4th edition

# INTERNATIONAL BUSINESS

ODED SHENKAR, YADONG LUO AND TAILAN CHI



## Contents

## List of Exhibits

1	International Business in an Age of Globalization	1
	OPENING CASE: THE COCA-COLA COMPANY 2	
	An Age of Globalization 3	
	What Does Globalization Mean to You? 4	
	The Face of Globalization 5	
	Who Benefits from Globalization? 6	
	The Impact of Globalization 9	
	Globalization in Transition 14	
	Globalization and International Business 16	
	What is International Business? 16	
	International versus Domestic Business 18	
	Industry/Country Box: Sinostone Comes to Elberton 19	
	Why Expand Internationally? 20	
	The Structure of this Book 22	
	Pedagogical Thrust 23	
Pa	art I Concepts and Theories in International Business	27
2	International Trade Theory and Application	29
	Opening Case: Banana Wars 29	
	International Trade Theories 30	
	The Mercantilist Doctrine 31	
	Absolute Advantage Theory 32	
	Comparative Advantage Theory 32	
	Heckscher-Ohlin Theorem 34	
	The Leontief Paradox 36	
	Human Skills and Technology-Based Views 36	
	The Product Life-Cycle Model 38	
	Infant Industry Argument 40	

Linder's Income-Preference Similarity Theory 42

The New Trade Theory 43

XX

INDUSTRY BOX: THE GLOBAL AUTOMOTIVE INDUSTRY 4	15
Theory Assessment 45	

International Trade Patterns 49

International Trade Volume and Growth 49

Service Trade 50

Trade Measurement 53

Major Exporters and Importers 55

US Trade Partners 56

Trade Balance 60

Arguments for Trade Restrictions 62

The Sovereignty Argument 63

The Lowest Common Denominator Argument 64

Trade Reciprocity and Retaliation against Unfair Trade Practices 64 Optimal Tariff Theory 65

Types of Trade Barriers 66

Tariff Barriers 67

Non-Tariff Barriers 69

COUNTRY BOX: US TRADE POLICIES UNDER THE TRUMP ADMINISTRATION AND TRADE WAR WITH CHINA 75

Anti-Globalization Backlash and Intensification of Trade Conflicts 78

85

## **3** Foreign Direct Investment Theory and Application

OPENING CASE: JAPAN CHANGES ITS MIND ABOUT FDI, BUT NEEDS TO DO MORE TO ATTRACT IT 85

Definition and Types of Foreign Direct Investment 87 FDI versus Foreign Portfolio Investment 88 Types of FDI 88 Entry Mode 89 The Strategic Logic of FDI 89 How the MNE Benefits from Foreign Direct Investment 90 Enhancing Efficiency from Location Advantages 90 Improving Performance from Structural Discrepancies 91 Increasing Return from Ownership Advantages 91 Ensuring Growth from Organizational Learning 92 The Impact of FDI on the Host (Destination) and Home (Origin) Countries 93 Employment 93 FDI Impact on Domestic Enterprises in the Host Country 94 Current Theories on FDI 96 Product Life-Cycle Theory 96 Monopolistic Advantage Theory 97

Internalization Theory and other Transaction Cost-Based Theories 98 The Eclectic Paradigm 100 Learning and Capability-Based Perspectives 102 The Dynamic Capability Perspective 102 The Evolutionary Perspective 103 INDUSTRY BOX: MNES AND FDI IN THE AUTOMOTIVE INDUSTRY 105 The Real Option Perspective 106 The Integration-Responsiveness Perspective 107 Patterns of FDI 109 Outward FDI 112 Inward FDI 117 FDI Entry Forms 120 The Investment Environment 123 FDI Decision Criteria 124

COUNTRY BOX: FDI IN ISRAEL 125

## **4** The Multinational Enterprise

**OPENING CASE: JOHNSON & JOHNSON 131** What is a Multinational Enterprise? 132 The Degree of Internationalization 133 History of the MNE 134 The World's Largest MNEs 135 The Growth of Service MNEs 138 The Image of the MNE 141 The MNE in the Public Eye 141 The Borderless Corporation: Myth or Reality? 143 The Competitive Advantage of the MNE 144 Capabilities and Competitive Advantage 144 The MNE from Emerging/Developing Economies (DMNE) 147 The Largest Developing Country MNEs 148 Obstacles Facing MNEs from Developing Economies 150 DMNE Advantage in Global Markets 152 Typical Features of DMNEs 152 COUNTRY BOX: AN ISRAELI FIRM BECOMES THE WORLD'S LARGEST GENERIC DRUG MAKER 155 The Small and Medium-Sized International Enterprise (SMIE) 156 What is an SMIE? 157 **Obstacles to SMIE Internationalization** 158 SMIE Advantages in Internationalization 161 SMIE Internationalization Features 161 INDUSTRY BOX: INVESTMENT MANAGEMENT AND THE SMIE 167

Pa	rt II Endowments and Environments of	
International Business		173
5	Country Competitiveness	175
	Opening Case: Singapore's Changing Competitive Advantage in	
	the Hard Disk Drive Industry 175	
	Defining Country Competitiveness 177	
	Country Competitiveness and MNEs 178	
	Country-Level Determinants 180	
	Institutional System 180	
	Infrastructure 183	
	Macroeconomic Soundness 184	
	Science, Education, and Innovation 187	
	Internationalization 190	
	Industry-Level Determinants 191	
	INDUSTRY BOX: E-COMMERCE AS AN ELEMENT OF COUNTRY COMPETITIVENESS 195	
	Firm-Level Determinants 196	
	Individual-Level Determinants 198	
	COUNTRY BOX: ITALY: OWNER SNEAKS FACTORY TO POLAND 200	
	Interplay of the Four-Level Determinants 201	
	Government Role 202	
	A Historical Review 202	
	A Renewed Recognition of Government Role 203	
	Industrial Policy 205	

## 6 The Cultural Environment

OPENNG CASE: REMAULT-NISSAN ALLIANCE 211 What is Culture? 213 Culture and International Business 213 Culture Does Not Explain Everything 214 Correlates of Culture 215 National Culture Classifications 219 Hofstede's Dimensions of Culture 222 COUNTRY BOX: TOYOTA—A SHIFT IN TOYOTA'S CORPORATE CULTURE 224 Schwartz's Classification 228 The GLOBE Classification 229 Trompenaars and Hampden-Turner's Classification 229 Other Dimensions of Culture 231 National Culture Clustering 232 Subsistence and Rice Theories 232 Measuring Cultural Differences 234

The Positive Role of Cultural Differences 235 The Friction Framework 235 Corporate Culture 236 Other Layers of Culture 237 *Ethnicity 237 Industry 237 Ideology 237 Demographics 238 Cultural Etiquette 238 Cultural Stereotypes 238 Convergence and Divergence 239 INDUSTRY BOX: ISLAMIC FINANCE 242* 

## 7 The Political and Legal Environment

OPENING CASE: BOLIVIA NATIONALIZES NATURAL GAS 249

The Political Environment 251
Political System 252
The Institutional Context 256
Geopolitics and International Business Environment 257
The MNE–Government Relationship 259
The MNE Relationship with the Host Government 259
The MNE and its Home Government 262
Coalition Building and Influence Tactics 263
INDUSTRY BOX: MANAGING POLITICS IN THE AUTOMOTIVE INDUSTRY 264
Economic Freedom 264
Political Risk 266
Regional-Level Politics 270
Micro-Region Political Processes 270
The Legal Environment 271
The Institutional Context 271
Country Box: Indonesia: Manufacturers Life Weathers the Storm in Indonesia 274
Legal Jurisdiction 274
Legal Issues of Interest to the MNE 276

## Part IIIGlobal Markets and Institutions285

8	<b>International Economic</b>	Integration and Institutions	287
---	-------------------------------	------------------------------	-----

OPENING CASE: 3M'S RESPONSE TO EUROPEAN MARKET INTEGRATION 288 International Economic Integration 288 Global-Level Cooperation Among Nations 291

The World Trade Organization (WTO) 292 COUNTRY BOX: RUSSIA JOINS THE WTO 296 The International Monetary Fund (IMF) 297 The World Bank Group 298 Other International Economic Organizations 300 Regional-Level Cooperation Among Nations 302 Postwar Regional Integration 302 North America: The US-Mexico-Canada Agreement (USMCA), Formerly North American Free Trade Agreement (NAFTA) 305 Europe: The European Union (EU) 307 INDUSTRY BOX: SIEMENS SHARPENS ITS FOCUS TO RESPOND TO THE SINGLE MARKET 311 Asia Pacific 311 Latin America 315 Africa and the Middle East 316 Efficiency-Enhancing and Efficiency-Reducing Effects of Regionalization 318 Commodity-Level Cooperation Among Nations 320 Organization of Petroleum Exporting Countries (OPEC) 320 Other Commodity Agreements 323 Strategic Responses of MNEs 323

#### 9 The International Monetary System and Financial Markets 329

OPENING CASE: FOREIGN EXCHANGE CRISIS IN MEXICO 329

History of the International Monetary System 330 The Gold Standard Period (1876–1914) 332 The Inter-War Years and World War II (1914–1944) 332 The Bretton Woods System (1944–1973) 332 The Post-Bretton Woods System (1973–Present) 333 Contemporary Exchange Rate Systems 338 Fixed-Rate System 338 Crawling Peg System 339 COUNTRY BOX: HONG KONG: SHOULD THE HONG KONG DOLLAR RETAIN THE FIXED PEG TO THE US DOLLAR? 340 Target-Zone Arrangement 341 Managed Float System 342 Independent Float System 342 Advantages and Disadvantages of the Floating System 342 Determination of Foreign Exchange Rates 344 Foreign Exchange Rate Quotations 345 Gold Standard 346 Purchasing Power Parity (PPP) 347

379

Interest Rate Parity (IRP) 348
Foreign Exchange Rate Overshooting 349
Implications for MNEs: Foreign Exchange Forecasting 351
The Balance of Payments 353
BOP Accounts 353
Exchange Rates and BOP Imbalances 356
International Foreign Exchange Markets 359
Landscape of the International Foreign Exchange Market 359
Market Participants and Functions 360
Transaction Forms 360
Foreign Exchange Arbitrage 362
Black Market and Parallel Market 363
International Capital Markets 364
International Money Markets 364
International Bond Markets 365
INDUSTRY BOX: US FIRMS FIND CHEAPER FINANCING FROM FOREIGN SOURCES 365
International Stock Markets 366
International Loan Markets 367
Major International Financial Crises in Recent Times 369
The Asian Financial Crisis 369
The Global Financial Crisis 372

## Part IV International Business Strategies

10	International Entry Strategies
	OPENING CASE: DUPONT'S ENTRY STRATEGIES INTO CHINA 379
	Dimensions of a Market Entry Strategy 380
	International Location Selection (Where) 382
	Locational Determinants 383
	Country Box: Federal Express Shifts its Hub from Subic Bay to Guangzhou, China 390
	Decision Framework 390
	Timing of Entry (When) 393
	Uncertainty and Potential for Learning 393
	Competitive Preemption and Pioneering Costs 394
	Decision Framework 398
	Entry Mode Selection (How) 400
	Entry Mode Choices 400
	Trade-Centered Entry Modes 401
	Transfer-Centered Entry Modes 405

FDI-Centered Entry Modes 408 Decision Framework 413 Greenfield Investment, Acquisition, and Merger 415 INDUSTRY BOX: UNILEVER'S ACQUISITIONS IN LATIN AMERICA 417 The Evolutionary Path 417

423

## 11 MNE Organization Structure and Design

OPENING CASE: PROCTER & GAMBLE: WORLDWIDE STRUCTURE 423 International Strategy and Organization Design 424 Global Integration and Local Responsiveness 425 MNE Strategy and Design 426 Subsidiary Roles and Imperatives 427 MNE Organizational Structures 429 The National Subsidiary Structure 429 The International Division Structure 430 The Global Functional Structure 430 The Global Geographic Structure 431 COUNTRY BOX: INTERNATIONALIZING THE BOARD OF DIRECTORS 434 The Global Product Structure 436 INDUSTRY BOX: "FORD 2000" 438 The Global Matrix Structure 439 Integrating Global Operations 445 Tools for Global Integration 446 The Transition Challenge 447 The Corporate Headquarters 449

#### 12 Building and Managing Global Strategic Alliances (GSAs) 453

**OPENING CASE:** THE FORD-VOLKSWAGEN ALLIANCE 454 Defining Global Strategic Alliances 454 Types of GSAs 454 Rationales for Building GSAs 456 Challenges Facing GSAs 458 Building Global Strategic Alliances 461 Selecting Local Partners 461 Negotiating Alliance Contracts 465 Structuring Global Strategic Alliances 466 COUNTRY BOX: FUJITSU IN SPAIN: BARRIERS TO ALLIANCE MANAGEMENT 468 Managing Global Strategic Alliances 469 Managing Inter-Partner Learning 470 Exercising Managerial Control 471

Heightening Cooperation 474 Thinking Ahead of Exit 476 INDUSTRY BOX: WISDOM GAINED FROM EXPERIENCE IN BUILDING GSAs 478

13	Managing Global Research and Development (R&D)	483
	OPENING CASE: INTEL'S R&D NETWORK IN DEVELOPING COUNTRIES 483	
	Why Globalize R&D? 484	
	Benefits and Challenges of Global R&D 487	
	COUNTRY BOX: INDIA: R&D CENTERS OF GLOBAL COMPANIES IN INDIA 490	
	Designing and Structuring Global R&D 491	
	Types of Foreign R&D Units 491	
	Selecting R&D Location 493	
	INDUSTRY BOX: FORD LOCATES ITS R&D CENTER IN AACHEN, GERMANY 495	
	Structuring Global R&D Activities 495	
	Managing and Operating Global R&D 499	
	Human Resource Management 499	
	Autonomy Setting 499	
	Global Planning 500	
	Communication Improvement 501	
	Technology Transfer across Borders 503	
Pa	rt V Functional International Rusiness Areas	509
Pa	rt V Functional International Business Areas	509
	rt V Functional International Business Areas Financial Management for Global Operations	509 511
	Financial Management for Global Operations	
	<b>Financial Management for Global Operations</b> <i>Opening Case: Minimizing Exposure in RTZ</i> 511	
	<b>Financial Management for Global Operations</b> <i>OPENING CASE: MINIMIZING EXPOSURE IN RTZ</i> 511 Why Learn Financial Management? 512	
	<b>Financial Management for Global Operations</b> <i>OPENING CASE: MINIMIZING EXPOSURE IN RTZ</i> 511 Why Learn Financial Management? 512 International Trade Finance 514	
	<b>Financial Management for Global Operations</b> <i>OPENING CASE: MINIMIZING EXPOSURE IN RTZ</i> 511 Why Learn Financial Management? 512 International Trade Finance 514 <i>International Trade Payment 514</i>	
	<b>Financial Management for Global Operations</b> <i>OPENING CASE: MINIMIZING EXPOSURE IN RTZ</i> 511 Why Learn Financial Management? 512 International Trade Finance 514 <i>International Trade Payment 514</i> <i>Export Financing 519</i>	
	<b>Financial Management for Global Operations</b> <i>OPENING CASE: MINIMIZING EXPOSURE IN RTZ</i> 511 Why Learn Financial Management? 512 International Trade Finance 514 <i>International Trade Payment 514</i> <i>Export Financing 519</i> Financing for Global Business 523	
	<b>Financial Management for Global Operations</b> <i>OPENING CASE: MINIMIZING EXPOSURE IN RTZ</i> 511 Why Learn Financial Management? 512 International Trade Finance 514 <i>International Trade Payment 514</i> <i>Export Financing 519</i> Financing for Global Business 523 <i>Intercompany Financing 524</i>	
	Financial Management for Global Operations OPENING CASE: MINIMIZING EXPOSURE IN RTZ 511 Why Learn Financial Management? 512 International Trade Finance 514 International Trade Payment 514 Export Financing 519 Financing for Global Business 523 Intercompany Financing 524 Equity Financing 524	
	Financial Management for Global Operations OPENING CASE: MINIMIZING EXPOSURE IN RTZ 511 Why Learn Financial Management? 512 International Trade Finance 514 International Trade Payment 514 Export Financing 519 Financing for Global Business 523 Intercompany Financing 524 Equity Financing 524 Debt Financing 525	
	<b>Financial Management for Global Operations</b> <i>OPENING CASE: MINIMIZING EXPOSURE IN RTZ</i> 511 Why Learn Financial Management? 512 International Trade Finance 514 <i>International Trade Payment 514</i> <i>Export Financing 519</i> Financing for Global Business 523 <i>Intercompany Financing 524</i> <i>Equity Financing 524</i> <i>Debt Financing 525</i> <i>Local Currency Financing 526</i>	

Foreign Exchange Risk and Exposure 528

Transaction and Economic Exposures 529

Managing Transaction Exposure 531

INDUSTRY BOX: NETTING IN PHILIPS 538 Global Coordination of Exposure Management 539 COUNTRY BOX: INDIA FACES DILEMMA ON FOREIGN EXCHANGE HEDGING 541 Working Capital Management 542 Cash Management 542 Foreign Receivable Management 543

## 15 International Accounting for Global Operations

**OPENING CASE: MULTINATIONALS FACE HEFTIER TAX FOR FOREIGN OPERATIONS 547** 

Country Differences in Accounting 548 Why Accounting Systems Differ Among Countries 548 INDUSTRY BOX: ACCOUNTING DIVERSITY IN SIEMENS 553 National Accounting Zones 553 International Accounting Harmonization 554 International Accounting Standards 557 COUNTRY BOX: AUSTRALIA: ACCOUNTING IN AUSTRALIA 559 Foreign Currency Translation 559 Commonly Used Translation Methods 561 Harmonization of Translation Methods 563 International Accounting Information Systems 564 Transfer Pricing and Taxation Strategies 566 Why Transfer Pricing? 566 Transfer Pricing Techniques 567 Transfer Pricing Regulations and Penalties 568 Tax Havens, Treaties, and Strategies 569 Tax Havens 570 Tax Treaties 571 Other Tax Strategies for MNEs 571

#### 16 Global Marketing and Supply Chain

OPENING CASE: DOMINO'S PIZZA 575 The International Marketing Challenge 576 Assessing Market Potential 578 The Luxury Market 581 Globalization and Localization in International Markets 581 Globalization Forces 582 Localization Forces 584 Product Adaptation 585 COUNTRY BOX: KIMCHI WARS 588 Country-of-Origin Effect 589

547

Branding 591 Channel Decisions 596 Promotion 598 Marketing Alliances 599 The Global Supply Chain 600 The Globalization of Supply Chains 602 Global Sourcing 603 Customizing the Supply Chain 603 Packaging 605 Transportation Modes 605 Crossing National Borders 609 INDUSTRY BOX: GLOBAL LOGISTICS AT WAL-MART 609

## 17 Global Human Resource Management

OPENING CASE: MANAGING GLOBAL HUMAN RESOURCES AT HSBC 619 Strategic IHRM 621 Staffing the MNE 623 The Globalization of Boards of Directors 623 INDUSTRY BOX: AIRLINE PILOTS GO GLOBAL 625 COUNTRY BOX: KOREAN COMPANIES SEEK GLOBAL TALENT 626 Staffing the MNE Ranks 626 Country-Specific Issues 629 The Expatriate Workforce 629 Types and Distribution of Expatriates 629 Using Expatriates: Pros and Cons 630 Expatriate Failure 631 Expatriate Selection 632 Preparing for a Foreign Assignment 633 Compensation 635 Culture and Compensation 641 Repatriation 642 HRM in International Affiliates 643 Human Resource Problems in Foreign Affiliates 643

## Part VI Emerging Issues in International Business 651

18	Digital Connectivity and Global Strategies	653
	OPENING CASE: IBM ACQUIRES RED HAT TO SHARPEN DIGITAL GLOBAL CONNECTIVITY	653
	Internet and Global E-Commerce 654	
	Digital Global Connectivity 655	

619

What Is Digital Global Connectivity? 655 New Forms of Digital Global Connectivity 657 INDUSTRY BOX: SIEMENS'S DIGITAL GLOBAL STRATEGY 659 How Digital Globalization Changes International Business 660 Intangible Commerce Booms 660 Knowledge Diffusion Grows 661 Digital Infrastructure Vitalizes 661 Mini-MNEs Rise 662 Global Consumers Shake Up 662 Emerging Economies Leapfrog 662 Global Business Ecosystems Thrive 663 Rewards and Risks of Digital Global Connectivity 664 Rewards from Digital Global Connectivity 664 Risks from Digital Global Connectivity 666 Assessing Digital Infrastructure 669 Physical Digital Infrastructure 669 Science, Education, and Innovation in Digitization 669 COUNTRY BOX: DIGITAL INFRASTRUCTURE IN THE PHILIPPINES AND MALAYSIA 671 Institutional and Regulatory Environment of Digitalization 672 Building Digital Global Connectivity Capabilities 674 Global Business Platforms 677 INDUSTRY BOX: EQUINIX AS A GLOBAL PLATFORM 679

## 19 Global Sustainability and Social Responsibility

683

**OPENING CASE: SHELL'S BRENT SPAR PROJECT 683** Global Sustainability 684 Corporate Social Responsibility in International Business 686 MNE Social Responsibilities 688 INDUSTRY BOX: SOCIAL IMPACT ASSESSMENT STEPS AT SHELL 691 Global Guidelines and Mandates 692 A Culture of Social Responsibility 692 Auditing and Assessing MNE Social Responsibility 694 Corruption in International Business 694 Definition and Magnitude of Corruption 694 The Origins of Corruption 695 Drawbacks of Corruption 696 Corruption Rankings 696 Types of Corrupt Practices 698 Smuggling 698 Money Laundering 699 Piracy and Counterfeiting 699

Bribe Paying 700 The Foreign Corrupt Practices Act (FCPA) 701 The Globalization of the Fight Against Corruption 702 COUNTRY BOX: DRUG COMPANIES FACE BRIBERY PROBE ON PAYMENTS TO OFFICIALS OF FOREIGN EMERGING MARKETS 703

## 20 International Entrepreneurship

OPENING CASE: WILL ENTREPRENEURSHIP HELP JAPAN REGAIN ITS LOST DECADES? 707 Defining International Entrepreneurship 708 Comparative Entrepreneurship 709 Culture and Entrepreneurship 714 Funding New Ventures 714 Cross-Border Entrepreneurship 718 Internationalizing the Born Global Enterprise 721 INDUSTRY BOX: ISRAELI START-UPS IN THE GLOBAL MARKETPLACE 722

Index

727

707