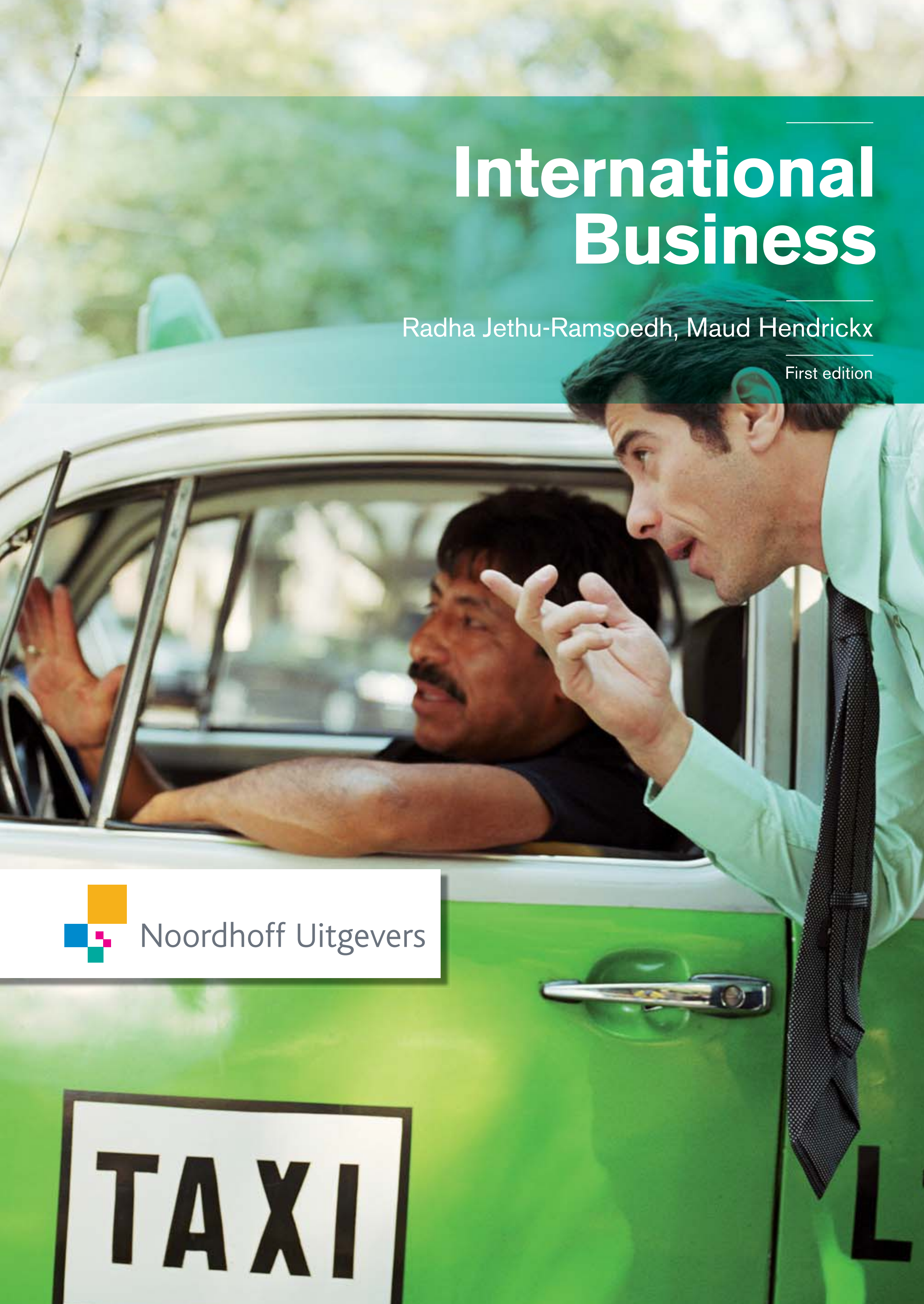
International Business

Radha Jethu-Ramsoedh, Maud Hendrickx

First edition



Noordhoff Uitgevers

International Business

An introduction

Radha Jethu-Ramsoedh LLM
Maud Hendrickx Bsc

First edition

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Preface

The open nature of the economy and the internationalisation of trade and industry have resulted in a growing need for well-trained students with a broad knowledge of the different aspects of international business. In our opinion, a book for English-language bachelor courses in higher education describing the basic principles of international business was not available. Therefore, we deemed it necessary to compile a guideline that provides an introduction to international business for students who encounter the subject regularly in their curriculum. Students are made aware of the fact that international business transactions are not only based on abstract theories, but that day-to-day reality plays an important part as well. Facts, figures and relevant case studies have been added to explain the text material.

Theories and general principles serve as an introductory explanation of the dynamic international environment. The book has been written in industry-wide terms, which means the book provides suitable textmaterial for various forms of higher professional training, in which international business, international trade, international management and globalisation are part of the curriculum. As nearly all companies have suppliers or customers of foreign origin, this book is recommended to anyone working in an international company with hardly any expertise in the field of conducting business in an international environment.

We would appreciate receiving remarks and comments of students and lecturers so that we can improve the quality level of this book. Finally, we would like to express our thanks to all those who have supported us with their advice and suggestions: Martin Zuurhout MBA (Martin Delta), Louise van Weerden (Saxion University, the Netherlands) Sharro Jethu (Optimal Synergy), Marijn Mulders (Avans University of Applied Sciences, the Netherlands), Hendrie van Maanen (Christian University of Applied Sciences, the Netherlands), Ron Harmsen (Radio Gelderland), Vishwa Jethu, Jennifer Evans (students of the Economics & Business Faculty at the Utrecht University, the Netherlands) and our colleagues at the European Fashion Business School. Furthermore, we wish to thank all those from the business community who offered us practical advice: Eric Verbeek (AON Insurance company). A special word of thanks goes to Irene Sueters, Reshmi Nannan Panday and Ageeth Bergsma (Noordhoff Publishers) our excellent coach, and to our families for their encouragement.

Radha Jethu-Ramsoedh
Maud Hendrickx

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Effective studying

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Apple admits to using child labour

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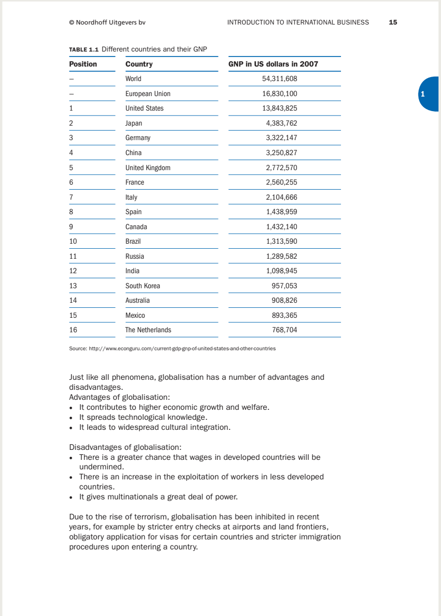
Apple has admitted that child labour was used at the factories that build its computers, iPods and mobile phones. At least eleven 15-year-old children were discovered to be working in three factories that supply Apple last year.
The company did not name the offending factories, or say where they were based, but the majority of its goods are assembled in China. Apple also has factories in Taiwan, Singapore, the Philippines, Malaysia, Thailand, the Czech Republic and the United States.
Apple said the child workers are now no longer being used, or are no longer underage. "In each of the three facilities, we required a review of all employment records for the year as well as a complete analysis of the hiring process to clarify how underage people had been able to gain employment," Apple said, in an annual report on its suppliers.
Apple has been repeatedly criticized for using factories that abuse workers and where conditions are poor. Last year, an employee at Foxconn, the Taiwanese company that is one of Apple's biggest suppliers, committed suicide after being accused of stealing a prototype for the iPhone.
China Labor Watch, a New York-based NGO, accused Foxconn of having an "inhumane and militant" management, which neglects basic human rights. Apple admitted that at least 55 of the 102 factories that produce its goods were ignoring Apple's rule that staff cannot work more than 60 hours a week.
The technology companies own guidelines are already in breach of China's widely ignored labour law, which sets out a maximum 49-hour week for workers. Apple also said that one of its factories had repeatedly falsified its records. "When we investigated, we uncovered records and conducted worker interviews that revealed excessive working hours and seven days of continuous work." Only 65 per cent of the factories were paying their staff the correct wages and benefits, and Apple found 24 factories where workers had not even been paid China's minimum wage of around 800 Yuan a month.

Edited source: The Telegraph, 27 February 2010

Case at the beginning of each chapter



© Noordhoff Uitgevers bv INTRODUCTION TO INTERNATIONAL BUSINESS 15

TABLE 1.1 Different countries and their GNP

Position	Country	GNP in US dollars in 2007
–	World	54,311,608
–	European Union	16,830,100
1	United States	13,843,825
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6	France	2,560,255
7	Italy	2,104,666
8	Spain	1,438,959
9	Canada	1,432,140
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11	Russia	1,289,582
12	India	1,098,945
13	South Korea	957,053
14	Australia	908,826
15	Mexico	893,365
16	The Netherlands	768,704

Source: http://www.econguru.com/current-gdp-gnp-of-united-states-and-other-countries

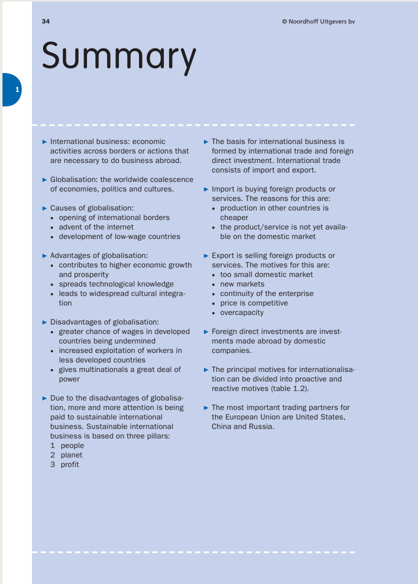
1

Just like all phenomena, globalisation has a number of advantages and disadvantages.
Advantages of globalisation:
- It contributes to higher economic growth and welfare.
- It spreads technological knowledge.
- It leads to widespread cultural integration.

Disadvantages of globalisation:
- There is a greater chance that wages in developed countries will be undermined.
- There is an increase in the exploitation of workers in less developed countries.
- It gives multinationals a great deal of power.

Due to the rise of terrorism, globalisation has been inhibited in recent years, for example by stricter entry checks at airports and land frontiers, obligatory application for visas for certain countries and stricter immigration procedures upon entering a country.

Facts and figures from international industry



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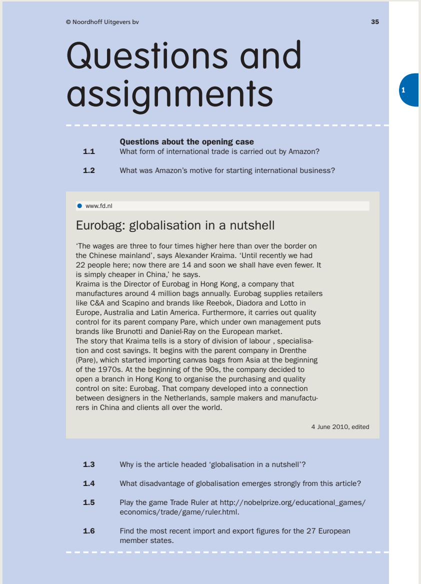
Summary

1

- International business: economic activities across borders or actions that are necessary to do business abroad.
- Globalisation: the worldwide coalescence of economies, politics and cultures.
- Causes of globalisation:
  - opening of international borders
  - advent of the internet
  - development of low-wage countries
- Advantages of globalisation:
  - contributes to higher economic growth and prosperity
  - spreads technological knowledge
  - leads to widespread cultural integration
- Disadvantages of globalisation:
  - greater chance of wages in developed countries being undermined
  - increased exploitation of workers in less developed countries
  - gives multinationals a great deal of power
- Due to the disadvantages of globalisation, more and more attention is being paid to sustainable international business. Sustainable international business is based on three pillars:
  1 people
  2 planet
  3 profit
- The basis for international business is formed by international trade and foreign direct investment. International trade consists of import and export.
- Import is buying foreign products or services. The reasons for this are:
  - production in other countries is cheaper
  - the product/service is not yet available on the domestic market
- Export is selling foreign products or services. The motives for this are:
  - too small domestic market
  - new markets
  - continuity of the enterprise
  - price is competitive
  - overcapacity
- Foreign direct investments are investments made abroad by domestic companies.
- The principal motives for internationalisation can be divided into proactive and reactive motives (table 1.2).
- The most important trading partners for the European Union are United States, China and Russia.

Summary



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Questions and assignments

1

Questions about the opening case

1.1 What form of international trade is carried out by Amazon?

1.2 What was Amazon's motive for starting international business?

www.fd.nl

Eurobag: globalisation in a nutshell

'The wages are three to four times higher here than over the border on the Chinese mainland', says Alexander Kraima. 'Until recently we had 22 people here; now there are 14 and soon we shall have even fewer. It is simply cheaper in China,' he says.
Kraima is the Director of Eurobag in Hong Kong, a company that manufactures around 4 million bags annually. Eurobag supplies retailers like C&A and Scapino and brands like Reebok, Diadora and Lotto in Europe, Australia and Latin America. Furthermore, it carries out quality control for its parent company Pare, which under own management puts brands like Brunotti and Daniel-Ray on the European market.
The story that Kraima tells is a story of division of labour , specialisation and cost savings. It begins with the parent company in Drenthe (Pare), which started importing canvas bags from Asia at the beginning of the 1970s. At the beginning of the 90s, the company decided to open a branch in Hong Kong to organise the purchasing and quality control on site: Eurobag. That company developed into a connection between designers in the Netherlands, sample makers and manufacturers in China and clients all over the world.

4 June 2010, edited

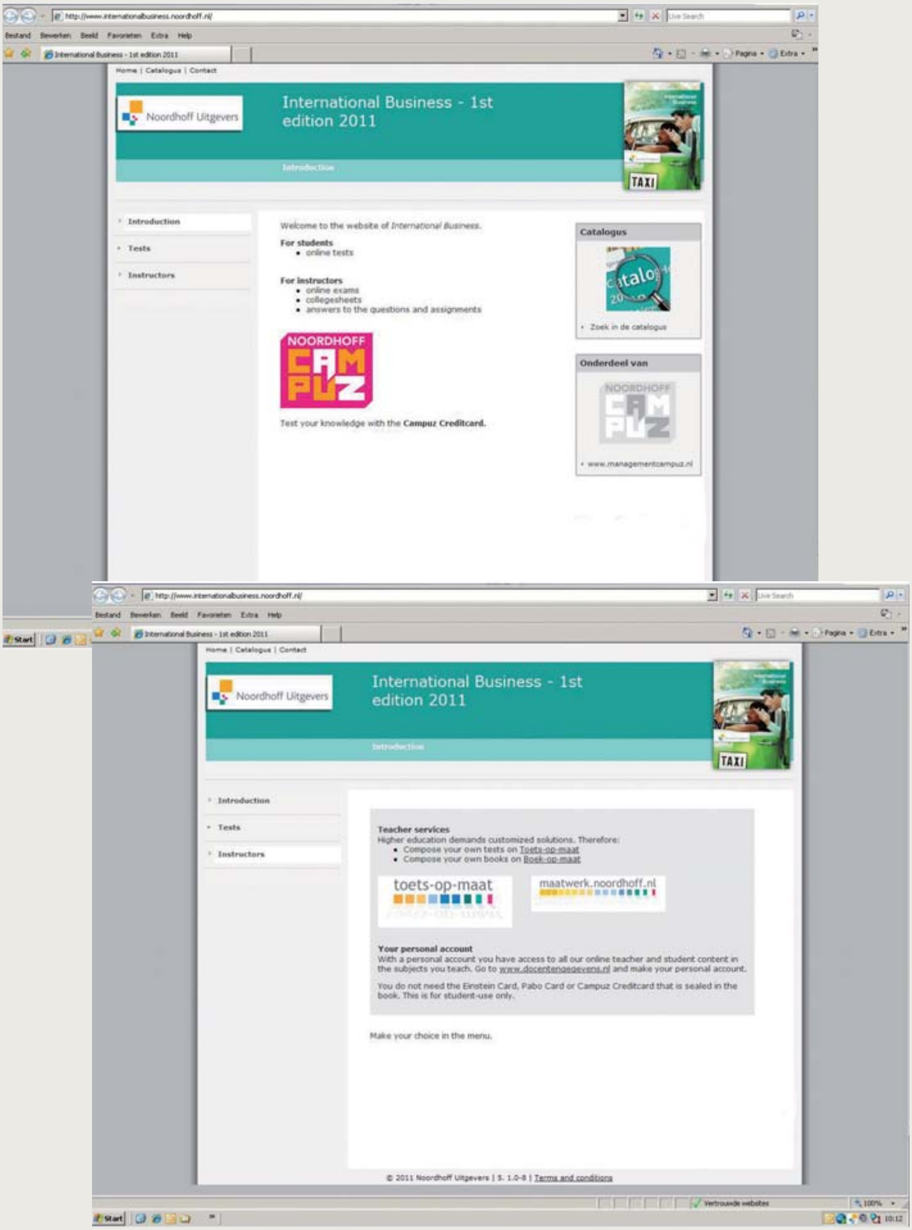
1.3 Why is the article headed 'globalisation in a nutshell'?

1.4 What disadvantage of globalisation emerges strongly from this article?

1.5 Play the game Trade Ruler at http://nobelprize.org/educational_games/economics/trade/game/ruler.html.

1.6 Find the most recent import and export figures for the 27 European member states.

Questions and assignments in each chapter



website www.internationalbusiness.noordhoff.nl with test questions for students.

1 Introduction to international business

In this introductory chapter, we discuss the essence of international business and its context. Furthermore, we look at what motivates companies to cross borders. A number of terms that will repeatedly occur in this book, such as import and export, are discussed here. Finally, we zoom in on the performance of the European Union member states concerning international business.

1

Amazon seeks to expand globally

Amazon says it plans to revamp its international e-commerce platform to make it easier for the company to reach customers in new markets.
The online retailer, the world's largest by number of visitors, operates online businesses in six countries outside the US. It says it has set up a new team that will create "the architectural underpinnings to greatly simplify country expansions", by translating content into different languages and adjusting taxes, prices and delivery options to better suit customers' locations.
The move underlines the increasing globalisation of online retailing, as companies such as Gap, the US clothing retailer, and Walmart, the world's largest retailer by sales, seek to use e-commerce sites and cross-border shipping to reach a wider audience.
Walmart, one of Amazon's main online rivals in the US, has invested heavily in a global e-commerce platform over the past two years, which it says it plans to use to reach customers both in existing markets and in countries where it has no physical stores.

Japan's largest online retailer, Rakuten, has also recently acquired or launched sites in the US, Europe and China for its Ebay-style online marketplaces.
Amazon operates websites in Canada, China, Japan, the UK, Germany and France, and offers customers ordering from other countries the ability to pay for purchases in their own currencies. But it has not entered a new country since 2004, when it acquired Joyo.com, its Chinese site. Instead, it has focused on steadily expanding the new product categories on its range of global sites.
The retailer is now seeking to recruit senior software engineers for what it says is "a new team that is gearing up to make a substantial impact on how Amazon does business around the world".
A job posting says the team is "tackling interesting problems like rendering content in multiple languages and calculating tax, price and shipping variations on the fly based on the customer's preferred shipping destination".
Gap has recently launched a UK-based e-commerce site aimed both at the UK and other western European countries, although customers can only pay in sterling, not Euros. Gap has recently launched its first e-commerce sites in Canada and China, while Walmart has said it will shortly open an e-commerce site for its Sam's Club discount warehouse stores in China. Marks and Spencer, the UK general retailer, has said it hopes to use e-commerce to expand its international sales, once its current agreement to rely on a site run by Amazon expires in 2013. Tesco, the UK supermarket group, also said this month that it planned to open e-commerce sites in China, Poland and the Czech Republic.

Edited source: www.ft.com, 23 December 2010

1.1 What is international business?

If European consumers consider the origin of their products, they rapidly become aware that few products are manufactured in Europe. 'Made in China' is a common label in or on various products. The market for products and services is not limited to European borders, but extends across the whole world. Furthermore, there are many foreign companies that operate worldwide. These companies are called multinationals. They include Daimler, Suez, BP en Metro. But even small and medium-size companies are not limited to doing business in their own country any longer. Gradually small companies are venturing across their national borders: for example, through web shops that are set up abroad.

www.bndestem.nl

Source: Qilai Shen/EPA

Made in China

SHANGHAI – A man waits for the opening of the 20th East China Fair in Shanghai among an array of colourful storage jars.
With around 6,000 exhibitors, this is China's largest trade show for consumer articles and is primarily focused on export. Last year, around 50,000 buyers from more than 100 countries came to the show.

4 March 2010

1

International business

Low-wage countries

International business is a broad definition. It covers more than marketing and selling goods and services abroad. It is also related to the development of international commerce or the actions that are necessary to do business on an international level. Companies increasingly seek collaborations with partners abroad. They outsource activities to low-wage countries to increase their productivity or reduce their labour costs. They share knowledge with foreign partners to obtain a stronger competitive position, or they work with others to realise economies of scale. Since international business is much more complicated than national business, we wish to focus with as many aspects as possible which differ from domestic business practice.

1.1.1 Globalisation

Globalisation

Why has international business expanded so enormously? Due to the opening of borders, it has become increasingly easy to buy products or services from, or sell them to, other countries. The advent of the internet has made a significant contribution to this. It has become easier and cheaper to be connected worldwide. Due to the industrialisation process of low-wage countries such as China, India and Bangladesh, manufacturing can be done more cheaply. Globalisation does refer to goods and services but also to capital, knowledge and labour which find their way around the globe. Due to the abolition of frontiers, people travel more than ever. Because of this, political systems, economies and cultures influence each other. This can be seen in metropolises: more and more cities are starting to look alike. Look, for example, at McDonald's, which has an outlet in every metropolis.

Gross National Product

BRIC countries

The last ten years often referred to as 'the age of globalisation'. However, globalisation is not a phenomenon of recent decades. Nevertheless, its development has changed in the last decade. Considering the growth of the Gross National Product (GNP) of countries together, we notice that more than half of this growth comes from the new industrial countries (emerging markets). These countries play an increasingly important role in globalisation – the BRIC countries (Brazil, Russia, India and China) in particular, where enormous growth in GNP is expected in the coming years. This is in contrast to Western countries, whose economies have stagnated, due to the effects of the current credit crisis.

Gross National Product (GNP)

The extent to which a country participates in international trade depends primarily on its GNP. The Gross National Product of a country is the total of what is produced in that country in terms of goods and services by firms that are nationally owned, plus the income derived from nationally-owned firms abroad, which is received as a reward for making production facilities available. GNP is an important measure of the economic performance of a country. Table 1.1 lists several countries and their GNP.

TABLE 1.1 Different countries and their GNP

Position	Country	GNP in US dollars in 2007
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Source: http://www.econguru.com/current-gdp-gnp-of-united-states-and-other-countries

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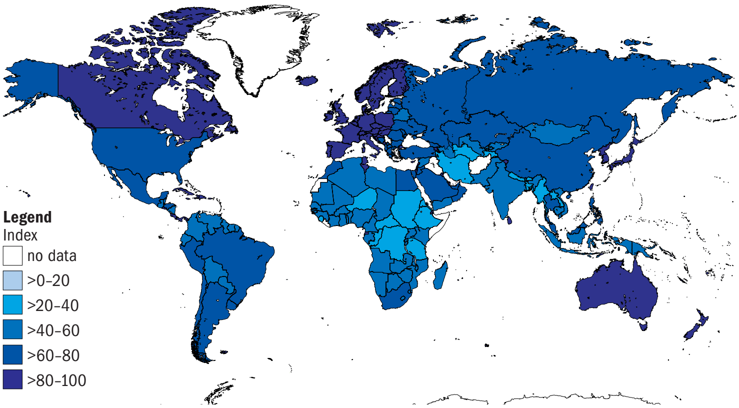
Due to the rise of terrorism, globalisation has been inhibited in recent years, for example by stricter entry checks at airports and land frontiers, obligatory application for visas for certain countries and stricter immigration procedures upon entering a country.

1

1.1.2 Europe and globalisation

How globalised is Europe, with its open and developed economy and multicultural society? From figure 1.1 it can be observed that Europe is very globalised.

FIGURE 1.1 KOF Index of Globalisation 2007



Source: http://globalization.kof.ethz.ch/map/#

From an investigation by the KOF Swiss Economic Institute in 2010, it seems that Belgium comes first in the globalization stakes. Austria, which was in 3rd place last year, now ranks 2nd. The Netherlands ranks 3rd. This year's fast climber is Luxembourg, which advanced from 21st place to 14th place. Switzerland still comes 4th on the globalization index. The emerging markets in Eastern Europe and Central Asia are recording the biggest jump on the KOF Globalization Index. Although the degree of globalization is highest in the industrialised nations and Western Europe, it has stagnated for quite some time. In East Asia and the Pacific region, the globalization process has slowed down compared to the previous year, while index rankings actually went down in the Near East and North Africa.

While economic and political globalization is advancing, social globalization is stagnating. The economic dimension of the KOF Index quantifies not only actual trade and investment flows, but also the extent to which countries protect themselves by imposing restrictions on trade and capital movements. The social dimension of globalization reflects the flow of ideas and information, while the political dimension examines the degree of political cooperation between countries.

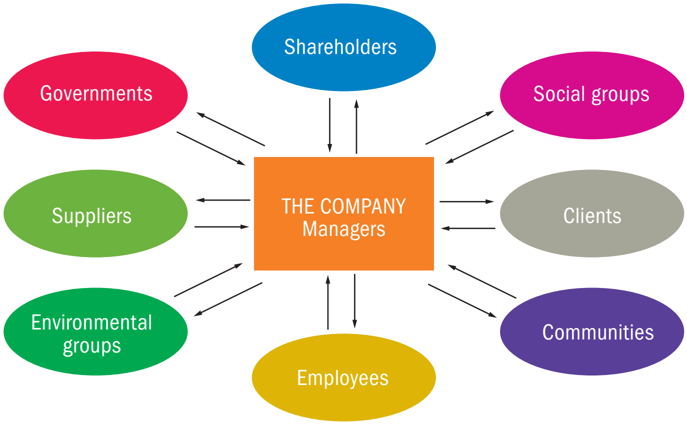
1.1.3 Sustainable international business

The globalisation has placed pressures on the global environment and natural resources and exposing human dependence on our environment. Hence, this book focuses on sustainable international business, which makes companies conscious of the way in which they do business and the consequences, not only for mankind and the environment, but also for society.

Sustainable international business

The core of sustainable international business is the stakeholder. A stakeholder is a group or individual who influences or is influenced by an organisation or company. Figure 1.2 gives an overview of the types of stakeholder in a company. **Stakeholder**

FIGURE 1.2 Overview of Stakeholders



Source: derived from Donaldson & Preston, 1995

Shareholders often focus only on economic results. Not all stakeholders have the same priority. Hence, as well as profit, business should embrase sustainability for innovation and business growth. Therefore, sustainable international business consists of three pillars, namely:
1 People
2 Planet
3 Profit

Ad 1 People

'People' relates to the human side of sustainable international business. It covers people inside and outside the companies, and aspects such as health and safety in the workplace, employment laws, human rights, wages, training and child labour. This is an important pillar, especially when production takes place in low-wage countries, where working conditions are often poor. **People**

Ad 2 Planet

'Planet' means care for the environment. Because our natural resources are becoming exhausted, we shall have to look for alternatives. Aspects such as the efficient use of raw materials and waste management are part of this pillar. A lot of attention has recently been paid to recycling, where products are made from components that can be re-used after the lifetime of the original product. **Planet**

Ad 3 Profit

Of course, profit is a condition for the continuation of an enterprise, but a number of other important aspects contribute towards its prosperity. 'Profit' therefore includes aspects such as location policy, profitability, profit appropriation, dividend distribution, sponsoring and charity policy. **Profit**

For companies, the challenge is to find a good balance among these three pillars, referred to as the triple bottom line.

Due to increasing globalisation, more and more products are produced abroad, and it is not always clear where the raw materials for these products come from. We also do not always know under what circumstances they have been produced. More and more companies accept responsibility for the whole production chain, and therefore more and more companies are participating in 'fair trade' – in the coffee and clothing sector, for example. These 'fair trade' products are made from raw materials for which a fair price has been paid, from which farmers can earn a living. The production process is monitored, and therefore undesirable factors such as child labour and poor working conditions can be avoided. In short, sustainable business does not cease at the home frontier!

Source: http://fairtradelifestyle.files.wordpress.com/2009/05/world-fair-trade-day-logo.jpg

1.2 Why do companies cross borders?

If companies do business abroad, they internationalise. Why do companies make this choice? We will discuss this in this section. First, the basis for international business, international trade, will be explained. Next we will look at another aspect of internationalisation, namely foreign investment. In conclusion, the motives for companies to do business internationally will be explained.

1.2.1 International trade

International trade

As indicated previously, the basis for internationalisation is often the trade of goods or services, called international trade. Europe has been familiar with this throughout history, for example through the trade in spices. European countries have had good trade relations with some countries for centuries.

ECONOMIST, 17 DECEMBER 1998

The history of spices is the history of trade

SOON after dawn on May 21st 1498, Vasco da Gama and his crew arrived at Calicut after the first direct sea voyage from Europe to Asia. If history's modern age has a beginning, this is it. Europe's ignorance of, and isolation from, the cosmopolitan intellectual and commercial life of Asia were ended forever. With ships, weaponry and a willingness to use them both, the countries of Europe were about to colonize the rest of the world. To support this expansion, its merchant classes would invent new forms of commercial credit and the first great corporations, vital parts of capitalism's operating system, and spread their trading networks across the seven seas. And what did the men shout as they came ashore? "For Christ and spices!" Today spices are chiefly flavourings for food, but a hundred other uses have contributed to the demand through history. In ancient Egypt cassia and cinnamon fetched a high price because they were essential for embalming; so too were anise, marjoram and cumin, used to rinse out the innards of the worthy dead. Hammurabi's legal code, which called for severe punishment of sloppy or unsuccessful surgeons, did much to encourage the use of medicinal spices in Sumeria.

Why does international trade arise?
International trade has existed since time immemorial, but only in the last 250 years have theories about it arisen. In the past, people attempted to explain the origin of international trade from an economic viewpoint.
The classic economists soon came to the conclusion that macro-economic conditions in the home market – such as national income, the employment situation, national consumption, investment and general price levels – could partly determine international competitive strength.

The viewpoint of (neo-)classical economists was that the origin of international trade can best be explained in terms of differences in (cost) prices and productivity between countries. The country that can manufacture products at the lowest cost will sell them to other countries. After theories of absolute and comparative costs (Ricardo 1817) came Heckscher and Ohlin (1933) with the viewpoint that the availability and cost of production facilities determined the extent of international trade. In this way, India, which in comparison to Switzerland has a large amount of labour available, must concentrate on the production of labour-intensive goods. Switzerland, with more capital than labour, must specialise in capital-intensive products. Modern trade theories, which have been introduced in the past 40 years, emphasize factors other than price elements, such as quality, economies of scale, knowledge, technological development and product differentiation.

The traditional theories, according to Kol and Mennes (1989), are most successful at explaining why there is international trade but they can only partly explain the differences in competitive strength between countries.
In 1990, in his book *The Competitive Advantage of Nations*, Porter tried to build a bridge between the viewpoints of the neo-classicists and modern trade theories. In his explanation of national competitive strength, Porter does not concentrate on any one factor at macro level but on several factors at meso level (industrial branch level). The following factors are involved in distinguishing among sectors:
- the extent and nature of domestic competition
- the presence of an adequate supply industry
- the conditions in the home market (infrastructure, capital, labour)
- the demand level (responding to the diversity in customer demand)

Because of these factors, it is possible that some industrial branches remain largely confined to their home country while others internationalise at an early stage. Ilustrations include computers (Silicon Valley in the United States), logistics (Rotterdam in the Netherlands), software outsourcing (Bangalore in India) and fashion (Paris in France).

There are different types of international trade, which are explained below:
- import
- export

These terms often appear in this book.

Import

Import

Importing is buying foreign products, which are shipped into the home country. A company buys goods or services from an exporting company with the objective of selling them at a profit. Because the world is becoming ever smaller, there are products or components on the shelves that have been manufactured thousands of kilometres away. This can happen for two reasons:

- The production of goods or components is cheaper in other countries, as a result of which products are often developed in Europe and produced in that particular country. This occurs for various reasons:
  - In the country of origin, labour costs are lower than in Europe.
  - The raw materials are easily available in the country of origin. The processing of the raw materials in the country of origin not only produce time benefits, it also has the advantage that the knowledge that is necessary for the production of the product is available on site.
- The product or service has not been supplied in Europe.

VOLKSKRANT, 23 FEBRUARY 2010

Cadillac will try again in Europe

ZURICH – The American car manufacturer General Motors will make a fresh attempt to establish the Cadillac brand in Europe. To this end, the subsidiary company Cadillac Europe has been established, the company reported on Monday.

The 2011 Cadillac CTS Coupé (Reuters)

The new business unit will import and sell models that have been designed specifically for the European market. A network of dealers and service companies will also be set up.

Several years ago, Cadillac attempted to storm the European market.

Cadillac is presenting its CTS Coupé next month at the Autosalon in Geneva. This will be its European premiere.

Export

Export

Exporting is the selling of domestic products or services to foreign importers. Exporting is thus the opposite of importing. The most significant motives for entering a foreign market are the following:

- New technologies and new products constitute a challenge. In a less-developed market, demand for such products will be greater than in an already developed market.
- The domestic market is too small for the product; there is too little demand or too much supply of a similar type of product.
- To assure the continuity of the company, there must be a constant search for new markets.
- The cost price of the product that the company supplies makes it competitive in the foreign market.
- If the company is suffering from overcapacity, it is attractive to sell products in a foreign market.

1

www.ft.com

Songwriters enjoy royalties to tune of £166m

Robust international demand and tighter licensing laws helped British and Irish songwriters more than double their royalties from music exports in the past decade. According to PRS for Music, the royalties collection society representing songwriters and composers, British and Irish musical talent earned £166.6m from overseas markets in 2009, up from £66m in 1999.
The figures strike an unusually positive note amid the travails of the wider music industry, which has seen revenues from recorded music sales collapse and is still struggling to find a sustainable digital revenue model.

Britain is one of only three net exporters of music in the world, second after the US and ahead of Sweden. The largest segment of international royalty in-come in 2009 was derived from music used in television programmes and ad-vertising, which generated more than £50m in revenue, up from £15m in 2000, while radio play yielded over £35m, compared with £23m at the start of the decade.

Karen Buse, international director at PRS for Music, said the successful export of British television formats such as X Factor, Who Wants To Be a Millionaire and The Weakest Link – which use music written by British composers – had bolstered royalties from broadcast. Meanwhile global tours by bands including Take That and U2 helped lift royalties income from live performances in 2009 to £18m, from under £14m in the previous year and less than £2m in 2000.

The most significant demand for British and Irish music came from the US, France, Germany and Japan. But growing appetite from emerging markets, including central and eastern Europe and South America, has also boosted royalties.

22 January 2011

1.2.2 Foreign investment

Besides engaging in international trade, companies can invest abroad, so-called foreign direct investment. This takes place when there is direct investment in production in another country, by building a factory, for example. It can also occur by starting up a company in another country, by taking over a local company or by merging with another company.

Foreign direct investment

● www.fdiintelligence.com

Proceeding with caution: the post-crisis world of FDI

According to data from Greenfield investment monitor fDi Markets, the most active foreign investor since the figures started being collected in 2003 has been the German trading and retail company Metro. In the past seven years, this firm has made 406 investments on a truly global basis. But in the past year, the firm appears to have slowed down the scale of its investments and expansion strategy. This year fDi Markets shows Metro has remained largely in the European market. Perhaps an indication of risk aversion. Apart from investments in Russia, Turkey and a few in Eastern Europe, the data suggests that Metro has greater interest in more developed economies. However, Metro's CFO, Olaf Koch, told fDi Magazine that Eastern Europe and Asia will figure largely in its expansion plans for 2011, specifically mentioning China, Russia and Turkey. He says: "Our international activities account for more than 60% of our sales volume. We want to accelerate our international growth with a focus on Eastern Europe and Asia. In particular, the fast-growing countries in Asia will play an increasingly important role in our expansion programme." Mr Koch cites new developments in China that will take place near Beijing, the Yangtze River Delta, Shanghai and the Pearl River Delta with Guangzhou.

25 January 2011

1.2.3 Motives

There are many reasons why a company may decide to do business abroad. In some cases, it just happens. The company stumbles across an interesting product abroad and decides to bring this product to Europe. Or one of its representatives accidentally meets a Turkish entrepreneur while on holiday in Turkey. They start talking and decide to collaborate, with the result that a truckload of ceramics comes from Turkey to Europe every month. Naturally, the most important reason is to earn money, but that is often not the case. Table 1.2 lists the principal motives. These can be divided into proactive and reactive motives. Proactive motives are derived from the policy that a company establishes to do business internationally, while reactive motives derive from a threat in the home market or the nature of the product.

Proactive motives

Reactive motives

TABLE 1.2 Motives for internationalisation

Proactive motives	Reactive motives
Profit and growth goals	Competitive pressure
Managerial urge	Small and/or saturated home market
Distinctiveness of the product	Utilisation of overproduction/excess capacity
Anticipating foreign market opportunities	Reduction of dependence on customers/ suppliers
Economies of scale	Stabilisation of seasonal factors
Integration of the supply chain	Proximity of customers/suppliers
Tax benefits	Perishable products

Source: Albaum et al., 2008, p. 76

An explanation of these motives follows at present.

Proactive motives
As stated above, proactive motives are derived from the company policy, i.e. with no external influence or threats. Seven proactive motives can be identified.

1 Profit and growth goals
Companies can come to the conclusion that their growth goals are no longer feasible in the domestic market because that market is fully covered. To be able to meet the formulated growth targets, management can decide to enter foreign markets.
Especially in the current economic environment, cost saving is an important factor. By moving production to low-wage countries, companies can make savings on production costs, and achieve more profit.

2 Managerial urge
The management board of the company has decided to internationalise. Management and staff are ready to accept this new challenge; travelling may be involved. This decision is sometimes strengthened because the management board consists of people from different cultures who see opportunities in their country of birth.

3 Distinctiveness of the product
A company can profile itself abroad with a product that positively distinguishes itself from other products.
Examples of distinguishing features are low price, superiority of the product quality, speed of delivery, design and good service. A company may supply goods or services that are not yet available worldwide. A product with high distinctiveness is difficult for competitors to copy. Some products have technological advantages in a certain area. It is, however, open to question how long these technological advantages will continue to exist because, of course, competitors will not just stand still.

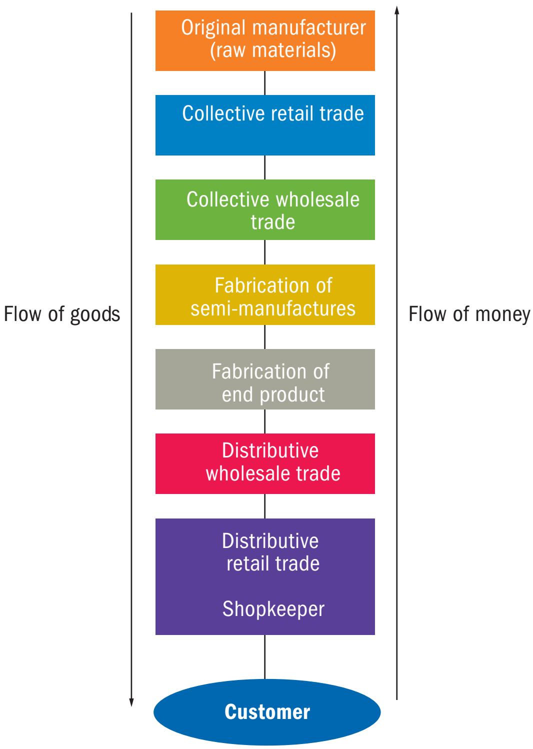
4 Anticipating foreign market opportunities
International businesses often see more opportunities for growth in rapidly expanding countries than in countries where growth has clearly lagged

behind the rest of the world. For this reason, their investment policy is often focused on rapidly growing markets.
Sometimes it is cheaper to produce in one country than another. This depends on the costs of labour, raw materials, capital and infrastructure. The total of these costs determines where the product can be produced at the lowest price. The company will be interested in countries where its products can be made most cheaply, while maintaining good quality.

5 Economies of scale
Economists have shown that it is in some cases possible to reduce the cost price per unit by 10–30 % with every doubling of production quantity. This occurs above all if the production process can be standardised. A company can increase production by entering the international market. This can lead to a reduction in production costs, through which the company's competitive strength in the domestic market also increases.

6 Integration of the supply chain
Some companies practise forward or backward integration to gain more control over the whole chain, from the producer to the customer. The supply chain (see figure 1.3) can consist of: production of raw materials, production of components, production of finished product, wholesaling, retailing and after-sales service. Backward integration, for instance, may involve takeovers of production locations abroad. Forward integration can consist

FIGURE 1.3 Example of a supply chain



Source: http://www.businessmodellen.com

of taking over a chain of shops abroad. Various benefits arise from integration of the supply chain, such as savings on transaction costs, more power to negotiate with suppliers and purchasers about prices, less chance of products being out of stock and a reduction in overhead costs.

7 Tax benefits
Doing business abroad can also produce tax benefits, as in the case of withholding tax (tax that is deducted when interest, royalties or dividends are received from another country), which for certain countries can lead to exemption or restitution in Europe. Furthermore, no VAT has to be paid on foreign sales.

Reactive motives
Reactive motives arise from external influences or threats and not from the company policy.
Here, too, seven motives can be identified.

1 Competitive pressure
Some companies perceive the competition for a certain product on the domestic market as too intense, as a result of which profit margins can come under pressure, for example. A certain foreign market where the competition is less intense can offer an opportunity to make a reasonable profit. Increasing competition from foreign companies in the home market may also force the company, for financial or human reasons, to compensate for the loss of turnover by exporting products.

2 Small and/or saturated home market
When a product reaches the maturity stage or decline stage of its lifecycle, pressure on the price increases because of intensified competition. Suppose that in another country the market for this product is still in a growth stage. This can result in a decision of the company to enter the other, more lucrative, foreign market.
The size of the market naturally plays an important part in this decision. The market in Europe is small in comparison with markets in China, India and the US.

3 Utilisation of overproduction/excess capacity
If the production capacity is insufficiently utilised because no more products can be sold in the domestic market, entering a foreign market is an ideal way to utilise that capacity. By doing so, the total profit of an enterprise can finally increase.
Surplus stock can sometimes be sold to foreign markets, reducing stock costs to an acceptable level.

4 Reduced dependence on customers/suppliers
In general, the more suppliers a company has, the less chance there is of stock shortages. By doing business with suppliers in several countries, as soon as trade with a certain country declines, a company can switch over to suppliers in other countries.
The more clients a company has, the greater the spread of sales and the lower the risk of loss of turnover if a client is lost. Companies that do business with countries characterised by political instability, high inflation, a balance of payments deficit or sluggish economic growth are especially wise to spread their risk.

5 Stabilisation of seasonal factors
Some companies are troubled by seasonal factors, due to which their turnover in certain months is higher than in other months. For example, a European company sells more golf carts in the spring and summer than in the winter. By supplying golf carts to customers in countries where it is summer when it is winter in Europe (such as Australia and South Africa), seasonal fluctuations in turnover can be reduced.

6 Proximity of customers/suppliers
Because the distances within Europe are relatively small, it is fairly easy to enter these markets. That is why countries within Europe are the main business partners for European enterprises.

7 Perishable products
With perishable products (such as vegetables and flowers) and products that deteriorate in quality over time (such as washing powder), it would be a good idea to sell them abroad before it loses its quality.

Reactive motive: perishable product

1.3 European Union and international business

In this section we look at the performance of the European Union on the international stage. International trade as well as foreign direct investment are discussed. The prospects for world trade are also discussed. In the last section, a summary is given of agencies that assist entrepreneurs in international business.

1.3.1 European Union and international trade
According to data from Eurostat, import as well as export from all 27 EU member states increased compared to 2009. Especially Bulgaria, Latvia

1

and Estonia show an increase in export. Sweden, Lithuania and Czech Republic illustrate the greatest growth when it comes to import.

The main business partners for the member states are the other member states. The main business partners outside the EU are the United States, China and Russia. Exports to Brazil even rose with 53%, but more has been exported also to China (+39%) and Turkey (+36%). Imports from Russia (+37%), China (+30%) and India (+28%) have also increased since 2009.

It seems that the European member states (see table 1.3) mostly import primary goods (food&beverages, raw materials and energy). Otherwise the member states have exported more processed goods (chemicals, machines & transportation) and services.

TABLE 1.3 Member States total trade (intra-EU + extra-EU)

	Total exports			Total imports			Trade balance	
	Jan–Sep 2009	Jan–Sep 2010	Growth	Jan–Sep 2009	Jan–Sep 2010	Growth	Jan–Sep 2009	Jan–Sep 2010
Belgium	195.6	230.5	18%	185.7	216.4	16%	9.8	14.1
Bulgaria	8.5	11.3	33%	12.5	13.5	9%	-4.0	-2.3
Czech Republic	59.4	72	21%	55.0	68.2	24%	4.4	3.7
Denmark	49.9	54.3	9%	44.1	46.8	6%	5.7	7.5
Germany	590.8	701.5	19%	492.9	588.0	19%	97.9	113.5
Estonia	4.8	6.1	28%	5.3	6.6	23%	-0.6	-0.5
Ireland	63.8	65.3	2%	33.8	33.4	-1%	30.0	31.8
Greece	10.7	11.0	3%	32.6	28.8	-12%	-21,8	-17,7
Spain	119.3	135.0	13%	153.3	174.0	13%	-34.0	-39.0
France	257.4	289.3	12%	295.1	335.7	14%	-37.7	-46.3
Italy	215.4	246.2	14%	219.5	265.4	21%	-4.1	-19.2
Cyprus	0.7	0.8	13%	4.2	4.5	8%	-3.5	-3.7
Latvia	4.0	5.1	29%	5.2	6.1	18%	-1.2	-1.0
Lithuania	8.6	11.0	28%	9.6	12.4	29%	-1.1	-1.4
Luxembourg	11.3	10.8	-4%	13.1	13.3	2%	-1.8	-2.5
Hungary	43.2	52.4	21%	40.7	48.4	19%	2.5	4.0
Malta	1.2	1.4	15%	2.3	2.3	3%	-1.1	-1.0
Netherlands	260.3	314.9	21%	231.8	284.3	23%	28.5	30.6
Austria	72.4	83.8	16%	75.7	87.0	15%	-3.3	-3.2
Poland	71.3	88.8	25%	78.3	95.9	22%	-7.1	-7.0
Portugal	23.4	27.0	16%	37.7	41.6	10%	-14.3	-14.6
Romania	21.2	26.8	26%	28.4	33.8	19%	-7.1	-7.0

	Total exports			Total imports			Trade balance	
	Jan–Sep 2009	Jan–Sep 2010	Growth	Jan–Sep 2009	Jan–Sep 2010	Growth	Jan–Sep 2009	Jan–Sep 2010
Slovenia	13.9	16.2	17%	13.9	16.3	17%	–0.1	–0.1
Slovakia	28.9	35.2	22%	28.7	35.6	24%	0.1	–0.4
Finland	32.6	37.0	14%	32.2	37.2	15%	0.4	–0.1
Sweden	69.0	86.2	25%	62.3	81.2	30%	6.7	5.0
United Kingdom	184.8	222.8	21%	255.3	307.6	20%	–70.5	–84.8

Source: http://epp.eurostat.ec.europa.eu/portal/page/portal/eurostat/home/

As shown by table 1.3, the 27 member states of the EU export more than they import. This is called an active trade balance; there is a trade surplus. This is often perceived as positive for a country, because more money comes into the country (money is paid for the products and services are exported) than is spent on imports. The opposite of this is a trade deficit, also called a passive trade balance. Because more money goes out of the country than comes in, this is often perceived as negative. Many developing countries have a passive trade balance. They are dependent on foreign countries for many goods and/or services.

Active trade balance
Trade surplus

Trade deficit
Passive trade balance

1.3.2 Europe and foreign direct investment

According to Eurostat, EU Foreign Direct Investment (FDI) flows have been severely affected by the global economic and financial crisis. They hit a record peak in 2007, but dropped sharply in 2008, for both inward and outward FDI flows (34 % for outflows, 52 % for inflows). While incoming FDI flows recovered slightly in 2009, EU investments abroad continued to decline (by 24%).

TABLE 1.4 EU-27 outward and inward FDI flows in 2006-2009 (EUR bn)

	Outward FDI flows					Inward FDI flows				
	2006	2007	2008	2009p	Share (%) in 2008	2006	2007	2008	2009p	Share (%) in 2008
Extra EU-27	313.0	530.7	347.7	263.3	100.0%	229.0	411.4	198.7	221.7	100.0%
Europe (non-EU, including EFTA) of which	74.1	130.6	103.7		29.8%	66.4	64.0	45.8		23.0%
Switzerland	21.9	39.9	34.0	44.8	9.8%	24.8	29.5	10.6	31.7	5.4%
Russia	11.3	17.2	25.6	–1.0	7.4%	1.5	9.9	2.3	3.1	1.2%
Croatia	4.5	2.7	2.0		0.6%	0.0	0.0	–0.2		–0.1%
Turkey	12.3	15.4	6.3		1.8%	–0.3	0.6	–0.2		–0.1%
Ukraine	2.1	3.0	4.8		1.4%	–0.1	0.4	0.5		0.2%

	Outward FDI flows					Inward FDI flows				
	2006	**2007**	**2008**	**2009p**	**Share (%) in 2008**	**2006**	**2007**	**2008**	**2009p**	**Share (%) in 2008**
Africa of which	11.7	17.9	18.5		5.3%	1.8	4.8	6.0		3.0%
Egypt	2.8	2.0	9.8		2.8%	0.1	-0.1	3.4		1.7%
South Africa	5.1	5.1	2.7		0.8%	0.9	1.8	0.5		0.2%
North America of which	135.8	198.7	129.3		37.2%	85.4	190.5	65.8		33.1%
Canada	31.0	29.8	7.8	2.8	2.3%	11.3	6.9	15.3	11.4	7.7%
United States	104.7	168.9	121.4	69.0	34.9%	74.1	183.5	50.5	96.8	25.4%
Central America of which	38.5	101.5	2.1		0.6%	33.0	75.6	-13.6		
Mexico	1.7	6.5	5.7		1.6%	0.3	0.4	0.9		0.5%
South America of which	13.0	17.6	9.6		2.7%	2.3	27.0	13.4		6.7%
Argentina	3.4	2.4	4.4		1.3%	0.0	0.1	-0.3		-0.1%
Brazil	5.4	14.3	-1.1	6.9	-0.3%	1.5	24.7	10.7	2.8	5.4%
Asia of which	28.5	53.9	70.1		20.2%	34.5	39.0	83.5		42.0%
Gulf Arabian Countries	2.3	4.6	18.9		5.4%	10.1	2.3	63.2		31.8%
China (excl. Hong Kong)	6.7	6.6	4.7	5.3	1.4%	2.2	0.8	-0.1	0.3	0.0%
Hong Kong	3.5	7.3	6.2	3.4	1.8%	-0.2	6.7	2.0	-0.2	1.0%
Japan	-1.6	10.3	5.9	0.1	1.7%	16.0	17.8	7.2	-2.3	3.6%
India	2.4	4.0	3.3	3.2	0.9%	0.5	1.0	3.7	0.4	1.9%
Singapore	9.5	8.5	15.2		4.4%	6.0	10.4	2.6		1.3%
Oceania of which	7.2	9.1	14.2		4.1%	7.0	6.7	-1.3		
Australia	6.7	8.6	12.8		3.7%	6.2	6.7	-0.9		-0.5%
Offshore Financial centers	58.9	150.8	39.4	60.3	11.3%	74.2	106.5	19.6	39.8	9.9%

2006–2008 annual FDI data. Preliminary figures for 2009 are based on annualised quarterly data.
Source: Eurostat

As can be concluded from table 1.4, the other EU member states are the main partners in the area of foreign direct investment in the EU. However the United States and the Arabic Gulf countries play a more important role in direct investments in the EU. It seems that FDI from Russia, China and India has increased substantially in the past few years. Especially the service sector in the EU is a prime sector for foreign investors.

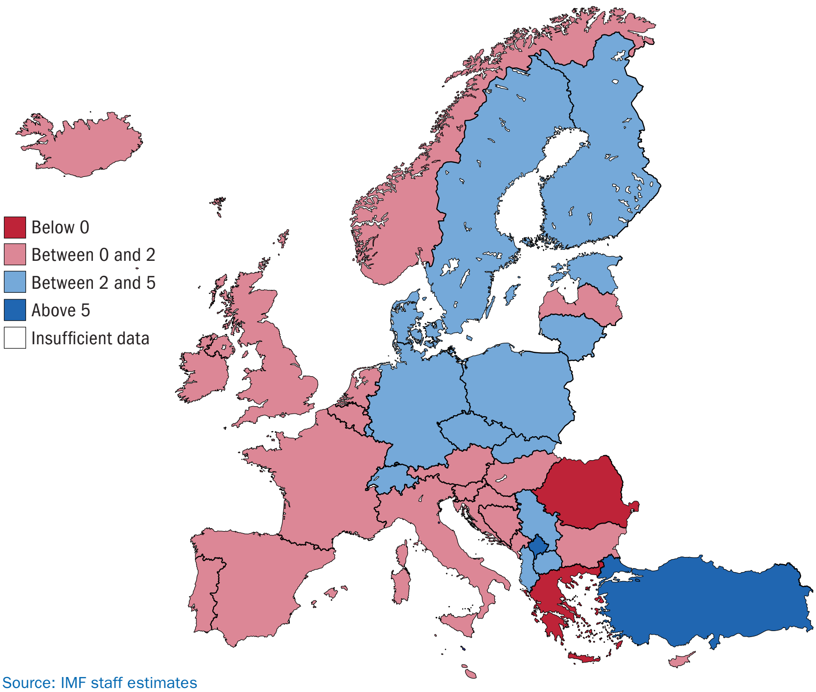
1.3.3 Prospects for international business

The future of international as well as European trade is being influenced by the economic crisis. As can be seen from the article below, after a fierce year, slight growth in world trade is predicted for 2010.

Nevertheless, this slight recovery is fragile. According to the Central Plan Bureau in the Netherlands, this is above all due to the powerful recovery of the economy in Asia. Growth in Gross National Product (GNP) in the euro area is estimated at 1.25 per cent in 2010 and 1.75 per cent in 2011. That is very low in comparison with the pace that is usually achieved after a recession. The European Union is the world's biggest trader, accounting for 20% of global imports and exports. By 2015, 90 % of world growth will be generated outside Europe, with a third from China alone. So in the years to come, the EU needs to seize the opportunity of higher levels of growth abroad, especially in East and South Asia. Developing and emerging countries are likely to account for nearly 60 % of world GDP by 2030. This is compared to less than 50 % today.
China, now the EU's second biggest trade partner, is a source of both major opportunities and challenges. Given its tremendous growth potential, China is a major attraction for exports and investments. But there is no denying that some of China's industrial and macro-economic policies imply an approach based on state capitalism. There are similar issues in relation to Russia; the EU's biggest near neighbour.

Figure 1.4 shows that the biggest growth from GDP will be in Asia and South America. In these regions are the opportunities for the future.

FIGURE 1.4 Average Projected Real GDP Growth during 2010–2011 in percentage



Source: IMF staff estimates

According to the World Trade Organization (WTO) extra-EU trade (external trade between the EU and the rest of the world) rose considerably faster than trade within the EU, which remained constrained by low economic activity. Asian exports rose by about 30% in the third quarter of 2010, as compared to the corresponding period of 2009. Exports from Africa and the Middle East were 22% higher than in the corresponding period of 2009 mainly due to the rebound of commodity prices after the crisis.

www.parool.nl

WTO foresees 9.5 per cent growth in world trade

GENEVA – World trade is expected to grow by 9.5 per cent this year. This expectation was expressed by Pascal Lamy, Director of the World Trade Organization (WTO).

Pascal Lamy, Director of the World Trade Organization (WTO)

'After the biggest economic contraction since the Second World War, in 2009, our economists foresee growth in trade again in 2010,' says Lamy. Trade in developing countries will increase by 11 per cent and in industrialised countries by 7.5 per cent, said the WTO Director. 'This means that there is again light at the end of the tunnel and that is good news for the world economy.'

World trade shrank by 12 per cent in 2009 as a result of the worldwide economic crisis.

6 April 2010

1.4 International business organisations

There are many organisations that support and help companies to collect the right data. Advice that is given can relate to all aspects of international business. Table 1.5 lists these organisations by subject with relevant website addresses.

TABLE 1.5 Organisations that help with international business

Subject	Organisation	Internet address
International business	International Trade Centre	www.intracen.org
Exports	Market Acces Database	www.madb.europa.eu
Imports	Centre for the Promotion of Imports from Developing Countries	www.cbi.eu
Globalisation	Swiss Economic Institute (KOF)	www.globalization.kof.ethz.ch
		www.globalisation.com
	United Nations	www.unsystem.org
	United Nations Conference on Trade and Development	www. unctad.org
	G20	www.g20.org
International competitive strength	IMD	www.imd.ch
	World Economic Forum	www.weforum.org

Summary

- International business: economic activities across borders or actions that are necessary to do business abroad.

- Globalisation: the worldwide coalescence of economies, politics and cultures.

- Causes of globalisation:
  - opening of international borders
  - advent of the internet
  - development of low-wage countries

- Advantages of globalisation:
  - contributes to higher economic growth and prosperity
  - spreads technological knowledge
  - leads to widespread cultural integration

- Disadvantages of globalisation:
  - greater chance of wages in developed countries being undermined
  - increased exploitation of workers in less developed countries
  - gives multinationals a great deal of power

- Due to the disadvantages of globalisation, more and more attention is being paid to sustainable international business. Sustainable international business is based on three pillars:
  1. people
  2. planet
  3. profit

- The basis for international business is formed by international trade and foreign direct investment. International trade consists of import and export.

- Import is buying foreign products or services. The reasons for this are:
  - production in other countries is cheaper
  - the product/service is not yet available on the domestic market

- Export is selling foreign products or services. The motives for this are:
  - too small domestic market
  - new markets
  - continuity of the enterprise
  - price is competitive
  - overcapacity

- Foreign direct investments are investments made abroad by domestic companies.

- The principal motives for internationalisation can be divided into proactive and reactive motives (table 1.2).

- The most important trading partners for the European Union are United States, China and Russia.

Questions and assignments

Questions about the opening case

1.1 What form of international trade is carried out by Amazon?

1.2 What was Amazon's motive for starting international business?

www.fd.nl

Eurobag: globalisation in a nutshell

'The wages are three to four times higher here than over the border on the Chinese mainland', says Alexander Kraima. 'Until recently we had 22 people here; now there are 14 and soon we shall have even fewer. It is simply cheaper in China,' he says.
Kraima is the Director of Eurobag in Hong Kong, a company that manufactures around 4 million bags annually. Eurobag supplies retailers like C&A and Scapino and brands like Reebok, Diadora and Lotto in Europe, Australia and Latin America. Furthermore, it carries out quality control for its parent company Pare, which under own management puts brands like Brunotti and Daniel-Ray on the European market.
The story that Kraima tells is a story of division of labour , specialisation and cost savings. It begins with the parent company in Drenthe (Pare), which started importing canvas bags from Asia at the beginning of the 1970s. At the beginning of the 90s, the company decided to open a branch in Hong Kong to organise the purchasing and quality control on site: Eurobag. That company developed into a connection between designers in the Netherlands, sample makers and manufacturers in China and clients all over the world.

4 June 2010, edited

1.3 Why is the article headed 'globalisation in a nutshell'?

1.4 What disadvantage of globalisation emerges strongly from this article?

1.5 Play the game Trade Ruler at http://nobelprize.org/educational_games/economics/trade/game/ruler.html.

1.6 Find the most recent import and export figures for the 27 European member states.