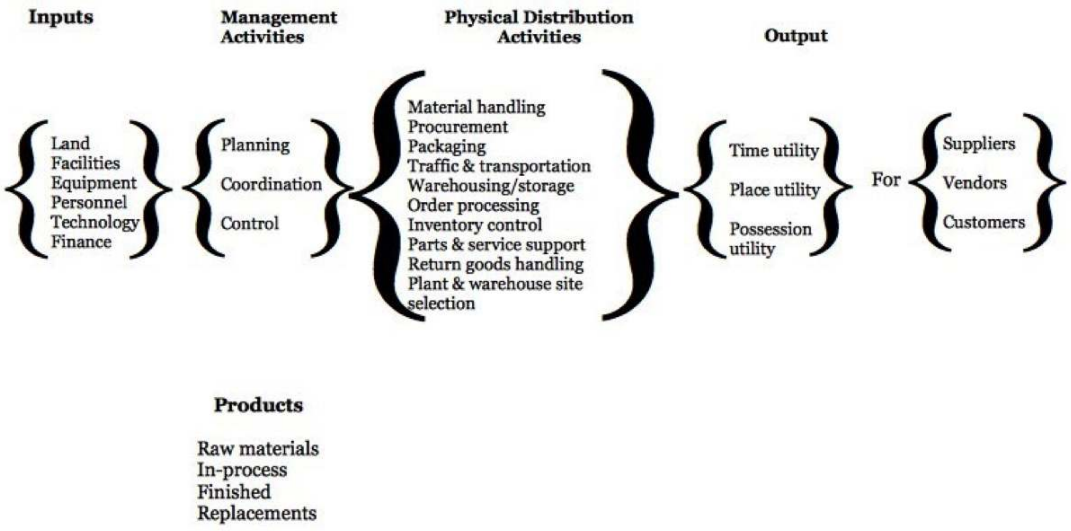


Figure 10.2.5: The physical distribution management process

As you can see in Figure Figure 10.2.5 successful management of the flow of goods from a source of supply (raw materials) to the final customer involves effective planning, implementation, and control of many distribution activities. These involve raw material, in-process inventories (partially completed products not ready for resale), and finished products. Effective physical distribution management results initially in the addition of time, place, and possession utility of products; and ultimately, the efficient movement of products to customer and the enhancement of the firm's marketing efforts.

Physical distribution represents both a cost component and a marketing tool for the purpose of stimulating customer demand. The major costs of physical distribution include transportation, warehousing, carrying inventory, receiving and shipping, packaging, administration, and order processing. The total cost of physical distribution activities represents 13.6 per cent for reseller companies. Poorly managed physical distribution results in excessively high costs, but substantial savings can occur via proper management.

Physical distribution also represents a valuable marketing tool to stimulate consumer demand. Physical distribution improvements that lower prices or provide better service are attractive to potential customers. Similarly, if finished products are not supplied at the right time or in the right places, firms run the risk of losing customers.

Footnotes

(36): Murra Raphel, "Up Against the Wal-Mart," Direct Marketing, April 1999, pp. 82-84; Adrienne Sanders, "Yankee Imperialists," Forbes December 13,1999, p. 36; Jack Neff, "Wal-mart Stores Go Private (Label)," Advertising Age, November 29,1999, pp. 1, 34, 36; Alice Z. Cuneo, "Wal-Mart's Goal: To Reign Over Web," Advertising Age, July 5 1999, pp. 1, 27.

(37): Herb Greenberg, "Dead Mall Walking," Fortune, July 8, 2000, p. 304; Calmetla Y. Coleman, "Making Malls (Gasp!) Convenient," The Wall Street Journal, February 8 , 2000, pp. B 1, B2; Bill Briggs. "Birth and Death of the American Mall," The Denver Post, June 4, 2000, pp. D1 D4.

(38): Heather Green, "Shake Out E- Tailers," Business Week, May 15, 2000, pp. 103-106; Ellen Neubome, "It's the Service, Stupid," Business Week, April 3. 2000. p. E8; Chris Ott; "Will Online Shopping Kill Traditional Retail?" The Denver Business Journal, Oct. 28. 1999, p. 46A; Steve Caulk, "Online Merchants Need More Effective Web Sites," Rocky Mountain News. Thursday, March 8. 2001 , p. 5B.

Sources

Section 10.1 Basics of Distribution Channels is adapted from the chapter '10. Channel concepts: distributing the product' from the textbook 'Introducing Marketing, First Edition, 2011' authored by John Burnett – this book was published under The Global Text Project, funded by the Jacobs Foundation, Zurich, Switzerland.

The following changes were made to the most recent edition: Divided ‘Chapter 10. Channel concepts: distributing the product’’ into three sections; Removed Created new title for Figure featuring Anderson ad.; Removed box titled ‘In Practice’ from wsj.com; Removed case application at the end of chapter; Added learning objectives.

This page titled 10.2: Basics of Distribution Channels is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

10.3: Global Supply Chains

Learning Objectives

After reading this section, students should be able to …

1. define a supply chain
2. explain the traditional to the new supply-chain model

A supply chain refers to the flow of physical goods and associated information from the source to the consumer. Key supply-chain activities include production planning, purchasing, materials management, distribution, customer service, and sales forecasting. These processes are critical to the success manufacturers, wholesalers, or service providers alike.

Student Example

As a major producer of material products, Vietnam plays a major role in manufacturing for a majority of businesses around the world; including Nike, Adidas, The North Face. and Puma. These products are then shipped to locations around the world to be sold at many different retail locations. The global supply chain of these products is a lot more complex than many other brands around the world as they have outsourced the manufacturing to best suit their needs and the customers' needs (quality, price, speed…etc…).

Hollis Cherry

Class of 2020

Electronic commerce and the Internet have fundamentally changed the nature of supply chains and have redefined how consumers learn about, select, purchase, and use products and services. The result has been the emergence of new business-to-business supply chains that are consumer-focused rather than product-focused. They also provide customized products and services.

In the traditional supply-chain model, raw material suppliers define one end of the supply chain. They were connected to manufacturers and distributors, which, in turn, were connected to a retailer and the end customer. Although the customer is the source of the profits, they were only part of the equation in this "*push*" model. The order and promotion process, which involves customers, retailers, distributors, and manufacturers, occurred through time-consuming paperwork. By the time customers' needs were filtered through the agendas of all the members of the supply chain, the production cycle ended up serving suppliers every bit as much as customers.

Driven by e-commerce's capabilities to empower clients, most companies have moved from the traditional "push" business model, where manufacturers, suppliers, distributors, and marketers have most of the power, to a customer-driven "pull" model. This new business model is less product-centric and more directly focused on the individual consumer. As a result, the new model also indicates a shift in the balance of power from suppliers to customers.

Whereas in the old "push" model, many members of the supply chain remained relatively isolated from end users, the new "pull" model has each participant scrambling to establish direct electronic connections to the end customer. The result is that electronic supply-chain connectivity gives end customers the opportunity to become better informed through the ability to research and give direction to suppliers. The net result is that customers now have a direct voice in the functioning of the supply chain, and companies can better serve customer needs, carry less inventory, and send products to market more quickly.

Minicase: Zara's Global Business, ModelCapell, Kamenev, and Saminather, N. (2006, September 4)

Inditex, the parent company of cheap, chic-fashion chain Zara, has transformed itself into Europe's leading apparel retailer over the past 10 years and has racked up impressive results in Asia and the United States. Since 2000, Inditex has more than quintupled its sales and profits as it has tripled the number of stores of its eight brands. (Zara is the biggest, accounting for two-thirds of total revenues.) More recently, Inditex increased its year-on-year net sales by 6% in the first nine months of its 2009

fiscal year to 7,759 million euros. Net income grew to 831 million euros. The retailer launched 266 new stores in the first nine months, bringing the group's total number of stores to 4,530 by the end of October 2009.

Key highlights for the period included openings in Asian markets, with 90 new establishments inaugurated by October 31, 2009. These store openings reflect the strategic importance of Asian markets for the group and underscore a year of robust growth in China, Japan, and South Korea. High points of store launches so far this year include flagship locations in Japan and Mainland China.

In Japan, Zara now has a total of 50 stores, including a second flagship location in Tokyo's Shibuya district, which is a must-see global fashion destination. Prior to this opening, Zara had already welcomed shoppers at another upscale store in Shibuya. Zara thus enhances its excellent retail presence in Tokyo's four key shopping areas: the two aforementioned flagship stores in Shibuya, two each in Ginza and Shinjuku, and one in Harajuku.

Meanwhile, in Beijing, the group celebrated the opening of a flagship location in one of the Chinese capital's busiest shopping hubs. The store, which opened its doors on the pedestrian Wangfujing Street, brings the group's number of stores in China to more than 60. The company's firm commitment to expansion in the Chinese fashion market is reflected in its decision to locate shops not only in Beijing and Shanghai but also in emerging cities such as Harbin, Dalian, Qingdao, Changchun, and Kunming.

To get where it is today, Zara has turned globalization on its head, distributing all of its merchandise, regardless of origin, from Spain. With more outlets in Asia and the United States, replenishing stores twice a week—as Zara does now—will become increasingly complex and expensive. The strain is already starting to show. Costs are climbing and growth in same-store sales is slowing: at outlets open for 2 years or more, revenues were up by 5% last year, compared with a 9% increase in 2004. So far, the company has managed to offset that problem by charging more for its goods as it gets farther from headquarters. For instance, Zara's prices in the United States are some 65% higher than in Spain, brokerage Lehman Brothers, Inc., estimates.

Zara has succeeded by breaking every rule in retailing. For most clothing stores, running out of best-selling items is a disaster, but Zara encourages occasional shortages to give its products an air of exclusivity. With new merchandise arriving at stores twice a week, the company trains its customers to shop and shop often. And forget about setting trends—Zara prefers to follow them. Its aim is to give customers plenty of variety at a price they can afford. Zara made 30,000 different items last year, about triple what the Gap did.

Zara does not collaborate with big-name designers and or use multimillion-dollar advertising campaigns. Instead, it uses its spacious, minimalist outlets—more Gucci than Target—and catwalk-inspired clothing to build its brand. Their advertising is their stores. To get shoppers' attention, Zara is located on some of the world's priciest streets: New York's Fifth Avenue, Tokyo's Ginza, Rome's Via Condotti, and the Champs-Elysees in Paris.

Keeping those locations flush with an ever-changing supply of new clothing means striking the right balance between flexibility and cost. So while rivals outsource to Asia, Zara makes its most fashionable items—half of all its merchandise—at a dozen company-owned factories in Spain. Clothes with a longer shelf life, such as basic T-shirts, are outsourced to low-cost suppliers, mainly in Asia and Turkey.

The tight control makes Zara more fleet-footed than its competitors. While rivals push their suppliers to churn out goods in bulk, Zara intentionally leaves extra capacity in the system. That results in fewer fashion mistakes, which means Zara sells more at full price, and when it discounts, it does not have to go as deep. The chain books 85% of the full ticket price for its merchandise, while the industry average is 60%.

Zara's nerve center is an 11,000-square-foot hall at its headquarters in Arteixo, a town of 25,000 in Galicia. That is where hundreds of twenty-something designers, buyers, and production planners work in tightly synchronized teams. It is there that the company does all of its design and distribution and half of its production. The concentrated activity enables it to move a dress, blouse, or coat from drawing board to shop floor in just 2 weeks, less than a quarter of the industry average.

Consider how Zara managed to latch onto one of hottest trends in just 4 weeks in 2006. The process started when trend-spotters spread the word back to headquarters: white eyelet—cotton with tiny holes in it—was set to become white-hot. A quick telephone survey of Zara store managers confirmed that the fabric could be a winner, so in-house designers got down to work. They zapped patterns electronically to Zara's factory across the street, and the fabric was cut. Local subcontractors stitched

white-eyelet v-neck belted dresses and finished them in less than a week. The $129 dresses were inspected, tagged, and transported through a tunnel under the street to a distribution center. From there, they were quickly dispatched to Zara stores from New York to Tokyo, where they were flying off the racks just 2 days later.

Supply-Chain Management

Supply-chain management (SCM) has three principal components: (a) creating the supply-chain network structure, (b) developing supply-chain business processes, and (c) managing the supply-chain activities, Lambert and Cooper (2000, January).

The supply-chain network structure consists of the member firms and the links between these firms. Primary members of a supply chain include all autonomous companies or strategic business units that carry out value-adding activities in the business processes designed to produce a specific output for a particular customer or market. Supporting members are companies that simply provide resources, knowledge, utilities, or assets for the primary members of the supply chain. For example, supporting companies include those that lease trucks to a manufacturer, banks that lend money to a retailer, or companies that supply production equipment, print marketing brochures, or provide administrative assistance.

Supply chains have three structural dimensions: horizontal, vertical, and the horizontal position of the focal company within the endpoints of the supply chain. The first dimension, horizontal structure, refers to the number of tiers across the supply chain. The supply chain may be long, with numerous tiers, or short, with few tiers. As an example, the network structure for bulk cement is relatively short. Raw materials are taken from the ground, combined with other materials, moved a short distance, and used to construct buildings. The second dimension, vertical structure, refers to the number of suppliers or customers represented within each tier. A company can have a narrow vertical structure, with few companies at each tier level, or a wide vertical structure with many suppliers or customers at each tier level. The third structural dimension is the company's horizontal position within the supply chain. A company can be positioned at or near the initial source of supply, be at or near to the ultimate customer, or be somewhere between these end points of the supply chain.

Business processes are the activities that produce a specific output of value to the customer. The management function integrates the business processes across the supply chain. Traditionally, in many companies, upstream and downstream portions of the supply chain were not effectively integrated. Today, competitive advantage increasingly depends on integrating eight key supply-chain processes—customer relationship management, customer service management, demand management, order fulfillment, manufacturing flow management, procurement, product development and commercialization, and managing returns—into an effective value delivery network, Lambert , Guinipero, and Ridenhower (1998).

Regarding the supply-chain management function itself, in some companies, management emphasizes a functional structure, others a process structure, and yet others a combined structure of processes and functions. The number of business processes that it is critical or beneficial to integrate and manage between companies will likely vary. In some cases, it may be appropriate to link just one key process, and, in other cases, it may be appropriate to link multiple or all the key business processes. However, in each specific case, it is important that executives thoroughly analyze and discuss which key business processes to integrate and manage. With the shift from the traditional "push" to the modern "pull" model, supply-chain management has changed—the integration of e-commerce has produced (a) greater cost efficiency, (b) distribution flexibility, (c) better customer service, and (d) the ability to track and monitor shipments.

Supply-Chain Agility and Resiliency

The best companies create supply chains that can respond to sudden and unexpected changes in markets. Agility—the ability to respond quickly and cost-effectively to unexpected change—is critical because in most industries, both demand and supply fluctuate more rapidly and widely than they used to. In fact, the best companies use agile supply chains to differentiate themselves from rivals. For instance, Zara has become Europe's most profitable apparel brands by building agility into every link of their supply chains. At one end of the product pipeline, Zara has created an agile design process. As soon as designers spot possible trends, they create sketches and order fabrics. That gives them a head start over competitors because fabric suppliers require the longest lead times. However, the company approves designs and initiates manufacturing only after it gets feedback from its stores. This allows Zara to make products that meet consumer tastes and reduces the number of items they must sell at a discount. At the other end of supply chain, the company has created a superefficient distribution system. In part because of these decisions, Zara has grown at more than 20% annually since the late 1990s, and its double-digit net profit margins are the envy of the industry.

Student Example

Starbucks was able to transform its supply chain when they recognized that costs were getting to be too high and sales were cooling. They noticed that their supply chain was not functioning in a way that was best benefiting the company, so they used agility to quickly turn things around. They did this by appointing a new head for the company's supply chain who quickly evaluated what was going wrong in the supply chain. He discovered that service quality was not as high as it should be and that outsourcing led to cost inflation. To combat this, he simplified the supply chain structure and clearly defined functional roles. This ended up greatly benefiting the company.

Kaylee Hogsed

Class of 2020

Agility and resiliency have become more critical in recent years because sudden shocks to supply chains have become more frequent. The terrorist attack in New York in 2001, the dockworkers' strike in California in 2002, and the SARS epidemic in Asia in 2003, for instance, disrupted many companies' supply chains.

Agility and resiliency help supply chains recover more quickly from such sudden setbacks. When, in September 1999, an earthquake hit Taiwan, shipments of computer components to the United States were delayed by weeks and, in some cases, by months. Most computer manufacturers, such as Compaq, Apple, and Gateway, could not deliver products to customers on time and incurred losses. One exception was Dell. The company changed the prices of PC configurations overnight to steer consumer demand away from hardware built with components that were not available to machines that did not require those parts. Dell could do this because it had contingency plans in place. Not surprisingly, Dell gained market share in the earthquake's aftermath, Lee (2004, October).

Supply-chain agility and resilience no longer imply merely the ability to manage risk. It now assumes that the ability to manage risk means being better positioned than competitors to deal with—and even gain advantage from—disruptions. Key to increasing agility and resilience is building flexibility into the supply-chain structure, processes, and management, Sheffi (2005, October).

GLOBAL SUPPLY CHAINS

Global companies must be able to adapt their supply networks when markets or strategies change. The best companies tailor their supply chains to the nature of the markets they serve. They often end up with more than one supply chain, which can be expensive, but, in return, they secure the best manufacturing and distribution capabilities for each offering. Cisco, for example, uses contract manufacturers in low-cost countries such as China for standard, high-volume networking products. For its broad line of mid-value items, the company uses vendors in low-cost countries to build core products, but it customizes those products itself in major markets such as the United States and Europe. And for highly customized, low-volume products, Cisco uses vendors close to main markets, such as Mexico for the United States and Eastern European countries for Europe. Despite the fact that it uses three different supply chains at the same time, the company is careful not to become less agile. Because it uses flexible designs and standardized processes, Cisco can switch the manufacture of products from one supply network to another, when necessary, Sheffi (2005, October).

Companies that compete primarily on the basis of operational excellence typically focus on creating supply chains that deliver goods and services to consumers as quickly and inexpensively as possible. They invest in state-of-the-art technologies and employ metrics and reward systems aimed at boosting supply-chain performance.

For companies competing on the basis of customer intimacy or product leadership, a focus on efficiency is not enough—agility is a key factor. Customer-intimate companies must be able to add and delete products and services as customer needs change; product leadership companies must be able to adapt their supply chains to changes in technology and to capitalize on new ideas.

All companies must align their supply-chain infrastructure and management with their underlying value proposition to achieve sustainable competitive advantage. That is, they must align the interests of all the firms in the supply network so that companies optimize the chain's performance when they maximize their interests.

Minicase: Nikon, With the Help of UPS, Focuses on Supply-Chain Innovation[1]

To support the launch of its new digital cameras, Nikon, with the help of UPS Supply Chain Solutions, reengineered its distribution network to keep retailers well supplied. Nikon knew that customer service capabilities needed to be completely up to speed from the start and that distributors and retailers would require up-to-the-minute information about product availability. While the company had previously handled new product distribution in-house, this time Nikon realized that burdening its existing infrastructure with a new, demanding, high-profile product line could impact customer service performance adversely. So Nikon applied its well-known talent for innovation to creating an entirely new distribution strategy, and it took the rare step of outsourcing distribution of an entire consumer-electronics product line. With UPS Supply Chain Solutions on board, Nikon was able to quickly execute a synchronized supply-chain strategy that moves products to retail stores throughout the United States, Latin America, and the Caribbean, and allows Nikon to stay focused on the business of developing and marketing precision optics.

Starting at Nikon's manufacturing centers in Korea, Japan, and Indonesia, UPS Supply Chain Solutions now manages air and ocean freight and related customs brokerage. Nikon's freight is directed to Louisville, Kentucky, which not only serves as the all-points connection for UPS's global operations but is also home to the UPS Supply Chain Solutions Logistics Center main campus. Here, merchandise can be either "kitted" with accessories such as batteries and chargers or repackaged to in-store display specifications. Finally, the packages are distributed to literally thousands of retailers across the United States or shipped for export to Latin American or Caribbean retail outlets and distributors, using any of UPS's worldwide transportation services to provide the final delivery.

With the UPS Supply Chain Solutions system in place, the process calibrates the movement of goods and information by providing SKU-level visibility within complex distribution and information technology (IT) systems. UPS also provides Nikon advance shipment notifications throughout the U.S., Caribbean, and Latin American markets. The result: a "snap shot" of the supply chain that rivals the performance of a Nikon camera.

Nikon has already seen the results of its innovation in both digital technology and product distribution. The consumer digital-camera sector is one of Nikon's fastest-growing product lines. In addition, supply-chain performance and customer service have measurably improved. Products leaving Nikon manufacturing facilities in Asia can now be on a retailer's shelf in as few as 2 days. While products are en route, Nikon also has the ability to keep retailers informed of delivery times and to adjust them as needed so that no retailer needs to miss sales opportunities due to lack of product availability.

Leading companies take care to align the interests of all the firms in their supply chain with their own. This is important, because every supply-chain partner firm—whether a supplier, an assembler, a distributor, or a retailer—will focus on its own interests. If any company's interests differ from those of the other organizations in the supply chain, its actions will not maximize the chain's performance.

One way companies align their partners' interests with their own is by redefining the terms of their relationships so that firms share risks, costs, and rewards equitably. Another involves the use of intermediaries, for example, when financial institutions buy components from suppliers at hubs and resell them to manufacturers. Everyone benefits because the intermediaries' financing costs are lower than the vendors' costs. Although such an arrangement requires trust and commitment on the part of suppliers, financial intermediaries, and manufacturers, it is a powerful way to align the interests of companies in supply chains.

A prerequisite to creating alignment is the availability of information so that all the companies in a supply chain have equal access to forecasts, sales data, and plans. Next, partner roles and responsibilities must be carefully defined so that there is no scope for conflict. Finally, companies must align incentives so that when companies try to maximize returns, they also maximize the supply chain's performance.

Minicase: Nestlé Pieces Together Its Global Supply Chain, Steinert-Threlkeld (2006, January)

A few years ago, Nestlé, the world's largest food company, set out to standardize how it operates around the world. It launched GLOBE (Global Business Excellence), a comprehensive program aimed at implementing a single set of procurement, distribution, and sales management systems. The logic behind the $2.4-billion project was impeccable: implementing a

standardized approach to demand forecasting and purchasing would save millions and was critical to Nestlé's operating efficiency in 200 countries around the world.

Nestlé's goal was simple: to replace its 14 different SAP enterprise-planning systems—in place in different countries—with a common set of processes, in factory and in administration, backed by a single way of formatting and storing data and a single set of information systems for all of Nestlé's businesses.

For Nestlé, this was not an everyday project. When it built a factory to make coffee, infant formula, water, or noodles, it would spend $30 to $40 million; committing billions in up-front capital to a backroom initiative was unheard of, or, as someone noted, "Nestlé makes chocolate chips, not electronic ones."

The GLOBE project also stood as the largest-ever deployment of mySAP.com. But whether the software got rolled out to 230,000 Nestlé employees or 200 was not the point. The point was to make Nestlé the first company to operate in hundreds of countries in the same manner as if it operated in one. And that had not been achieved by any company—not even the British East India Company at the peak of its tea-trading power—in the history of global trade.

Consider the complexities. Nestlé was the world's largest food company, with almost $70 billion in annual sales. By comparison, the largest food company based in the United States, Kraft Foods, was less than half that size. Nestlé's biggest Europe-based competitor, Unilever, had about $54 billion in sales. In addition, Nestlé grew to its huge size by selling lots of small-ticket items—Kit Kat, now the world's largest-selling candy bar; Buitoni spaghetti; Maggi packet soups; Lactogen dried milk for infants; and Perrier sparkling water.

The company operated in some 200 nations, including places that were not yet members of the United Nations. It ran 511 factories and employed 247,000 executives, managers, staff, and production workers worldwide.

What is more, for Nestlé, nothing was simple. The closest product to a global brand it had was Nescafé; more than 100 billion cups were consumed each year. But there were more than 200 formulations, made to suit local tastes. All told, the company produced 127,000 different types and sizes of products. Keeping control of its thousands of supply chains, scores of methods of predicting demand, and its uncountable variety of ways of invoicing customers and collecting payments was becoming evermore difficult and eating into the company's bottom line.

The three baseline edicts for project GLOBE were: harmonize processes, standardize data, and standardize systems. This included how sales commitments were made, factory production schedules established, bills to customers created, management reports pulled together, and financial results reported. Gone would be local customs, except where legal requirements and exceptional circumstances mandated an alternative manner of, say, finding a way to pay the suppliers of perishable products like dairy or produce in a week rather than 30 days. And when was this all to be done? In just 3 and a half years. The original GLOBE timeline, announced by Nestlé's executive board, called for 70% of the company's $50 billion business to operate under the new unified processes by the end of 2003.

Mission impossible? The good news was that in one part of the world, Asia, market managers had shown they could work together and create a common system for doing business with their customers. They had used a set of applications from a Chicago supplier, SSA Global, that allowed manufacturers operating worldwide to manage the flow of goods into their factories, the factories themselves, and the delivery of goods to customers while making sure the operations met all local and regional legal reporting requirements. The system was adopted in Indonesia, Malaysia, the Philippines, Thailand, even South Africa, and was dubbed the "Business Excellence Common Application."

But this project was orders of magnitude more involved and more complex. Instead of just a few countries, it would affect 200 of them. Change would have to come in big, not small, steps. Using benchmarks they could glean from competitors such as Unilever and Danone, and assistance from PricewaterhouseCoopers consultants and SAP's own deployment experts, the executives in charge of the GLOBE project soon came to a conclusion they had largely expected going in: this project would take more people, more money, and more time than the board had anticipated. Instead of measuring workers in the hundreds, and Swiss francs in the hundreds of millions, as originally expected, the team projected that 3,500 people would be involved in GLOBE at its peak. The new cost estimate was 3 billion Swiss francs, about $2.4 billion. And the deadline was pushed back as well. The new target: putting the "majority of the company's key markets" onto the GLOBE system by the end of 2005, not 2003.

To lead this massive undertaking, GLOBE's project manager chose a group of business managers, not technology managers, from all of Nestlé's key functions—manufacturing, finance, marketing, and human resources—and from all across the world—Europe, Asia, the Americas, Africa, and Australia.

These were people who knew how things actually worked or should work. They knew how the company estimated the demand for each of its products, how supplies were kept in the pipeline, even mundane things like how to generate an invoice, the best way to process an order, how to maintain a copier or other office equipment, and how to classify all the various retail outlets, from stores to vending machines, that could take its candy bars and noodles. The system would allow managers to manage it all from the web.

The process for the team of 400 executives started with finding, and then documenting, the four or five best ways of doing a particular task, such as generating an invoice. Then, the GLOBE team brought in experts with specific abilities, such as controlling financial operations, and used them as "challengers." They helped eliminate weaknesses, leaving the best practices standing.

At the end of that first year, the project teams had built up the basic catalog of practices that would become what they would consider the "greatest asset of GLOBE": its "Best Practices Library." This was an online repository of step-by-step guides to the 1,000 financial, manufacturing, and other processes that applied across all Nestlé businesses. Grouped into 45 "solution sets," like demand planning or closing out financial reports, the practices could now be made available online throughout the company, updated as necessary, and commented on at any time.

It was not always possible to choose one best practice. Perhaps the hardest process to document was "generating demand." With so many thousands of products, hundreds of countries, and local tastes to deal with, there were "many different ways of going to market," many of which were quite valid. This made it hard to create a single software template that would serve all market managers.

So GLOBE executives had to practice a bit more tolerance on that score. The final GLOBE template included a half-dozen or so different ways of taking products to market around the world. But no such tolerance was shown for financial reporting. The 400 executives were determined to come up with a rigorous step-by-step process that would not change.

Experts were brought in along the way to challenge each process. But in the end, one standard would, in this case, have to stand. Financial terms would be consistent. The scheme for recording dates and amounts would be the same. The timing of inputting data would be uniform; only the output could change. In Thailand, there would have to be a deviation so that invoices could be printed out in Thai characters so that they could be legal and readable. In the Philippines, dates would have to follow months, as in the United States. Most of the rest of the world would follow the European practice of the day preceding the month.

Progress was slow, however. Nestlé managers had always conducted their businesses as they saw fit. As a consequence, even standardizing on behind-the-scenes practices, like how to record information for creating bills to customers met, with resistance. As country managers saw it, decision making was being taken out of local markets and being centralized. Beyond that, someone had to pay the bill for the project itself. That would be the countries, too.

By the fall of 2005, almost 25% of Nestlé was running on the GLOBE templates. And GLOBE's project manager was confident that 80% of the company would operate on the new standardized processes by the end of 2006. The greatest challenge was getting managers and workers to understand that their jobs would change—in practical ways. In many instances, workers would be entering data on raw materials as they came into or through a factory. Keeping track of that would be a new responsibility. Doing it on a computer would be a wholly new experience. And figuring out what was happening on the screen could be a challenge. Minutia? Maybe. Considerable change? Definitely.

But the templates got installed and business went on—in Switzerland, Malaysia-Singapore, and the Andean region. In each successive rollout, the managers of a given market had 9 months or more to document their processes and methodically adjust them to the templated practices. In 2003, Thailand, Indonesia, and Poland went live. In 2004, Canada, the Philippines, and the Purina pet food business in the United Kingdom joined the network. But, by then, the system was bumping up against some technical limits. In particular, the mySAP system was not built for the unusual circumstances of the Canadian food retailing market. Food manufacturers have lots of local and regional grocery chains to sell to, and promotional campaigns are rife.

MySAP was not built to track the huge amount of trade promotions engaged in by Nestlé's Canadian market managers: there were too many customers, too many products, and too many *data points*.

In India, changing over in mid-2005 was complicated by the fact that not only was Nestlé overhauling all of its business processes, but it also did not know what some of the key financial processes would have to be. At the same time it was converting to the GLOBE system, India was changing its tax structure in all 29 states and six territories. Each would get to choose whether, and how, to implement a fee on the production and sale of products, known as a value-added tax. Meeting the scheduled go-live date proved difficult.

And all over the world, managers learned that the smallest problem in standardized systems means that product can get stopped in its tracks. In Indochina, for instance, pallets get loaded with 48 cases of liquids or powders, and are then moved out. If a worker fails to manually check that the right cases have been loaded on a particular pallet, all dispatching stops are held up until the pallet is checked.

These setbacks notwithstanding, GLOBE taught Nestlé how to operate as a truly global company. For example, managers from the water businesses initially rejected the idea of collecting, managing, and disseminating data in the same way as their counterparts in chocolate and coffee. Some managers figured that if they were able to produce all the water or all the chocolate they needed for their market locally, that should be enough. But the idea was to get Nestlé's vast empire to think, order, and execute as one rather than as a collection of disparate companies. This meant that a particular manufacturing plant in a particular manager's region might be asked to produce double or triple the amount of coffee it had in the past. Or it might mean that a particular plant would be closed.

So, while the company did away with data centers for individual countries, each one does now have a data manager. The task is to make sure that the information that goes into GLOBE's data centers is accurate and complete. That means that country managers can concentrate more on what really matters: serving customers.

References

1. http://www.ups-scs.com/solutions/cas...s/cs_nikon.pdf

Sources

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- "Supply Chains: From Push to Pull", section 9.1 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.
- "Supply-Chain Management", section 9.2 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.
- "Supply-Chain Agility and Resiliency", section 9.3 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.
- "Making Supply Chains Adaptable", section 9.4 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.
- "Creating Supply-Chain Alignment", section 9.5 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

10.3: Global Supply Chains is shared under a CC BY-NC-SA license and was authored, remixed, and/or curated by LibreTexts.

10.4: Global Sourcing and Distribution

Learning Objectives

After reading this section, students should be able to …

1. outline the advantages of global sourcing.
2. know the pros and cons of sole-sourcing and multisourcing.
3. describe the distribution-management choices companies have when entering new international markets.

Global sourcing refers to buying the raw materials or components that go into a company's products from around the world, not just from the headquarters' country. For example, Starbucks buys its coffee from locations like Colombia and Guatemala. The advantages of global sourcing are quality and lower cost. Global sourcing is possible to the extent that the world is flat—for example, buying the highest-quality cocoa beans for making chocolate or buying aluminum from Iceland, where it's cheaper because it's made using free geothermal energy.

When making global-sourcing decisions, firms face a choice of whether to sole-source (i.e., use one supplier exclusively) or to multisource (i.e., use multiple suppliers). The advantage of sole-sourcing is that the company will often get a lower price by giving all of its volume to one supplier. If the company gives the supplier a lot of business, the company may have more influence over the supplier for preferential treatment. For example, during a time of shortage or strained capacity, the supplier may give higher quantities to that company rather than to a competitor as a way of rewarding the company's loyalty.

Student Example

Nestlé is a global company, comprising brands such as Kit Kat, Nesquick, and Stouffer's, as well as other food brands and baby formulas. To source their raw materials, they follow a multisource model. A specific example within Nestle is that they are sourcing some of their global palm oil from five smallholder farms in Indonesia, Malaysia, Ghana, Côte d'Ivoire, and Peru. This multisourcing benefits Nestlé because they can source their palm oil from various countries, allowing for a supply chain with less uncertainty. If one palm oil supplier were to go out of business or provide less than expected, one of the other suppliers would be able to make up for the slack. A side benefit is these smallholders gain a foothold in the global market.

Zach Harper

Class of 2020

On the other hand, using multiple suppliers gives a company more flexibility. For instance, if there's a natural disaster or other disruption at one of their suppliers, the company can turn to its other suppliers to meet its needs. For example, when Hurricane Mitch hit Honduras with 180-mile-per-hour winds, 70 to 80 percent of Honduras's infrastructure was damaged and 80 percent of its banana crop was lost. Both Dole Food Company and Chiquita bought bananas from Honduras, but Dole relied more heavily on bananas from Honduras than from other countries. As a result, Dole lost 25 percent of its global banana supply, but Chiquita lost only 15 percent.[1]

Sole-Sourcing Advantages

- Price discounts based on higher volume
- Rewards for loyalty during tough times
- Exclusivity brings differentiation
- Greater influence with a supplier

Sole-Sourcing Disadvantages

- Higher risk of disruption
- Supplier has more negotiating power on price

Multisourcing Advantages

- More flexibility in times of disruption
- Negotiating lower rates by pitting one supplier against another

Multisourcing Disadvantages

- Quality across suppliers may be less uniform
- Less influence with each supplier
- Higher coordination and management costs

Whichever sourcing strategy a company chooses, it can reduce risk by visiting its suppliers regularly to ensure the quality of products and processes, the financial health of each supplier, and the supplier's adherence to laws, safety regulations, and ethics.

Ethics in Action

The Case of Global Sourcing

While there is little systematic research on questions related to ethics and global sourcing, one recent survey in the context of clothing manufacturers identified the following most encountered issues:[2]

- **Child labor.** Forty-three percent of the respondents had encountered factories where child labor was being used. India, China, Thailand, and Bangladesh were cited as the worst offenders in this regard, partly because of the absence or unreliability of birth certificates, but also because of the difficulty that Westerners have in assessing the age of workers in these countries. Buyers relied on the management of the factory to check on documents supplied by the employee.
- **Dangerous working conditions and health and safety issues.** Forty-three percent of the respondents had encountered dangerous working conditions in factories. These included unsafe machinery (e.g., machine guards having been removed to speed up production), workers failing to use safety equipment such as cutting gloves, and the use and storage of hazardous chemicals (e.g., those used for dyeing and printing). Fire regulations were also sometimes inadequate, both in factories and in the dormitory accommodation often provided for workers who live away from their home regions. Sometimes fire exits were locked, and fire extinguishers were missing.
- **Bribery and corruption.** Thirty-one percent of respondents said that they had experienced bribery and corruption. One blatantly fraudulent practice mentioned was for suppliers to mislead the buyer over the true source of production. Many suppliers claim that goods are made in one factory, then transfer the production elsewhere, making it difficult for the retailer to audit.
- **Exploitation of the workforce.** Twenty-five percent of respondents mention some aspect of exploitation of the workforce, encompassing the issues of child labor and health and safety. However, it can also cover low wages being paid to workers and excessive overtime being expected by employers. Respondents specifically mentioned that they had encountered worker exploitation. Many spoke of long working hours in factories, especially at peak periods, with employees often working over seventy hours per week.

Student Example

Apple uses global sourcing to acquire most of their products. I learn that their products are made in factories in China. In the past, they have allegedly experienced ethical issues, like child labor and dangerous working conditions. It was reported in the news that they had children working in those factories. Also, they were allegedly working in very harsh conditions; so harsh that workers started committing suicide. If this is true, global sourcing can be risky for the reason that they may not have complete control over what happens in the factories, and might not even know what goes on inside them.

Elizabeth Garcia

Class of 2020

Distribution Management

Selling internationally means considering how your company will distribute its goods in the market. Developed countries have good infrastructure—passable roads that can accommodate trucks, retailers who display and sell products, and reliable communications infrastructure and media choices. Emerging markets, on the other hand, often have very fragmented distribution networks, limited logistics, and much smaller retailer outlets. Hole-in-the-wall shops, door-to-door peddlers, and street vendors play a much larger role in emerging-market countries. In the emerging countries of Africa, for example, books might be sold from the back of a moped.

In addition, the standards of living in emerging countries vary widely. Most of the middle class lives in cities, but the percentage of the population that lives in rural areas varies by country. In India, 70 percent of the population lives in rural areas, whereas in Latin America only 30 percent does.

Rural logistics are especially problematic. Narrow dirt roads, weight-limited bridges, and mud during the rainy season hamper the movement of goods. An executive at computer storage device manufacturer EMC noted that sometimes the company's refrigerator-sized, data-storage systems have had to be transported on horse-drawn wagons.

How Nokia Tackles Distribution Challenges

Nokia is a $59 billion company with over 123,000 employees.[3] It sells 150 different devices, of which 50 to 60 are newly introduced each year. Each device can be customized on many variants, including language and content. This variation adds greatly to the devices' complexity; three hundred to four hundred components need to arrive on time at factories in order for the devices to be built. Approximately one billion people use Nokia devices worldwide. Countries like China, India, and Nigeria, which ten years ago had almost zero penetration of mobile phones, now have twenty million to forty million users each. Emerging markets now account for over half of Nokia's annual sales.

Nokia has the challenge of selling a growing variety of mobile devices in hundreds of thousands of tiny retail outlets in the developing world. To tackle reaching its rural customers in developing countries, Nokia has 350,000 points of presence in rural areas, from small kiosks and corner shops to organized retail outlets. Nokia has 100,000 such point-of-sale (POS) outlets in India, 80,000 in China, and 120,000 in the Middle East and Africa.

To train salespeople in developing countries, Nokia created an internal university to educate the people who sell its phones in these POS locations—an average of five people per location. Nokia Academy teaches local salespeople about the features of the phones and how to sell them. As Nokia expands further into these emerging markets, it will penetrate deeper into the rural areas and will distribute through local providers.

Nokia's challenge is to maintain its strong brand name—the fifth most recognized brand in the world—across these POS locations. Meeting this challenge has taken years. One way that Nokia maintains control of its brand across these locations is by having managers visit the outlets on a regular basis and using their mobile phones to photograph the shelf layout at each location. This lets Nokia control quality and improve merchandizing techniques at all locations.

Distribution-Management Choices: Partner, Acquire, or Build from Scratch

There are typically three distribution strategies for entering a new market. First, companies can do a joint-venture or partnership with a local company. This is the strategy Walmart used when entering Mexico. A second strategy is to acquire a local company to have immediate access to large-scale distribution. The Home Depot pursued this strategy in China when it acquired a partner with whom it had been working for quite some time. Third, a company can to build its own distribution from scratch. Retailer Carrefour chose this route in China years ago, because it knew China would offer a big opportunity, and Carrefour wanted to develop its own local capabilities. Which strategy the company chooses depends on its timetable for volume in the market, local foreign-ownership laws, and the availability of suitable partners or acquisition targets.

? Spotlight on International Strategy and Entrepreneurship

Unilever Solves Distribution Issues in India

Hindustan Unilever Limited (HUL), Unilever's Indian subsidiary, wanted to reach the 70 percent of Indians who live in rural villages. This underserved market is very hard to reach. Not only is marketing to remote villages difficult, but the physical

transport of products is no easier. Most of the villages lack paved roads, making traditional truck-based distribution arduous. The only way to reach many of these remote villages is by single-track dirt trails.

In response to these conditions, HUL has created Project Shakti (the word means “strength”) and developed a network of 14,000 women and women-owned cooperatives to serve 50,000 villages. The women handle the logistics and door-to-door retailing of a range of personal-care products. To address the needs of the market and this novel distribution system, HUL has packaged its products in much smaller sizes. The effort has created $250 million in new revenues for HUL, of which 10 percent is used for financing the women entrepreneurs. By using this approach, HUL doesn’t have to deal with the problem of moving products in rural India. The women or their employees come to the company’s urban distribution centers to get the products.

? Key Takeaways

- Global sourcing refers to buying the raw materials or components that go into a company’s products from around the world, not just from the headquarters’ country. The advantages of global sourcing include access to higher quality or lower prices.
- When making sourcing decisions, companies must decide whether to sole-source (i.e., to use one supplier exclusively) or to use two or more suppliers. Sole-sourcing can bring advantages of price discounts based on volume and may give the company greater influence over a supplier or preferential treatment during times of constrained capacity Sole-sourcing can also bring advantages of differentiation or high quality. The disadvantages of sole-sourcing, however, are that the company faces a higher risk of disruption if something happens to that supplier. Also, the supplier may hold more negotiating power on price.
- A company typically has three distribution strategies for entering a new market—to engage in a joint venture, to acquire a local company, or to build its own distribution network from scratch. Establishing a partnership or joint venture is the least costly approach, followed by acquisition. Building a distribution network from scratch is the most costly and time consuming, but it may give the company the most local experience and capabilities for the long term.
- Distribution channels in emerging markets are less developed, which means that companies may need to seek novel solutions to distributing their products, such as Hindustan Unilever Limited creating its own distribution network of 14,000 female independent distributors and cooperatives or Nokia creating Nokia Academy to train salespeople.

References

1. Yossi Sheffi, The Resilient Enterprise (Cambridge, MA: MIT Press, 2005), 216–17. In the aftermath, Chiquita’s revenues increased, while Dole’s decreased.
2. Mike Pretious and Mary Love, “Sourcing Ethics and the Global Market: The Case of the UK Retail Clothing Sector,” International Journal of Retail & Distribution Management 34, no. 12 (2006): 892–903.
3. “Nokia Corporation Company Profile,” Hoovers, accessed August 6, 2010, http://www.hoovers.com/company/Nokia...-1-1njdap.html.

Sources

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- “Competing Effectively through Global Marketing, Distribution, and Supply-Chain Management”, chapter 14 from the book Challenges and Opportunities in International Business (v. 1.0)under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.
- “Supply-Chain Management”, section 9.2 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.
- “Supply-Chain Agility and Resiliency”, section 9.3 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.
- “Making Supply Chains Adaptable”, section 9.4 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

- “Creating Supply-Chain Alignment”, section 9.5 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

This page titled 10.4: Global Sourcing and Distribution is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

10.5: Organizing The Channel

Learning Objectives

After reading this section, students should be able to …

- list the methods used in organizing channels
- outline the management of underlying behavioral dimensions present in most channels

ORGANIZING THE CHANNEL

Either through a planned process or through a natural evolution, channels of distribution reflect an observable organization structure. Three types are most common: conventional channels, vertical marketing systems, and horizontal channel systems.

Conventional channels

The *conventional channel* of distribution could be described as a group of independent businesses, each motivated by profit, and having little concern about any other member of the distribution sequence. There are no all-inclusive goals, and in many instances, the assignment of tasks and the evaluation process are totally informal. Consequently, channel frameworks might be working against one another, tasks may go undone, and ineffective channel member relationships may last for years. Despite these deficiencies, this type of channel structure remains most common, and there are numerous examples of such networks working.

Vertical marketing systems

Vertical marketing systems have emerged as a solution to the problems of conventional networks. A *vertical marketing system* (VMS) comes about when a member of the distribution channel (usually the manufacturer) assumes a leadership role and attempts to coordinate the efforts of the channel so that mutually beneficial goals can be attained. Three forms of vertical integration are now common.

Administered VMS

The *administered VMS* is very close to the conventional network, but differs in that it is informally guided by goals and programs developed by one or a limited number of firms in the existing channel. This framework is the source of the concept of a channel captain, in that administrative skills and the power of one individual may be the driving force of the channel. Often the dominant brands, as in the case of Xerox or Procter & Gamble, are able to manifest this cooperation.

Through the recognition of a channel leader, the distribution networks function better, sales and profits are higher, product exposure improves, inventory management systems are initiated, and the coordination of promotional activities becomes a reality. An administered system is not without its problems. Often, this effort is placed on the shoulders of a single individual. Another drawback is the tendency of polarizing channel members. Businesses either become part of the VMS or remain strongly independent. Eventually these independents may find themselves at a tremendous competitive disadvantage, and may even be deprived of certain channel benefits.

Contractual VMS

There are instances when channel members wish to formalize their relationship by employing a contractual agreement, known as a *contractual VMS*. This provides additional control, and either explicitly or implicitly spells out the marketing functions to be performed by all the members of the channel. This is the most popular form of vertical marketing arrangement.

Corporate VMS

When channel members on different levels are owned and operated by one organization, a *corporate vertical marketing system* is said to exist. Such integration can be forward or backward. A manufacturer who owns the various intermediaries in its channel network has engaged in *forward* integration. A retailer who takes over the wholesaling and manufacturing tasks is *backward* integrating. This process can entail either the organization's purchasing the institutions, or establishing its own facilities. Although partial forward or backward integration is most common, total integration is becoming more popular. Manufacturers who have recently integrated through to the retail level are Dannon Yogurt, Blue Bell Ice Cream, and Pepperidge Farms. Sears and Safeway

stores are two retailers that have successfully integrated backward. American Hospital Supply Corporation is an example of a wholesaler that has integrated both backward and forward.

Horizontal channel systems

There are instances where two or more companies are unable to acquire the capital, or do not have the technical or production know-how, to effectively market their products alone. In such cases, these companies may establish a temporary or quasi-permanent relationship in order to work with each other, and create the channel mechanism required to reach their target markets. This arrangement has been labeled a *horizontal channel system*. For example, two small manufacturers might combine their shipments to common markets in order to gain full carload transportation rates that each could not obtain separately. Another common scenario is for a large retailer to buyout several competing small retailers in order to gain entry into certain markets or with certain customers.

THE CHANNEL MANAGEMENT PROCESS

Evidence suggests that a channel should be managed just like the product, promotion, and pricing functions.

This channel management process contains five steps.

Analyze the consumer

We begin the process of channel management by answering two questions. First, to whom shall we sell this merchandise immediately? Second, who are our ultimate users and buyers? Depending upon a host of factors, including the type of product, functions performed in the channel, and location in the channel, the immediate and ultimate customers may be identical or they may be quite separate. In both cases, some fundamental questions would apply. There is a need to know what the customer needs, where they buy, when they buy, why they buy from certain outlets, and how they buy.

It is best that we first identify the traits of the ultimate user, since the results of this evaluation might determine the other channel institutions we would use to meet these needs. For example, the buying characteristics of the purchaser of a high-quality VCR might be as follows:

- purchased only from a well-established, reputable dealer
- purchased only after considerable shopping to compare prices and merchandise characteristics
- purchaser willing to go to some inconvenience (time and distance) to locate the most acceptable brand
- purchased only after extended conversations involving all interested parties, including dealer, users, and purchasers
- purchase may be postponed
- purchased only from a dealer equipped to render prompt and reasonable product service

These buying specifications illustrate the kinds of requirements that the manufacturer must discover. In most cases, purchase specifications are fairly obvious and can be discovered without great difficulty. On the other hand, some are difficult to determine. For example, certain consumers will not dine at restaurants that serve alcohol; others will patronize only supermarkets that exhibit definite ethnic characteristics in their merchandising. Nonetheless, by careful and imaginative research, most of the critical factors that bear on consumer buying specifications can be determined.

Knowing the buying specifications of consumers, the channel planner can decide on the type or types of wholesaler or retailer through which a product should be sold. This requires that a manufacturer contemplating distribution through particular types of retailers become intimately familiar with the precise location and performance characteristics of those he is considering.

In much the same way that buying specifications of ultimate users are determined, the manufacturers must also discover buying specifications of resellers. Of particular importance is the question, “from whom do my retail outlets prefer to buy?” The answer to this question determines the types of wholesalers (if any) that the manufacturer should use. Although many retailers prefer to buy directly from the manufacturers, this is not always the case. Often, the exchange requirements of manufacturers (e.g. infrequent visit, large order requirements, and stringent credit terms) are the opposite of those desired by retailers. Such retailers would rather buy from local distributors who have lenient credit terms and offer a wide assortment of merchandise.

Establish the channel objectives

The channel plan is derived from channel objectives. They are based on the requirements of the purchasers and users, the overall marketing strategy, and the long-run goals of the corporation. However, in cases when a company is just getting started, or an older company is trying to carve out a new market niche, the channel objectives may be the dominant objectives. For example, a small manufacturer wants to expand outside the local market. An immediate obstacle is the limited shelf space available to this manufacturer. The addition of a new product to the shelves generally means that space previously assigned to competitive products must be obtained. Without this exposure, the product is doomed.

As one would expect, there is wide diversity of form that channel objectives can take. The following areas encompass the major categories:

- Growth in sales by reaching new markets, and/or increasing sales in existing markets.
- Maintenance or improvement of market share–educate or assist channel components in their efforts to increase the amount of product they handle.
- Achieve a pattern of distribution–structure the channel in order to achieve certain time, place, and form utilities.
- Create an efficient channel–improve channel performance by modifying various flow mechanisms.

Specify distribution tasks

After the distribution objectives are set, it is appropriate to determine the specific distribution tasks (functions) to be performed in that channel system. The channel manager must be far more specific in describing the tasks, and must define how these tasks will change depending upon the situation. An ability to do this requires the channel manager to evaluate all phases of the distribution network. Tasks must be identified fully, and costs must be assigned to these tasks. For example, a manufacturer might delineate the following tasks as being necessary in order to profitably reach the target market:

- provide delivery within 48 hours after order placement
- offer adequate storage space
- provide credit to other intermediaries
- facilitate a product return network
- provide readily available inventory (quantity and type)
- provide for absorption of size and grade obsolescence

Evaluate and select from channel alternatives

Determining the specific channel tasks is a prerequisite for the evaluation and selection process. There are four bases for channel alternatives: number of levels, intensity at the various levels, types of intermediaries at each level, and application of selection criterion to channel alternatives.

Number of levels

Channels can range in levels from two to several (five being typical). The two-level channel (producer to consumer) is a direct channel and is possible only if the producer or customer are willing to perform several of the tasks performed by intermediaries. The number of levels in a particular industry might be the same for all the companies simply because of tradition. In other industries, this dimension is more flexible and subject to rapid change.

Intensity at each level

Once the number of levels has been decided, the channel manager needs to determine the actual number of channel components involved at each level. How many retailers in a particular market should be included in the distribution network? How many wholesalers? Although there are limitless possibilities, the categories shown in Tabvle 10.2 describes the general alternatives.

The intensity decision is extremely critical, because it is an important part of the firm’s overall marketing strategy. Companies such as Coca-Cola and Timex watches have achieved high levels of success through their intensive distribution strategy.

Types of intermediaries

As discussed earlier, there are several types of intermediaries that operate in a particular channel system. The objective is to gather enough information to have a general understanding of the distribution tasks these intermediaries perform. Based on this

background information, several alternatives will be eliminated.

1. Exclusive distribution (such as Ethan Allen and Drexel Heritage Furniture)
    1. the use of a single or very few outlets
    2. creates high dealer loyalty and considerable sales support
    3. provides greater control
    4. limits potential sales volume
    5. success of the product is dependent upon the ability of a single intermediary
2. Intensive distribution (such as candy)—the manufacturer attempts to get as many intermediaries of a particular type as possible to carry the product
    1. provides for increased sales volume, wider consumer recognition, and considerable impulse purchasing
    2. low price, low margin, and small order sizes often result
    3. extremely difficult to stimulate and control this large number of intermediaries
3. Selective distribution (such as Baskin-Robbins)–an intermediary strategy, with the exact number of outlets in any given market dependent upon market potential, density of population, dispersion of sales, and competitors' distribution policies
    1. contains some of the strengths and weaknesses of the other two strategies
    2. it is difficult to determine the optimal number of intermediaries in each market

Table 10.2: Levels of channel intensity.

Having identified several possible alternative channel structures, the channel manager is now at a place where he or she can evaluate these alternatives with respect to some set of criteria. Company factors, environmental trends, reputation of the reseller, experience of reseller are just a few examples.

Who should lead

Regardless of the channel framework selected, channels usually perform better if someone is in charge, providing some level of leadership. Essentially, the purpose of this leadership is to coordinate the goals and efforts of channel institutions. The level of leadership can range from very passive to quite active-verging on dictatorial. The style may range from very negative, based on fear and punishment, to very positive, based on encouragement and reward. In a given situation, any of these leadership styles may prove effective.

Given the restrictions inherent in channel leadership, the final question is "who should lead the channel?" Two important trends are worth noting, since they influence the answer. First, if we look at the early years of marketing, i.e. pre-1920, the role of the wholesaler (to bring the producer and consumer together) was most vital. Consequently, during this period, the wholesaler led most channels. This is no longer true. A second trend is the apparent strategy of both manufacturers and retailers to exert power through size. In a type of business cold war, manufacturers and retailers are constantly trying to match each other's size. The result has been some serious warfare to gain channel superiority.

Under which conditions should the manufacturers lead? The wholesaler? The retailer? While the answer is contingent upon many factors, in general, the manufacturer should lead if control of the product (merchandising, repair) is critical and if the design and redesign of the channel is best done by the manufacturer. The wholesaler should lead where the manufacturers and retailers have remained small in size, large in number, relatively scattered geographically, are financially weak, and lack marketing expertise. The retailer should lead when product development and demand stimulation are relatively unimportant and when personal attention to the customer is important.

Evaluating channel member performance

The need to evaluate the performance level of the channel members is just as important as the evaluation of the other marketing functions. Clearly, the marketing mix is quite interdependent and the failure of one component can cause the failure of the whole. There is one important difference, with the exception of the corporate VMS; the channel member is dealing with independent business firms, rather than employees and activities under the control of the channel member, and their willingness to change is lacking.

Sales is the most popular performance criteria used in channel evaluation. Sales might further be subdivided into current sales compared with historical sales, comparisons of sales with other channel members, and comparisons of the channel member's sales

with predetermined quotas. Other possible performance criteria are: maintenance of adequate inventory, selling capabilities, attitudes of channel intermediaries toward the product, competition from other intermediaries and from other product line carried by the manufacturers own channel members.

Correcting or modifying the channel

As a result of the evaluation process, or because of other factors such as new competition, technology, or market potential, changes will be made in the channel structure. Because channel relationships have tended to be longterm, and the channel decision has such a pervasive impact on the business, great care should be taken before changing the status quo.

Terminations of channel members not performing at minimum performance standards should be employed only as a last resort. Corrective actions are far less destructive and maintain the goodwill that is so crucial in channel relationships. This requires that the channel manager attempt to find out why these channel members have performed poorly and then implement a strategy to correct these deficiencies.

Sometimes a producer decides that an entirely new channel needs to be added, or an existing one deleted. A manufacturer of camera accessories might decide that he wants to reach the skilled amateur market in addition to the professional photographer market. This would mean designing a different channel, and learning about a different set of intermediaries.

THE HUMAN ASPECT OF DISTRIBUTION

A channel of distribution by its very nature is made up of people. Ideally, a channel member should coordinate his or her efforts with other members in such a way that the performance of the total distribution system to which he or she belongs is enhanced. This is rarely the case. Part of this lack of cooperation is due to the organization structure of many channels, which encourages a channel member to be concerned only with channel members immediately adjacent to them, from whom they buy and to whom they sell. A second reason is the tendency of channel members to exhibit their independence as separate business operations. It is difficult to gain cooperation under this arrangement. Four human dimensions have been incorporated into the study of channel behavior: roles, communication, conflict, and power. It is assumed that an understanding of these behavioral characteristics will increase the effectiveness of the channel.

Role

Most channel members participate in several channels. Establishing the *role* of a channel member means defining what the behavior of the channel member should be. For example, a basic role prescription of the manufacturer may be to maximize the sales of his or her particular brand of product. This connotes that the manufacturer is to actively compete for market share, and aggressively promote his or her brand. The role prescriptions of independent wholesalers, however, are likely to be quite different. Since wholesalers may represent several competing manufacturers, his or her role would be to build sales with whatever brands are most heavily demanded by retailers. Therefore, a major issue in channel management relates to defining the role prescriptions of the various participants in order to achieve desired results. This is accomplished through a careful appraisal of the tasks to be performed by each channel member and clear communication of these roles to the members.

Communication

Channel communication is sending and receiving information that is relevant to the operation of the channel. It is critical for the success of the channel member to work to create and foster an effective flow of information within the channel. Communication will take place only if the channel member is aware of the pitfalls that await. The channel manager should therefore try to detect any behavioral problems that tend to inhibit the effective flow of information through the channel and try to solve these problems before the communication process in the channel becomes seriously distorted.

Conflict

Anytime individuals or organizations must work together and rely on each other for personal success, conflict is inevitable. *Conflict*, unlike friendly competition, is personal and direct and often suggests a confrontation. Because it is so pervasive in distribution, a great deal of research has been conducted in attempts to identify its causes, outcomes, and solutions.

There is also a need to manage conflict in the channel. This consists of (a) establishing a mechanism for detecting conflict, (b) appraising the effects of the conflict, and (c) resolving the conflict. This last consideration is most difficult to implement.

Techniques such as a channel committee, joint goal setting, and bringing in an arbitrator have all been used. There are even cases when conflict is necessary. Such is the case in the e-marketplace. For example, Eric Schmidt, Chairman and CEO of Google Inc., notes: “From my experience the most successful companies are the ones where there is enormous conflict. Conflict does not mean killing one another, but instead means there is a process by which there is a disagreement. It is okay to have different points of view and disagree, because tolerance of multiple opinions and people often leads to the right decision through some kind of process.”

Power

Power is our willingness to use force in a relationship. It is often the means by which we are able to control or influence the behavior of another party. In the channel mechanism, *power*refers to the capacity of a particular channel member to control or influence the behavior of another channel member. For instance, a large retailer may want the manufacturer to modify the design of the product or perhaps be required to carry less inventory. Both parties may attempt to exert their power in an attempt to influence the other’s behavior. The ability of either of the parties to achieve this outcome will depend upon the amount of power that each can bring to bear.

REFERENCES

1 Wroe Alderson, “Factors Governing the Development of Marketing Channels,” in R.M. Clewett (ed.), *Marketing Channels for Manufactured Products*, Homewood, IL: Richard D. Irwin. 1954, pp. 5-22.

2 James L. Heskett, *Marketing*, New York: Macmillan Publishing Co., Inc., 1976, pp. 265-267.

3 Roger M. Pegram, “Selecting and Evaluating Distributors,” New York: The Conference Board, Business Policy Study No. 116, 1965, p. 24.

4 Louis W. Stem, and Ronald H. Gorman, “Conflict in Distribution Channels: An Exploration,” in *Distribution Channels*: Behavioral Dimensions, ed. Louis W. Stern, New York: Houghton-Mifflin Co., 1969, p. 156.

Sources

Section 10.4 Organizing The Channel is adapted from chapter ‘10. Channel concepts: distributing the product’ from the textbook ‘Introducing Marketing, First Edition, 2011’ authored by John Burnett – this book was published under The Global Text Project, funded by the Jacobs Foundation, Zurich, Switzerland.

The following changes were made to the most recent edition: Divided ‘Chapter 10. Channel concepts: distributing the product’’ into three sections; Removed Created new title for Figure featuring Anderson ad.; Removed box titled ‘In Practice’ from wsj.com; Removed case application at the end of chapter; Added learning objectives.

This page titled 10.5: Organizing The Channel is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

11: Global Promotions

11.1: Global Promotions Summary

11.2: Changes in Promotion

11.3: Global Communication Platform

11.4: Global Communication Strategies

This page titled 11: Global Promotions is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

11.1: Global Promotions Summary

Summary

Marketing communications—the promotion P of the marketing mix—includes advertising, public relations, sales promotion, and personal selling. When a company embraces integrated marketing communications (IMC), it recognizes that the various elements of a company's communication strategy must be carefully coordinated. Advertising is a sponsored , paid message that is communicated through nonpersonal channels. Global advertising consists of the same advertising appeals, messages, artwork, and copy in campaigns around the world. The effort required to create a global campaign forces a company to determine whether or not a global market exists for its product. The trade-off between standardized and adapted advertising is often accomplished by means of pattern advertising, which can be used to create localized global advertising. Many advertising agencies are part of larger advertising organizations. Advertisers may place a single global agency in charge of worldwide advertising; it is also possible to use one or more agencies on a regional or local basis.

The starting point in ad development is the creative strategy, a statement of what the message will say. The people who create ads often seek a big idea that can serve as the basis for memorable, effective messages. The advertising appeal is the communication approach—rational or emotional—that best relates to buyer motives. Rational appeals speak to the mind: emotional appeals speak to the heart. The selling proposition is the promise that captures the reason for buying the product. The creative execution is the way an appeal or proposition is presented. Art direction and copy must be created with cultural considerations in mind. Perceptions of humor, male-female relationships, and sexual imagery vary in different parts of the world. Media availability varies considerably from country to country. When selecting media, marketers are sometimes as constrained by laws and regulations as by literacy rates.

A company utilizes public relations (PR) to foster goodwill and understanding among constituents both inside and outside the company. In particular, the PR department attempts to generate favorable publicity about the company and its products and brands. The PR department must also manage corporate communications when responding to negative publicity. The most important PR tools are press releases, media kits, interviews, and tours. Many global companies make use of various types of corporate advertising, including image advertising and advocacy advertising. Public relations is also responsible for providing accurate, timely information, especially in the event of a crisis.

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- Chapter 14 and Chapter 15 from the course note from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM) Copyright (c) is by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license.

I would like to thank Andy Schmitz for his work in maintaining and improving the HTML versions of these textbooks. This textbook is adapted from his HTML version, and his project can be found here.

This page titled 11.1: Global Promotions Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

11.2: Changes in Promotion

Learning Objectives

After reading this section, students should be able to …

1. list driving factors in global promotion decisions
2. outline the steps in changing the global promotional mix

Changes in Promotion

Before a company decides to become global, it must consider a multitude of factors unique to the international marketing environment. These factors are social, cultural, political, legal, competitive, economic, and even technological in nature. Ultimately, at the global marketing level, a company trying to speak with one voice is faced with many challenges when creating a worldwide marketing plan. Unless a company holds the same position against its competition in all markets (market leader, low cost, etc.), it is impossible to launch identical marketing plans worldwide. Thus, global companies must be nimble enough to adapt to changing local market trends, tastes, and needs.

Global Promotion

Language is usually one element that is customized in a global promotional mix.

For global advertisers, there are four potentially competing business objectives that must be balanced when developing worldwide advertising: building a brand while speaking with one voice, developing economies of scale in the creative process, maximizing local effectiveness of advertisements, and increasing the company's speed of implementation. Global marketers can use the following approaches when executing global promotional programs: exporting executions, producing local executions, and importing ideas that travel.

Factors in Global Promotion

To successfully implement these approaches, brands must ensure their promotional campaigns take into how consumer behavior is shaped by internal conditions (e.g., demographics, knowledge, attitude, beliefs) and external influences (e.g., culture, ethnicity, family, lifestyle) in local markets.

- **Language**– The importance of language differences is extremely crucial in global marketing, as there are almost 3,000 languages in the world. Language differences have caused many problems for marketers in designing advertising campaigns and product labels. Language becomes even more significant if a country's population speaks several languages.
- **Colors**– Colors also have different meanings in different cultures. For example, in Egypt, the country's national color of green is considered unacceptable for packaging because religious leaders once wore it. In Japan, black and white are colors of mourning and should not be used on a product's package. Similarly, purple is unacceptable in Hispanic nations because it is associated with death.
- **Values**– An individual's values arise from his or her moral or religious beliefs and are learned through experiences. For example, Americans place a very high value on material well-being and are much more likely to purchase status symbols than people in India. In India, the Hindu religion forbids the consumption of beef.
- **Business norms**– The norms of conducting business also vary from one country to the next. For example, in France, wholesalers do not like to promote products. They are mainly interested in supplying retailers with the products they need.
- **Religious beliefs**– A person's religious beliefs can affect shopping patterns and products purchased in addition to his or her values. In the United States and other Christian nations, Christmas time tends to be a major sales period. In other religions, significant religious holidays may or may not serve as popular times for purchasing products.

There are many other factors, including a country's political or legal environment, monetary circumstances, and technological environment that can impact a brand's promotional mix. Companies have to be ready to quickly respond and adapt to these challenges as they evolve and fluctuate in the market of each country.

Changing the Global Promotional Mix

When launching global advertising, public relations or sales campaigns, global companies test promotional ideas using marketing research systems that provide results comparable across countries. The ability to identify the elements or moments of an advertisement that contribute to the success of a product launch or expansion is how economies of scale are maximized in marketing communications. Market research measures such as flow of attention, flow of emotion, and branding moments provide insight into what is working in an advertisement in one or many countries. These measures can be particularly helpful for marketers since they are based on visual, not verbal, elements of the promotion.

Considering these measures along with conducting extensive market research is essential to determining the success of promotional tactics in any country or region. Once brands discover what works (and what does not) in their promotional mix, those ideas can be imported by any other market. Likewise, companies can use this intelligence to modify various elements in their promotional mix that are receiving minimal or unfavorable response from global audiences.

Key Takeaways

- To successfully implement global marketing strategies, brands must ensure their promotional campaigns take into account how consumer behavior is shaped by internal conditions and external influences.
- Global companies must be nimble enough to adapt changing local market trends, tastes, and needs to their promotional mix.
- When launching global advertising, public relations or sales campaigns, global companies test promotion ideas to provide results that are comparable across countries.
- Using measures can be particularly helpful for marketers since they are based on visual, not verbal, elements of the promotion.

Terms

- *Measure*: To ascertain the quantity of a unit of material via calculated comparison with respect to a standard.
- *Demographics:* The observable characteristics of a population, such as physical traits, economic traits, occupational traits, and more.

Source

The above content was adapted from Boundless Business. Authored by: Boundless. Provided by: Boundless. Located at: https://www.boundless.com/business/. License: CC BY-SA: Attribution-ShareAlike under a Creative Commons Attribution-NonCommercial-ShareAlike License.

Image of Potato Chips. Authored by: kevin dooley. Located at: https://www.flickr.com/photos/pagedo...89227/sizes/l/. License: CC BY: Attribution.

This page titled 11.2: Changes in Promotion is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

11.3: Global Communication Platform

Learning Objectives

After reading this section, students should be able to …

1. appreciate the trade-off between creating global efficiencies and adaptation

One way around the trade-off between creating global efficiencies and adapting to local requirements and preferences is to design a global product or communication platform that can be adapted efficiently to different markets. This modularized approach to global product design has become particularly popular in the automobile industry. One of the first "world car platforms" was introduced by Ford in 1981. The Ford Escort was assembled simultaneously in three countries—the United States, Germany, and the United Kingdom—with parts produced in 10 countries. The U.S. and European models were distinctly different but shared standardized engines, transmissions, and ancillary systems for heating, air conditioning, wheels, and seats, thereby saving the company millions of dollars in engineering and development costs.

Minicase: Creating the Perfect Fit: New Car-Seat, DesignBuss (2009)

Imagine the challenge of being an automotive-seat engineer these days, and picture one of the hugest men you know—a large, American male weighing about 275 lbs. Now consider a petite woman, and throw in someone with lower-back pain. Your challenge: design a single seat that comfortably accommodates each of these physically and physiologically diverse individuals, not just for a few minutes but for a 4-hour drive. Welcome to the global automotive design challenge.

While the economic pressures to standardize are becoming stronger, car buyers are getting more size-diverse, more ergonomically distressed, and more demanding of power adjustments and other amenities. Seat developers are responding: they are using more versatile materials, new engineering techniques, digital technologies, and novel designs to make sitting in a car as, or even more, comfortable as sitting in your living room.

This concern for comfort is relatively new; hard benches were the standard during the industry's earliest days. Even into the 1980s, most cars and trucks had simple bench seating in both the front and rear of the automobile. Automotive seat design only became a crucial discipline during the last generation as Americans began to spend more and more time in their vehicles and as interior comfort and appointments became a major competitive issue.

Federal regulations affect seat design only minimally, with the most important requirements focusing on headrests. And there are distance requirements between the driver's body and the steering wheel, an issue that can also be addressed with telescoping steering wheels and adjustable pedals. In the end, automakers must mainly make sure the seat design helps the car pass the government's crash-safety standards.

Consumers are far more demanding. Comfort and ergonomic functionality have become the focal points of seat design. Americans are getting bigger and heavier, and automakers try to design seats that can accommodate everyone from the smallest females to the largest males. This is not a simple feat, with the 95th-percentile American man now weighing about 24 lbs more than 2 decades ago. At the same time, while U.S. women in general also have gotten larger, the influx of immigrants from Asia actually kept the overall increase in the size of the 5th-percentile American woman down to under 5 lbs over the last 2 decades.

And just as airlines and home-furniture manufacturers have had to respond to wider girths by making seats bigger, auto companies are also faced with having to squeeze bigger people into cabins that are getting smaller as gas prices rise. At the same time, seats must secure tiny drivers and allow them to see clearly over the steering wheel and reach the accelerator and brake pedals.

The aging of the American population poses special difficulties. Younger demographics like their seats harder, but baby boomers and older customers are used to a soft seat. Whether this is best ergonomically is not important, despite the fact that more and more consumers are carrying specific maladies of aging into their cars, including back pain, aching knees, and a general decline in the basic nimbleness required to get in and out of an automobile.

> It is one thing to design a single seat that can accommodate the frames of the smallest to the largest Americans. Now add the globalization challenge. As automakers seek to globalize vehicle platforms, their seats also have to be able to accommodate the diverse body proportions, size ranges, and consumer preferences of people around the world.
>
> For example, while Europeans definitely prefer longer cushions, and Asians like shorter ones, Americans are somewhere in between. And in China, the second row must be as comfortable as the first because as many as 40% of car owners have a driver, and the owners tend to sit in the right rear seat.

Source

The above content was adapted from “Combining Aggregation and Adaptation: Global Product Platforms”, section 6.3 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

I would like to thank Andy Schmitz for his work in maintaining and improving the HTML versions of these textbooks. This textbook is adapted from his HTML version, and his project can be found here.

This page titled 11.3: Global Communication Platform is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

11.4: Global Communication Strategies

Learning Objectives

After reading this section, students should be able to …

1. outline the generic global strategies in the value proposition globalization matrix
2. explain usgae of gobal message strategies

A useful construct for analyzing the need to adapt the offer and message (positioning) dimensions is the value proposition globalization matrix shown in Figure 11.1 “The Value Proposition Globalization Matrix”, which illustrates four generic global strategies:

1. A pure aggregation approach (also sometimes referred to as a “global marketing mix” strategy) under which both the offer and the message are the same
2. An approach characterized by an identical offer (product/service aggregation) but different positioning (message adaptation) around the world (also called a “global offer” strategy)
3. An approach under which the offer might be different in various parts of the world (product adaptation) but where the message is the same (message aggregation; also referred to as a “global message” strategy)
4. A “global change” strategy under which both the offer and the message are adapted to local market circumstances

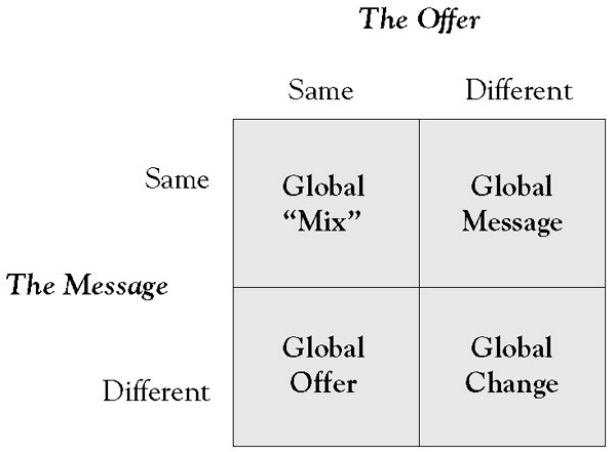


Figure 11.4.1: The Value Proposition Globalization Matrix (CC-BY-NC-SA; Lardbucket)

Global mix or pure aggregation strategies are relatively rare because only a few industries are truly global in all respects. They apply (a) when a product’s usage patterns and brand potential are homogeneous on a global scale, (b) when scale and scope cost advantages substantially outweigh the benefits of partial or full adaptation, and (c) when competitive circumstances are such that a long-term, sustainable advantage can be secured using a standardized approach. The best examples are found in industrial product categories such as basic electronic components or certain commodity markets.

Global offer strategies are feasible when the same offer can be advantageously positioned differently in different parts of the world. There are several reasons for considering differential positioning. When fixed costs associated with the offer are high, when key core benefits offered are identical, and when there are natural market boundaries, adapting the message for stronger local advantage is tempting. Although such strategies increase local promotional budgets, they give country managers a degree of flexibility in positioning the product or service for maximum local advantage. The primary disadvantage associated with this type of strategy is that it could be difficult to sustain or even dangerous in the long term as customers become increasingly global in their outlook and confused by the different messages in different parts of the world.

Mini Case: Starwood's Branding in China, Palmeri and Balfour (2009, September 7)

Check into a Four Points Hotel by Sheraton in Shanghai and you will get all the perks of a quality international hotel: a free Internet connection, several in-house restaurants, a mah-jongg parlor, and an assortment of moon cakes, a Chinese delicacy. All this for $80 a night, about 20% less than the average cost of a room in Shanghai.

For travelers who associate the Sheraton brand with plastic ice buckets and polyester bedspreads in the United States, this may come as a surprise. Like Buick, Kentucky Fried Chicken (KFC), and Pizza Hut, Sheraton is one of those American names that, to some, seems past its prime at home, but it is still popular and growing abroad. The hotel brand has particular cachet in China, going back to 1985, when it opened the Great Wall Sheraton Hotel Beijing. Local developers still compete to partner with Sheraton's parent company—Starwood Hotels & Resorts Worldwide—to develop new properties. In the near future, the company will have more rooms in Shanghai than it does in New York.

Like many other U.S. companies experiencing pressure at home, Starwood sees China as one of its best hopes for growth. The company, which also owns the upscale St. Regis, Westin, W, and Le Meridien brands, expects much of this growth will come from outlying regions. Big cities such as Beijing now have plenty of rooms, thanks in part to the Olympics, but there is growing demand for business-class accommodation in second- and third-tier cities such as Jiangyin and Dalian. Lower construction costs and inexpensive labor mean the company's Chinese hotel owners can offer guests a lot more than comparably priced U.S. properties.

In recent years, the focus in China has shifted from international travelers to Chinese consumers. Starwood now asks its hotel staff to greet guests in Mandarin instead of English, which was long used to convey a sense of prestige. Many of its hotels do not label their fourth floors as such because four is considered an unlucky number.

Starwood is not alone in recognizing the potential of the Chinese market. Marriott International hopes to increase its China presence by 50%, to 61 hotels by 2014. And InterContinental Hotels Group, parent of Holiday Inn, plans to double the 118 hotels it has in China over the next 3 years.

One major perk Starwood can offer over local competitors is its extensive global network and loyalty perks. More than 40% of its Chinese business comes through its preferred-guest program, and Chinese membership in the program is increasing rapidly. But local customers are not particularly focused on accruing points to earn a free stay. They are more interested in "status," using points to get room upgrades, a free breakfast, or anything that accords them conspicuous VIP treatment. Among other things, the preferred guest system allows staffers to see people's titles immediately. That makes it easier to give better rooms to managers than the subordinates they are traveling with and to greet them first when a party arrives.

After a long period in which Starwood paid more attention to its hipper W and Westin brands, the company has recently been remodeling its U.S. Sheratons. Among mainland Chinese travelers, the Sheraton name has continued to exude an aura of international class. While that is helpful for Sheraton's domestic Chinese business, the real potential will only be realized when they start to travel. The company's goal is to lock in the loyalty of mainland customers so they will stay at a Sheraton when they travel abroad. Indeed, if the experience with Japanese tourists in the mid-1980s is any guide, Starwood could be looking at 100 million or more outbound trips from China.

Global message strategies use the same message worldwide but allow for local adaptation of the offer. McDonald's, for example, is positioned virtually identical worldwide, but it serves vegetarian food in India and wine in France. The primary motivation behind this type of strategy is the enormous power behind a global brand. In industries in which customers increasingly develop similar expectations, aspirations, and values; in which customers are highly mobile; and in which the cost of product or service adaptation is fairly low, leveraging the global brand potential represented by one message worldwide often outweighs the possible disadvantages associated with factors such as higher local research and development (R&D) costs. As with global-offer strategies, however, global message strategies can be risky in the long run—global customers might not find elsewhere what they expect and regularly experience at home. This could lead to confusion or even alienation.

Mini Case: KFC Abroad[1]

KFC is synonymous with chicken. It has to be because chicken is its flagship product. One of the more recent offers the company created—all around the world—is the marinated hot and crispy chicken that is "crrrrisp and crunchy on the outside, and soft and juicy on the inside." In India, KFC offers a regular Pepsi with this at just 39 rupees. But KFC also made sure not to alienate the vegetarian community—in Bangalore, you can be vegetarian and yet eat at KFC. Why? Thirty-five percent of the Indian population is vegetarian, and in metros such as Delhi and Mumbai, the number is almost 50%. Therefore, KFC offers a wide range of vegetarian products, such as the tangy, lip-smacking Paneer Tikka Wrap 'n Roll, Veg De-Lite Burger, Veg Crispy Burger. There are munchies such as the crisp golden veg fingers and crunchy golden fries served with tangy sauces. You can combine the veg fingers with steaming, peppery rice and a spice curry. The mayonnaise and sauces do not have egg in them.

While the vegetarian menu is unique to India because of the country's distinct tastes, KFC's "standard" chicken products are also adapted to suit local tastes. For example, chicken strips are served with a local sauce, or the sauce of the wrap is changed to local tastes. Thus, KFC tries to balance aggregation with adaptation: standardization of those parts of the value offering that travel easily (KFC's core products and positioning), tailoring of standard chicken products with a different topping or sauce, and offering a vegetarian menu.

This adaptation strategy is used in every country that KFC serves: the U.S. and European markets have a traditional KFC menu based on chicken burgers and wraps, while Asian offerings like those in India are more experimental and adventurous and include rice meals, wraps, and culture-appropriate sides.

Global change strategies define a "best fit" approach and are by far the most common. As we have seen, for most products, some form of adaptation of both the offer and the message is necessary. Differences in a product's usage patterns, benefits sought, brand image, competitive structures, distribution channels, and governmental and other regulations all dictate some form of local adaptation. Corporate factors also play a role. Companies that have achieved a global reach through acquisition, for example, often prefer to leverage local brand names, distribution systems, and suppliers rather than embark on a risky global one-size-fits-all approach. As the markets they serve and the company become more global, selective standardization of the message and the offer itself can become more attractive.

Mini Case: Targeting Muslim Customers, Power (2009, June 1)

Muslims often experience culture shock while staying in Western hotels. Minibars, travelers in bikinis, and loud music, among other things, embarrass Muslim travelers.

That is no longer necessary. A growing number of hotels has started to cater to Muslim travelers. In one, the lobby—decorated in white leather, brick, and glass, with a small waterfall—is quiet. Men in *dishdashas* and veiled women mingle with Westerners who are sometimes discreetly reminded to respect local customs. Minibars are stocked not with alcohol but with Red Bull, Pepsi, and the malt drink Barbican.

"Buying Muslim" used to mean avoiding pork and alcohol and getting your meat from a halal butcher, who slaughtered in accordance with Islamic principles. But the halal food market has exploded in the past decade and is now worth an estimated $632 billion annually, according to the *Halal Journal*, a Kuala Lumpur–based magazine. That amounts to about 16% of the entire global food industry. Throw in the fast-growing Islam-friendly finance sector and the myriad of other products and services—cosmetics, real estate, hotels, fashion, insurance, for example—that comply with Islamic law and the teachings of the Koran, and the sector is worth well over $1 trillion a year.

Seeking to tap that huge market, multinationals like Tesco, McDonald's, and Nestlé have expanded their Muslim-friendly offerings and now control an estimated 90% of the global halal market. Governments in Asia and the Middle East are pouring millions into efforts to become regional "halal hubs," providing tailor-made manufacturing centers and "halal logistics"—systems to maintain product purity during shipping and storage. The intense competition has created some interesting partnerships in unusual places. Most of Saudi Arabia's chicken is raised in Brazil, which means Brazilian suppliers had to build elaborate halal slaughtering facilities. Abattoirs in New Zealand, the world's biggest exporter of halal lamb, have hosted

delegations from Iran and Malaysia. And the Netherlands, keen to exploit Rotterdam's role as Europe's biggest port, has built halal warehouses so that imported halal goods are not stored next to pork or alcohol.

It is not just about food. Major drug companies now sell halal vitamins free of the gelatins and other animal derivatives that some Islamic scholars say make mainstream products *haram*, or unlawful. The Malaysia-based company Granulab produces synthetic bone-graft material to avoid using animal bone, while Malaysian and Cuban scientists are collaborating on a halal meningitis vaccine. For Muslim women concerned about skin-care products containing alcohol or lipsticks that use animal fats, a few cosmetics firms are creating halal makeup lines.

The growing Islamic finance industry is trying to win non-Muslim customers. Investors are attracted by Islamic banking's more conservative approach: Islamic law forbids banks from charging interest (though customers pay fees), and many scholars discourage investment in excessively leveraged companies. Though it currently accounts for just 1% of the global market, the Islamic finance industry's value is growing at around 15% a year, and it could reach $4 trillion in 5 years, according to a 2008 report from Moody's Investors Service.

References

1. http://www.kfcbd.com/aboutus_kfcbang.htm

Source

The above content was adapted from "Adaptation or Aggregation: The Value Proposition Globalization Matrix", section 6.2 from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

I would like to thank Andy Schmitz for his work in maintaining and improving the HTML versions of these textbooks. This textbook is adapted from his HTML version, and his project can be found here.

This page titled 11.4: Global Communication Strategies is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

12: Global Pricing

12.1: Global Pricing Summary
12.2: Basics of Pricing
12.3: Introduction to Global Pricing
12.4: Global Pricing Approaches
12.5: Currency Fluctuations and Global Pricing
12.6: Tariffs and Global Pricing
12.7: Quotas and Dumping

This page titled 12: Global Pricing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

12.1: Global Pricing Summary

Summary

Pricing decisions are a critical element of the marketing mix that must reflect costs, competitive factors, and customer perceptions regarding value of the product. In a true global market, the law of one price would prevail. Pricing strategies include market skimming, market penetration, and market holding. Novice exporters frequently use cost-plus pricing. International terms of a sale such as ex-works, F.A.S., F.O.B., and C.I.F. are known as Incoterms and specify which party to a transaction is responsible for covering various costs. These and other costs lead to export price escalation, the accumulation of costs that occurs when products are shipped from one country to another.

Expectations regarding currency fluctuations, inflation, government controls, and the competitive situation must also be factored into pricing decisions. The introduction of the euro has impacted price strategies in the EU because of improved price transparency. Global companies can maintain competitive prices in world markets by shifting production sources as business conditions change. Overall, a company's pricing policies can be categorized as ethnocentric, polycentric, or geocentric.

Several additional pricing issues are related to global marketing. The issue of gray market goods arises because price variations between different countries lead to parallel imports. Dumping is another contentious issue that can result in strained relations between trading partners. Price fixing among companies is anticompetitive and illegal.

Transfer pricing is an issue because of the sheer monetary volume of intra-corporate sales and because country governments are anxious to generate as much tax revenue as possible. Various forms of countertrade play an important role in today's global environment. Barter, counter purchase, offset, compensation trading, and switch trading are the main countertrade options.

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

Chapter 11 from the course note from the 'Global Marketing' course published online by Centre for Teaching and Learning (CTL) of Universiti Teknologi Malaysia (UTM) Copyright (c) is by Dr. Inda Sukati and made available under a Attribution-Noncommercial-Share Alike 3.0 license.

I would like to thank Andy Schmitz for his work in maintaining and improving the HTML versions of these textbooks. This textbook is adapted from his HTML version, and his project can be found here.

This page titled 12.1: Global Pricing Summary is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

12.2: Basics of Pricing

Learning Objectives

After reading this section, students should be able to …

- outline the sellers' objectives in making pricing decisions

Pricing objectives

Firms rely on price to cover the cost of production, to pay expenses, and to provide the profit incentive necessary to continue to operate the business. We might think of these factors as helping organizations to: (a) survive, (b) earn a profit, (c) generate sales, (d) secure an adequate share of the market, and (e) gain an appropriate image

- **Survival:** It is apparent that most managers wish to pursue strategies that enable their organizations to continue in operation for the long term. So survival is one major objective pursued by most executives. For a commercial firm, the price paid by the buyer generates the firm's revenue. If revenue falls below cost for a long period of time, the firm cannot survive.
- **Profit:** Survival is closely linked to profitability. Making a USD 500,000 profit during the next year might be a pricing objective for a firm. Anything less will ensure failure. All business enterprises must earn a longterm profit. For many businesses, long-term profitability also allows the business to satisfy their most important constituents–stockholders. Lower-than-expected or no profits will drive down stock prices and may prove disastrous for the company.
- **Sales:** Just as survival requires a long-term profit for a business enterprise, profit requires sales. As you will recall from earlier in the text, the task of marketing management relates to managing demand. Demand must be managed in order to regulate exchanges or sales. Thus marketing management's aim is to alter sales patterns in some desirable way.
- **Market share:** If the sales of Safeway Supermarkets in the Dallas-Fort Worth metropolitan area of Texas, USA, account for 30 per cent of all food sales in that area, we say that Safeway has a 30 per cent market share. Management of all firms, large and small, are concerned with maintaining an adequate share of the market so that their sales volume will enable the firm to survive and prosper. Again, pricing strategy is one of the tools that is significant in creating and sustaining market share. Prices must be set to attract the appropriate market segment in significant numbers.
- **Image:** Price policies play an important role in affecting a firm's position of respect and esteem in its community. Price is a highly visible communicator. It must convey the message to the community that the firm offers good value, that it is fair in its dealings with the public, that it is a reliable place to patronize, and that it stands behind its products and services.

Developing a pricing strategy

While pricing a product or service may seem to be a simple process, it is not. As an illustration of the typical pricing process, consider the following quote: "Pricing is guesswork. It is usually assumed that marketers use scientific methods to determine the price of their products. Nothing could be further from the truth. In almost every case, the process of decision is one of guesswork." (2)

Good pricing strategy is usually based on sound assumptions made by marketers. It is also based on an understanding of the two other perspectives discussed earlier. Clearly, sale pricing may prove unsuccessful unless the marketer adopts the consumer's perspective toward price. Similarly, a company should not charge high prices if it hurts society's health. Hertz illustrates how this can be done in "Integrated marketing" below.

A pricing decision that must be made by all organizations concerns their competitive position within their industry. This concern manifests itself in either a competitive pricing strategy or a nonprice competitive strategy. Let us look at the latter first.

Nonprice competition

Nonprice competition means that organizations use strategies other than price to attract customers. Advertising, credit, delivery, displays, private brands, and convenience are all example of tools used in nonprice competition. Businesspeople prefer to use nonprice competition rather than price competition, because it is more difficult to match nonprice characteristics.

Student Example

Amazon uses creative methods to deliver an experience to consumers that makes them competitive rather than providing just a price advantage. More specifically, an example of this is the new Amazon Go stores. These stores feature a completely different approach than a regular retail store. Most stores feature the typical shop, wait in line, check out, and leave. At Amazon Go, you can simply pick up the items you want and walk out the door. All you need is the Amazon Go app downloaded on your phone which will process your order to your account. Through the use of carefully designed technology, there is little to no hassles for the end-user. Amazon really emphasizes the idea of no checkouts, no lines, no registers to persuade consumers on convenience. They are using other methods to make them competitive rather than price.

Mitchel Mertins

Class of 2020



Figure 12.2.1: An example of nonprice competition.

Competing on the basis of price may also have a deleterious impact on company profitability. Unfortunately, when most businesses think about price competition, they view it as matching the lower price of a competitor, rather than pricing smarter. In fact, it may be wiser not to engage in price competition for other reasons. Price may simply not offer the business a competitive advantage (employing the value equation).

Competitive pricing

Once a business decides to use price as a primary competitive strategy, there are many well established tools and techniques that can be employed. The pricing process normally begins with a decision about the company's pricing approach to the market.

Approaches to the market

Price is a very important decision criteria that customers use to compare alternatives. It also contributes to the company's position. In general, a business can price itself to match its competition, price higher, or price lower. Each has its pros and cons.

Pricing to meet competition

Many organizations attempt to establish prices that, on average, are the same as those set by their more important competitors. Automobiles of the same size and having equivalent equipment tend to have similar prices. This strategy means that the organization uses price as an indicator or baseline. Quality in production, better service, creativity in advertising, or some other element of the marketing mix are used to attract customers who are interested in products in a particular price category.

The keys to implementing a strategy of meeting competitive prices are an accurate definition of competition and knowledge of competitor's prices. A maker of hand-crafted leather shoes is not in competition with mass producers. If he/she attempts to compete with mass producers on price, higher production costs will make the business unprofitable. A more realistic definition of competition for this purpose would be other makers of handcrafted leather shoes. Such a definition along with a knowledge of their prices would allow a manager to put the strategy into effect. Banks shop competitive banks every day to check their prices.

Pricing above competitors

Pricing above competitors can be rewarding to organizations, provided that the objectives of the policy are clearly understood and that the marketing mix is used to develop a strategy to enable management to implement the policy successfully.

Pricing above competition generally requires a clear advantage on some nonprice element of the marketing mix. In some cases, it is possible due to a high price-quality association on the part of potential buyers. Such an assumption is increasingly dangerous in today's information-rich environment. Consumer Reports and other similar publications make objective product comparisons much simpler for the consumer. There are also hundreds of dot.com companies that provide objective price comparisons. The key is to prove to customers that your product justifies a premium price.

Student Example

Starbucks is a great example of a company that prices above the competition. Although they are a high priced coffee shop, people will still buy from them. The company needs to provide a reason for people to pay more for their coffee over other businesses. They believe that because they are getting high-quality products, people are more likely to pay more for it. That is true since Starbucks is the leading coffee company and has the largest market share as well. In this case, pricing above competition works.

Taylor Stone

Class of 2020

Pricing below competitors

While some firms are positioned to price above the competition, others wish to carve out a market niche by pricing below competitors. The goal of such a policy is to realize a large sales volume through a lower price and profit margins. By controlling costs and reducing services, these firms are able to earn an acceptable profit, even though profit per unit is usually less.

Student Example

There are many airlines that operate in the United States, and each one has something different to offer. Spirit Airlines is one of the lesser-known airlines, but it is generally the cheapest. Their slogan is "Less Money. More Go." By pricing their airline tickets extremely low, consumers can fly to their locations by ease. These discounts do not come without reduced services, though; purchasing a ticket through Spirit Airlines comes with a reduction in 'luxury' services such as carry-ons, checked baggage, and snacks. These services are reduced because Spirit Airlines has positioned itself in a market niche that is best for daily commuters or those making short trips without luggage.

Zach Harper

Class of 2020

Such a strategy can be effective if a significant segment of the market is price-sensitive and/or the organization's cost structure is lower than competitors. Costs can be reduced by increased efficiency, economies of scale, or by reducing or eliminating such things as credit, delivery, and advertising. For example, if a firm could replace its field sales force with telemarketing or online access, this

function might be performed at a lower cost. Such reductions often involve some loss in effectiveness, so the tradeoff must be considered carefully.

Historically, one of the worst outcomes that can result from pricing lower than a competitor is a “price war”. Price wars usually occur when a business believes that price-cutting produces increased market share, but does not have a true cost advantage. Price wars are often caused by companies misreading or misunderstanding competitors. Typically, price wars are overreactions to threats that either is not there at all or are not as big as they seem.

Another possible drawback when pricing below competition is the company’s inability to raise price or image. A retailer such as K-mart, known as a discount chain, found it impossible to reposition itself as a provider of designer women’s clothiers. Can you imagine Swatch selling a USD 3,000 watch?

How can companies cope with the pressure created by reduced prices? Some are redesigning products for ease and speed of manufacturing or reducing costly features that their customers do not value. Other companies are reducing rebates and discounts in favor of stable, everyday low prices (EDLP). In all cases, these companies are seeking shelter from pricing pressures that come from the discount mania that has been common in the US for the last two decades.

Price lines

You are already familiar with price lines. Ties may be priced at USD 15, USD 17, USD 20, and USD 22.50; bluejeans may be priced at USD 30, USD 32.95, USD 37.95, and USD 45. Each price must be far enough apart so that buyers can see definite quality differences among products. Price lines tend to be associated with consumer shopping goods such as apparel, appliances, and carpeting rather than product lines such as groceries. Customers do very little comparison-shopping on the latter.

Price lining serves several purposes that benefit both buyers and sellers. Customers want and expect a wide assortment of goods, particularly shopping goods. Many small price differences for a given item can be confusing. If ties were priced at USD 15, USD 15.35, USD 15.75, and so on, selection would be more difficult; the customer could not judge quality differences as reflected by such small increments in price. So, having relatively few prices reduces confusion.

From the seller’s point of view, price lining holds several benefits. First, it is simpler and more efficient to use relatively fewer prices. The product/service mix can then be tailored to selected price points. Price points are simply the different prices that make up the line. Second, it can result in a smaller inventory than would otherwise be the case. It might increase stock turnover and make inventory control simpler. Third, as costs change, either increasing or decreasing the prices can remain the same, but the quality in the line can be changed. For example, you may have bought a USD 20 tie 15 years ago. You can buy a USD 20 tie today, but it is unlikely that today’s USD 20 tie is of the same fine quality as it was in the past. While customers are likely to be aware of the differences, they are nevertheless still able to purchase a USD 20 tie. During inflationary periods the quality/price point relationship changes. From the point of view of salespeople, offering price lines will make selling easier. Salespeople can easily learn a small number of prices. This reduces the likelihood that they will misquote prices or make other pricing errors. Their selling effort is, therefore, more relaxed, and this atmosphere will influence customers positively. It also gives the salesperson flexibility. If a customer cannot afford a USD 2,800 Gateway system, the USD 2,200 system is suggested.

Price flexibility

Another pricing decision relates to the extent of price flexibility. A flexible pricing policy means that the price is bid or negotiated separately for each exchange. This is a common practice when selling to organizational markets where each transaction is typically quite large. In such cases, the buyer may initiate the process by asking for bidding on a product or service that meets certain specifications. Alternatively, a buyer may select a supplier and attempt to negotiate the best possible price. Marketing effectiveness in many industrial markets requires a certain amount of price flexibility.

Student Example

In car sales or furniture sales, the advertised price is not necessarily the final price because the customer can negotiate a better deal. Since the salespeople work on commission, they are also working to get the customer to make a purchase, and using price flexibility makes the customer more inclined to purchase. One thing that I often see with price flexibility is discounting and promotions, where a firm will advertise an item for $13,999 with an automatic $1,000 off, and even then, there is price flexibility because the customer can negotiate for a better deal. These firms will have a minimum price they can take, but the

customer is unaware of what that price is. Pricing strategies can be combined and used together, but for car and furniture sales, one that is used most often is price flexibility.

Natalie Vazquez-Lopez

Class of 2020

Discounts and allowances

In addition to decisions related to the base price of products and services, marketing managers must also set policies related to the use of discounts and allowances. There are many different types of price reductions–each designed to accomplish a specific purpose.

Quantity discounts are reductions in base price given as the result of a buyer purchasing some predetermined quantity of merchandise. A noncumulative quantity discount applies to each purchase and is intended to encourage buyers to make larger purchases. This means that the buyer holds the excess merchandise until it is used, possibly cutting the inventory cost of the seller and preventing the buyer from switching to a competitor at least until the stock is used. A cumulative quantity discount applies to the total bought over a period of time. The buyer adds to the potential discount with each additional purchase. Such a policy helps to build repeat purchases. Building material dealers, for example, find such a policy quite useful in encouraging builders to concentrate their purchase with one dealer and to continue with the same dealer over time. It should be noted that such cumulative quantity discounts are extremely difficult to defend if attacked in the courts.



Figure Runaway argument for \eatSpaces?: A rebate can be a very effective price discount.

Seasonal discounts are price reductions given or out-of-season merchandise. An example would be a discount on snowmobiles during the summer. The intention of such discounts is to spread demand over the year. This can allow fuller use of production facilities and improved cash flow during the year. Electric power companies use the logic of seasonal discounts to encourage customers to shift consumption to off-peak periods. Since these companies must have the production capacity to meet peak demands, the lowering of the peak can lessen the generating capacity required.

Cash discounts are reductions on base price given to customers for paying cash or within some short time period. For example, a 2 percent discount on bills paid within 10 days is a cash discount. The purpose is generally to accelerate the cash flow of the organization.

Trade discounts are price reductions given to middlemen (e.g. wholesalers, industrial distributors, retailers) to encourage them to stock and give preferred treatment to an organization's products. For example, a consumer goods company may give a retailer a 20 percent discount to place a larger order for soap. Such a discount might also be used to gain shelf space or a preferred position in the store.

Personal allowances are similar devices aimed at middlemen. Their purpose is to encourage middlemen to aggressively promote the organization's products. For example, a furniture manufacturer may offer to pay some specified amount toward a retailer's advertising expenses if the retailer agrees to include the manufacturer's brand name in the ads.

Some manufacturers or wholesalers also give prize money called spiffs for retailers to pass on to the retailer's sales clerks for aggressively selling certain items. This is especially common in the electronics and clothing industries, where it is used primarily with new products, slow movers, or high margin items.

Trade-in allowances also reduce the base price of a product or service. These are often used to allow the seller to negotiate the best price with a buyer. The trade-in may, of course, be of value if it can be resold. Accepting trade-ins is necessary for marketing many types of products. A construction company with a used grader worth USD 70,000 would not likely buy a new model from an equipment company that did not accept trade-ins, particularly when other companies do accept them.

Price bundling

A very popular pricing strategy, price bundling, is to group similar or complementary products and to charge a total price that is lower if they were sold separately. Comcast, Direct TV, and Telstra all follow this strategy by combining different products and services for a set price. Customers assume that these computer experts are putting together an effective product package and they are paying less. The underlying assumption of this pricing strategy is that the increased sales generated will more than compensate for a lower profit margin. It may also be a way of selling a less popular product by combining it with popular ones. Clearly, industries such as financial services and telecommunications are big users of this.

Student Example

Bath and Body Works is a business that sells candles, body sprays, and shower items. Individually shampoo, conditioner, body wash, scrubs, etc., are very expensive. However, this shop will bundle items and drop the price to ensure that all items are purchased from them. Ultimately, if you shop here, it does end up being cheaper for the customer. Most people want to buy both shampoo and conditioner from the same brand, so having some bundles on sale regarding this purchase is very helpful.

Jennika Bond

Class of 2020

Psychological aspects of pricing

Price, as is the case with certain other elements in the marketing mix, appears to have meaning to many buyers that goes beyond a simple utilitarian statement. Such meaning is often referred to as the psychological aspect of pricing. Inferring quality from price is a common example of the psychological aspect. A buyer may assume that a suit priced at USD 500 is of higher quality than one priced at USD 300. From a cost-of-production, raw material, or workmanship perspective, this may or may not be the case. The seller may be able to secure the higher price by nonprice means such as offering alterations and credit or the benefit to the buyer may be in meeting some psychological need such as ego enhancement. In some situations, the higher price may be paid simply due to lack of information or lack of comparative shopping skills. For some products or services, the quantity demanded may actually rise to some extent as the price is increased. This might be the case with an item such as a fur coat. Such a pricing strategy is called prestige pricing.

Products and services frequently have customary prices in the minds of consumers. A customary price is one that customers identify with particular items. For example, for many decades a five-stick package of chewing gum cost USD 0.05 and a six-ounce bottle of Coca-Cola cost USD 0.05. Candy bars now cost 60 cents or more, a customary price for a standard-sized bar.

Manufacturers tend to adjust their wholesale prices to permit retailers in using customary pricing. However, as we have witnessed during the past decade, prices have changed so often that customary prices are weakened.

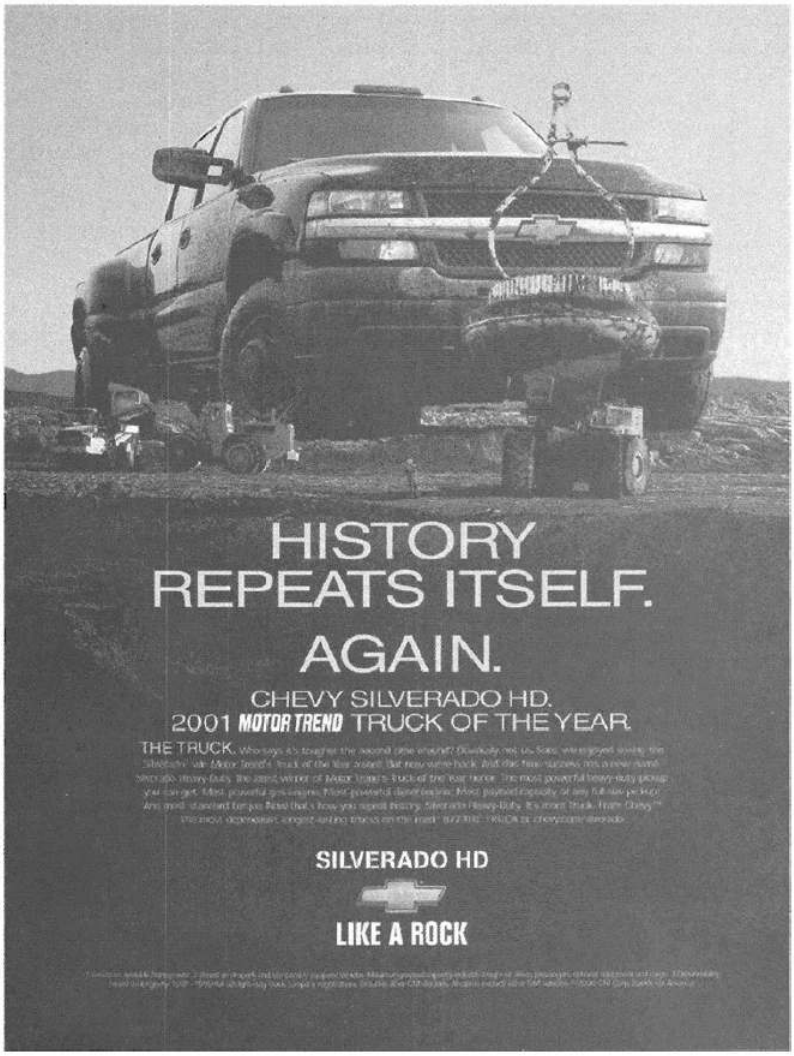


Figure 12.2.3: Winning an award is a psychological aspect of price

Another manifestation of the psychological aspects of pricing is the use of odd prices 3 We call prices that end in such digits as 5, 7, 8, and 9 “odd prices” (e.g. USD 2.95, USD 15.98, or USD 299.99). Even prices are USD 3, USD 16, or USD 300. For a long time marketing people have attempted to explain why odd prices are used. It seems to make little difference whether one pays USD 29.95 or USD 30 for an item. Perhaps one of the most often heard explanations concerns the psychological impact of odd prices on customers. The explanation is that customers perceive even prices such as USD 5 or USD 10 as regular prices. Odd prices, on the other hand, appear to represent bargains or savings and therefore encourage buying. There seems to be some movement toward even pricing; however, odd pricing is still very common. A somewhat related pricing strategy is combination pricing. Examples are two-for-one, buy-one-get-one-free. Consumers tend to react very positively to these pricing techniques.

This page titled 12.2: Basics of Pricing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

12.3: Introduction to Global Pricing

Learning Objectives

After reading this section, students should be able to …

1. define pricing
2. apply the basics of pricing to global pricing decisions
3. appreciate the global marketer's view of price

Price is the value of a product offering that can be created through the different marketing mix elements, such as through product, distribution and communication decisions. Therefore, global pricing decisions are related to other marketing mix variables.

At its basic level, pricing is the process of determining what a company will receive in exchange for its products. As one of the four "Ps" in the marketing mix, pricing is the only revenue generating element. Several factors affect the global pricing of a product, e.g., manufacturing cost, market place, competition, market condition, and quality of product, distribution channels, country factors and company factors (Alon and Jaffe 2013). According to Clarke and Wilson (2009), international pricing decisions also need to take account of tariffs, quotas, local taxes, subsidies, grants, currency exchange, rates, local purchasing power, local business and consumer characteristics. Figure 12.1 shows the drivers of international pricing.

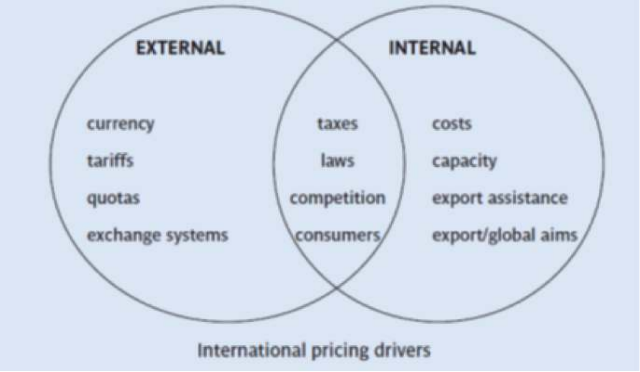


Figure 12.3.1: (*Clarke and Wilson (2009)*)

Prices can be used both to set values and provide signals in international markets (Eden and Rodriguez 2004). From a customer's point of view, value is the sole justification for price. Many times customers lack an understanding of the cost of materials and other costs that go into the making of a product. But those customers can understand what that product does for them in the way of providing value. It is on this basis that customers make decisions about the purchase of a product.

Effective pricing meets the needs of consumers and facilitates the exchange process. It requires that marketers understand that not all buyers want to pay the same price for products, just as they do not all want the same product, the same distribution outlets, or the same promotional messages. Therefore, in order to effectively price products, markets must distinguish among various market segments. The key to effective pricing is the same as the key to effective product, distribution, and promotion strategies. Marketers must understand buyers and price their products according to buyer needs if exchanges are to occur. However, one cannot overlook the fact that the price must be sufficient to support the plans of the organization, including satisfying stockholders. Price charged remains the primary source of revenue for most businesses.

Although making the global pricing decision is usually a marketing decision, making it correctly requires an understanding of both the customer and society's view of price as well. In some respects, price setting is the most important decision made by a business. A price set too low may result in a deficiency in revenues and the demise of the business. A price set too high may result in poor response from customers and, unsurprisingly, the demise of the business. The consequences of a poor pricing decision, therefore, can be dire. We begin our discussion of pricing by considering the perspective of the customer.

The customer's view of price

A customer can be either the ultimate user of the finished product or a business that purchases components of the finished product. It is the customer that seeks to satisfy a need or set of needs through the purchase of a particular product or set of products. Consequently, the customer uses several criteria to determine how much they are willing to expend in order to satisfy these needs. Ideally, the customer would like to pay as little as possible to satisfy these needs. Therefore, for the business to increase value (i.e. create the competitive advantage), it can either increase the perceived benefits or reduce the perceived costs. Both of these elements should be considered elements of price. To a certain extent, perceived benefits are the mirror image of perceived costs. For example, paying a premium price (e.g. USD 650 for a piece of Lalique crystal) is compensated for by having this exquisite work of art displayed in one's home. Other possible perceived benefits directly related to the price-value equation are status, convenience, the deal, brand, quality, choice, and so forth. Many of these benefits tend to overlap. Thus, providing value-added elements to the product has become a popular strategic alternative. Computer manufacturers now compete on value-added components such as free delivery setup, training, a 24-hour help line, trade-in, and upgrades.

Student Example

A great example of this concept is Sherwin-Williams. Our contractor segment (residential painters) wants the best product to use on their projects, yet they want to pay as little as possible. There are cases when they will use higher quality products if their customers want the best finish possible, however, once more everything comes down to cost. When the sales representative sets prices for individual contractors, they are not always the lowest. Whether a contractor purchases a low-grade, mid-grade, or high-grade product, we (store employees) try to add value to their purchase by providing exceptional services. This can range from many things such as carrying all of their paint out to their vehicles and loading it for them while having a small conversation; to reminding them about future sales; providing quick delivery services; and accepting orders by phone; or simply providing free-coffee all day. Expressing our appreciation by having cook-outs every few months also helps the contractors feel more at home with us, which is great because it helps build loyalty to our brand which is one of the main reasons why we have over 70% of the total paint and coatings market share in the world.

Silviano Espana Silva

Class of 2020

Perceived costs include the actual dollar amount printed on the product, plus a host of additional factors. As noted, these perceived costs are the mirror-opposite of the benefits. When finding a gas station that is selling its highest grade for USD 0.06 less per gallon, the customer must consider the 16 mile (25.75 kilometer) drive to get there, the long line, the fact that the middle grade is not available, and heavy traffic. Therefore, inconvenience, limited choice, and poor service are possible perceived costs. Other common perceived costs include risk of making a mistake, related costs, lost opportunity, and unexpected consequences, to name but a few. A new cruise traveler discovers he or she really does not enjoy that venue for several reasons–e.g. he or she is given a bill for incidentals when she leaves the ship, has used up her vacation time and money, and receives unwanted materials from this company for years to come. In the end, viewing price from the customer's perspective pays off in many ways. Most notably, it helps define value–the most important basis for creating a competitive advantage.

Price from a societal perspective

Price, at least in dollars and cents, has been the historical view of value. Derived from a bartering system (exchanging goods of equal value), the monetary system of each society provides a more convenient way to purchase goods and accumulate wealth. Price has also become a variable society employs to control its economic health. Price can be inclusive or exclusive. In many countries, such as Russia, China, and South Africa, high prices for products such as food, health care, housing, and automobiles, means that most of the population is excluded from purchase. In contrast, countries such as Denmark, Germany, and Great Britain charge little for health care and consequently make it available to all.

The Global marketer's view of price

Price is important to global marketing, because it represents marketers' assessment of the value customers see in the product or service and are willing to pay for a product or service. A number of factors have changed the way marketers undertake the pricing

of their products and services.

- Local competition puts pressure on the global firms' pricing strategies. Many local-made products are high in quality and compete in global markets on the basis of lower price for good value.
- Local competitors often try to gain market share by reducing their prices. The price reduction is intended to increase demand from customers who are judged to be sensitive to changes in price.
- New products are far more prevalent today than in the past. Pricing a new product can represent a challenge, as there is often no historical basis for pricing new products. If a new product is priced incorrectly, the marketplace will react unfavorably and the "wrong" price can do long-term damage to a product's chances for marketplace success.
- Technology has led to existing products having shorter marketplace lives. New products are introduced to the market more frequently, reducing the "shelf life" of existing products. As a result, marketers face pressures to price products to recover costs more quickly. Prices must be set for early successes including fast sales growth, quick market penetration, and fast recovery of research and development costs.

This page titled 12.3: Introduction to Global Pricing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

12.4: Global Pricing Approaches

Learning Objectives

After reading this section, students should be able to …

1. list the alternative approaches to determining global prices
2. explain penetration and skimming in global pricing

Global pricing decisions can be based on a number of factors, including cost, demand, competition, value, or some combination of factors. However, while many marketers are aware that they should consider these factors, pricing remains somewhat of an art. For purposes of discussion, we categorize the alternative approaches to determining price as follows: (a) cost-oriented pricing; (b) demand-oriented pricing; and (c) value-based approaches.

Cost-oriented pricing: cost-plus and mark-ups

The cost-plus method, sometimes called gross margin pricing, is perhaps most widely used by marketers to set price. The manager selects as a goal a particular gross margin that will produce a desirable profit level. Gross margin is the difference between how much the goods cost and the actual price for which it sells. This gross margin is designated by a per cent of net sales. The per cent selected varies among types of merchandise. That means that one product may have a goal of 48 per cent gross margin while another has a target of 33.5 per cent or 2 per cent.

A primary reason that the cost-plus method is attractive to marketers is that they do not have to forecast general business conditions or customer demand. If sales volume projections are reasonably accurate, profits will be on target. Consumers may also view this method as fair, since the price they pay is related to the cost of producing the item. Likewise, the marketer is sure that costs are covered.

A major disadvantage of cost-plus pricing is its inherent inflexibility. For example, department stores have often found difficulty in meeting competition from discount stores, catalog retailers, or furniture warehouses because of their commitment to cost-plus pricing. Another disadvantage is that it does not take into account consumers' perceptions of a product's value. Finally, a company's costs may fluctuate so constant price changing is not a viable strategy.

When middlemen use the term mark-up, they are referring to the difference between the average cost and price of all merchandise in stock, for a particular department, or for an individual item. The difference may be expressed in dollars or as a percentage. For example, a man's tie costs USD 4.60 and is sold for USD 8. The dollar mark-up is USD 3.40. The mark-up may be designated as a per cent of selling price 0r as a per cent of cost of the merchandise. In this example, the mark-up is 74 per cent of cost (USD 3.40/USD 4.60) or 42.5 per cent of the retail price (USD 3.40/USD 8).

There are several reasons why expressing mark-up as a percentage of selling price is preferred to expressing it as a percentage of cost. One is that many other ratios are expressed as a percentage of sales. For instance, selling expenses are expressed as a percentage of sales. If selling costs are 8 per cent, this means that for each USD 100,000 in net sales, the cost of selling the merchandise is USD 8,000. Advertising expenses, operating expenses, and other types of expenses are quoted in the same way. Thus, there is a consistency when making comparisons in expressing all expenses and costs, including mark-up, as a percentage of sales (selling price).

Middlemen receive merchandise daily and make sales daily. As new shipments are received, the goods are marked and put into stock. Cumulative mark-up is the term applied to the difference between total dollar delivered cost of all merchandise and the total dollar price of the goods put into stock for a specified period of time. The original mark-up at which individual items are put into stock is referred to as the initial mark-up.

Maintained mark-up is another important concept. The maintained mark-up percentage is an essential figure in estimating operating profits. It also provides an indication of efficiency. Maintained mark-up, sometimes called gross cost of goods, is the difference between the actual price for which all of the merchandise is sold and the total dollar delivered cost of the goods exclusive of deductions. The maintained mark-up is typically less than the initial mark-up due to mark-downs and stock shrinkages from theft,

breakage, and the like. Maintained mark-up is particularly important for seasonal merchandise that will likely be marked-down substantially at the end of the season.

Although this pricing approach may seem overly simplified, it has definite merit. The problem facing managers of certain types of businesses such as retail food stores is that they must price a very large number of items and change many of those prices frequently. The standard mark-up usually reflects historically profitable margins and provides a good guideline for pricing.

Certainly costs are an important component of pricing. No firm can make a profit until it covers its costs. However, the process of determining costs and then setting a price based on costs does not take into consideration what the customer is willing to pay at the marketplace. As a result, many companies that have set out to develop a product have fallen victim to the desire to continuously add features to the product, thus adding cost. When the product is finished, these companies add some percentage to the cost and expect customers to pay the resulting price. These companies are often disappointed, as customers are not willing to pay this cost-based price.

Break-even analysis

A somewhat more sophisticated approach to cost-based pricing is the break-even analysis. The information required for the formula for break-even analysis is available from the accounting records in most firms. The break even price is the price that will produce enough revenue to cover all costs at a given level of production. Total cost can be divided into fixed and variable (total cost = fixed cost + variable cost). Recall that fixed cost does not change as the level of production goes up or down. The rent paid for the building to house the operation might be an example. No cost is fixed in the long run, but in the short run, many expenses cannot realistically be changed. Variable cost does change as production is increased or decreased. For example, the cost of raw material to make the product will vary with production.

A second shortcoming of break-even analysis is it assumes that variable costs are constant. However, wages will increase with overtime and shipping discounts will be obtained. Third, break-even assumes that all costs can be neatly categorized as fixed or variable. Where advertising expenses are entered, break-even analysis will have a significant impact on the resulting break-even price and volume.

Target rates of return

Break-even pricing is a reasonable approach when there is a limit on the quantity which a firm can provide and particularly when a target return objective is sought. Assume, for example, that the firm with the costs illustrated in the previous example determines that it can provide no more than 10,000 units of the product in the next period of operation. Furthermore, the firm has set a target for profit of 20 per cent above total costs. Referring again to internal accounting records and the changing cost of production at near capacity levels, a new total cost curve is calculated. From the cost curve profile, management sets the desirable level of production at 80 per cent of capacity or 8,000 units. From the total cost curve, it is determined that the cost for producing 8,000 units is USD 18,000. 20 per cent of USD 18,000 is USD 3,600. Adding this to the total cost at 8,000 units yields the point at that quantity through which the total revenue curve must pass. Finally, USD 21,600 divided by 8,000 units yields the price of USD 2.70 per unit; here the USD 3,600 in profit would be realized. The obvious shortcoming of the target return approach to pricing is the absence of any information concerning the demand for the product at the desired price. It is assumed that all of the units will be sold at the price which provides the desired return.

It would be necessary, therefore, to determine whether the desired price is in fact attractive to potential customers in the marketplace. If break-even pricing is to be used, it should be supplemented by additional information concerning customer perceptions of the relevant range of prices for the product. The source of this information would most commonly be survey research, as well as a thorough review of pricing practices by competitors in the industry. In spite of their shortcomings, break-even pricing and target return pricing are very common business practices.

Demand-oriented pricing

Demand-oriented pricing focuses on the nature of the demand curve for the product or service being priced. The nature of the demand curve is influenced largely by the structure of the industry in which a firm competes. That is, if a firm operates in an industry that is extremely competitive, price may be used to some strategic advantage in acquiring and maintaining market share.

On the other hand, if the firm operates in an environment with a few dominant players, the range in which price can vary may be minimal.

Value-based pricing

If we consider the three approaches to setting price, cost-based is focused entirely on the perspective of the company with very little concern for the customer; demand-based is focused on the customer, but only as a predictor of sales; and value-based pricing focuses entirely on the customer as a determinant of the total price/value package. Marketers who employ value-based pricing might use the following definition: “It is what you think your product is worth to that customer at that time.” Moreover, it acknowledges several marketing/price truths:

- To the customer, price is the only unpleasant part of buying.
- Price is the easiest marketing tool to copy.
- Price represents everything about the product

Still, value-based pricing is not altruistic. It asks and answers two questions : (a) what is the highest price I can charge and still make the sale? and (b) am I willing to sell at that price? The first question must take two primary factors into account: customers and competitors. The second question is influenced by two more: costs and constraints. Let us discuss each briefly.

Many customer-related factors are important in value-based pricing. For example, it is critical to understand the customer buying process. How important is price? When is it considered? How is it used? Another factor is the cost of switching. Have you ever watched the television program “The Price is Right”? If you have, you know that most consumers have poor price knowledge. Moreover, their knowledge of comparable prices within a product category —e.g. ketchup—is typically worse. So price knowledge is a relevant factor. Finally, the marketer must assess the customers’ price expectations. How much do you expect to pay for a large pizza? Color TV? DVD? Newspaper? Swimming pool? These expectations create a phenomenon called “sticker shock” as exhibited by gasoline, automobiles, and ATM fees.

A second factor influencing value-based pricing is competitors. As noted in earlier chapters, defining competition is not always easy. Of course there are like-category competitors such as Toyota and Nissan. We have already discussed the notion of pricing above, below, and at the same level of these direct competitors. However, there are also indirect competitors that consumers may use to base price comparisons. For instance, we may use the price of a vacation as a basis for buying vacation clothes. The cost of eating out is compared to the cost of groceries. There are also instances when a competitor, especially a market leader, dictates the price for everyone else. Weyerhauser determines the price for lumber. Kellogg establishes the price for cereal.

If you are building a picnic table, it is fairly easy to add up your receipts and calculate costs. For a global corporation, determining costs is a great deal more complex. For example, calculating incremental costs and identifying avoidable costs are valuable tasks. Incremental cost is the cost of producing each additional unit. If the incremental cost begins to exceed the incremental revenue, it is a clear sign to quit producing. Avoidable costs are those that are unnecessary or can be passed onto some other institution in the marketing channel. Adding costly features to a product that the customer cannot use is an example of the former. As to the latter, the banking industry has been passing certain costs onto customers.

Another consideration is opportunity costs. Because the company spent money on store remodeling, they are not able to take advantage of a discounted product purchase. Finally, costs vary from market-to-market as well as quantities sold. Research should be conducted to assess these differences.

Although it would be nice to assume that a business has the freedom to set any price it chooses, this is not always the case. There are a variety of constraints that prohibit such freedom. Some constraints are formal, such as government restrictions in respect to strategies like collusion and price-fixing. This occurs when two or more companies agree to charge the same or very similar prices. Other constraints tend to be informal. Examples include matching the price of competitors, a traditional price charged for a particular product, and charging a price that covers expected costs.

Ultimately, value-based pricing offers the following three tactical recommendations:

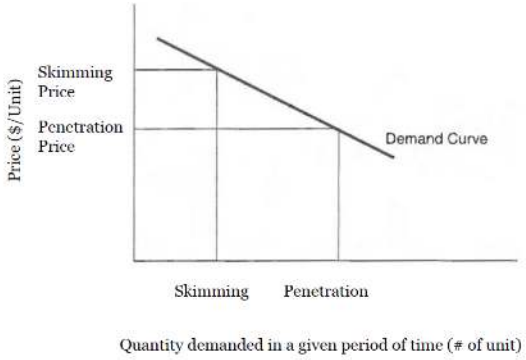
- Employ a segmented approach toward price, based on such criteria as customer type, location, and order size.
- Establish highest possible price level and justify it with comparable value.
- Use price as a basis for establishing strong customer relationships

Penetration and Skimming Pricing

Penetration pricing is usually used in the introductory stage of a new product's life cycle, and involves accepting a lower profit margin and to price relatively low. Such a strategy should generate greater sales and establish the new product in the market more quickly. Price skimming involves the top part of the demand curve. Price is set relatively high to generate a high profit margin and sales are limited to those buyers willing to pay a premium to get the new product (see Figure).

Penetration pricing can be used to achieve market share as a competitive strategy to achieve market leadership. Other times, it can also be used to increase market and sales growth. For example, when Sony was developing the Walkman in 1979, although a retail price of ¥50,000 ($249) was required to achieve breakeven. However, a price of ¥35,000 ($170) was needed to attract the youth market segment. Although after a long processes of cost cutting, a breakeven price of ¥40,000 was achieved, Chairman Akio Morita insisted on a retail price of ¥33,000 ($165) to commemorate Sony's 33rd anniversary. Sony also used this approach when its camcorder market became very competitive with price competition from Samsung, Hitachi and Panasonic. Another example is Google's penetration pricing strategy, where they offered their Google Checkout service at a break-even price or at a loss, trying to gain market share against Paypal.

Which strategy is best depends on a number of factors. A penetration strategy would generally be supported by the following conditions: price-sensitive consumers, opportunity to keep costs low, the anticipation of quick market entry by competitors, a high likelihood for rapid acceptance by potential buyers, and an adequate resource base for the firm to meet the new demand and sales.



Skimming generates a higher profit margin while penetration generates greater volume.

Figure 12.4.1: Penetration and skimming: pricing strategies as they relate to the demand curve.

A skimming strategy is most appropriate when the opposite conditions exist. A premium product generally supports a skimming strategy. In this case, "premium" does not just denote high cost of production and materials; it also suggests that the product may be rare or that the demand is unusually high. An example would be a USD 500 ticket for the World Series or an USD 80,000 price tag for a limited-production sports car. Having legal protection via a patent or copyright may also allow for an excessively high price. Intel and their Pentium chip possessed this advantage for a long period of time. In most cases, the initial high price is gradually reduced to match new competition and allow new customers access to the product.

A skimming strategy may be used when the company is the only marketer of a new or innovative product, so as to maximize profits until competition forces a lower price (Li and Li 2008). Several electronic products that were very innovative during their introduction, such as DVRs, CR payers, Flat Screen TVs, were priced very high during the initial introduction phase; then the prices dropped steeply. According to Cateora, Graham and Gilly 2016), this strategy can also be used when their markets have only two income levels: the super-rich and the very poor, as when Johnson & Johnson priced their diapers in Brazil before the arrival of P&G. As the company's cost structure will not allow the setting of a low enough price for the low income segment, the company will cater to the wealthier segment using a premium price.

This page titled 12.4: Global Pricing Approaches is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

12.5: Currency Fluctuations and Global Pricing

Learning Objectives

After reading this section, students should be able to …

1. explain the role of currency fluctuations and global pricing
2. outline what happens when home currency is weak and strong

Briefly, currency is any form of money in general circulation in a country. What exactly is a foreign exchange? In essence, foreign exchange is money denominated in the currency of another country or—now with the euro—a group of countries. Simply put, an exchange rate is defined as the rate at which the market converts one currency into another.

Any company operating globally must deal in foreign currencies. It has to pay suppliers in other countries with a currency different from its home country's currency. The home country is where a company is headquartered. The firm is likely to be paid or have profits in a different currency and will want to exchange it for its home currency. Even if a company expects to be paid in its own currency, it must assess the risk that the buyer may not be able to pay the full amount due to currency fluctuations.

If you have traveled outside of your home country, you may have experienced the currency market—for example, when you tried to determine your hotel bill or tried to determine if an item was cheaper in one country versus another. In fact, when you land at an airport in another country, you're likely to see boards indicating the foreign exchange rates for major currencies. For example, imagine you're on vacation in Thailand and the exchange rate board indicates that the Bangkok Bank is willing to exchange currencies at the following rates (see the following figure). GBP refers to the British pound; JPY refers to the Japanese yen; and HKD refers to the Hong Kong dollar, as shown in the following figure. Because there are several countries that use the dollar as part or whole of their name, this chapter clearly states "US dollar" or uses US$ or USD when referring to American currency.

Table 12.5.1: Foreign Exchange Rates: Bangcock Bank

Currancy/Baht	Banknotes Buy	Banknotes Sell
USC	31.67	32.32
GBP	50.19	51.80
Euro	41.74	43.00
JOY	36.56	39.01
HKC	4.03	4.22

This chart tells us that when you land in Thailand, you can use 1 US dollar to buy 31.67 Thai baht. However, when you leave Thailand and decide that you do not need to take all your baht back to the United States, you then convert baht back to US dollars. We then have to use more baht—32.32 according to the preceding figure—to buy 1 US dollar. The spread between these numbers, 0.65 baht, is the profit that the bank makes for each US dollar bought and sold. The bank charges a fee because it performed a service—facilitating the currency exchange. When you walk through the airport, you'll see more boards for different banks with different buy and sell rates. While the difference may be very small, around 0.1 baht, these numbers add up if you are a global company engaged in large foreign exchange transactions.

Companies, investors, and governments want to be able to convert one currency into another. A company's primary purposes for wanting or needing to convert currencies is to pay or receive money for goods or services. Imagine you have a business in the United States that imports wines from around the world. You'll need to pay the French winemakers in euros, your Australian wine suppliers in Australian dollars, and your Chilean vineyards in pesos. Obviously, you are not going to access these currencies physically. Rather, you'll instruct your bank to pay each of these suppliers in their local currencies. Your bank will convert the currencies for you and debit your account for the US dollar equivalent based on the exact exchange rate at the time of the exchange.

Understand How to Determine Exchange Rates

How to Quote a Currency

There are several ways to quote currency, but let's keep it simple. In general, when we quote currencies, we are indicating how much of one currency it takes to buy another currency. This quote requires two components: the base currency and the quoted currency. The quoted currency is the currency with which another currency is to be purchased. In an exchange rate quote, the quoted currency is typically the numerator. The base currency is the currency that is to be purchased with another currency, and it is noted in the denominator. For example, if we are quoting the number of Hong Kong dollars required to purchase 1 US dollar, then we note HKD 8 / USD 1. (Note that 8 reflects the general exchange rate average in this example.) In this case, the Hong Kong dollar is the quoted currency and is noted in the numerator. The US dollar is the base currency and is noted in the denominator. We read this quote as "8 Hong Kong dollars are required to purchase 1 US dollar." If you get confused while reviewing exchanging rates, remember the currency that you want to buy or sell. If you want to sell 1 US dollar, you can buy 8 Hong Kong dollars, using the example in this paragraph.

Direct Currency Quote and Indirect Currency Quote

Additionally, there are two methods—the American terms and the European terms—for noting the base and quoted currency. These two methods, which are also known as direct and indirect quotes, are opposite based on each reference point. Let's understand what this means exactly.

The American terms, also known as US terms, are from the point of view of someone in the United States. In this approach, foreign exchange rates are expressed in terms of how many US dollars can be exchanged for one unit of another currency (the non-US currency is the *base currency*). For example, a dollar-pound quote in American terms is USD/GP (US$/£) equals 1.56. This is read as "1.56 US dollars are required to buy 1 pound sterling." This is also called a direct quote, which states the domestic currency price of one unit of foreign currency. If you think about this logically, a business that needs to buy a foreign currency needs to know how many US dollars must be sold in order to buy one unit of the foreign currency. In a direct quote, the domestic currency is a variable amount and the foreign currency is fixed at one unit.

Conversely, the European terms are the other approach for quoting rates. In this approach, foreign exchange rates are expressed in terms of how many currency units can be exchanged for a US dollar (the US dollar is the base currency). For example, the pound-dollar quote in European terms is £0.64/US$1 (£/US$1). While this is a direct quote for someone in Europe, it is an indirect quote in the United States. An indirect quote states the price of the domestic currency in foreign currency terms. In an indirect quote, the foreign currency is a variable amount and the domestic currency is fixed at one unit.

A direct and an indirect quote are simply reverse quotes of each other. If you have either one, you can easily calculate the other using this simple formula:

direct quote = 1 / indirect quote.

To illustrate, let's use our dollar-pound example. The direct quote is US$1.56 = 1/£0.64 (the indirect quote). This can be read as

1 divided by 0.64 equals 1.56.

In this example, the direct currency quote is written as US$/£ = 1.56.

While you are performing the calculations, it is important to keep track of which currency is in the numerator and which is in the denominator, or you might end up stating the quote backward. The direct quote is the rate at which you buy a currency. In this example, you need US$1.56 to buy a British pound.

Tip: Many international business professionals become experienced over their careers and are able to correct themselves in the event of a mix-up between currencies. To illustrate using the example mentioned previously, the seasoned global professional knows that the British pound is historically higher in value than the US dollar. This means that it takes more US dollars to buy a pound than the other way around. When we say "higher in value," we mean that the value of the British pound buys you more US dollars. Using this logic, we can then deduce that 1.56 US dollars are required to buy 1 British pound. As an international businessperson, we would know instinctively that it cannot be less—that is, only 0.64 US dollars to buy a British pound. This would imply that the dollar value was higher in value. While major currencies have changed significantly in value vis-à-vis each

other, it tends to happen over long periods of time. As a result, this self-test is a good way to use logic to keep track of tricky exchange rates. It works best with major currencies that do not fluctuate greatly vis-à-vis others.

Exchange fluctuations and global prices

The strengthening or weakening of a home (exporting) country's currency vis-à-vis that of the host (foreign) country, can have far-reaching effects on the price setting in the foreign country, as well as other elements of the global marketer's marketing strategy. For example, if the value of the U.S. dollar relative to the euro was U.S.$1 to 1.8315 euros in 2001, and U.S.$1 to 0.8499 euros in 2003, then the exchange rate U.S.$1 to 1.8315 euros is said to be stronger for the US dollar, and the exchange rate U.S.$1 to 0.8499 euros is said to be weaker for the US dollar. Similarly, if the value of the U.S. dollar relative to the Indian Rupee was U.S.$1 to INR 50 in 2001, and U.S.$1 to INR 70 in 2018, then the exchange rate U.S.$1 to INR 50 is said to be weaker for the US dollar than the exchange rate U.S.$1 to INR 70. A weaker exchange rate (e.g. U.S.$1 to 0.8499 euros and U.S.$1 to INR 50) will fetch lesser money in terms of the foreign currency, while a stronger exchange rate will fetch more money in terms of the foreign currency.

When the home currency of the global marketer weakens, the exchange rates are supposed be favorable to the global marketer, because the home currency will fetch lesser in terms of the foreign currency, and hence the prices of the exported product in the foreign country's currency will come down. Therefore, the global marketer can cut prices in the foreign country, and hence, increase market share. On the other hand, the global marketer can also decide to maintain the higher prices, in which case the global marketer will see windfall revenue, and increased margins. Thus if the exchange rate of the US dollar relative to the Japanese Yen weakens (lesser Yen for each dollar), then it is good for US companies manufacturing their products in the US and selling them in Japan (e.g. Boeing, Caterpillar, GE). On the other hand, it is not a good pricing scenario for Japanese companies (e.g. Canon and Olympus) who manufacture and sell in Japan against their US competitors. This context is also unfavorable to American tourists who are shopping for cameras, because they would be paying in Yen, and their US dollars would get lesser Yen, relative to what it would have fetched if the US dollar was stronger.

When the domestic (home) currency of the US global marketer strengthens (e.g. U.S.$1 to 1.8315 euros and U.S.$1 to INR 70), where the US dollar will fetch more money in terms of the foreign currency, then this price situation is said to be bad for global marketers who manufacture their products in the US and sell them in the foreign (host) country, priced in the foreign currency. Although each dollar gets more in terms of the foreign currency, what it really means is that the US company will now get lesser dollars after conversion into the US dollar, for the same amount of foreign currency, after the exchange rate strengthening. Thus, the US company may not be able to cover its costs which are specified in US dollars. One strategy to overcome this effect is to manufacture or source their products in the host country, and maximize all expenditures in the local currency (remember, each dollar gets more local currency!).

Since the strengthening of the home (domestic) currency results in more foreign currency, this conversion results in higher prices, which are specified in the local currency. This is usually not a problem if the demand for a product is inelastic. Otherwise, the global marketer has to cut costs in his home country, or improve quality and service to make up for the increased price levels. A drastic strategy to counter this situation would be to absorb some of the costs, which will result in a reduced margin.

Table 12.5.2: Exchange fluctuations and global prices

1. Stress price benefits	1. Engage in nonprice competition by improving quality, delivery, and after-sale service.
2. Expand product line and add more costly features.	2. Improve productivity and engage in cost reduction.
3. Shift sourcing to domestic market.	3. Shift sourcing outside home country.
4. Exploit market opportunities in all markets.	4. Give priority to exports to countries with stronger currencies.
5. Use full-costing approach, but employ marginal-cost pricing to penetrate new or competitive markets.	5. Trim profit margins and use marginal-cost pricing.
6. Speed repatriation of foreign-earned income and collections.	6. Keep the foreign-eamed income in host country: slow down collections.
7. Minimize expenditures in local (host-country) currency.	7. Maximize expenditures in local (host-country) currency.
8. Buy advertising, insurance, transportation, and other services in domestic market.	8. Buy needed services abroad and pay for them in local currencies.
9. Bill foreign customers in their own currency.	9. Bill foreign customers in the domestic currency.

Adapted from: Keegan and Green (2011)

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- “What Do We Mean by Currency and Foreign Exchange?”, section 7.1 from the book Challenges and Opportunities in International Business (v. 1.0). under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

This page titled 12.5: Currency Fluctuations and Global Pricing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

12.6: Tariffs and Global Pricing

Learning Objectives

After reading this section, students should be able to …

1. explain the effects of a tariff on global prices

As we learned in Chapter 2 (Section 2.3: Understanding Tariffs), a tariff is any tax or fee collected by a government. Two of the price effects of a tariff are worthy of emphasis. First, although a tariff represents a tax placed solely on imported goods, the domestic price of both imported and domestically produced goods will rise. In other words, a tariff will cause local producers of the product to raise their prices. Why?

When the price of imported goods rises due to the tariff, consumers will shift their demand from foreign to domestic suppliers. The extra demand will allow domestic producers an opportunity to raise output and prices to clear the market. In so doing, they will also raise their profit. Thus as long as domestic goods are substitutable for imports and as long as the domestic firms are profit seekers, the price of the domestically produced goods will rise along with the import price.

The average consumer may not recognize this rather obvious point. For example, suppose the United States places a tariff on imported automobiles. Consumers of U.S.-made automobiles may fail to realize that they are likely to be affected. After all, they might reason, the tax is placed only on imported automobiles. Surely this would raise the imports' prices and hurt consumers of foreign cars, but why would that affect the price of U.S. cars? The reason, of course, is that the import car market and the domestic car market are interconnected. Indeed, the only way U.S.-made car prices would not be affected by the tariff is if consumers were completely unwilling to substitute U.S. cars for imported cars *or* if U.S. automakers were unwilling to take advantage of a profit-raising possibility. These conditions are probably unlikely in most markets around the world.

The second interesting price effect arises because the importing country is large. When a large importing country places a tariff on an imported product, it will cause *the foreign price to fall*. The reason? The tariff will reduce imports into the domestic country, and since its imports represent a sizeable proportion of the world market, world demand for the product will fall. The reduction in demand will force profit-seeking firms in the rest of the world to lower output and price in order to clear the market.

The effect on the foreign price is sometimes called the terms of trade effect. The terms of trade is sometimes defined as the price of a country's *export goods* divided by the price of its *import goods*. Here, since the importing country's import good will fall in price, the country's terms of trade will rise. Thus a tariff implemented by a large country will cause an improvement in the country's terms of trade.

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- The book "International Trade: Theory and Policy" v. 1.0 published by Saylor Academy under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work's original creator or licensor.

This page titled 12.6: Tariffs and Global Pricing is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

12.7: Quotas and Dumping

Learning Objectives

After reading this section, students should be able to …

1. explain the effects of quotas and dumping on global prices

Quotas

A quota imposes limits on the quantity of a good that can be imported over a period of time. Quotas are used to protect specific industries, usually new industries or those facing strong competitive pressure from foreign firms. U.S. import quotas take two forms. An absolute quota fixes an upper limit on the amount of a good that can be imported during the given period. A tariff-rate quota permits the import of a specified quantity and then adds a high import tax once the limit is reached.

Sometimes quotas protect one group at the expense of another. To protect sugar beet and sugar cane growers, for instance, the United States imposes a tariff-rate quota on the importation of sugar—a policy that has driven up the cost of sugar to two to three times world prices.[1] These artificially high prices push up costs for American candy makers, some of whom have moved their operations elsewhere, taking high-paying manufacturing jobs with them. Life Savers, for example, were made in the United States for ninety years but are now produced in Canada, where the company saves $10 million annually on the cost of sugar.[2]

An extreme form of quota is the embargo, which, for economic or political reasons, bans the import or export of certain goods to or from a specific country. The United States, for example, bans nearly every commodity originating in Cuba.

Quotas reduce the quantity, and therefore increase the market price, of imported goods. Their economic effect is therefore similar to that of tariffs, except that the tax revenue gain from a tariff will instead be distributed to those who receive import licenses. This explains why economists often suggest that import licenses be auctioned to the highest bidder or that import quotas be replaced by an equivalent tariff.

Dumping

A common political rationale for establishing tariffs and quotas is the need to combat dumping: the practice of selling exported goods below the price that producers would normally charge in their home markets (country of origin), and often below the cost of producing the goods. Dumping is said to occur when imports sold in a foreign market are priced at either levels that represent less than the cost of production in that country plus an 8% profit margin or at levels below those prevailing in the producing countries. Usually, nations resort to this practice to gain entry and market share in foreign markets, but it can also be used to sell off surplus or obsolete goods. Dumping creates unfair competition for domestic industries, and governments are justifiably concerned when they suspect foreign countries of dumping products on their markets. They often retaliate by imposing punitive tariffs that drive up the price of the imported goods. For example, in 2003, the International Trade Commission allowed the U.S. Dept. of Commerce to raise duty rates on shrimp from India, China, Brazil, Vietnam, Ecuador, and Thailand, when the Southern Shrimp Alliance protested that the six countries were dumping shrimp in the U.S.

According to Clarke and Wilson (2009), there are considered to be three types of dumping activity: sporadic dumping, which occurs when unsold inventories are disposed of in export markets, while predatory dumping helps a global firm to gain market access and undercut the competition. Persistent dumping is a permanent approach that is undertaken when production and labor costs are much lower in the home country (Onkvisit and Shaw, 1993).

References

1. Chris Edwards, “The Sugar Racket,” CATO Institute, Tax and Budget, June 2007, http://www.cato.org/pubs/tbb/tbb_0607_46.pdf (accessed August 24, 2011).
2. See George Will, “Sugar Quotas Produce Sour Results,” Detroit News, February 13, 2004, http://www.detnews.com/2004/editoria.../all-62634.htm (accessed October 17, 2004).

Source

This page is licensed under a Creative Commons Attribution Non-Commercial Share-Alike License (Links to an external site) Links to an external site and contains content from a variety of sources published under a variety of open licenses, including:

- “Doctrines”, section 1.1 (from appendix 1) from the book Global Strategy (v. 1.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.
- “Trade Controls”, section 3.4 from the book An Introduction to Business (v. 2.0) under a Creative Commons Attribution-NonCommercial-ShareAlike 3.0 License without attribution as requested by the work’s original creator or licensor.

This page titled 12.7: Quotas and Dumping is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

CHAPTER OVERVIEW

13: The International Marketing Plan

13.1: Marketing Plan Basics
13.2: Writing the International Marketing Plan

This page titled 13: The International Marketing Plan is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

13.1: Marketing Plan Basics

Learning Objectives

After reading this section, students should be able to …

1. outline the functions of a marketing plan.
2. explain how to write a marketing plan.

A marketing plan should do the following:

1. Identify customers' needs.
2. Evaluate whether the organization can meet those needs in some way that allows for profitable exchanges with customers to occur.
3. Develop a mission statement, strategy, and organization centered on those needs.
    1. Create offerings that are the result of meticulous market research.
    2. Form operations and supply chains that advance the successful delivery of those offerings.
4. Pursue advertising, promotional, and public relations campaigns that lead to continued successful exchanges between the company and its customers.
5. Engage in meaningful communications with customers on a regular basis.

The Marketing Plan's Outline

The actual marketing plan you create will be written primarily for executives, who will use the forecasts in your plan to make budgeting decisions. These people will make budgeting decisions not only for your marketing activities but also for the firm's manufacturing, ordering, and production departments, and other functions based on your plan

In addition to executives, many other people will use the plan. Your firm's sales force will use the marketing plan to determine its sales strategies and how many salespeople are needed. The entire marketing staff will rely on the plan to determine the direction and nature of their activities. The advertising agency you hire to create your promotional campaigns will use the plan to guide its creative team. Figure 13.2 "Marketing Plan Outline" shows a complete outline of a marketing plan (you may also want to go to http://www.morebusiness.com/ templates_worksheets/bplans/printpre.brc for an example).

Next, we will discuss the elements in detail so you will know how to prepare a marketing plan.

The Marketing Plan: An Outline

I. Executive Summary

II. The Business Challenge

a. A brief description of the offering and the goals of the plan. This section serves as an introduction.

III. The Market

a. Customers: Who are they, and what do they need?
b. Company analysis: Your firm's strengths and weaknesses relative to this market and the offering.
c. Collaborators: Your collaborators could include suppliers and/or distributors or retailers.
d. Competitors: Who are they, and what are they doing?
e. Business climate:The business climate includes the opportunities and threats created by environmental forces, such as government regulations and legislation, the economy, and social, cultural, and technological forces.

IV. The Strategy

a. The strategy: Why did you choose the strategy you did? Consider including a brief discussion of alternatives that were considered and discarded.
b. The offering: Provide details on the features and benefits of the offering, as well as its pricing options.

c. The communication plan: How will the offering be launched? What will the ongoing communication strategies be? This section is likely to be fairly broad and will require collaboration with communication partners such as your firm's advertising agency.
d. Distribution: How will the offering be sold? Who will sell it? Who will ship it? Who will service it?

V. Budget

a. Investment: Provide details about the budget needed to launch and maintain the offering.
b. Return: List both the short-term and long-term financial goals of the offering, including its projected sales, costs, and net income.
c. Other resources required.

VI. Conclusion

The Executive Summary

A marketing plan starts with an executive summary. An executive summary should provide all the information your company's executives need to make a decision without reading the rest of the plan. The summary should include a brief description of the market, the product to be offered, the strategy behind the plan, and the budget. Any other important information, such as how your competitors and channel partners will respond to the actions your firm takes, should also be summarized. Because most executives will be reading the plan to make budgeting decisions, the budgeting information you include in the summary is very important. If the executives want more detail, they can refer to the "budget" section, which appears later in the plan. The executive summary should be less than one page long; ideally, it should be about a half page long. Most marketing plan writers find it easier to write a plan's summary last, even though it appears first in the plan. A summary is hard to write when you don't know the whole plan, so waiting until the plan is complete makes writing the executive summary easier.

The Business Challenge

In the "business challenge" section of the plan, the planner describes the offering and provides a brief rationale for why the company should invest in it. In other words, why is the offering needed? How does it fit in with what the company is already doing and further its overall business goals? In addition, the company's mission statement should be referenced. How does the offering and marketing plan further the company's mission?



Figure 13.1.1: Convincing stakeholders Your marketing plan has to convince busy executives and other stakeholders that your idea is worth investing in (Richter Frank-Jurgen – Horasis Global China Business Meeting 2013 – CC BY-SA 2.0.)

Remember that a marketing plan is intended to be a persuasive document. You are trying not only to influence executives to invest in your idea but also to convince other people in your organization to buy into the plan. You are also trying to tell a compelling story that will make people outside your organization—for example, the director of the advertising agency you work with, or a potential supplier or channel partner—invest money, time, and effort into making your plan a success. Therefore, as you write the

plan you should constantly be answering the question, “Why should I invest in this plan?” Put your answers in the business challenge section of the plan.

The Market

The market section of the plan should describe your customers and competitors, any other organizations with which you will collaborate, and the state of the market. We suggest that you always start the section by describing the customers who will purchase the offering. Why? Because customers are central to all marketing plans. After that, discuss your competitors, the climate, and your company in the order you believe readers will find most persuasive. In other words, discuss the factor you believe is most convincing first, followed by the second-most convincing factor, and so on.

Customers

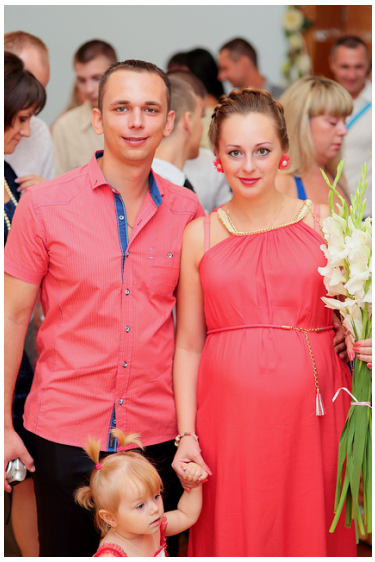


Figure 13.1.2: Customer segments Progresso Soups may divide their market into several groups. This family photo might actually represent three different markets: a person who eats lunch at his or her desk at work and needs something quick and filling; a retired but active couple that wants something hot and nourishing; and a busy young family looking for easy meals to prepare. (Vladimir Pustovit – Family – CC BY 2.0.)

Who does your market consist of? What makes these people decide to buy the products they do, and how do they fulfill their personal value equations? What is their buying process like? Which of their needs does your offering meet?

Break the market into customer segments and describe each segment completely, answering those questions for each segment. When you write your plan, begin with the most important segment first and work your way to the least important segment. Include in your discussion the market share and sales goals for each segment.

For example, Progresso Soups’ primary market segments might include the following:

- Families in colder regions
- People who need a good lunch but have to eat at their desks
- Busy young singles
- Older, perhaps retired, empty-nesters

These segments would be based on research that Progresso has completed showing that these are the groups that eat the most soup.

Your discussion of each segment should also include how to reach the customers within it, what they expect or need in terms of support (both presales and postsales support), and other information that helps readers understand how each segment is different from the others. After reading the section, a person should have a good grasp of how the segments differ yet understand how the needs of each are satisfied by the total offering.

Audio Clip

Katie Scallan-Sarantakes

http://app.wistia.com/embed/medias/4e5cbb5411

A marketing plan has to account for many factors: customers, competitors, and more. Listen as Katie Scallan-Sarantakes describes how she had to consider these factors when creating marketing plans for Toyota.

Company Analysis

Include the results of your analysis of your company's strengths and weaknesses in this section. How is the company perceived by the customers you described earlier? Why is the company uniquely capable of capitalizing on the opportunity outlined in the plan? How sustainable is the competitive advantage you are seeking to achieve?

You will also need to identify any functional areas in which your company might need to invest for the plan to succeed. For example, money might be needed for new production or distribution facilities and to hire new marketing or sales employees and train existing ones.

One tool that is useful for framing these questions is the SWOT analysis. SWOT stands for strengths, weaknesses, opportunities, and threats. Strengths and weaknesses are internal, meaning they are conditions of the company. Either these conditions are positive (strengths) or negative (weaknesses). Opportunities and threats are external to the company, and could be due to potential or actual actions taken by competitors, suppliers, or customers. Opportunities and threats could also be a function of government action or changes in technology and other factors.

When working with executives, some consultants have noted the difficulty executives have in separating opportunities from strengths, weaknesses from threats. Statements such as "We have an opportunity to leverage our strong product features" indicate such confusion. An opportunity lies in the market, not in a strength. Opportunities and threats are external; strengths and weaknesses are internal. Assuming demand (an external characteristic) for a strength (an internal characteristic) is a common marketing mistake. Sound marketing research is therefore needed to assess opportunity.

Other factors that make for better SWOT analysis are these:

- Honest. A good SWOT analysis is honest. A better way to describe those "strong" product features mentioned earlier would be to say "strong reputation among product designers," unless consumer acceptance has already been documented.
- Broad. The analysis has to be broad enough to capture trends. A small retail chain would have to look beyond its regional operating area in order to understand larger trends that may impact the stores.
- Long term. Consider multiple time frames. A SWOT analysis that only looks at the immediate future (or the immediate past) is likely to miss important trends. Engineers at Mars (makers of Skittles, M&Ms, and Snickers) visit trade shows in many fields, not just candy, so that they can identify trends in manufacturing that may take a decade to reach the candy industry. In this way, they can shorten the cycle and take advantage of such trends early when needed.
- Multiple perspectives. SWOT analyses are essentially based on someone's perception. Therefore, a good SWOT should consider the perspective of all areas of the firm. Involve people from shipping, sales, production, and perhaps even from suppliers and channel members.

The SWOT analysis for a company, or for any organization, is both internal and external in focus. Some of the external areas for focus are collaborators (suppliers, distributors, and others), competitors, and the business climate.

Collaborators

Along with company strengths and weaknesses, identify any actual or potential partners needed to pull the plan off. Note that collaborators are more than just a list of suppliers and distributors. Collaborators are those organizations, either upstream or downstream in the value chain, you need to partner with to cocreate value.

For example, AT&T collaborated with Apple to develop the iPhone. AT&T is downstream in the value chain, providing the needed cell service and additional features that made the iPhone so revolutionary. At the same time, however, AT&T was a part of the development of the iPhone and the attendant marketing strategy; the partnership began well before the iPhone was launched.

Competitors

Your marketing plan, if it is any good at all, is likely to spark retaliation from one or more competitors. For example, Teradata and Unica operate in the same market. Both sell data-warehousing products to companies. Teradata primarily focuses on the information technology departments that support the data warehouse, whereas Unica focuses on the marketing departments that actually use the data warehouse. Nonetheless, Teradata is well aware of Unica's marketing strategy and is taking steps to combat it by broadening its own market to include datawarehousing users in marketing departments. One step was to teach their salespeople what marketing managers do and how they would use a data warehouse as part of their job so that when these salespeople are talking to marketing managers, they can know what they're talking about.

Teradata marketing planners also have to be aware of potential competitors. What if IBM or HP decided to enter the market? Who is most likely to enter the market, what would their offering look like, and how can we make it harder for them to want to enter the market? If your company captures their market before they can enter, then they may choose to go elsewhere.

Identify your competitors and be honest about both their strengths and weaknesses in your marketing. Remember that other people, and perhaps other organizations, will be using your plan to create their own plans. If they are to be successful, they have to know what competition they face. Include, too, in this section of the plan how quickly you expect your competitors to retaliate and what the nature of that retaliation will be. Will they lower their prices, create similar offerings, add services to drive up the value of their products, spend more on advertising, or a combination of these tactics?

A complete competitive analysis not only anticipates how the competition will react; it also includes an analysis of the competition's financial resources. Do your competitors have money to invest in a competitive offering? Are they growing by acquiring other companies? Are they growing by adding new locations or new sales staff? Or are they growing simply because they are effective? Maybe they are not growing at all. To answer these questions, you will need to carefully review your competitors' financial statements and all information publicly available about them. This can include an executive quoted in an article about a company's growth for a particular product or an analyst's projection for future sales within a specific market.

Business Climate

You may have already addressed some of the factors in the business environment that are creating the opportunity for your offering. For example, when you discussed customers, you perhaps noted a new technology they are beginning to use.

A complete coverage of the climate would include the following (the PEST analysis):

- Political climate
- Economic climate
- Social and cultural environment
- Technological environment

A scan of the political climate should include any new government regulations as well as legislation. For example, will changes in the tax laws make for more or less disposable income among our customers? Will the tightening of government regulations affect how salespeople can call on doctors, for example, hindering your marketing opportunity? Will federal policies that affect exchange rates or tariffs make global competitors stronger or weaker? For example, the government introduced the Cash for Clunkers program to encourage people to buy new cars. Within only a few weeks, 250,000 new cars were sold through the program and it ran out of money. Auto dealers were caught unprepared and many actually ran out of popular vehicles.

The economic climate is also important to consider. While 2008 saw tremendous swings in gas prices, other factors such as the subprime lending crisis and decline of the housing market affected everything from the price of corn to the sales of movie tickets. Such volatility is unusual, but it is important nonetheless to know what the economy is doing.



Figure 13.1.3:The economic climate. The housing crisis was caused by a failure in the subprime lending market, an economic condition that affected many other businesses. (Jeff Turner – Sign Of The Times – Foreclosure – CC BY 2.0)

The social and cultural environment is also important to watch. Marketers, for example, may note the rise in the Hispanic population as a market segment, but it is also important to recognize the influence of the Hispanic culture. Understanding the Hispanic culture is important in reaching this market segment with the right marketing mix. In creating marketing campaigns for something such as a financial product, it's very important to understand the history that Hispanics have had with financial institutions in their home countries. Understanding that culturally Hispanics might not trust financial institutions and developing campaigns that generate positive word of mouth, such as refer-a-friend and influencer tactics, can be explosive once the wall has been torn down.

Finally, the technological environment should be considered. Technology is the application of science to solve problems. It encompasses more than just information (computer) technology. For example, consider a pacemaker. New technology could be related to the battery used to power the pacemaker, the materials used in the leads (the wires that connect the pacemaker to the body), or even the material that encases the pacemaker. Understanding the technological environment can provide you with a greater understanding of a product's life cycle and the direction the market is taking when it comes to newer technologies.

Many of the environmental factors we mentioned impact other factors. For example, technological changes are altering the social and cultural environment. Instead of writing letters to one another, families and friends use e-mail and social networking sites to communicate and maintain relationships. Online communication has affected any number of businesses, including the greeting card business and the U.S. Postal Service, which recently announced it was closing many facilities.

Likewise, the economic environment influences the political environment and vice versa. The huge bailout of the banks by the government is an example of how the economic environment affects the political environment. The laws passed as a result of the bank bailout, which include more-restrictive lending practices, are affecting banks, businesses, and consumers. Any looming changes in the business climate such as this need to be included in your marketing plan.

The Strategy

The next section of the plan details the strategy your organization will use to develop, market, and sell the offering. This section is your opportunity to create a compelling argument as to what you intend to do and why others should invest in the strategy. Your reader will be asking, "Why should we adopt this strategy?" To answer that question, you may need to include a brief discussion of the strategic alternatives that were considered and discarded. When readers complete the section, they should conclude that the strategy you proposed is the best one available.

The Offering

Provide detail on the features and benefits of the offering, including pricing options, in this section. For example, in some instances, your organization might plan for several variations of the offering, each with different pricing options. The different options should be discussed in detail, along with the market segments expected to respond to each option. Some marketing professionals like to specify the sales goals for each option in this section, along with the associated costs and gross profit margins for each. Other planners prefer to wait until the budget section of the plan to provide that information.

The plan for the offering should also include the plan for introducing offerings that will follow the initial launch. For example, when should Progresso introduce new soup flavors? Should there be seasonal flavors? Should there be smaller sizes and larger sizes, and should they be introduced all at the same time or in stages?

Part of an offering is the service support consumers need to extract the offering's full value. The support might include presales support as well as postsales support. For example, Teradata has a team of finance specialists who can help customers document the return on investment they would get from purchasing and implementing a Teradata data warehouse. This presales support helps potential buyers make a stronger business case for buying Teradata's products with executives who control their companies' budgets.

Postsales support can include technical support. In B2B (business-to-business) environments, sellers frequently offer to train their customers' employees to use products as part of their postsales support. Before you launch an offering, you need to be sure your firm's support services are in place. That means training service personnel, creating the appropriate communication channels for customers to air their technical concerns, and other processes.



Figure 13.1.1: Service support .Prior to launching a new offering, the pre-sales and postsales support personnel for it have to be trained and the appropriate work processes created so that the right level of support is provided. These call-center technicians had to first learn the offering's technical processes before it could be launched. *(CWCS Managed Hosting – customer service assistant on phone – CC BY 2.0.)*

The Communication Plan

How will the offering be launched? Will it be like Dow Corning's launch of a new silicon acrylate copolymer, a product used to add color to cosmetics? That product was announced at the In-Cosmetics trade show in Barcelona. Or will you invite customers, media, and analysts from around the globe to your company's offices for the launch, as SAS did with its SAS 9 software product?

In addition to the announcement of the new product, the communication plan has to specify how ongoing customer communications will be conducted. The mechanisms used to gather customer feedback as well as how the offering will be promoted to customers need to be spelled out. For example, will you create an online community like Laura Carros did with the JCPenney Ambrielle line?

The discussion of the communication plan can be fairly broad. You can put additional details in a separate planning document that outlines the product's advertising strategies, event strategies (such as trade shows and special events like customer golf tournaments that will be used to promote the product), and sales strategies.

Distribution

This section should answer questions about where and how the offering will be sold. Who will sell it? Who will ship it? Who will service and support it? In addition, the distribution section should specify the inventories that need to be maintained in order to meet customer expectations for fast delivery and where those inventories should be kept

Budget

The budget section is more than just a discussion of the money needed to launch the new offering. A complete budget section will cover all the resources, such as new personnel, new equipment, new locations, and so forth, for the launch to be a success. Of course, these resources have costs associated with them. In some instances, the budget might require that existing resources be redeployed and a case made for doing so.

The first portion of the budget will likely cover the investment required for the launch. The plan might point out that additional funds need to be allocated to the offering to make it ready for the market. For example, perhaps additional beta testing or product development over and above what the firm normally commits to new products is needed. Certainly, marketing funds will be needed to launch the offering and pay for any special events, advertising, promotional materials, and so forth. Funds might also be needed to cover the costs of training salespeople and service personnel and potentially hiring new staff members. For example, Teradata introduced a new offering that was aimed at an entirely new market. The new market was so different that it required a new sales force. Details for the sales force, such as how many salespeople, sales managers, and support personnel will be needed, would go in this section.

The budget section should include the costs associated with maintaining the amount of inventory of the product to meet customers' needs. The costs to provide customers with support services should also be estimated and budgeted. Some products will be returned, some services will be rejected by the consumer, and other problems will occur. The budget should include projections and allowances for these occurrences.

The budget section is also the place to forecast the product's sales and profits. Even though the plan likely mentioned the sales goals set for each market segment, the budget section is where the details go. For example, the cost for advertising, trade shows, special events, and salespeople should be spelled out. The projections should also include timelines. The sales costs for one month might be estimated, as well as two months, six months, and so forth, as Figure 13.7 "A Marketing Plan Timeline Illustrating Market Potential, Sales, and Costs" shows.

Note that Figure 13.7 "A Marketing Plan Timeline Illustrating Market Potential, Sales, and Costs" shows that the product's costs are high early on and then decrease before leveling out. That cost line assumes there is a heavy upfront investment to launch the offering, which is usually true for new products. The sales of the offering should grow as it gathers momentum in the market. However, the market potential stays the same, assuming that the potential number of customers stays the same. That might not always be the case, though. If we were targeting mothers of babies, for example, the market potential might vary based on the projected seasonality in birth rates because more babies tend to be born in some months than others.



Figure 13.1.1: A Marketing Plan Timeline Illustrating Market Potential, Sales, and Costs

Conclusion

In the conclusion, repeat the highlights. Summarize the target market, the offer, and the communication plan. Your conclusion should remind the reader of all the reasons why your plan is the best choice.

Of course, the written plan is itself a marketing tool. You want it to convince someone to invest in your ideas, so you want to write it down on paper in a compelling way. Figure 13.8 “Tips for Writing an Effective Marketing Plan” offers some tips for effectively doing so. Also, keep in mind that a marketing plan is created at a single point in time. The market, though, is dynamic. A good marketing plan includes how the organization should respond to various scenarios if the market changes. In addition, the plan should include “triggers” detailing what should happen under the scenarios. For example, it might specify that when a certain percentage of market share is reached, then the price of the product will be reduced (or increased). Or the plan might specify the minimum amount of the product that must be sold by a certain point in time—say, six months after the product is launched—and what should happen if the mark isn’t reached. Also, it should once again be noted that the marketing plan is a communication device. For that reason, the outline of a marketing plan may look somewhat different from the order in which the tasks in the outline are actually completed.\

Tips for Writing an Effective Marketing Plan

- Be brief—executives are busy.
- Anticipate and answer questions your organization's executives might have.
- Use active (not passive) voice when you write your plan.
- Use visuals and bullet points. Some people are visual learners and others are verbal. Meet the needs of both types of people.
- Read, proofread, and have someone else proofread the plan.
-

? Review

- A marketing plan’s executive summary should include a brief summary of the market, the product to be offered, the strategy behind the plan, and the budget, as well as any other important information.
- In this section of the plan, the planner describes the offering and a brief rationale for why the company should invest in it.
- The market section of the plan should describe a firm’s customers, competitors, any other organizations with which it will collaborate, and the climate of the market.
- The strategy section details the tactics the organization will use to develop, market, and sell the offering.
- When readers complete the strategy section, they should conclude that the proposed strategy is the best one available.
- The budget section of the marketing plan covers all the resources, such as new personnel, new equipment, new locations, and so forth, needed to successfully launch the product, as well as details about the product’s costs and sales forecasts.

Source

Section 13.1 Marketing Plan Basics is adapted from the chapter ‘Chapter 13: The Marketing Plan’ from the textbook ‘Principles of Marketing,’ authored by University of Minnesota Libraries Publishing edition, 2015 – this book was adapted from a work originally produced in 2010 by a publisher who has requested that it not receive attribution.

The following changes were made to the most recent edition: Combined Sections ‘The Marketing Plan’ and ‘Marketing Planning Roles’ were combined into one section titled ‘Section 13.1 The Marketing Plan’; Created new title for Figure 13.1: Marketing plans at the division level; Created new title for Figure 13.3: Convincing stakeholders; Created new title for Figure 13.4: Customer segments; Created new title for Figure 13.5: The economic climate; Created new title for Figure 13.6: Service support; Created new title for Figure 13.9: Market dynamics; Created new title for Figure 13.10: Test markets; Added learning objectives.

This page titled 13.1: Marketing Plan Basics is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

13.2: Writing the International Marketing Plan

Learning Objectives

After reading this section, students should be able to …

- outine the decision sequence in international marketing
- explain how the marketing mix elements are integrated in the international marketing plan

The International marketing plan

It should be apparent by now that companies and organizations planning to compete effectively in world markets need a clear and well-focused international marketing plan that is based on a thorough understanding of the markets in which the company is introducing its products. The challenge, then, of international marketing is to ensure that any international strategy has the discipline of thorough research, and an understanding and accurate evaluation of what is required to achieve the competitive advantage. As such, the decision sequence in international marketing is much larger than that of domestic markets. As noted in the next “Integrated marketing”, it is also more complicated.

Copy and Paste
Image here.
Delete this
placeholder image

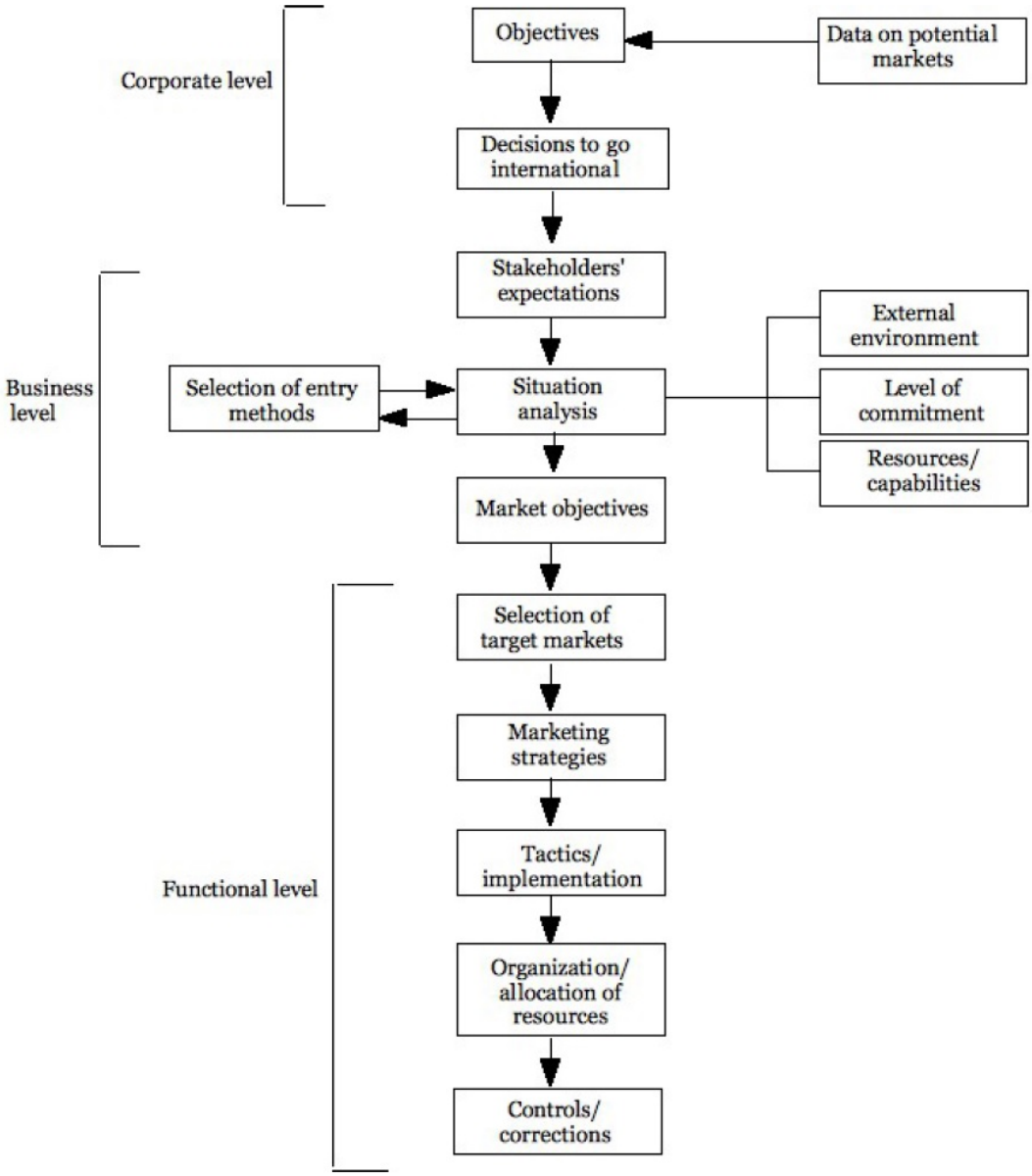


Figure 13.2.1: The decision sequence in international marketing

The corporate level

We begin at the corporate level, where firms decide whether to become involved in international markets and determine the resources they are willing to commit. Thus, this stage is primarily concerned with the analysis of international markets. Decisions here will be dependent on matching the results of that analysis with the company's objectives. These objectives, in turn, will be

determined by the many motivating factors we have discussed in the earlier sections. The level of resources that the company is willing to commit should be determined by the strategy that is needed to achieve the objectives that have been set.

The business level

Business-level considerations begin with the assessment of the stakeholders involved in the business. It is important to clearly identify the different stakeholder groups, understand their expectations, and evaluate their power, because the stakeholders provide the broad guidelines within which the firm operates. In the case of international marketing, it is particularly important to address the concerns of the stakeholders in the host company.

The situation analysis concerns a thorough examination of the factors that influence the businesses' ability to successfully market a product or service. The results lead to a realistic set of objectives. Conducting a situation analysis in an international setting is a bit more extensive. It not only includes the normal assessment of *external environmental* factors and *resources /capabilities*, it also includes a determination of the *level of commitment* exhibited by the business, as well as possible methods of entry. These last two factors are interrelated in that a company's level of commitment to international markets will directly influence whether they employ exporting, a joint venture, or some other method of entry.

In turn, level of commitment and method of entry are influenced by the evaluation of environmental factors as well as resources and capabilities. The latter audits not only the weaknesses of the company, but also the strengths of the company, which are often taken for granted. This is particularly important in international markets; for example, customer brand loyalty may be much stronger in certain markets than others, and products may be at the end of their life in the domestic market but may be ideal for less sophisticated markets. It is important, too, to evaluate the capacity of the firm to be flexible, adaptable, and proactive, as these are the attributes necessary, for success in a highly competitive and rapidly changing world.

Undoubtedly, environmental factors have received the most attention from marketers considering international markets.

? Integrated Marketing

Going Global takes Coordination

Importing technology and the evolution of a global economy has made global marketing a reality for many American companies. Larger corporations are not alone in their pursuit of business abroad: the US Department of Commerce reports that 60 per cent of American firms exporting products today have fewer than 100 employees. American businesses have plenty of reasons to market their products in other countries. According to consulting firm Deloitte and Touche, about 95 per cent of the world's population and two-thirds of its total purchasing power are currently located outside the US.

Moreover, the decision to distribute products in other countries not only opens new markets, but can also greatly expand a company's business. For example, if a US bicycle manufacturer focuses only on the US market, it loses the opportunity to increase revenues in countries where bicycles are a primary mode of transportation. Global marketing can also breathe life into a foundering product, and may even extend its lifespan. Additionally, a foreign product often can command a higher price simply because consumers around the world expect foreign items to cost more.

However, implementing a global strategy requires a great deal of coordination. For example, many companies that have successfully built a strong brand in the US have found that their domestic identity has little, if any, impact in markets where they are relatively unknown. An advertising campaign is one way to deal with this problem. Attaching your corporate identity to a known, respected entity in your target market is another. When FedEx, for example, wanted to increase its name recognition in Europe, the company teamed with clothing manufacturer Benetton, an established name there. FedEx sponsors one of Benetton's formula racing cars in Europe.

Karen Rogers, manager of key customer marketing at FedEx, added that sponsoring events domestically or internationally also gives a company the opportunity to meet with perspective customers in a social setting and affords a series of spin-offs, such as promotions and product giveaways.

In distributing products globally, many American corporations team with large multinational companies that do not offer competitive products but have the resources and expertise to distribute and market those goods. This can be a cost-effective alternative to setting up operations outside the US.

> Many small and mid-sized companies that are uncertain whether to open operations in another country investigate the possibility of using an export management company. These companies typically provide services that range from research to negotiating contracts with overseas distributors.(21)

The functional level

Having set the objectives for the company, both at the corporate level and the business level, the company can now develop a detailed program of functional activities to achieve the objectives. Following the integrated approach employed throughout this text, each of the functional elements (e.g. finance, human resources, research) must be considered jointly. The best international marketing strategy is doomed to failure if human resources can not find and train the appropriate employees, or research cannot modify the product so that it is acceptable to consumers in another country. Ultimately, this coordination between business functions is contingent on the market entry strategy employed as well as the degree of standardization or customization deemed.

Having integrated at the function level, we next consider integration of the marketing mix elements.

Product/promotion

Keegan (11) has highlighted the key aspect of marketing strategy as a combination of standardization or adaptation of product and promotion elements of the mix and offers five alternative and more specific approaches to product policy:

- One product, one message, worldwide. While a number of writers have argued that this will be the strategy adopted for many products in the future, in practice only a handful of products might claim to have achieved this already.
- Product extension, promotion adaptation. While the product stays the same this strategy allows for the adaptation of the promotional effort either to target new customer segments or to appeal to the particular tastes of individual countries.
- Product adaptation, promotion extension. This strategy is used if a promotional campaign has achieved international appeal, but the product needs to be adapted because of local needs.
- Dual adaptation. By adapting both products and promotion for each market, the firm is adopting a totally differentiated approach.
- Product invention. Firms, usually from advanced nations, that are supplying products to less well-developed countries adopt product invention.

Another critical element that is closely aligned with the product and promotion is the brand. Anthony O'Reilly, Chairman of H J Heinz, believes that the communications revolution and the convergence of cultures have now set the stage for truly global marketing. The age of the global brand is at hand. For example, Heinz was looking to expand its 9 Lives cat food brand and Morris the Cat logo into Moscow. Although it is a stable and successful brand in the US, testing and research done by Dimitri Epimov, a local marketing manager in Moscow, led Heinz executives to make a marketing change to ensure the product's success in Russia. Namely, a fatter-looking Morris was created for packaging. Another discovery: while Americans tend to treat their kitties with tuna, Russian cat lovers prefer to serve beef-flavored food.

As discussed earlier, product positioning is a key success factor and reflects the customer's perceptions of the product or service. However, in countries at different stages of economic development, the customer segments that are likely to be able to purchase the product and the occasions on which it is bought may be significantly different.

For example, while Kentucky Fried Chicken (KFC) and McDonald's restaurants aim at everyday eating for the mass market in the developed countries, in less-developed countries they are perceived as places for special-occasion eating, and are beyond the reach of the poorest segments of the population. The product positioning, therefore, must vary in some dimensions. In confirming the positioning of a product or service in a specific market or region, it is therefore necessary to establish in the consumer perception exactly what the product stands for and how it differs from existing and potential competition by designing an identity that confirms the value of the product.

Pricing

Pricing products in foreign nations is complicated by exchange rate fluctuations, tariffs, governmental intervention, and shipping requirements. A common strategy involves a marketer setting a lower price for their products in foreign markets. This strategy is consistent with the low income levels of many foreign countries, and the lower price helps to build market share. Pricing strategies are also strongly influenced by the nature and intensity of the competition in the various markets.

For these reasons, it is important to recognize at the outset that the development and implementation of pricing strategies in international markets should follow the following stages:

1. Analyzing the factors that influence international pricing, such as the cost structures, the value of the product, the market structure, competitor pricing levels, and a variety of environmental constraints.
2. Confirming the impact the corporate strategies should have on pricing policy.
3. Evaluating the various strategic pricing options and selecting the most appropriate approach.
4. Implementing the strategy through the use of a variety of tactics and procedures to set price.
5. Managing prices and financing international transactions.

Perhaps the most critical factor to be considered when developing a pricing strategy in international markets, however, is how the customers and competitors will respond. Nagle (12) has suggested nine factors that influence the sensitivity of customers to prices, and all have implications for the international marketer. Price sensitivity reduces:

The more distinctive the product is;

- the greater the perceived quality;
- the less aware consumers are of substitutes in the market;
- if it is difficult to make comparisons;
- if the price of a product represents a small proportion of total expenditure of the customer;
- as the perceived benefit increases;
- if the product is used in association with a product bought previously;
- if costs are shared with other parties;
- if the product cannot be stored.

Finally, there are several inherent problems associated with pricing in international markets. Often companies find it difficult to coordinate and control prices across their activities in order to enable them to achieve effective financial performance and their desired price positioning. Simply, how can prices be coordinated by the company across the various markets and still make the necessary profit? Difficulty answering this question has led to two serious problems.

Dumping (when a firm sells a product in a foreign country below its domestic price or below its actual costs) is often done to build a company's share of the market by pricing at a competitive level. Another reason is that the products being sold may be surplus or cannot be sold domestically and are therefore already a burden to the company. When companies price their products very high in some countries but competitively in others, they engage in a gray market strategy.

A *gray market*, also called *parallel importing*, is a situation where products are sold through unauthorized channels of distribution. A gray market comes about when individuals buy products in a lower-priced country from a manufacturer's authorized retailer, ship them to higher-priced countries,and then sell them below the manufacturer's suggested price through unauthorized retailers.

Considerable problems arise in foreign transactions because of the need to buy and sell products in different currencies. Questions to consider are: What currency should a company price its products? How should a company deal with fluctuating exchange rates?

Finally, obtaining payment promptly and in a suitable currency from less developed countries can cause expense and additional difficulties. How should a company deal with selling to countries where there is a risk of nonpayment? How should a company approach selling to countries that have a shortage of hard currency?

Distribution and logistics

Distribution channels are the means by which goods are distributed from the manufacturer to the end user. *Logistics*, or physical distribution management, is concerned with the planning, implementing, and control of physical flows of materials and final goods from points of origin to points of use to meet customer needs at a profit.

Essentially there are three channel links between the seller and buyer. The first link is the seller's headquarters organization, which is responsible for supervising the channel, and acts as part of the channel itself. Channels between countries represent the second link. They are responsible for getting products to overseas markets and payment in return. Finally, the third link is the channel structure (logistics) within countries, which distributes the products from their point of entry to the final consumer.

Distribution strategies within overseas markets are affected by various uncontrollable factors. First, wholesaling and retailing structure differs widely from one nation to the next. So, too, does the quality of service provided. Differences in the size and nature of retailers are even more pronounced. Retailers more closely reflect the economic conditions and culture of that country; many small retailers dominate most of these countries. Physical distribution to overseas markets often requires special marketing planning. Many countries have inadequate docking facilities, limited highways, various railroad track gauges, too few vehicles, and too few warehouses. Managing product inventories requires consideration of the availability of suitable warehousing, as well as the costs of shipping in small quantities.

? Review

1. The international marketing plan includes concern for:
   a. corporate level considerations-determining the resources to be allocated
   b. business level considerations, including:
   i. assessment of stakeholders
   ii. the situation analysis
   c. functional level considerations that delineate the various activities that will achieve objectives

Source

Section 13.2 Writing the International Marketing Plan is adapted from the chapter ‘Chapter 2 Marketing in global markets’ from the textbook ‘Introducing Marketing, First Edition, 2011’ authored by John Burnett – this book was published under The Global Text Project, funded by the Jacobs Foundation, Zurich, Switzerland.

The following changes were made to the most recent edition: Divided ‘Chapter 2: Marketing in Global Markets’ into three sections; Removed Case application Unilever’s global brand at end of Chapter 2; Added learning objectives.

This page titled 13.2: Writing the International Marketing Plan is shared under a CC BY-NC-SA 4.0 license and was authored, remixed, and/or curated by Babu John-Mariadoss via source content that was edited to the style and standards of the LibreTexts platform.

Index

D

dire

https://biz.libretexts.org/@go/page/84736

Glossary

Sample Word 1 | Sample Definition 1

Detailed Licensing

Overview

Title: Core Principles of International Marketing (Mariadoss)

Webpages: 110

Applicable Restrictions: Noncommercial

All licenses found:

- CC BY-NC-SA 4.0: 93.6% (103 pages)
- Undeclared: 6.4% (7 pages)

By Page

- Core Principles of International Marketing (Mariadoss) - *CC BY-NC-SA 4.0*
  - Front Matter - *CC BY-NC-SA 4.0*
    - TitlePage - *Undeclared*
    - InfoPage - *CC BY-NC-SA 4.0*
    - Table of Contents - *Undeclared*
    - Acknowledgements - *Undeclared*
    - Licensing - *Undeclared*
    - Dedication - *Undeclared*
    - Introduction - *Undeclared*
  - 1: Introduction to International Marketing - *CC BY-NC-SA 4.0*
    - 1.1: Introduction to International Marketing Summary - *CC BY-NC-SA 4.0*
    - 1.2: Defining Marketing - *CC BY-NC-SA 4.0*
    - 1.3: Defining International Marketing - *CC BY-NC-SA 4.0*
    - 1.4: The Motivation for International Marketing - *CC BY-NC-SA 4.0*
    - 1.5: Stages in International Marketing - *CC BY-NC-SA 4.0*
    - 1.6: Why International Marketing Matters - *CC BY-NC-SA 4.0*
    - 1.7: Challenges of Global Marketing - *CC BY-NC-SA 4.0*
    - 1.8: What is Globalization - *CC BY-NC-SA 4.0*
    - 1.9: The Globalization Debate - *CC BY-NC-SA 4.0*
    - 1.10: Standardization and Customization - *CC BY-NC-SA 4.0*
  - 2: International Business and Trade - *CC BY-NC-SA 4.0*
    - 2.1: International Business and Trade Summary - *CC BY-NC-SA 4.0*
    - 2.2: International Trade - *CC BY-NC-SA 4.0*
    - 2.3: International Economic Cooperation among Nations - *CC BY-NC-SA 4.0*
    - 2.4: Understanding Tariffs - *CC BY-NC-SA 4.0*
    - 2.5: Regional Economic Integration - *CC BY-NC-SA 4.0*
    - 2.6: The United Nations and the Impact on Trade - *CC BY-NC-SA 4.0*
    - 2.7: Trade Controversies - *CC BY-NC-SA 4.0*
    - 2.8: Foreign Direct Investment - *CC BY-NC-SA 4.0*
  - 3: Social and Cultural Environment - *CC BY-NC-SA 4.0*
    - 3.1: Social and Cultural Environment Summary - *CC BY-NC-SA 4.0*
    - 3.2: Factors Shaping the Global Marketing Environment - *CC BY-NC-SA 4.0*
    - 3.3: The Social and Cultural Environment - *CC BY-NC-SA 4.0*
    - 3.4: Importance of Culture on Markets - *CC BY-NC-SA 4.0*
    - 3.5: What is Culture - *CC BY-NC-SA 4.0*
    - 3.6: Describing Culture - *CC BY-NC-SA 4.0*
    - 3.7: Marketing Across Cultures - *CC BY-NC-SA 4.0*
  - 4: The Economic and Political Environment - *CC BY-NC-SA 4.0*
    - 4.1: The Economic and Political Environment Summary - *CC BY-NC-SA 4.0*
    - 4.2: The Economic Environment - *CC BY-NC-SA 4.0*
    - 4.3: The Political Environment - *CC BY-NC-SA 4.0*
    - 4.4: Political Risk - *CC BY-NC-SA 4.0*
    - 4.5: Legal Risk - *CC BY-NC-SA 4.0*
  - 5: Economic Development in the World - *CC BY-NC-SA 4.0*
    - 5.1: Chapter 5- Economic Development in the World - *CC BY-NC-SA 4.0*
    - 5.2: World Economies - *CC BY-NC-SA 4.0*
    - 5.3: Classifying World Economies - *CC BY-NC-SA 4.0*

- 5.4: Understanding the Developed World - *CC BY-NC-SA 4.0*
- 5.5: The Developing World - *CC BY-NC-SA 4.0*
- 5.6: Emerging Markets - *CC BY-NC-SA 4.0*

- 6: Global Market Planning - *CC BY-NC-SA 4.0*
  - 6.1: Global Market Planning Summary - *CC BY-NC-SA 4.0*
  - 6.2: Measuring Market Attractiveness - *CC BY-NC-SA 4.0*
  - 6.3: Global Market Opportunity Assessment – PESTEL Analysis - *CC BY-NC-SA 4.0*
  - 6.4: Global Market Opportunity Assessment – CAGE Analysis - *CC BY-NC-SA 4.0*
  - 6.5: Global Market Opportunity Assessment – Scenario Planning and Analysis - *CC BY-NC-SA 4.0*
  - 6.6: Selecting the Countries to Enter - *CC BY-NC-SA 4.0*
  - 6.7: Global Market Segmentation - *CC BY-NC-SA 4.0*
  - 6.8: Using Demographics to Guide Global Marketing Strategy - *CC BY-NC-SA 4.0*
  - 6.9: Target Market Selection - *CC BY-NC-SA 4.0*
  - 6.10: Global Positioning - *CC BY-NC-SA 4.0*
  - 6.11: Basics of Positioning - *CC BY-NC-SA 4.0*
- 7: Global Market Entry Modes - *CC BY-NC-SA 4.0*
  - 7.1: Global Market Entry Modes Summary - *CC BY-NC-SA 4.0*
  - 7.2: International Entry Modes - *CC BY-NC-SA 4.0*
  - 7.3: 7.02- Exporting - *CC BY-NC-SA 4.0*
  - 7.4: Licensing - *CC BY-NC-SA 4.0*
  - 7.5: Franchising - *CC BY-NC-SA 4.0*
  - 7.6: Contract Manufacturing - *CC BY-NC-SA 4.0*
  - 7.7: Joint Ventures - *CC BY-NC-SA 4.0*
- 8: Global Products - *CC BY-NC-SA 4.0*
  - 8.1: Global Products Summary - *CC BY-NC-SA 4.0*
  - 8.2: Global Product Development - *CC BY-NC-SA 4.0*
  - 8.3: Global Products and Services - *CC BY-NC-SA 4.0*
  - 8.4: Product Adaptation Decisions - *CC BY-NC-SA 4.0*
  - 8.5: Global Innovation - *CC BY-NC-SA 4.0*
  - 8.6: Global Innovation at the BOP - *CC BY-NC-SA 4.0*
- 9: Global Branding - *CC BY-NC-SA 4.0*
  - 9.1: Global Branding Summary - *CC BY-NC-SA 4.0*
  - 9.2: Formulating a Global Brand Strategy - *CC BY-NC-SA 4.0*
  - 9.3: Global Branding - *CC BY-NC-SA 4.0*
  - 9.4: Global Brand Structures - *CC BY-NC-SA 4.0*
  - 9.5: Determinants of Global Brand Structure - *CC BY-NC-SA 4.0*
  - 9.6: Managing Key Strategic Brands - *CC BY-NC-SA 4.0*
- 10: Global Channels and Supply Chains - *CC BY-NC-SA 4.0*
  - 10.1: Global Channels and Supply Chains Summary - *CC BY-NC-SA 4.0*
  - 10.2: Basics of Distribution Channels - *CC BY-NC-SA 4.0*
  - 10.3: Global Supply Chains - *CC BY-NC-SA 4.0*
  - 10.4: Global Sourcing and Distribution - *CC BY-NC-SA 4.0*
  - 10.5: Organizing The Channel - *CC BY-NC-SA 4.0*
- 11: Global Promotions - *CC BY-NC-SA 4.0*
  - 11.1: Global Promotions Summary - *CC BY-NC-SA 4.0*
  - 11.2: Changes in Promotion - *CC BY-NC-SA 4.0*
  - 11.3: Global Communication Platform - *CC BY-NC-SA 4.0*
  - 11.4: Global Communication Strategies - *CC BY-NC-SA 4.0*
- 12: Global Pricing - *CC BY-NC-SA 4.0*
  - 12.1: Global Pricing Summary - *CC BY-NC-SA 4.0*
  - 12.2: Basics of Pricing - *CC BY-NC-SA 4.0*
  - 12.3: Introduction to Global Pricing - *CC BY-NC-SA 4.0*
  - 12.4: Global Pricing Approaches - *CC BY-NC-SA 4.0*
  - 12.5: Currency Fluctuations and Global Pricing - *CC BY-NC-SA 4.0*
  - 12.6: Tariffs and Global Pricing - *CC BY-NC-SA 4.0*
  - 12.7: Quotas and Dumping - *CC BY-NC-SA 4.0*
- 13: The International Marketing Plan - *CC BY-NC-SA 4.0*
  - 13.1: Marketing Plan Basics - *CC BY-NC-SA 4.0*
  - 13.2: Writing the International Marketing Plan - *CC BY-NC-SA 4.0*
- Back Matter - *CC BY-NC-SA 4.0*
  - Index - *CC BY-NC-SA 4.0*
  - Glossary - *CC BY-NC-SA 4.0*
  - Detailed Licensing - *Undeclared*