# **UNIT-5**

**BUSINESS ENVIRONMENT**

# **International Business: Scope, Trends, Challenges and Opportunities**

### **Scope**

International business is much broader than international trade. It includes not only international trade (i.e., export and import of goods and services), but also a wide variety of other ways in which the firms operate internationally. International Management professionals are familiar with the language, culture, economic and political environment, and business practices of countries in which multinational firms actively trade and invest.

Major forms of business operations that constitute international business are as follows.

**(i) Merchandise exports and imports:** Merchandise means goods that are tangible, i.e., those that can be seen and touched. When viewed from this perceptive, it is clear that while merchandise exports means sending tangible goods abroad, merchandise imports means bringing tangible goods from a foreign country to one’s own country.

**(ii) Service exports and imports:** Service exports and imports involve trade in intangibles. It is because of the intangible aspect of services that trade in services is also known as invisible trade.

**(iii) Licensing and franchising:** Permitting another party in a foreign country to produce and sell goods under your trademarks, patents or copy rights in lieu of some fee is another way of entering into international business. It is under the licensing system that Pepsi and CocaCola are produced and sold all over the world by local bottlers in foreign countries.

**(iv) Foreign investments:** Foreign investment is another important form of international business. Foreign investment involves investments of funds abroad in exchange for financial return. Foreign investment can be of two types: direct and portfolio investments.

### **Trends**

As the economy grows slowly at home, your business may have to look at selling internationally to remain profitable. Before examining foreign markets, you have to be aware of the major trends in international business so you can take advantage of those that might favor your company. International markets are evolving rapidly, and you can take advantage of the changing environment to create a niche for your company.

### **Growing Emerging Markets**

Developing countries will see the highest economic growth as they come closer to the standards of living of the developed world. If you want your business to grow rapidly, consider selling into one of these emerging markets. Language, financial stability, economic system and local cultural factors can influence which markets you should favor.

### **Demographic Shifts**

The population of the industrialized world is aging while many developing countries still have very youthful populations. Businesses catering to well-off pensioners can profit from a focus on developed countries, while those targeting young families, mothers and children can look in Latin America, Africa and the Far East for growth.

### **Speed of Innovation**

The pace of innovation is increasing as many new companies develop new products and improved versions of traditional items. Western companies no longer can expect to be automatically at the forefront of technical development, and this trend will intensify as more businesses in developing countries acquire the expertise to innovate successfully.

### **More Informed Buyers**

More intense and more rapid communications allow customers everywhere to purchase products made anywhere around the globe and to access information about what to buy. As pricing and quality information become available across all markets, businesses will lose pricing power, especially the power to set different prices in different markets.

### **Increased Competition**

As more businesses enter international markets, Western companies will see increased competition. Because companies based in developing markets often have lower labor costs, the challenge for Western firms is to keep ahead with faster and more effective innovation as well as a high degree of automation.

### **Slower Growth**

The motor of rapid growth has been the Western economies and the largest of the emerging markets, such as China and Brazil. Western economies are stagnating, and emerging market growth has slowed, so economic growth over the next several years will be slower. International businesses must plan for profitability in the face of more slowly growing demand.

### **Clean Technology**

Environmental factors are already a major influence in the West and will become more so worldwide. Businesses must take into account the environmental impact of their normal operations. They can try to market environmentally friendly technologies internationally. The advantage of this market is that it is expected to grow more rapidly than the overall economy.

### **Challenges and Opportunities**

Inevitably such challenges and opportunities vary between companies and sectors but some frequently cited opportunities and challenges include:

|  |  |
| --- | --- |
| **Opportunities** | **Challenges** |
| Access to customers in new countries | New competition for existing customers in domestic markets |
| Learning about customers in new markets | Adjusting products to local tastes and cultural peculiarities |
| Access to new, cheaper sources of finance | Global financial contagion |
| Government incentives to relocate | Costs of meeting a multitude of local/national laws and regulations |
| Access to regional trading agreements/avoidance of trade barriers | Exchange rate fluctuations |
| Economies of scale | Managing long supply chains |
| Access to new resources (e.g. cheap of skilled labour, natural resources) | New competition for local resources (e.g. more demand for labour pushing up local wage costs) |
|   | Cross-cultural communication e.g. language barriers, differing body language and etiquette |
|   | Corporate social responsibility issues |
|   | Capricious political environments/political risk /bias in favour of domestic companies |

# **International Business: Introduction, Concept, Definition**

With the globalization of the world economy, there has been a concomitant rise in the number of companies that operate globally. Though international business as a concept has been around since the time of the East India Company and continued into the early decades of the 20th century, there was a lull in the international expansion of companies because of the Two World Wars. After that, there was a hesitant move towards internationalizing the operations of multinational companies.

What really provided a fillip to the global expansion of companies was the Chicago School of Economic Thought propelled by the legendary economist, Milton Friedman, which championed neoliberal globalization. This ideology, which started in the early 1970s gradually, became a major force to reckon with in the 1980s and became the norm in the 1990s. The result of all this was the frenzied expansion of global companies across the world.

Thus, **international businesses grew in scope and size to the point where at the moment; the global economy is dominated by multinationals from all countries in the world**. What was primarily a phenomenon of western corporations has now expanded to include companies from the East (from countries like India and China). This module examines the phenomenon of international businesses from different aspects like the characteristics of international business, their effect on the local, target economies, and the ways and means with which they would have to operate and succeed in the global competition for ideas and profits.

Above all, international businesses have to ensure that they blend the global outlook and the local adaptation resulting in a “Glocal” phenomenon wherein they would have to think global and act local. Further, **international businesses need to ensure that they do not fall afoul of local laws and at the same time repatriate profits back to their home countries**. Apart from this, the questions of employability and employment conditions that dictate the operations of global businesses have to be taken into consideration as well.

Considering the fact that many third world countries are liberalizing and opening up their economies, there can be no better time than now for international businesses. This is balanced by the countervailing force of the ongoing economic crisis that has dealt a severe blow to the global economy. The third force that determines international businesses are that not only is the third world countries eager to welcome foreign investment, they seek to emulate the international businesses and become like them. Hence, these aspects would be discussed in detail in the subsequent articles.

Finally, international businesses have to ensure that they have a set of operating procedures and norms that are sensitive to the local culture and customs and at the same time, they stick to their brand that has been developed for global markets. This is the challenge that we discussed earlier as “Glocal” orientation.

Any business that involves operations in more than one country can be called an international business. International business is related to the trade and investment operations done by entities across national borders.

Firms may assemble, acquire, produce, market, and perform other value-addition-operations on international scale and scope. Business organizations may also engage in collaborations with business partners from different countries.

Apart from individual firms, governments and international agencies may also get involved in international business transactions. Companies and countries may exchange different types of physical and intellectual assets. These assets can be products, services, capital, technology, knowledge, or labor.

**Internationalization of Business**

Let’s try to explore the reasons why a business would like to go global. It is important to note that there are many challenges in the path of internationalization, but we’ll focus on the positive attributes of the process for the time-being.

There are five major reasons why a business may want to go global −

* **First-mover Advantage**− It refers to getting into a new market and enjoy the advantages of being first. It is easy to quickly start doing business and get early adopters by being first.
* **Opportunity for Growth**− Potential for growth is a very common reason of internationalization. Your market may saturate in your home country and therefore you may set out on exploring new markets.
* **Small Local Markets**− Start-ups in Finland and Nordics have always looked at internationalization as a major strategy from the very beginning because their local market is small.
* **Increase of Customers**− If customers are in short supply, it may hit a company’s potential for growth. In such a case, companies may look for internationalization.
* **Discourage Local Competitors**− Acquiring a new market may mean discouraging other players from getting into the same business-space as one company is in.

**Advantages of Internationalization**

There are multiple advantages of going international. However, the most striking and impactful ones are the following four.

**Product Flexibility**

International businesses having products that don’t really sell well enough in their local or regional market may find a much better customer base in international markets. Hence, a business house having global presence need not dump the unsold stock of products at deep discounts in the local market. It can search for some new markets where the products sell at a higher price.

A business having international operations may also find new products to sell internationally which they don’t offer in the local markets. International businesses have a wider audience and thus they can sell a larger range of products or services.

**Less Competition**

Competition can be a local phenomenon. International markets can have less competition where the businesses can capture a market share quickly. This factor is particularly advantageous when high-quality and superior products are available. Local companies may have the same quality products, but the international businesses may have little competition in a market where an inferior product is available.

**Protection from National Trends and Events**

Marketing in several countries reduces the vulnerability to events of one country. For example, the political, social, geographical and religious factors that negatively affect a country may be offset by marketing the same product in a different country. Moreover, risks that can disrupt business can be minimized by marketing internationally.

**Learning New Methods**

Doing business in more than one country offers great insights to learn new ways of accomplishing things. This new knowledge and experience can pave ways to success in other markets as well.

**Globalization**

Although globalization and internationalization are used in the same context, there are some major differences.

* Globalization is a much larger process and often includes the assimilation of the markets as a whole. Moreover, when we talk about globalization, we take up the cultural context as well.
* Globalization is an intensified process of internationalizing a business. In general terms, global companies are larger and more widespread than the low-lying international business organizations.
* Globalization means the intensification of cross-country political, cultural, social, economic, and technological interactions that result in the formation of transnational business organization. It also refers to the assimilation of economic, political, and social initiatives on a global scale.
* Globalization also refers to the costless cross-border transition of goods and services, capital, knowledge, and labor.

**Factors Causing Globalization of Businesses**

There are many factors related to the change of technology, international policies, and cultural assimilation that initiated the process of globalization. The following are the most important factors that helped globalization take shape and spread it drastically.

**The Reduction and Removal of Trade Barriers**

After World War II, the General Agreement on Tariffs and Trade (GATT) and the WTO have reduced tariffs and various non-tariff barriers to trade. It enabled more countries to explore their comparative advantage. It has a direct impact on globalization.

**Trade Negotiations**

The Uruguay Round of negotiations (1986–94) can be considered as the real boon for globalization. It is considerably a large set of measures which was agreed upon exclusively for liberalized trade. As a result, the world trade volume increased by 50% in the following 6 years of the Uruguay Round, paving the way for businesses to span their offerings at an international level.

**Transport Costs**

Over the last 25 years, sea transport costs have plunged 70%, and the airfreight costs have nosedived 3–4% annually. The result is a boost in international and multi-continental trade flows that led to Globalization.

**Growth of the Internet**

Expansion of e-commerce due to the growth of the Internet has enabled businesses to compete globally. Essentially, due to the availability of the Internet, consumers are interested to buy products online at a low price after reviewing best deals from multiple vendors. At the same time, online suppliers are saving a lot of marketing costs.

**Growth of Multinational Corporations**

Multinational Corporations (MNCs) have characterized the global interdependence. They encompass a number of countries. Their sales, profits, and the flow of production is reliant on several countries at once.

**The Development of Trading Blocs**

The ‘regional trade agreement’ (RTA) abolished internal barriers to trade and replaced them with a common external tariff against non-members. Trading blocs actually promote globalization and interdependence of economies via trade creation

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# **World Trade Organization (WTO)**

During great depression of 1930s the international trade was badly affected and various countries imposed import restriction for safeguarding their economies. This resulted in a sharp decline in the world trade in 1945. USA put forward many proposals for extending international trade and employment. On October 30, 1947, 23 countries at Geneva, signed an agreement related to tariffs imposed on trade.

This agreement is known as General Agreement on Tariffs and Trade (GATT). It came into force on January 1, 1948. Initially GATT was established in the form of a temporary arrangement but later on it took the shape of a permanent agreement. GATT’s headquarter was in Geneva. On December 12, 1995, GATT was abolished and replaced by World Trade Organisation (WTO), which came into existence on January 1, 1995.

The WTO was established on January 1, 1995. The WTO is the embodiment of the Uruguay Round results and the successor to GATT. 76 Governments became members of the WTO on its first day. As of September 1999, there are 134 members of the WTO and 34 countries have an observer status. There is a waiting list of 31 members. They account for more than 90 percent of the world trade.

### **Functions of WTO:**

**i)** The WTO shall facilitate the implementation, administration and operation, and further the objectives of the Multilateral Trade Agreements, and shall also provide the framework for the implementation, administration and operation of Plurilateral Trade Agreements.

**ii)** The WTO shall provide the forum for negotiations among its members concerning their multilateral trade relations in matters dealt with under the Agreements.

**iii)** The WTO shall administer the ‘Understanding on Rules and Procedures Governing the Settlement of Disputes’.

**iv)** The WTO shall administer the ‘Trade Review Mechanism’.

**v)** With a view to achieve greater coherence in global economic policy making, the WTO shall co-operate, as appropriate, with the IMF and IBRD and its affiliated agencies.

### **The General Council will serve four main functions:**

**i)** To supervise on a regular basis the operation of the revised agreements and ministerial declarations relating to: Goods, services, and TRIPs.

**ii)** To act as a Dispute Settlement Body,

**iii)** To serve as a Trade Review Mechanism,

**iv)** To establish Goods Council, Services Council and TRIPs Coun­cil, as subsidiary bodies.

The WTO is a more powerful body with enlarged functions than the GATT and is envisaged to play a major role in the world economic affairs. To become a member of the WTO, a country must completely accept the results of the Uruguay Round