Chapter 3
Competing in the Global Marketplace

This chapter examines the business world of the global marketplace. It focuses on the processes of taking a business global, such as licensing agreements and franchisees; the challenges that are encountered; and the regulatory systems governing the world market of the 21st century.

Today, global revolutions are under way in many areas of our lives: management, politics, communications, and technology. The word *global* has assumed a new meaning, referring to a boundless mobility and competition in social, business, and intellectual arenas. The purpose of this chapter is to explain how global trade is conducted. We also discuss the barriers to international trade and the organizations that foster global trade. The chapter concludes with trends in the global marketplace.

3.1 Global Trade in the United States

1. Why is global trade important to the United States, and how is it measured?

No longer just an option, having a global vision has become a business imperative. Having a global vision means recognizing and reacting to international business opportunities, being aware of threats from foreign competitors in all markets, and effectively using international distribution networks to obtain raw materials and move finished products to the customer.

U.S. managers must develop a global vision if they are to recognize and react to international business opportunities, as well as remain competitive at home. Often a U.S. firm’s toughest domestic competition comes from foreign companies. Moreover, a global vision enables a manager to understand that customer and distribution networks operate worldwide, blurring geographic and political barriers and making them increasingly irrelevant to business decisions. Over the past three decades, world trade has climbed from $200 billion a year to more than $1.4 trillion. U.S. companies play a major role in this growth in world trade, with 113 of the Fortune 500 companies making over 50 percent of their profits outside the United States. Among these companies are recognizable names such as Apple, Microsoft, Pfizer, Exxon Mobil, and General Electric.

Starbucks Corp. is among the fastest growing global consumer brands and one of the most visible emblems of U.S. commercial culture overseas. Of Starbucks’s 24,000 total stores, almost 66 percent are international stores that contribute a substantial amount to the company’s revenues, which have grown from $4.1 billion in 2003 to $21.3 billion in 2016.

Go into a Paris McDonald’s and you may not recognize where you are. There are no Golden Arches or utilitarian chairs and tables and other plastic features. The restaurants have exposed brick walls, hardwood floors, and armchairs. Some French McDonald’s even have faux marble walls. Most restaurants have TVs with continuous music videos. You can even order an espresso, beer, and a chicken on focaccia bread sandwich. It’s not America.

Global business is not a one-way street, where only U.S. companies sell their wares and services throughout the world. Foreign competition in the domestic market used to be relatively rare but now occurs in almost every industry. In fact, U.S. makers of electronic goods, cameras, automobiles, fine china, tractors, leather goods, and a host of other consumer and industrial products have struggled to maintain their domestic market shares against foreign competitors. Toyota now has 14 percent of the U.S. auto market, followed by Honda at 9 percent and Nissan with 8 percent. Nevertheless, the global market has created vast new business opportunities for many U.S. firms.

The Importance of Global Business to the United States

Many countries depend more on international commerce than the United States does. For example, France, Great Britain, and Germany all derive more than 55 percent of their gross domestic product (GDP) from world trade, compared to about 28 percent for the United States. Nevertheless, the impact of international business on the U.S. economy is still impressive:

Trade-dependent jobs have grown at a rate three times the growth of U.S.-dependent jobs.
Every U.S. state has realized a growth of jobs attributable to trade.
Trade has an effect on both service and manufacturing jobs.
These statistics might seem to imply that practically every business in the United States is selling its wares throughout the world, but most is accounted for by big business. About 85 percent of all U.S. exports of manufactured goods are shipped by 250 companies. Yet, 98 percent of all exporters are small and medium-size firms.

The Impact of Terrorism on Global Trade

The terrorist attacks on America on September 11, 2001, and the Charlie Hebdo terrorist attacks in Paris in 2015 have changed the way the world conducts business. The immediate impacts of these events have included a short-term shrinkage of global trade. Globalization, however, will continue because the world's major markets are too vitally integrated for globalization to stop. Nevertheless, terrorism has caused the growth to be slower and costlier.

Companies are paying more for insurance and to provide security for overseas staff and property. Heightened border inspections slow movements of cargo, forcing companies to stock more inventory. Tighter immigration policies curtail the liberal inflows of skilled and blue-collar workers that allowed companies to expand while keeping wages in check. The impact of terrorism may lessen over time, but multinational firms will always be on guard.

Measuring Trade between Nations

International trade improves relationships with friends and allies; helps ease tensions among nations; and—economically speaking—bolsters economies, raises people's standard of living, provides jobs, and improves the quality of life. The value of international trade is over $16 trillion a year and growing. This section takes a look at some key measures of international trade: exports and imports, the balance of trade, the balance of payments, and exchange rates.

Exports and Imports

The developed nations (those with mature communication, financial, educational, and distribution systems) are the major players in international trade. They account for about 70 percent of the world's exports and imports. Exports are goods and services made in one country and sold to others. Imports are goods and services that are bought from other countries. The United States is the largest importer and second largest exporter in the world.

Each year the United States exports more food, animal feed, and beverages than the year before. A third of U.S. farm acreage is devoted to crops for export. The United States is also a major exporter of engineering products and other high-tech goods, such as computers and telecommunications equipment. For more than 60,000 U.S. companies (the majority of them small), international trade offers exciting and profitable opportunities. Among the largest U.S. exporters are Apple, General Motors Corp., Ford Motor Co., Procter & Gamble, and Cisco Systems.

Despite our impressive list of resources and great variety of products, imports to the United States are also growing. Some of these imports are raw materials that we lack, such as manganese, cobalt, and bauxite, which are used to make airplane parts, exotic metals, and military hardware. More modern factories and lower labor costs in other countries make it cheaper to import industrial supplies (such as steel) and production equipment than to produce them at home. Most of Americans' favorite hot beverages—coffee, tea, and cocoa—are imported. Lower manufacturing costs have resulted in huge increases in imports from China.

Balance of Trade

The difference between the value of a country's exports and the value of its imports during a specific time is the country's balance of trade. A country that exports more than it imports is said to have a favorable balance of trade, called a trade surplus. A country that imports more than it exports is said to have an unfavorable balance of trade, or a trade deficit. When imports exceed exports, more money from trade flows out of the country than flows into it.

Although U.S. exports have been booming, we still import more than we export. We have had an unfavorable balance of trade throughout the 1990s, 2000s and 2010s. In 2016, our exports totaled $2.2 trillion, yet our imports were $2.7 trillion. Thus, in 2016 the United States had a trade deficit of $500 billion. America's exports continue to grow, but not as fast as our imports: The export of goods, such as computers, trucks, and airplanes, is very strong. The sector that is lagging in significant growth is the export of services. Although America exports many services—ranging from airline trips to education of foreign students to legal advice—part of the problem is due to piracy, which leads companies to restrict the distribution of their services to certain regions. The FBI estimates that the theft of intellectual property from products, books and movies, and pharmaceuticals totals in the billions every year.

Balance of Payments

Another measure of international trade is called the balance of payments, which is a summary of a country's international financial transactions showing the difference between the country's total payments to and its total receipts from other countries. The balance of payments includes imports and exports (balance of trade), long-term investments in overseas plants and equipment, government loans to and from other countries, gifts and foreign aid, military expenditures made in other countries, and money transfers in and out of foreign banks.

From 1900 until 1970, the United States had a trade surplus, but in the other areas that make up the balance of payments, U.S. payments exceeded receipts, largely due to the large U.S. military presence abroad. Hence, almost every year since 1950, the United

States has had an unfavorable balance of payments. And since 1970, both the balance of payments and the balance of trade have been unfavorable. What can a nation do to reduce an unfavorable balance of payments? It can foster exports, reduce its dependence on imports, decrease its military presence abroad, or reduce foreign investment. The U.S. balance of payments deficit was over $504 billion in 2016.

The Changing Value of Currencies
The exchange rate is the price of one country's currency in terms of another country's currency. If a country's currency appreciates, less of that country's currency is needed to buy another country's currency. If a country's currency depreciates, more of that currency will be needed to buy another country's currency.

How do appreciation and depreciation affect the prices of a country's goods? If, say, the U.S. dollar depreciates relative to the Japanese yen, U.S. residents have to pay more dollars to buy Japanese goods. To illustrate, suppose the dollar price of a yen is $0.012 and that a Toyota is priced at 2 million yen. At this exchange rate, a U.S. resident pays $24,000 for a Toyota ($0.012 × 2 million yen = $24,000). If the dollar depreciates to $0.018 to one yen, then the U.S. resident will have to pay $36,000 for a Toyota.

As the dollar depreciates, the prices of Japanese goods rise for U.S. residents, so they buy fewer Japanese goods—thus, U.S. imports decline. At the same time, as the dollar depreciates relative to the yen, the yen appreciates relative to the dollar. This means prices of U.S. goods fall for the Japanese, so they buy more U.S. goods—and U.S. exports rise.

Currency markets operate under a system called floating exchange rates. Prices of currencies "float" up and down based upon the demand for and supply of each currency. Global currency traders create the supply of and demand for a particular currency based on that currency's investment, trade potential, and economic strength. If a country decides that its currency is not properly valued in international currency markets, the government may step in and adjust the currency's value. In a devaluation, a nation lowers the value of its currency relative to other currencies. This makes that country's exports cheaper and should, in turn, help the balance of payments.

In other cases, a country's currency may be undervalued, giving its exports an unfair competitive advantage. Many people believe that China's huge trade surplus with the United States is partially because China's currency was undervalued. In 2017, the U.S. Department of Commerce issued a fact sheet detailing how it accused China of dumping steel on the U.S. market as well as providing financial assistance to Chinese companies to produce, manufacture, and export stainless steel to the United States from the People's Republic of China.

3.2 Why Nations Trade

2. Why do nations trade?

One might argue that the best way to protect workers and the domestic economy is to stop trade with other nations. Then the whole circular flow of inputs and outputs would stay within our borders. But if we decided to do that, how would we get resources like cobalt and coffee beans? The United States simply can't produce some things, and it can't manufacture some products, such as steel and most clothing, at the low costs we're used to. The fact is that nations—like people—are good at producing different things: you may be better at balancing a ledger than repairing a car. In that case you benefit by "exporting" your bookkeeping services and "importing" the car repairs you need from a good mechanic. Economists refer to specialization like this as advantage.

Absolute Advantage
A country has an absolute advantage when it can produce and sell a product at a lower cost than any other country or when it is the only country that can provide a product. The United States, for example, has an absolute advantage in reusable spacecraft and other high-tech items.

Suppose that the United States has an absolute advantage in air traffic control systems for busy airports and that Brazil has an absolute advantage in coffee. The United States does not have the proper climate for growing coffee, and Brazil lacks the technology to develop air traffic control systems. Both countries would gain by exchanging air traffic control systems for coffee.

Comparative Advantage
Even if the United States had an absolute advantage in both coffee and air traffic control systems, it should still specialize and engage in trade. Why? The reason is the principle of comparative advantage, which says that each country should specialize in the products that it can produce most readily and cheaply and trade those products for goods that foreign countries can produce most readily and cheaply. This specialization ensures greater product availability and lower prices.

For example, India and Vietnam have a comparative advantage in producing clothing because of lower labor costs. Japan has long held a comparative advantage in consumer electronics because of technological expertise. The United States has an advantage in computer software, airplanes, some agricultural products, heavy machinery, and jet engines.

Thus, comparative advantage acts as a stimulus to trade. When nations allow their citizens to trade whatever goods and services they choose without government regulation, free trade exists. Free trade is the policy of permitting the people and businesses of a country to buy and sell where they please without restrictions. The opposite of free trade is protectionism, in which a nation protects its home industries from outside competition by establishing artificial barriers such as tariffs and quotas. In the next section, we'll look at the various barriers, some natural and some created by governments, that restrict free trade.

The Fear of Trade and Globalization

The continued protests during meetings of the World Trade Organization and the protests during the convocations of the World Bank and the International Monetary Fund (the three organizations are discussed later in the chapter) show that many people fear world trade and globalization. What do they fear? The negatives of global trade are as follows:

- Millions of Americans have lost jobs due to imports or production shifting abroad. Most find new jobs, but often those jobs pay less.
- Millions of others fear losing their jobs, especially at those companies operating under competitive pressure.
- Employers often threaten to export jobs if workers do not accept pay cuts.
- Service and white-collar jobs are increasingly vulnerable to operations moving offshore.

Sending domestic jobs to another country is called outsourcing, a topic you can explore in more depth. Many U.S. companies, such as Dell, IBM, and AT&T, have set up call service centers in India, the Philippines, and other countries. Now even engineering and research and development jobs are being outsourced. Outsourcing and "American jobs" were a big part of the 2016 presidential election with Carrier's plan to close a plant in Indianapolis and open a new plant in Mexico. While intervention by President Trump did lead to 800 jobs remaining in Indianapolis, Carrier later informed the state of Indiana that it would cut 632 workers from its Indianapolis factory. The manufacturing jobs will move to Monterrey, Mexico, where the minimum wage is $3.90 per day.

Exhibit 3.3 Anti-globalization groups oppose America's free-trade stance, arguing that corporate interests are hurting the U.S. economy and usurping the power of the American people. The recent protests at the G20 meetings in Hamburg, Germany, expressed anti-free-trade sentiment, supporting the idea that multinational corporations wield too much power. Are fears expressed by anti-globalization activists and nationalists justified? (Credit: fiction of reality/ Flickr/ Attribution 2.0 Generic (CC BY 2.0))

So is outsourcing good or bad? If you happen to lose your job, it's obviously bad for you. However, some economists say it leads to cheaper goods and services for U.S. consumers because costs are lower. Also, it should stimulate exports to fast-growing countries. No one knows how many jobs will be lost to outsourcing in coming years. According to estimates, almost 2.4 million U.S. jobs were outsourced in 2015.

Benefits of Globalization

A closer look reveals that globalization has been the engine that creates jobs and wealth. Benefits of global trade include the following:

- Productivity grows more quickly when countries produce goods and services in which they have a comparative advantage. Living standards can increase faster. One problem is that big G20 countries have added more than 1,200 restrictive export and import measures since 2008.
- Global competition and cheap imports keep prices down, so inflation is less likely to stop economic growth. However, in some cases this is not working because countries manipulate their currency to get a price advantage.
- An open economy spurs innovation with fresh ideas from abroad.
- Through infusion of foreign capital and technology, global trade provides poor countries with the chance to develop economically by spreading prosperity.
- More information is shared between two trading partners that may not have much in common initially, including insight into local cultures and customs, which may help the two nations expand their collective knowledge and learn ways to compete globally.

3.3 Barriers to Trade

3. What are the barriers to international trade?
4.

International trade is carried out by both businesses and governments—as long as no one puts up trade barriers. In general, trade barriers keep firms from selling to one another in foreign markets. The major obstacles to international trade are natural barriers, tariff barriers, and nontariff barriers.

Natural Barriers

Natural barriers to trade can be either physical or cultural. For instance, even though raising beef in the relative warmth of Argentina may cost less than raising beef in the bitter cold of Siberia, the cost of shipping the beef from South America to Siberia might drive the price too high. Distance is thus one of the natural barriers to international trade.

Language is another natural trade barrier. People who can't communicate effectively may not be able to negotiate trade agreements or may ship the wrong goods.

Tariff Barriers

A **tariff** is a tax imposed by a nation on imported goods. It may be a charge per unit, such as per barrel of oil or per new car; it may be a percentage of the value of the goods, such as 5 percent of a $500,000 shipment of shoes; or it may be a combination. No matter how it is assessed, any tariff makes imported goods more costly, so they are less able to compete with domestic products.

Protective tariffs make imported products less attractive to buyers than domestic products. The United States, for instance, has protective tariffs on imported poultry, textiles, sugar, and some types of steel and clothing, and in March of 2018 the Trump administration added tariffs on steel and aluminum from most countries. On the other side of the world, Japan imposes a tariff on U.S. cigarettes that makes them cost 60 percent more than Japanese brands. U.S. tobacco firms believe they could get as much as a third of the Japanese market if there were no tariffs on cigarettes. With tariffs, they have under 2 percent of the market.

Arguments for and against Tariffs

Congress has debated the issue of tariffs since 1789. The main arguments for tariffs include the following:

- Tariffs protect infant industries. A tariff can give a struggling new domestic industry time to become an effective global competitor.
- Tariffs protect U.S. jobs. Unions and others say tariffs keep foreign labor from taking away U.S. jobs.
- Tariffs aid in military preparedness. Tariffs should protect industries and technology during peacetime that are vital to the military in the event of war.

The main arguments against tariffs include the following:

- Tariffs discourage free trade, and free trade lets the principle of competitive advantage work most efficiently.
- Tariffs raise prices, thereby decreasing consumers' purchasing power. In 2017, the United States imposed tariffs of 63.86 percent to 190.71 percent on a wide variety of Chinese steel products. The idea was to give U.S. steel manufacturers a fair market after the Department of Commerce concluded their antidumping and anti-subsidy probes. It is still too early to determine what the effects of these tariffs will be, but higher steel prices are likely. Heavy users of steel, such as construction and automobile industries, will see big increases in their production costs. It is also likely that China may impose tariffs on certain U.S. products and services and that any negotiations on intellectual property and piracy will bog down.

Nontariff Barriers
Governments also use other tools besides tariffs to restrict trade. One type of nontariff barrier is the **import quota**, or limits on the quantity of a certain good that can be imported. The goal of setting quotas is to limit imports to the specific amount of a given product. The United States protects its shrinking textile industry with quotas. A complete list of the commodities and products subject to import quotas is available on line at the U.S. Customs and Border Protection Agency website.

A complete ban against importing or exporting a product is an **embargo**. Often embargoes are set up for defense purposes. For instance, the United States does not allow various high-tech products, such as supercomputers and lasers, to be exported to countries that are not allies. Although this embargo costs U.S. firms billions of dollars each year in lost sales, it keeps enemies from using the latest technology in their military hardware.

Government rules that give special privileges to domestic manufacturers and retailers are called **buy-national regulations**. One such regulation in the United States bans the use of foreign steel in constructing U.S. highways. Many state governments have buy-national rules for supplies and services. In a more subtle move, a country may make it hard for foreign products to enter its markets by establishing customs regulations that are different from generally accepted international standards, such as requiring bottles to be quart size rather than liter size.

Exchange controls are laws that require a company earning foreign exchange (foreign currency) from its exports to sell the foreign exchange to a control agency, usually a central bank. For example, assume that Rolex, a Swiss company, sells 300 watches to Zales Jewelers, a U.S. chain, for US$600,000. If Switzerland had exchange controls, Rolex would have to sell its U.S. dollars to the Swiss central bank and would receive Swiss francs. If Rolex wants to buy goods (supplies to make watches) from abroad, it must go to the central bank and buy foreign exchange (currency). By controlling the amount of foreign exchange sold to companies, the government controls the amount of products that can be imported. Limiting imports and encouraging exports helps a government to create a favorable balance of trade.

3.4 Fostering Global Trade

4. How do governments and institutions foster world trade?

Antidumping Laws
U.S. firms don't always get to compete on an equal basis with foreign firms in international trade. To level the playing field, Congress has passed antidumping laws. **Dumping** is the practice of charging a lower price for a product (perhaps below cost) in foreign markets than in the firm's home market. The company might be trying to win foreign customers, or it might be seeking to get rid of surplus goods.

When the variation in price can't be explained by differences in the cost of serving the two markets, dumping is suspected. Most industrialized countries have antidumping regulations. They are especially concerned about *predatory dumping,* the attempt to gain control of a foreign market by destroying competitors with impossibly low prices.

The United States recently imposed tariffs on softwood lumber from Canada. Canada was found guilty of pricing softwood lumber at between 7.72 and 4.49 percent below their costs. U.S. customs officers will now levy tariffs on Canadian timber exports with tax rates from 17.41 percent to 30.88 percent, depending on the business.

From our discussion so far, it might seem that governments act only to restrain global trade. On the contrary, governments and international financial organizations work hard to increase it, as this section explains.

Trade Negotiations and the World Trade Organization
The **Uruguay Round** of trade negotiations is an agreement that dramatically lowers trade barriers worldwide. Adopted in 1994, the agreement has been now signed by 148 nations. The most ambitious global trade agreement ever negotiated, the Uruguay Round reduced tariffs by one-third worldwide, a move that is expected to increase global income by $235 billion annually. Perhaps the most notable aspect of the agreement is its recognition of new global realities. For the first time, an agreement covers services, intellectual property rights, and trade-related investment measures such as exchange controls.

As a follow-up to the Uruguay Round, a negotiating round started in the capital of Qatar in 2001 is called the Doha Round. To date, the round has shown little progress in advancing free trade. Developing nations are pushing for the reduction of farm subsidies in the United States, Europe, and Japan. Poor countries say that the subsidies stimulate overproduction, which drives down global agricultural prices. Because developing nations' primary exports are agricultural commodities, low prices mean that they cannot compete in the global marketplace. On the other hand, the United States and Europe are interested in bringing down trade barriers in services and manufacturing. The continuing talks have served as a lightning rod for protesters, who claim that the World Trade Organization (WTO) serves the interests of multinational corporations, promotes trade over preserving the environment, and treats poor nations unfairly.

The **World Trade Organization** replaces the old General Agreement on Tariffs and Trade (GATT), which was created in 1948. The GATT contained extensive loopholes that enabled countries to evade agreements to reduce trade barriers. Today, all WTO members must fully comply with all agreements under the Uruguay Round. The WTO also has an effective dispute settlement procedure with strict time limits to resolve disputes.

The WTO has emerged as the world's most powerful institution for reducing trade barriers and opening markets. The advantage of WTO membership is that member countries lower trade barriers among themselves. Countries that don't belong must negotiate trade agreements individually with all their trading partners. Only a few countries, such as North Korea, Turkmenistan, and Eritrea, are not members of the WTO.

Exhibit 3.4 Headquartered in Toulouse, France, Airbus is one of the world's top commercial aircraft manufacturers, operating design and manufacturing facilities in Europe, Japan, China, and the United States. The airliner's current product lineup of 12 jet-aircraft types ranging from 100 seats to 600 seats is heavy competition for Boeing, a top U.S. airline firm with which Airbus has ongoing subsidy-related disputes. *What is the World Trade Organization's role in settling disputes between competing multinational corporations?* (Credit: Bartlomiej Mostek/ Flickr/ Attribution 2.0 Generic (CC BY 2.0))

The United States has had mixed results in bringing disputes before the WTO. To date, it has won slightly fewer than half of the cases it has presented to the WTO. America has also won about one-third of the cases brought against it by other countries. One of America's recent losses came in a ruling where the U.S. claimed that tuna imported from Mexico was not meeting the "dolphin safe" criteria, meaning that dolphins were not being killed during the process to catching tuna. The WTO ruled in favor of Mexico. Recently, the United States targeted Europe, India, South Korea, Canada, and Argentina to file cases against. The disputes ranged from European aviation practices to Indian trade barriers affecting U.S. automakers.

One of the biggest disputes before the WTO involved the United States and the European Union. The United States claims that Europe has given Airbus $15 billion in aid to develop airplanes. The European Union claims that the U.S. government has provided $23 billion in military research that has benefited Boeing's commercial aircraft business. It also claimed that Washington State (the home of Boeing manufacturing) has given the company $3.2 billion in unfair tax breaks.[23]

The World Bank and International Monetary Fund

Two international financial organizations are instrumental in fostering global trade. The **World Bank** offers low-interest loans to developing nations. Originally, the purpose of the loans was to help these nations build infrastructure such as roads, power plants, schools, drainage projects, and hospitals. Now the World Bank offers loans to help developing nations relieve their debt burdens. To receive the loans, countries must pledge to lower trade barriers and aid private enterprise. In addition to making loans, the World Bank is a major source of advice and information for developing nations. The United States has granted the organization millions to create knowledge databases on nutrition, birth control, software engineering, creating quality products, and basic accounting systems.

The **International Monetary Fund (IMF)** was founded in 1945, one year after the creation of the World Bank, to promote trade through financial cooperation and eliminate trade barriers in the process. The IMF makes short-term loans to member nations that are unable to meet their budgetary expenses. It operates as a lender of last resort for troubled nations. In exchange for these emergency loans, IMF lenders frequently extract significant commitments from the borrowing nations to address the problems that led to the crises. These steps may include curtailing imports or even devaluing the currency.

Some global financial problems do not have a simple solution. One option would be to pump a lot more funds into the IMF, giving it enough resources to bail out troubled countries and put them back on their feet. In effect, the IMF would be turned into a real lender of last resort for the world economy.

The danger of counting on the IMF, though, is the “moral hazard” problem. Investors would assume that the IMF would bail them out and would therefore be encouraged to take bigger and bigger risks in emerging markets, leading to the possibility of even deeper financial crises in the future.

3.5 International Economic Communities

5. What are international economic communities?

Nations that frequently trade with each other may decide to formalize their relationship. The governments meet and work out agreements for a common economic policy. The result is an economic community or, in other cases, a bilateral trade agreement (an agreement between two countries to lower trade barriers). For example, two nations may agree upon a **preferential tariff**, which gives advantages to one nation (or several nations) over others. When members of the British Commonwealth (countries that are former British territories) trade with Great Britain, they pay lower tariffs than do other nations. For example, Canada and Australia are former British territories but still members of the British Commonwealth. You will note that Queen Elizabeth still appears on Canadian currency and the Union Jack is still incorporated into the Australian flag. In other cases, nations may form free-trade associations. In a **free-trade zone**, few duties or rules restrict trade among the partners, but nations outside the zone must pay the tariffs set by the individual members.

North American Free Trade Agreement (NAFTA)

The **North American Free Trade Agreement (NAFTA)** created the world’s largest free-trade zone. The agreement was ratified by the U.S. Congress in 1993. It includes Canada, the United States, and Mexico, with a combined population of 450 million and an economy of over $20.8 trillion.[24] NAFTA has since been modified by the U.S.-Mexico-Canada Agreement (USMCA). The USMCA was largely accepted and entered into force on July 1, 2020.

Canada, one of the largest U.S. trading partners, entered a free-trade agreement with the United States in 1988. Thus, most of the new long-run opportunities opened for U.S. business under NAFTA are in Mexico, America’s third-largest trading partner. Before NAFTA, tariffs on Mexican exports to the United States averaged just 4 percent, and most goods entered the United States duty-free, so NAFTA’s primary impact was to open the Mexican market to U.S. companies. When the treaty went into effect, tariffs on about half the items traded across the Rio Grande disappeared. Since NAFTA came into effect, U.S.-Mexican trade has increased from $80 billion to $515 billion annually. The pact removed a web of Mexican licensing requirements, quotas, and tariffs that limited transactions in U.S. goods and services. For instance, the pact allows U.S. and Canadian financial-services companies to own subsidiaries in Mexico for the first time in 50 years.

Exhibit 3.5 The softwood lumber dispute between the United States and Canada that has resulted in the U.S. imposing tariffs on Canadian softwood lumber imports is one of the longest trade disputes between the two nations. The dispute is the result of disagreements about Canadian lumber production and imports between the two nations. The main contention in the softwood lumber dispute is the U.S. claim that the Canadian government is unfairly subsidizing Canadian lumber production by providing access to public land while U.S. producers harvest softwood lumber on their own property. *Why do anti-free-trade groups support these tariffs when the result will be higher prices for softwood lumber?* (Credit: Jesse Wagstaff/ Flickr/ Attribution-NoDerivs 2.0 Generic (CC BY 2.0))

The real test of NAFTA and now USMCA will be whether it can deliver rising prosperity on both sides of the Rio Grande. For Mexicans, NAFTA must provide rising wages, better benefits, and an expanding middle class with enough purchasing power to keep buying goods from the United States and Canada. That scenario seems to be working. At the Delphi Corp. auto parts plant in Ciudad Juárez, just across the border from El Paso, Texas, the assembly line is a cross section of working-class Mexico. In the years since NAFTA lowered trade and investment barriers, Delphi has significantly expanded its presence in the country. Today it employs 70,000 Mexicans, who every day receive up to 70 million U.S.-made components to assemble into parts. The wages are modest by U.S. standards—an assembly-line worker with two years' experience earns about $2.30 an hour. But that's triple Mexico's minimum wage, and Delphi jobs are among the most coveted in Juárez. The United States recently notified the Canadian and Mexican governments that it intends to renegotiate aspects of the NAFTA agreement.

One of the largest new trade agreement is **Mercosur**, which includes Peru, Brazil, Argentina, Uruguay, and Paraguay. The elimination of most tariffs among the trading partners has resulted in trade revenues that currently exceed $16 billion annually. Recent recessions in Mercosur countries have limited economic growth, even though trade among Mercosur countries has continued to grow. Most recently, the largest new trade agreement is the Regional Comprehensive Economic Partnership (RCEP). This trade agreement includes fifteen (15) Asian States and signals to investors that the region is still committed to multilateral trade integration. One item that is most notable about this trade agreement is that the U.S. is not a member.

Central America Free Trade Agreement

The newest free trade agreement is the Central America Free Trade Agreement (CAFTA) passed in 2005. Besides the United States, the agreement includes Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, and Nicaragua. The United States is already the principal exporter to these nations, so economists don't think that it will result in a major increase in U.S. exports. It will, however, reduce tariffs on exports to CAFTA countries. Already, some 80 percent of the goods imported into the United States from CAFTA nations are tariff-free. CAFTA countries may benefit from the new permanent trade deal if U.S. multinational firms deepen their investment in the region.

The European Union

In 1993, the member countries of the European Community (EC) ratified the Maastricht Treaty, which proposed to take the EC further toward economic, monetary, and political union. Although the heart of the treaty deals with developing a unified European Market, Maastricht was also intended to increase integration among **European Union (EU)** members.

The EU has helped increase this integration by creating a borderless economy for the 28 European nations, shown on the map in **Exhibit 3.6**.

EU28 Member States:	**Candidate Countries:**
Austria Belgium Bulgaria Croatia Cyprus Czech Republic Denmark Estonia Finland France Germany Greece Hungary Ireland Italy Latvia Lithuania Luxembourg Malta The Netherlands	Albania Former Yugoslav Republic of Macedonia Montenegro Serbia Turkey

EU28 Member States:	Candidate Countries:
Poland Portugal Romania Slovakia Slovenia Spain Sweden	

European Union member states have set up common institutions to which they delegate some of their sovereignty so that decisions on specific matters of joint interest can be made democratically at the European level. This pooling of sovereignty is also called **European integration**. In 2016, citizens of the United Kingdom voted to leave the European Union, a plan known as Brexit, which could take several years to occur.

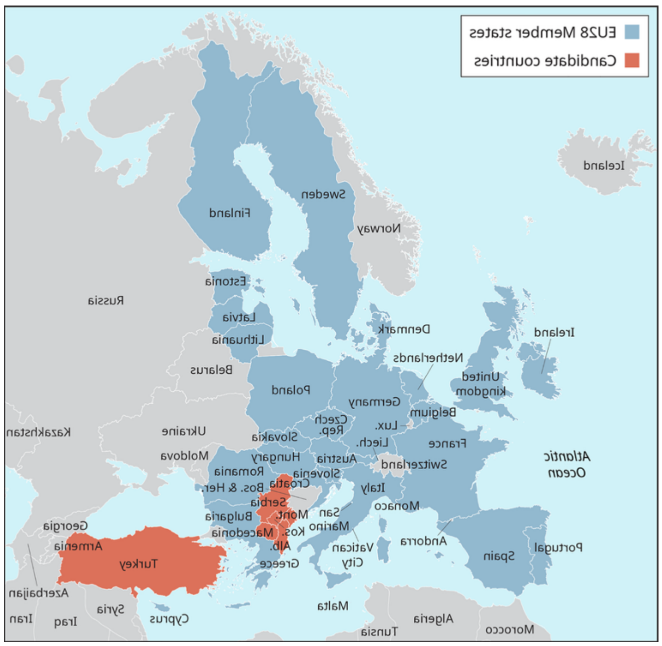

Exhibit 3.6 The European Union Source: Adapted from https://europa.eu/european-union/about-eu/countries/member-countries_en.

One of the principal objectives of the European Union is to promote economic progress of all member countries. The EU has stimulated economic progress by eliminating trade barriers, differences in tax laws, and differences in product standards, and by establishing a common currency. A new European Community Bank was created, along with a common currency called the euro. The European Union's single market has created 2.5 million new jobs since it was founded and generated more than $1 trillion in new wealth.[28] The opening of national EU markets has brought down the price of national telephone calls by 50 percent since 1998. Under pressure of competition, the prices of airfares in Europe have fallen significantly. The removal of national restrictions has enabled more than 15 million Europeans to go to another EU country to work or spend their retirement.

The EU is a very tough antitrust enforcer; some would say it is tougher than the United States. The EU, for example, fined Google $2.7 billion for favoring some of its own services in its search results.[29] Unlike in the United States, the EU can seal off corporate offices for unspecified periods to prevent destruction of evidence and enter the homes, cars, yachts, and other personal property of executives suspected of abusing their companies' market power or conspiring to fix prices.

Microsoft has been fighting the European Court since 2002, with no quick end in sight. The Court fined Microsoft for monopolizing internet access by offering Internet Explorer with its Windows software. The company is also appealing a Court decision requiring it to share code with "open source" companies. Another big U.S. company, Coca-Cola, settled a six-year antitrust dispute with the European Court by agreeing to strict limits on its sales tactics. Coke can't sign exclusive agreements with retailers that would ban competing soft drinks or give retailers rebates based on sales volume. Furthermore, it must give rivals, like Pepsi, 20 percent of the space in Coke coolers so Pepsi can stock its own brands. If Coke violates the terms of the agreement, it will be fined 10 percent of its worldwide revenue (over $2 billion).

An entirely different type of problem facing global businesses is the possibility of a protectionist movement by the EU against outsiders. For example, European automakers have proposed holding Japanese imports at roughly their current 10 percent market share. The Irish, Danes, and Dutch don't make cars and have unrestricted home markets; they are unhappy at the prospect of limited imports of Toyotas and Hondas. Meanwhile, France has a strict quota on Japanese cars to protect its own Renault and Peugeot. These local automakers could be hurt if the quota is raised at all.

Interestingly, a number of big U.S. companies are already considered more "European" than many European companies. Coke and Kellogg's are considered classic European brand names. Ford and General Motors compete for the largest share of auto sales on the continent. Apple, IBM, and Dell dominate their markets. General Electric, AT&T, and Westinghouse are already strong all over Europe and have invested heavily in new manufacturing facilities there.

The European Union proposed a constitution that would centralize powers at the Union level and decrease the powers of individual member countries. It also would create a single voice in world affairs by creating a post of foreign minister. The constitution also gave the EU control over political asylum, immigration, guaranteed freedom of speech, and collective labor bargaining. In order to become law, each EU country had to ratify the constitution. The two most powerful countries in the EU, France and Germany, voted "no" in the summer of 2005. Citizens of both countries were afraid that the constitution would draw jobs away from Western Europe and to the Eastern European EU countries. These new members of the EU have lower wage rates and fewer regulations. Voters were also worried that the constitution would result in free-market reforms along American or British lines over France and Germany's traditional social protections. Concerns over immigration also sparked the referendum vote that is leading to the United Kingdom leaving the European Union.

3.6 Participating in the Global Marketplace

6. How do companies enter the global marketplace?

Companies decide to "go global" for a number of reasons. Perhaps the most urgent reason is to earn additional profits. If a firm has a unique product or technological advantage not available to other international competitors, this advantage should result in major business successes abroad. In other situations, management may have exclusive market information about foreign customers, marketplaces, or market situations. In this case, although exclusivity can provide an initial motivation for going global, managers must realize that competitors will eventually catch up. Finally, saturated domestic markets, excess capacity, and potential for cost savings can also be motivators to expand into international markets. A company can enter global trade in several ways, as this section describes.

Exporting

When a company decides to enter the global market, usually the least complicated and least risky alternative is **exporting**, or selling domestically produced products to buyers in another country. A company, for example, can sell directly to foreign importers or buyers. Exporting is not limited to huge corporations such as General Motors or Apple. Indeed, small companies typically enter the global marketplace by exporting. China is the world's largest exporter, followed by the United States. Many small businesses claim that they lack the money, time, or knowledge of foreign markets that exporting requires. The U.S. Small Business Administration (SBA) now offers the Export Working Capital Program, which helps small and medium-size firms obtain working capital (money) to complete export sales. The SBA also provides counseling and legal assistance for small businesses that wish to enter the global marketplace. Companies such as American Building Restoration Products of Franklin, Wisconsin, have benefited tremendously from becoming exporters. American Building is now selling its chemical products to building restoration companies in Mexico, Israel, Japan, and Korea. Exports account for more than 5 percent of the firm's total sales.

Plenty of governmental help is available when a company decides to begin exporting. Export Assistance Centers (EAC) provide a one-stop resource for help in exporting. Over 700 EACs are placed strategically around the country. Often the SBA is located in the same building as the EAC. The SBA can guarantee loans of $50,000 to $100,000 to help an exporter grow its business. Online help is also available at http://www.ustr.gov. The site lists international trade events, offers international marketing research, and has practical tools to help with every step of the exporting process. Companies considering exporting for the first time can go to http://www.export.gov and get answers to questions such as: What's in it for me? Am I ready for this? What do I have to do? The site also provides a huge list of resources for the first-time exporter.

Licensing and Franchising

Another effective way for a firm to move into the global arena with relatively little risk is to sell a license to manufacture its product to a firm in a foreign country. **Licensing** is the legal process whereby a firm (the *licensor*) agrees to let another firm (the *licensee*) use a manufacturing process, trademark, patent, trade secret, or other proprietary knowledge. The licensee, in turn, agrees to pay the licensor a royalty or fee agreed on by both parties.

International licensing is a multibillion-dollar-a-year industry. Entertainment and character licensing, such as DVD movies and characters such as Batman, is the largest single category. Trademarks are the second-largest source of licensing revenue. Caterpillar licenses its brand for both shoes and clothing, which is very popular in Europe.

U.S. companies have eagerly embraced the licensing concept. For instance, Labatt Brewing Company has a license to produce Miller High Life in Canada. The Spalding Company receives more than $2 million annually from license agreements on its sporting goods. Fruit of the Loom lends its name through licensing to 45 consumer items in Japan alone, for at least 1 percent of the licensee's gross sales.

The licensor must make sure it can exercise sufficient control over the licensee's activities to ensure proper quality, pricing, distribution, and so on. Licensing may also create a new competitor in the long run if the licensee decides to void the license agreement. International law is often ineffective in stopping such actions. Two common ways that a licensor can maintain effective control over its licensees are by shipping one or more critical components from the United States and by locally registering patents and trademarks in its own name.

Franchising is a form of licensing that has grown rapidly in recent years. Many U.S. franchisors operate thousands of outlets in foreign countries. More than half of the international franchises are for fast-food restaurants and business services. McDonald's, however, decided to sell its Chinese stores to a group of outside investors for $1.8 billion, but retained 20 percent of the equity.[32] Having a big-name franchise doesn't always guarantee success or mean that the job will be easy. In China, Home Depot closed its stores after opening 12 to serve the large Chinese population. Had they done market research, they would have known that the majority of urban dwellers live in recently built apartments and that DIY (Do It Yourself) is viewed with disdain in Chinese society, where it is seen as a sign of poverty. When Subway opened its first sandwich shop in China, locals stood outside and watched for a few days. Patrons were so confused that the franchisee had to print signs explaining how to order. Customers didn't believe the tuna salad was made from a fish because they couldn't see the head or tail. And they didn't like the idea of touching their food, so they would hold the sandwich vertically, peel off the paper wrap, and eat it like a banana. Most of all, the Chinese customers didn't want sandwiches.

It's not unusual for Western food chains to adapt their strategies when selling in China. McDonald's, aware that the Chinese consume more chicken than beef, offered a spicy chicken burger. KFC got rid of coleslaw in favor of seasonal dishes such as shredded carrots or bamboo shoots.

Contract Manufacturing

In **contract manufacturing**, a foreign firm manufactures private-label goods under a domestic firm's brand. Marketing may be handled by either the domestic company or the foreign manufacturer. Levi Strauss, for instance, entered into an agreement with the French fashion house of Cacharel to produce a new Levi's line, Something New, for distribution in Germany.

The advantage of contract manufacturing is that it lets a company test the water in a foreign country. By allowing the foreign firm to produce a certain volume of products to specification and put the domestic firm's brand name on the goods, the domestic firm can broaden its global marketing base without investing in overseas plants and equipment. After establishing a solid base, the domestic firm may switch to a joint venture or direct investment, explained below.

Joint Ventures

Joint ventures are somewhat similar to licensing agreements. In a **joint venture**, the domestic firm buys part of a foreign company or joins with a foreign company to create a new entity. A joint venture is a quick and relatively inexpensive way to enter the global market. It can also be very risky. Many joint ventures fail. Others fall victim to a takeover, in which one partner buys out the other.

Sometimes countries have required local partners in order to establish a business in their country. China, for example, had this requirement in a number of industries until recently. Thus, a joint venture was the only way to enter the market. Joint ventures help reduce risks by sharing costs and technology. Often joint ventures will bring together different strengths from each member. In the General Motors-Suzuki joint venture in Canada, for example, both parties have contributed and gained. The alliance, CAMI Automotive, was formed to manufacture low-end cars for the U.S. market. The plant, which was run by Suzuki management, produces the Chevrolet Equinox and the Pontiac Torrent, as well as the new Suzuki SUV. Through CAMI, Suzuki has gained access to GM's dealer network and an expanded market for parts and components. GM avoided the cost of developing low-end cars and obtained models it needed to revitalize the lower end of its product line and its average fuel economy rating. After the successful joint venture, General Motors gained full control of the operation in 2011. The CAMI factory may be one of the most productive plants in North America. There GM has learned how Japanese automakers use work teams, run flexible assembly lines, and manage quality control.

Direct Foreign Investment

Active ownership of a foreign company or of overseas manufacturing or marketing facilities is **direct foreign investment**. Direct investors have either a controlling interest or a large minority interest in the firm. Thus, they stand to receive the greatest potential reward but also face the greatest potential risk. A firm may make a direct foreign investment by acquiring an interest in an existing company or by building new facilities. It might do so because it has trouble transferring some resources to a foreign operation or obtaining that resource locally. One important resource is personnel, especially managers. If the local labor market is tight, the firm may buy an entire foreign firm and retain all its employees instead of paying higher salaries than competitors.

Sometimes firms make direct investments because they can find no suitable local partners. Also, direct investments avoid the communication problems and conflicts of interest that can arise with joint ventures. IBM, in the past, insisted on total ownership of its foreign investments because it did not want to share control with local partners.

General Motors has done very well by building a $4,400 (RMB 29,800) minivan in China that gets 43 miles per gallon in city driving. The Wuling Sunshine has a quarter the horsepower of U.S. minivans, weak acceleration, and a top speed of 81 miles per hour. The seats are only a third of the thickness of seats in Western models, but look plush compared to similar Chinese cars. The minivans have made GM the largest automotive seller in China, and have made China a large profit center for GM.

Walmart now has over 6,000 stores located outside the United States. In 2016, international sales were over $116 billion. About one-third of all new Walmart stores are opened in global markets.

Not all of Walmart's global investments have been successful. In Germany, Walmart bought the 21-store Wertkauf hypermarket chain and then 74 unprofitable and often decrepit Interspar stores. Problems in integrating and upgrading the stores resulted in at least $200 million in losses. Like all other German stores, Walmart stores were required by law to close at 8 p.m. on weekdays and 4 p.m. on Saturdays, and they could not open at all on Sundays. Costs were astronomical. As a result, Walmart left the German retail market.

Walmart has turned the corner on its international operations. It is pushing operational authority down to country managers in order to respond better to local cultures. Walmart enforces certain core principles such as everyday low prices, but country managers handle their own buying, logistics, building design, and other operational decisions.

Global firms change their strategies as local market conditions evolve. For example, major oil companies like Shell Oil and ExxonMobil had to react to dramatic changes in the price of oil due to technological advances such as more efficient automobiles, fracking, and horizontal drilling.

Countertrade

International trade does not always involve cash. Today, countertrade is a fast-growing way to conduct international business. In **countertrade**, part or all of the payment for goods or services is in the form of other goods or services. Countertrade is a form of barter (swapping goods for goods), an age-old practice whose origins have been traced back to cave dwellers. The U.S. Commerce Department says that roughly 30 percent of all international trade involves countertrade. Each year, about 300,000 U.S. firms engage in some form of countertrade. U.S. companies, including General Electric, Pepsi, General Motors, and Boeing, barter billions of goods and services every year. Recently, the Malaysian government bought 20 diesel-powered locomotives from China and paid for them with palm oil.

3.7 Threats and Opportunities in the Global Marketplace

7. What threats and opportunities exist in the global marketplace?

To be successful in a foreign market, companies must fully understand the foreign environment in which they plan to operate. Politics, cultural differences, and the economic environment can represent both opportunities and pitfalls in the global marketplace.

Political Considerations

We have already discussed how tariffs, exchange controls, and other governmental actions threaten foreign producers. The political structure of a country may also jeopardize a foreign producer's success in international trade.

Intense nationalism, for example, can lead to difficulties. **Nationalism** is the sense of national consciousness that boosts the culture and interests of one country over those of all other countries. Strongly nationalistic countries, such as Iran and New Guinea, often discourage investment by foreign companies. In other, less radical forms of nationalism, the government may take actions to hinder foreign operations. France, for example, requires pop music stations to play at least 40 percent of their songs in French. This law was enacted because the French love American rock and roll. Without airtime, American music sales suffer. In another example of nationalism, U.S.-based PPG made an unsolicited bid to acquire Netherlands-based AzkoNobel NV. There was a chorus of opposition from Dutch politicians to the idea of a foreign takeover of AzkoNobel, the Dutch paint manufacturer. The government warned that it would move to defend AzkoNobel from a hostile takeover attempt. AzkoNobel played up the sentiment, tweeting about its rejection of the hostile takeover with the hashtag #DutchPride.

In a hostile climate, a government may *expropriate* a foreign company's assets, taking ownership and compensating the former owners. Even worse is *confiscation,* when the owner receives no compensation. This happened during rebellions in several African nations during the 1990s and 2000s.

Cultural Differences

Central to any society is the common set of values shared by its citizens that determine what is socially acceptable. Culture underlies the family, educational system, religion, and social class system. The network of social organizations generates overlapping roles and status positions. These values and roles have a tremendous effect on people's preferences and thus on marketers' options. For example, in China Walmart holds live fishing contests on the premises, and in South Korea the company hosts a food competition with variations on a popular Korean dish, kimchee.

Language is another important aspect of culture. Marketers must take care in selecting product names and translating slogans and promotional messages so as not to convey the wrong meaning. For example, Mitsubishi Motors had to rename its Pajero model in Spanish-speaking countries because the term refers to a sexual activity. Toyota Motor's MR2 model dropped the *2* in France because the combination sounds like a French swear word. The literal translation of Coca-Cola in Chinese characters means "bite the wax tadpole."

Each country has its own customs and traditions that determine business practices and influence negotiations with foreign customers. For example, attempting to do business in Western Europe during the first two weeks in August is virtually impossible. Businesses close, and everyone goes on vacation at the same time. In many countries, personal relationships are more important than financial considerations. For instance, skipping social engagements in Mexico may lead to lost sales. Negotiations in Japan often include long evenings of dining, drinking, and entertaining; only after a close personal relationship has been formed do business negotiations begin. **Table 3.1** presents some cultural dos and don'ts.

Cultural Dos and Don'ts Guidelines and Examples	
DO:	**DON'T:**
Always present your business card with both hands in Asian countries. It should also be right-side-up and print-side-showing so that the recipient can read it as it is being presented. If you receive a business card, accept it with gratitude and examine it carefully. Don't quickly put it into your pocket. Use a "soft-sell" and subtle approach when promoting a product in Japan. Japanese people do not feel comfortable with America's traditional hard-selling style. Understand the role of religion in business transactions. In Muslim countries, Ramadan is a holy month when most people fast. During this time everything slows down, particularly business. Have a local person available to culturally and linguistically interpret any advertising that you plan to do. When American Airlines wanted to promote its new first-class seats in the Mexican market, it translated the "Fly in Leather" campaign literally, which meant "Fly Naked" in Spanish.	Glad-hand, back-slap, and use first names on your first business meeting in Asia. If you do, you will be considered a lightweight. Fill a wine glass to the top if dining with a French businessperson. It is considered completely uncouth. Begin your first business meeting in Asia talking business. Be patient. Let your clients get to know you first.

Table 3.1

Economic Environment

The level of economic development varies considerably, ranging from countries where everyday survival is a struggle, such as Sudan and Eritrea, to countries that are highly developed, such as Switzerland and Japan. In general, complex, sophisticated industries are found in developed countries, and more basic industries are found in less developed nations. Average family incomes are higher in the more developed countries than in the least-developed markets. Larger incomes mean greater purchasing power and demand, not only for consumer goods and services but also for the machinery and workers required to produce consumer goods. **Table 3.2** provides a glimpse of global wealth.

Business opportunities are usually better in countries that have an economic infrastructure in place. **Infrastructure** is the basic institutions and public facilities upon which an economy's development depends. When we think about how our own economy works, we tend to take our infrastructure for granted. It includes the money and banking system that provide the major investment loans to our nation's businesses; the educational system that turns out the incredible varieties of skills and basic research that actually run our nation's production lines; the extensive transportation and communications systems—interstate highways, railroads, airports, canals, telephones, internet sites, postal systems, and television stations—that link almost every piece of our geography into one market; the energy system that powers our factories; and, of course, the market system itself, which brings our nation's goods and services into our homes and businesses.

Where the Money Is	
The Top 20	**Gross National Income Per Capita* US$**
Luxembourg	103,199
Switzerland	79,243
Norway	70,392
Ireland	62,562
Qatar	60,787
Iceland	59,629
United States	57,436
Denmark	53,744
Singapore	52,961
Australia	51,850
Sweden	51,165
San Marino	46,447
Netherlands	45,283
Austria	44,498
Finland	43,169
Canada	42,210

Gitman, L. J., McDaniel, C., Shah, A., Reece, M., Koffel, L., Talsma, B., & Hyatt, J. C. (2018). *Introduction to business*. OpenStax. https://openstax.org/books/introduction-business/pages/1-introduction

Where the Money Is	
The Top 20	**Gross National Income Per Capita* US$**
Germany	41,902
Belgium	41,283
United Kingdom	40,096
Japan	38,912
The Bottom Five	
Madagascar	391
Central African Republic	364
Burundi	325
Malawi	295
South Sudan	233
* **Gross National Income** is the value of the final goods and services produced by a country (Gross Domestic Product) together with its income received from other countries (such as interest and dividends) less similar payments made to other countries.	
Final goods are the goods ultimately consumed rather than used in the production of another good. For example, a car sold to a consumer is a final good; the components, such as tires sold to the car manufacturer, are not. They are intermediate goods used to make the final good. The same tires, if sold to a consumer, would be a final good.	
Sources: Some data refers to IMF staff estimates and some are actual figures for the year 2017, made on April 12, 2017. Adapted from the World Economic Outlook Database—April 2017, International Monetary Fund, accessed on April 18, 2017.	

Table 3.2

3.8 The Impact of Multinational Corporations

8. What are the advantages of multinational corporations?

Corporations that move resources, goods, services, and skills across national boundaries without regard to the country in which their headquarters are located are **multinational corporations**. Some are so rich and have so many employees that they resemble small countries. For example, the sales of both Exxon and Walmart are larger than the GDP of all but a few nations in the world. Multinational companies are heavily engaged in international trade. The successful ones take political and cultural differences into account.

Many global brands sell much more outside the United States than at home. Coca-Cola, Philip Morris's Marlboro brand, Pepsi, Kellogg, Pampers, Nescafe, and Gillette, are examples.

The Fortune 500 made over $1.5 trillion in profit in 2016. In slow-growing, developed economies like Europe and Japan, a weaker dollar helps, because it means cheaper products to sell into those markets, and profits earned in those markets translate into more dollars back home. Meanwhile, emerging markets in Asia, Latin America, and Eastern Europe are growing steadily. General Electric expects 60 percent of its revenue growth to come from emerging markets over the next decade. For Brown-Forman, the spirits

"Access for free at openstax.org."
Gitman, L. J., McDaniel, C., Shah, A., Reece, M., Koffel, L., Talsma, B., & Hyatt, J. C. (2018). *Introduction to business*. OpenStax. https://openstax.org/books/introduction-business/pages/1-introduction

company, a fifth of its sales growth of Jack Daniels, the Tennessee whiskey, is coming from developing markets like Mexico and Poland. IBM had rapid sales growth in emerging markets such as Russia, India, and Brazil.

The largest multinational corporations in the world are shown in **Table 3.3**.

Despite the success of American multinationals abroad, there is some indication that preference for U.S. brands may be slipping.

Exhibit 3.7 As overseas investment grows, so does the need for global branding. The Wisconsin National Guard picked NBA star Giannis Antetokounmpo to be the face of its recruiting and marketing effort. Recognizable to NBA fans the world over, Antetokounmpo personifies a youthful, dynamic spirit that transcends cultural and geographic boundaries. *Why is it increasingly important that multinational advertisers identify and sign celebrity spokespersons capable of bridging different cultures?* (Credit: Erik Drost/ Flickr/ Attribution-ShareAlike 2.0 Generic (CC BY 2.0))

The Multinational Advantage

Large multinationals have several advantages over other companies. For instance, multinationals can often overcome trade problems. Taiwan and South Korea have long had an embargo against Japanese cars for political reasons and to help domestic automakers. Yet Honda USA, a Japanese-owned company based in the United States, sends Accords to Taiwan and Korea. In another example, when the environmentally conscious Green movement challenged the biotechnology research conducted by BASF, a major German chemical and drug manufacturer, BASF moved its cancer and immune-system research to Cambridge, Massachusetts.

Another advantage for multinationals is their ability to sidestep regulatory problems. U.S. drugmaker SmithKline and Britain's Beecham decided to merge in part so that they could avoid licensing and regulatory hassles in their largest markets. The merged company can say it's an insider in both Europe and the United States. "When we go to Brussels, we're a member state [of the European Union]," one executive explains. "And when we go to Washington, we're an American company."

Exhibit 3.8 South Korea's Samsung is a leading manufacturer of giant high-definition TVs. Samsung produces the largest curved ultra-high-definition (UHD) screens for the worldwide home-theater market. Samsung's monster 110-inch curved UHD screen is among the world's largest such screens. Unfortunately, for most of the world's consumers, the giant Samsung TVs can be too costly, but the 88-inch version can be purchased for under $20,000. *How does being a multinational corporation enable Samsung to succeed in the high-end electronics market?* (Credit: Chris F/ Flickr/ Attribution 2.0 Generic (CC BY 2.0))

Multinationals can also shift production from one plant to another as market conditions change. When European demand for a certain solvent declined, Dow Chemical instructed its German plant to switch to manufacturing a chemical that had been imported from Louisiana and Texas. Computer models help Dow make decisions like these so it can run its plants more efficiently and keep costs down.

The World's Top 11 Largest Multinational Corporations			
RANK	COMPANY	Revenues ($M)	Home Country
1	Walmart	$482,130	United States
2	State Grid	$329,601	China
3	China National Petroleum	$299,271	China
4	Sinopec Group	$294,344	China
5	Royal Dutch Shell	$272,156	Netherlands
6	Exxon Mobil	$246,204	United States
7	Volkswagen	$236,600	Germany
8	Toyota Motor	$236,592	Japan
9	Apple	$233,715	United States
10	BP	$225,982	United Kingdom
11	Berkshire Hathaway	$210,821	United States

Table 3.3 Source: Adapted from "The World's Largest Corporations," *Fortune* http://fortune.com/global500/, accessed June 30, 2017.

Multinationals can also tap new technology from around the world. In the United States, Xerox has introduced some 80 different office copiers that were designed and built by Fuji Xerox, its joint venture with a Japanese company. Versions of the super-concentrated detergent that Procter & Gamble first formulated in Japan in response to a rival's product are now being sold under the Ariel brand name in Europe and under the Cheer and Tide labels in the United States. Also, consider Otis Elevator's development of the Elevonic 411, an elevator that is programmed to send more cars to floors where demand is high. It was developed by six research centers in five countries. Otis's group in Farmington, Connecticut, handled the systems integration, a Japanese group designed the special motor drives that make the elevators ride smoothly, a French group perfected the door systems, a German group handled the electronics, and a Spanish group took care of the small-geared components. Otis says the international effort saved more than $10 million in design costs and cut the process from four years to two.

Finally, multinationals can often save a lot in labor costs, even in highly unionized countries. For example, when Xerox started moving copier-rebuilding work to Mexico to take advantage of the lower wages, its union in Rochester, New York, objected because it saw that members' jobs were at risk. Eventually, the union agreed to change work styles and to improve productivity to keep the jobs at home.

3.9 Trends in Global Competition

9. What are the trends in the global marketplace?

In this section, we will examine several underlying trends that will continue to propel the dramatic growth in world trade. These trends are market expansion, resource acquisition, and the emergence of China and India.

Market Expansion

The need for businesses to expand their markets is perhaps the most fundamental reason for the growth in world trade. The limited

Gitman, L. J., McDaniel, C., Shah, A., Reece, M., Koffel, L., Talsma, B., & Hyatt, J. C. (2018). *Introduction to business*. OpenStax. https://openstax.org/books/introduction-business/pages/1-introduction

size of domestic markets often motivates managers to seek markets beyond their national frontiers. The economies of large-scale manufacturing demand big markets. Domestic markets, particularly in smaller countries like Denmark and the Netherlands, simply can't generate enough demand. Nestlé was one of the first businesses to "go global" because its home country, Switzerland, is so small. Nestlé was shipping milk to 16 different countries as early as 1875. Today, hundreds of thousands of businesses are recognizing the potential rich rewards to be found in international markets.

Resource Acquisition

More and more companies are going to the global marketplace to acquire the resources they need to operate efficiently. These resources may be cheap or skilled labor, scarce raw materials, technology, or capital. Nike, for example, has manufacturing facilities in many Asian countries in order to use cheaper labor. Honda opened a design studio in southern California to put that "California flair" into the design of some of its vehicles. Large multinational banks such as Bank of New York and Citigroup have offices in Geneva, Switzerland. Geneva is the private banking center of Europe and attracts capital from around the globe.

The Emergence of China and India

China and India—two of the world's economic powerhouses—are impacting businesses around the globe, in very different ways. The boom in China's worldwide exports has left few sectors unscathed, be they garlic growers in California, jeans makers in Mexico, or plastic-mold manufacturers in South Korea. India's impact has altered how hundreds of service companies from Texas to Ireland compete for billions of dollars in contracts.

The causes and consequences of each nation's growth are somewhat different. China's exports have boomed largely thanks to foreign investment: lured by low labor costs, big manufacturers have surged into China to expand their production base and push down prices globally. Now manufacturers of all sizes, making everything from windshield wipers to washing machines to clothing, are scrambling either to reduce costs at home or to outsource more of what they make in cheaper locales such as China and India.

Indians are playing invaluable roles in the global innovation chain. Hewlett-Packard, Cisco Systems, and other tech giants now rely on their Indian teams to devise software platforms and multimedia features for next-generation devices. Google principal scientist Krishna Bharat set up the Google Bangalore lab complete with colorful furniture, exercise balls, and a Yamaha organ—like Google's Mountain View, California, headquarters—to work on core search-engine technology. Indian engineering houses use 3-D computer simulations to tweak designs of everything from car engines and forklifts to aircraft wings for such clients as General Motors Corp. and Boeing Co. Barring unforeseen circumstances, within five years India should vault over Germany as the world's fourth-biggest economy. By mid-century, China should overtake the United States as number one. By then, China and India could account for half of global output.

An accelerating trend is that technical and managerial skills in both China and India are becoming more important than cheap assembly labor. China will stay dominant in mass manufacturing and is one of the few nations building multibillion-dollar electronics and heavy industrial plants. India is a rising power in software, design, services, and precision industry.