

CHAPTER 3

Business in the Global Economy

3-1 International Business Basics

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Planning a Career in...

INTERNATIONAL BUSINESS



Global business activities create many employment opportunities. Jobs could include directing foreign sales, negotiating with foreign distribution centers, arranging shipping, and planning conversion of products from American to foreign specifications. While the skills necessary to perform these tasks are increasingly important, job titles often will not reflect them directly because the people will also have duties unrelated to importing and exporting. Transportation managers, for example, oversee both foreign and domestic shipping, including settlements between shippers. U.S. Customs Service agents investigate persons, common carriers, and merchandise arriving in or departing from the United States to prevent prohibited importing or exporting.

Employment Outlook

- Strong growth is expected for interpreters and translators.
- Employment of inspectors and compliance officers is not usually affected by economic fluctuations. Recently, increased security concerns have expanded demand for federal, state, and local government examiners.
- Continued growth of many international business positions is expected as companies expand global operations.

Related Job Titles

- Customs Inspector
- Interpreter/Translator
- Global Purchasing Manager
- Transportation/Freight Inspector
- Cross-Cultural Trainer
- International Sales Representative
- International Marketing Manager
- Import/Export Coordinator
- Freight Forwarding Specialist

Needed Skills

- Language skills, cultural awareness, and knowledge of geography provide the foundation for most international business work.
- Many international business positions require knowledge in a field such as accounting, marketing, finance, or information technology.

What's it like to work in ... International Business

"I'm sorry, your shipment is being held at the Port of Hong Kong until the proper documentation is prepared."

These are words no exporter wants to hear. To avoid this type of situation, exporters turn to companies such as M.E. Day, which exist to help them ship their products around the world.

M.E. Day and other freight forwarders specialize in shipping goods to customers in other countries. These global intermediaries also help companies selling around the world with other services. Areas of expertise include export regulations, costs for various shipping methods, and the customs process.

M.E. Day also serves as a customs broker, helping international companies pass inspections when goods enter another country. Customs brokers prepare needed documents and make sure the required tariffs are paid.

What about you? What are some aspects of international business that you might find of interest in the future?



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3-1 International Business Basics



Goals

Describe importing and exporting activities.

Compare balance of trade and balance of payments.

List factors that affect the value of global currencies.

Key Terms

imports

exports

balance of trade

balance of payments

exchange rate

Focus on Real Life

What did you and your family have for breakfast this morning? Coffee, cereal, and sliced bananas, perhaps? If it were not for trading with Brazil for coffee and with Honduras for the bananas, you might have had only cereal. The sugar on your table may have come from the Philippines. Even the morning newspaper was printed on paper that may have come from Canada.

As you look around your home, you will find many products made in other countries. For example, you may find a TV made in Japan or Korea, an MP3 player made in Taiwan or China, clothing made in the Philippines or Honduras, kitchen appliances made in Hong Kong or Malaysia, and cocoa from Brazil or Colombia. Look around your classroom. Can you identify products made in other countries?

main idea

Describe importing and exporting activities.

TRADING AMONG NATIONS

Most business activities occur within a country's own borders. *Domestic business* is the making, buying, and selling of goods and services within a country. *International business* refers to business activities needed for creating, shipping, and selling goods and services across national borders. International business is frequently referred to as *foreign* or *world trade*. Evidence of foreign trade is everywhere.

Although the United States has many natural resources, a skilled labor force, and modern production facilities, American companies and consumers go beyond the U.S. borders to obtain many things. The United States conducts trade with more than 180 countries.

In the past, economies were viewed in terms of national borders. With international trade expanding every day, these boundaries are no longer fully valid in defining economies. Countries are interdependent and so are their economies. Consumers have come to expect goods and services from around the world.



What are some of the advantages and disadvantages of international trade?

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Absolute Advantage

Two economic principles define buying and selling among companies in different countries. *Absolute advantage* exists when a country can produce a good or service at a lower cost than other countries. This may result from an abundance of natural resources or raw materials in a country. For example, some South American countries have an absolute advantage in coffee production, and Saudi Arabia has an absolute advantage in oil production.

Comparative Advantage

A country may have an absolute advantage in more than one area. If so, it must decide how to maximize its economic wealth. A country may be able to produce both computers and clothing better than other countries. The world market for computers might be stronger than the market for clothing. This means it would be better for the country to produce computers but to buy clothing from other countries. *Comparative advantage* is a situation in which a country specializes in the production of a good or service at which it is relatively more efficient.

Importing

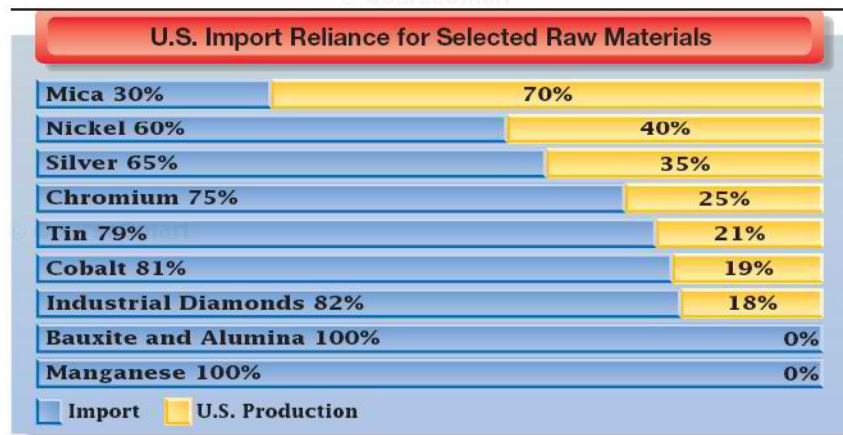
Imports are items bought from other countries. Did you know that imports

account for the total supply of bananas, coffee, cocoa, spices, tea, silk, and crude rubber in the United States? The United States buys about half of its crude oil and fish from other countries. Imports also account for 20 to 50 percent of the supply of carpets, sugar, leather gloves, dishes, and sewing machines. U.S. companies must import tin, chrome, manganese, nickel, copper, zinc, and several other metals to manufacture certain goods. Figure 3-1 shows how dependent the United States is on imported raw materials.

Without foreign trade, many things you buy would cost more or not be available. Other countries can produce some goods at a lower cost because they have the needed raw materials or have lower labor costs. Some consumers purchase foreign goods, even at higher prices, if they perceive the quality to be better than domestic goods. They may simply enjoy owning products made in other countries. French perfumes, Norwegian sweaters, and Swiss watches are examples.

Exporting

Goods and services sold to other countries are called **exports**. Just as imports benefit you, exports benefit consumers in other countries. Workers throughout the world use factory and farm machinery



Source: United States Geological Survey Minerals Information.

FIGURE 3-1

How would U.S. manufacturing be affected if these imports were not available?

made in the United States. They eat food made from U.S. agricultural products and use chemicals, fertilizers, medicines, and plastics from the United States. People in other countries like to view U.S. movies. They also watch CNN and ESPN. They read books, magazines, and newspapers published by U.S. companies. The goods and services exported by the United States create many jobs. One of every six jobs in the United States depends on international business. Figure 3-2 shows U.S. balance of trade with various nations.

U.S. Trade Balances			
GOODS EXPORTED (IN BILLIONS)	COUNTRY	GOODS IMPORTED (IN BILLIONS)	U.S. TRADE BALANCE
1,437.8	All Countries	2,201.0	-763.2
230.6	Canada	303.4	-72.8
134.2	Mexico	198.3	-64.1
59.6	Japan	148.0	-88.4
31.1	Netherlands	17.3	+13.8
17.8	Australia	8.2	+9.6
19.2	Brazil	26.4	-7.2
23.0	Taiwan	38.2	-15.2
55.2	China	287.8	-232.6
214.0	European Union	330.6	-116.6

Source: U.S. Census Bureau

FIGURE 3-2

Which country has the largest trade imbalance with the United States?

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How does importing differ from exporting?

main idea

Compare balance of trade and balance of payments.

MEASURING TRADE RELATIONS

A major reason people work is to earn money to buy things. First, they sell their labor for wages. They then spend the major part of those wages for goods and services. People usually try to keep their income and spending in balance. They know that if they spend more than they earn, they can experience financial problems. Nations are also concerned about balancing income with expenditures. When people buy more than their income allows, they go into debt. In the same way, when a country has an unfavorable balance of trade it owes money to others. *Foreign debt* is the amount a country owes to other countries.

Balance of Trade

The difference between a country's total exports and total imports is called the **balance of trade**. If a country exports (sells) more than it imports (buys), it has a *trade surplus*. Its trade position is said to be favorable. If it imports more than it exports, it has a *trade deficit* and its trade position is unfavorable.

A country can have a trade surplus with one country and a trade deficit with another. Overall, a country tries to keep its international trade in balance. Figure 3-3 shows the two possible trade

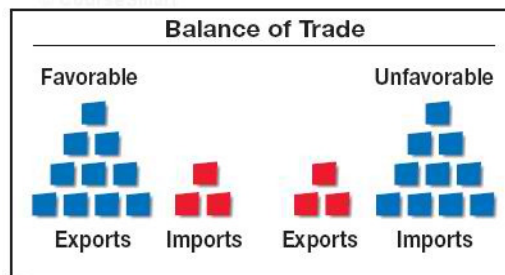


FIGURE 3-3

Why is it better to export more than you import?

positions. After a long history of a favorable balance of trade, the United States has had a trade deficit in recent years.

Balance of Payments

In addition to exporting and importing goods and services, other forms of exchange take place among nations. Money goes from one country to another through investments and tourism. A citizen of one country might invest in a corporation in another country. A business may invest in a factory in another country. One government might give financial or military aid to another nation. Banks may deposit funds in foreign banks.

When tourists travel, they add to the flow of money from their country to the country they are visiting. Some countries limit the amount of money their citizens can take out of the country when they travel.

Work as a Team

Countries attempt to have a favorable balance of payments. Create a list of actions a nation might take to improve its trade relations with other countries.



The **balance of payments** is the difference between the amount of money that comes into a country and the amount that goes out of it. A *positive* or *favorable* balance of payments occurs when a nation receives more money in a year than it pays out. A *negative* balance of payments is *unfavorable*. It is the result of a country sending more money out than it brings in.

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How does balance of trade differ from balance of payments?

A QUESTION OF ETHICS

Bribery and Gift Giving

In the United States, it is considered unethical for a businessperson to pay bribes to government officials or to other businesspersons in exchange for favorable treatment, such as the awarding of well-paid contracts. In fact, it is against the law, whether the recipient is an American or someone in another country. The Foreign Corrupt Business Practices Act of 1977 outlawed the payment of bribes by Americans to foreign officials, companies, or individuals. At times, not doing so may put U.S. businesses at a competitive disadvantage. In some countries, paying and accepting bribes of various sorts is common, even expected. As more countries recognize how harmful bribes are to

economic progress, the practice is ending.

While it is relatively easy to outlaw bribes, it is much harder to define and identify what is a bribe and what is a gift given as a token of appreciation. Gift giving among businesspeople is relatively limited and infrequent in the United States and Canada. In other cultures, it is very common and regarded as entirely appropriate. Many organizations have policies that limit the monetary value and type of gifts that are acceptable. Policing intent is much more difficult because it is highly subjective. A social dinner invitation is usually meant to influence the recipient's behavior, even if in a subtle way.

Think Critically

1. How can U.S. businesspeople handle situations in foreign countries where officials expect bribes to be paid as a condition for doing business there?
2. Suppose you work for a manufacturing company. A plastics supplier who is trying to get more business sends you a case of golf balls made with one of its high-tech composite materials. What would you do?

main idea

List factors that affect the value of global currencies.

INTERNATIONAL CURRENCY

One challenge faced by businesses involved in international trade is the various currencies used around the world. Nations have their own banking system and money. For instance, Russia uses the *ruble*; the European Union, the *euro*; Brazil, the *real*; India, the *rupee*; and Saudi Arabia, the *riyal*.

Foreign Exchange Rates

The process of exchanging one currency for another occurs in the *foreign exchange market*, which consists of banks that buy and sell different currencies. Most large banks provide currency services for businesses and consumers. The **exchange rate** is the value of a currency in one country compared with the value in another. Supply and demand affect the value of currency. The approximate values of various currencies on a recent date in relation to the U.S. dollar (USD) are given in Figure 3-4.

Travelers and businesspeople must deal with currency exchanges as they go from one country to another. Travelers in another country can go to a currency exchange window and buy any amount of local currency they want. The amount of local currency they receive depends on the value of the two currencies at that



Why do many countries use a variety of colors in their currency?

time. Current rates are posted at exchange windows. Although locations vary throughout the world, exchange windows generally are found at airports, train stations, hotels, and local banks. Operators of exchange windows charge a fee for their services.

Factors Affecting Currency Values

Three main factors affect currency exchange rates among countries: the country's balance of payments, economic conditions, and political stability.

Balance of Payments When a country has a favorable balance of payments, the value of its currency is usually

FIGURE 3-4

Which currency is worth the most in terms of U.S. dollars?

Recent Values of Currencies			
COUNTRY	CURRENCY	UNITS PER USD*	VALUE IN USD*
Britain	pound	0.50 pounds	1.99
Brazil	real	2.03 reals	0.49
Canada	dollar	1.13 dollars	0.88
European Union	euro	0.74 euro	1.35
Japan	yen	119.78 yen	0.0083
Saudi Arabia	riyal	3.75 riyal	0.27
South Africa	rand	7.09 rand	0.141
South Korea	won	931.35 won	0.00107
Venezuela	bolivar	2,144.00 bolivars	0.00047

*United States Dollar

constant or rising. An increased demand for both the nation's products and its currency causes this situation. When a nation has an unfavorable balance of payments, its currency usually declines in value.

Economic Conditions When prices increase and the buying power of the country's money declines, its currency is not as appealing. Inflation reduces the buying power of a currency. High inflation in Brazil, for example, would reduce the demand for the real.

Interest rates are the cost of using someone else's money. These rates can affect the value of a country's currency. Higher interest rates usually create lower consumer demand. This often results in a reduced demand for a nation's currency, causing a decline in its value.

Political Stability Companies and individuals want to avoid risk when they do business in other nations. If a government changes suddenly, this may create an unfriendly setting for



The U.S. dollar is the official currency of Ecuador, El Salvador, and Panama. A country may adopt a "dollarization" policy in an attempt to reduce economic troubles and enhance trade with other nations. The dollar is also the unofficial monetary unit for tourist transactions in countries such as the Bahamas and Haiti.

foreign business. A company could lose its building, equipment, or money on deposit in banks.

Political instability may also occur when new laws are put in place. These laws may not allow foreign businesses to operate as freely as they did under the old laws. Uncertainty in a country reduces the confidence that businesspeople have in its currency.

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What factors affect the value of a country's currency?

3-1

Assessment



Key Concepts

Determine the best answer.

- Which of the following would be an example of international business?
 - A farmer in Iowa using U.S. produced equipment
 - A sales staff in South Carolina representing a foreign producer
 - A restaurant in Chicago offering Asian menu items
 - A retail store in Oregon selling craft items from local artists
- When a country's imports exceed its exports, there is a trade

a. surplus	c. exchange
b. deficit	d. balance

- The value of a country's currency is likely to decline as a result of
 - higher inflation
 - lower interest rates
 - a trade surplus
 - a favorable balance of payments

Make Academic Connections

- Culture** While business knowledge is important, often cultural awareness in foreign markets is even more important. Interview someone who has lived in or visited another country about cultural factors that affect business activities in that country.
- Technology** Explain how the Internet and other technology help to expand international trade and global business activities.

3-2 The Global Marketplace



Goals

Describe the components of the international business environment.

Identify examples of formal trade barriers.

Explain actions to encourage international trade.

Key Terms

Infrastructure

trade barrier

quota

tariff

embargo

Focus on Real Life

Clear and complete exchange of ideas among international business partners is vital. A U.S. retail company contracted with a foreign shirt maker to make men's shirts. The contract stated that the shirts must be made of 60 percent cotton and 40 percent polyester. While the manufacturer supplied shirt labels to that effect, the actual shirts were 35 percent cotton and 65 percent polyester.

Without verifying the material content, the U.S. company accepted the shirts. It sold them with the incorrect information on the label. The Federal Trade Commission fined the company for deceptive labeling.

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main idea

Describe the components of the international business environment.

INTERNATIONAL BUSINESS ENVIRONMENT

Doing business in other countries requires knowledge of the differences that exist among people and places. As shown in Figure 3-5, businesses must consider four main factors—geography, cultural influences, economic development, and political and legal concerns.

Geography

The location, climate, terrain, seaports, and natural resources of a country influence business activity. Very hot weather will limit the types of crops that can be grown. A nation with many rivers or ocean seaports can easily ship products for foreign trade. Countries with few natural resources must depend on imports.

Cultural Influences

In some societies, hugging is an appropriate business greeting. In other societies, a handshake is the custom. These differences represent different cultures.

Culture is the accepted behaviors, customs, and values of a society. A society's culture has a strong influence on business activities. In Mexico, many businesses close in the afternoon by tradition while people enjoy lunch and a siesta (relaxing rest period).

The main cultural and social factors that affect international business are language, religion, values, customs, and social relationships. These relationships include interactions among families, labor unions, and other organizations.

Economic Development

Every country and every individual faces the problem of limited resources to satisfy needs and wants. You continually make decisions about the use of your time, money, and energy. In a similar way, every country plans the use of its land, natural resources, workers, and wealth to best serve the needs of its people.

In some countries, people travel on a high-speed bullet train to manage a

computer network in a high-rise building. In other countries, people go by oxcart to a grass hut to operate a hand loom to make cloth for people in their village. These differences in living and work environments reflect the level of economic development. The key factors that affect a country's level of economic development are:

- **Literacy Level** Countries with better education systems usually provide more and better goods and services for their citizens.
- **Technology** Automated production, distribution, and communications systems allow companies to create and deliver goods, services, and ideas quickly.
- **Agricultural Dependency** An economy that is largely involved in agriculture does not have the manufacturing base to provide citizens with great quantity and high quality of a product.

Another factor that supports international trade in industrialized countries is **infrastructure**. Infrastructure refers to a nation's transportation, communication, and utility systems. A country such as Germany—with its efficient rail system, high-speed highways, and computers—is better prepared for international business activities than other nations with a weaker infrastructure.

Political and Legal Concerns

Each day you come upon examples of government influence on business. Governments regulate fair advertising and enforce contracts. They require safety inspections of foods and medications. People in the United States have a great deal of freedom in their business activities. This is not true in all countries. In many places, the activities of consumers and business operators are restricted. The most common political and legal factors that affect international business activities

Work as a Team

Knowledge of the international business environment is important for all global activities. As a team, create a list of items for each of the following categories: geography, cultural influences, economic development, and political-legal concerns. Explain how these items could affect a company when doing business in another country.



include the type of government, the stability of the government, and government policies toward business.

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List the four main elements of the international business environment.



FIGURE 3-5

main idea

Identify examples of formal trade barriers.

INTERNATIONAL TRADE BARRIERS

Government actions can create **trade barriers**, which are restrictions to free trade. These political actions are *formal* trade barriers. Three common formal trade barriers are quotas, tariffs, and embargoes.

The culture, traditions, and religion of a country can create *informal* trade barriers. These situations are not based on formal government actions but they do restrict trade.

Quotas

To regulate international trade, governments set a limit on the quantity of a product that may be imported or exported within a given period. This limit is called a **quota**.

Quotas may be set for many reasons. Countries that export oil may put quotas on crude oil so that the supply will remain low and prices will stay at a certain level. Quotas may be set on imports from another country to express displeasure at the policies of that country.

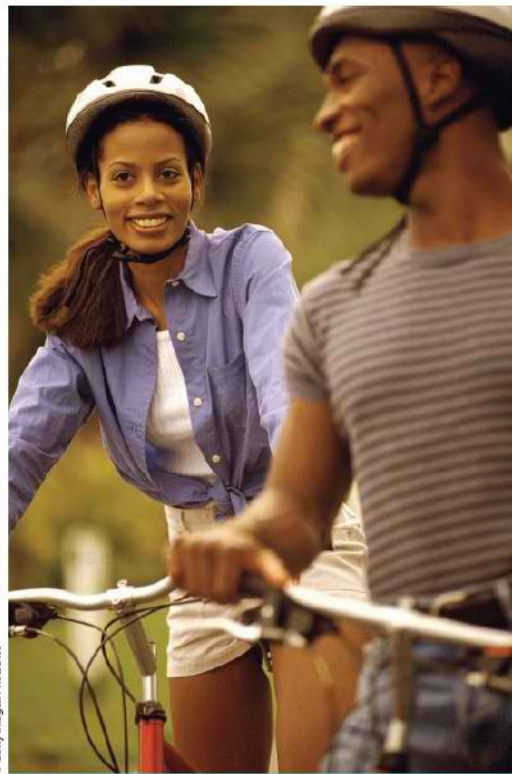
Quotas can also be set by a country to protect one of its industries from too much competition from abroad. This often is done by a nation to shield its “infant industries,” which need protection to get started. In the past, the U.S. government has imposed quotas on sugar, cattle, dairy products, and textiles.

Tariffs

Another device that governments use to control international trade is the tariff.

A **tariff** is a tax that a government places on certain imported products. Suppose you want to buy an imported bicycle. The producer charges \$140, but the government collects a 20 percent tariff (\$28) on the bicycle when it is imported. Therefore, you will have to pay \$168 plus shipping charges for the bike. The increased price may cause you to decide to buy a U.S. manufactured bike at a lower price.

Some tariffs are a set amount per pound, gallon, or other unit, while others are figured on the value of the good, as in the example of the bicycle. A tariff increases the price for an imported product. A high tariff tends to lower the demand for the product and reduce the quantity of that import. Many people believe that tariffs should be used to protect U.S. jobs from foreign competition.



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Do tariffs on imported goods help consumers or hurt them?

Embargoes

If a government wishes to do so, it can stop the export or import of a product completely. This action is called an **embargo**. Governments may impose an embargo for many reasons. They may wish to protect their own industries from international competition more than either the quota or the tariff will achieve. The government may wish to prevent sensitive products, especially those vital to the nation's defense, from falling into the hands of unfriendly groups or nations. A government sometimes imposes an embargo to express its disapproval of the actions or policies of another country.

checkpoint >>

What are three formal trade barriers?

ENCOURAGING INTERNATIONAL TRADE

Specific actions by governments can promote international business activities. Governments view exporting as an effective way to create jobs and foster economic prosperity. Common efforts to encourage international trade include free-trade zones, free-trade agreements, and common markets.

Free-Trade Zones

To promote international business, governments often create free-trade zones in their countries. A *free-trade zone* is a selected area where products can be imported duty-free and then stored, assembled, and/or used in manufacturing. A free-trade zone is usually located around a seaport or airport. The importer pays duty only when the product leaves the zone.

main idea

Explain actions to encourage international trade.



Language Translation

While on the job at an exporting company, you receive a phone call from a customer in Kenya. Unable to understand the caller's language, you switch on the language translation service. This software allows you to understand, in your language, the product questions of your customer.

Computerized translators recognize speech in one language and convert the spoken words into another language. In a language translation system, three components work together—speech recognition, machine translation, and speech synthesis. The computer

recognizes words spoken in the first language and converts them into a computer-readable file. Then, the words are translated into the second language. Finally, a voice synthesizer "speaks" the translated version.

Today, translation technology exists for all commonly used international business languages, such as Arabic, Chinese, English, French, German, Italian, Japanese, Korean, Portuguese, Russian, Spanish, and Vietnamese. In addition, hand-held, low-cost electronic language translators are available for use by businesspeople, travelers, and students.

These technologies allow you to say, "I would like to register for the conference" to a person who only speaks German. Then, using language translation technology, the German businessperson will hear, "Ich möchte für die Konferenz registrieren."

Think Critically

1. What are the possible benefits and drawbacks of computerized language translators?
2. Conduct a Web search to obtain information about the latest technologies for language translation systems.

Free-Trade Agreements

Many countries set up free-trade agreements with other nations. Under a *free-trade agreement*, member countries agree to remove duties, also called import taxes, and trade barriers on products traded among them. This results in increased trade between the members. For example, the United States, Canada, and Mexico began implementing the North American Free Trade Agreement (NAFTA) in 1994. This pact does away with tariffs on goods traded among the three countries and eases the movement of goods. NAFTA is designed to enlarge the markets and economic bases of the countries involved.

Common Markets

In a *common market*, members do away with duties and other trade barriers. They allow companies to invest freely in each member's country. They allow workers to move freely across borders. A common market is also called an *economic*



Why do you think U.S. businesses would be interested in exporting?

community. Common market members have a common external duty on products being imported from nonmember countries. Examples of common markets include the European Union (EU) and the Latin American Integration Association (LAIA). The goals are to expand trade among member nations and promote regional economic integration.

checkpoint >>

What actions could be taken to encourage international trade?

3-2

Assessment



Key Concepts

Determine the best answer.

- True or False. Infrastructure is a significant factor that affects the economic development of a country.
- True or False. An informal trade barrier is created by government actions.
- Religion is an element of the component of the international business environment.
 - geographic
 - economic
 - cultural
 - political
- A country that wishes to enhance international trade activities would most likely use
 - a tariff
 - a common market
 - an embargo
 - a quota

Make Academic Connections

- Law** Use the Internet to locate information about laws in foreign countries that are different from those in the United States.
- Geography** Using library resources or the Internet, obtain copies of maps for various geographic regions. On your map, indicate how the terrain, climate, and waterways might influence international trade activities. Present a 1–2 minute summary of your findings.
- History** Conduct research on the history of a common market such as the EU or the LAIA. Describe some of the benefits the community provides to its member nations.

3-3 International Business Organizations



Goals

Discuss activities of multinational organizations.

Explain common international business entry modes.

Describe activities of international trade organizations and agencies.

Key Terms

multinational company (MNC)
joint venture

Focus on Real Life

Before taking a new course of action, Ghana, located on the west coast of Africa, had many economic problems. Inflation was 120 percent. Exports had declined by 50 percent. The nation had a crumbling infrastructure. An overvalued currency did not promote widespread exporting of cocoa, Ghana's main export.

Ghana obtained suggestions from the International Monetary Fund. The actions that were implemented, along with lower tax rates, helped to improve the country's balance of payments and stimulate economic growth. Today, Ghana is one of the best-performing economies in Africa with consistent growth. Improved government policies and expanded investment in infrastructure and basic services have also helped reduce the country's poverty level.

MULTINATIONAL COMPANIES

A **multinational company (MNC)** is an organization that does business in several countries. MNCs usually consist of a parent company in a *home country* and divisions or separate companies in one or more host countries. The country in which the MNC places business activities is called the *host country*.

MNC Strategies

Multinational corporations can use either a global or multinational strategy. A *global strategy* uses the same product and marketing strategy worldwide. The same product is sold in essentially the same manner throughout the world. One example with which you are probably familiar is Coca-Cola.

A *multinational strategy* treats each country market differently. Firms develop products and marketing strategies that adapt to the customs, tastes, and buying habits of a distinct national market. Many restaurant chains employ a multinational strategy when they modify their menus to local tastes.

main idea

Discuss activities of multinational organizations.



What are some of the advantages of being a multinational corporation?



main idea

Explain common international business entry modes.

MNC Benefits

Many benefits are associated with international business. Consumers have a large amount of goods available. Often, these goods are at lower prices than goods made domestically. Career opportunities also expand as a company does business in a variety of countries.

Global business activities may also foster understanding, communication, and respect among people of different nations. Nations that are business partners usually try to maintain friendly relations for economic reasons.

Work as a Team

International business success often increases when a company works with a local business partner in another country. Choose a company or product that could be sold in other countries. Identify the types of companies that you might consider as a partner in the other countries. Then identify information sources that you might contact to make sure these potential partners would be suitable companies with which to do business.



Drawbacks of Multinational Companies

An MNC can become a major economic power in a host country. The workers of the host country may depend on the MNC for jobs. Consumers become dependent upon it for goods and services. The MNC may actually influence or control the political power of the country.

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What are two strategies commonly used by multinational companies?

GLOBAL MARKET ENTRY MODES

As companies expand into other countries, several methods are available for their use.

Licensing

Some companies want to produce items in other countries without being actively involved. They may allow a foreign company to use a procedure they own. *Licensing* is selling the right to use some intangible property (production process, trademark, or brand name) for a fee or royalty.

The Gerber Company started selling its baby food products in Japan by means of licensing. The use of television characters or sports team emblems on hats, shirts, jackets, notebooks, luggage, and other items also involves a licensing agreement. Licensing has a low financial investment, so the potential financial return is often low. The risk for the company is also low.

Franchising

Another method often used to expand into other countries is the *franchise*. A franchise is the right to use a company name or business process in a specific way. Organizations enter into contracts

with people in other countries to set up a business that looks and runs like the parent company. The company obtaining the franchise will usually adapt a range of business elements. Marketing elements such as food products, packaging, and advertising messages must meet both cultural sensitivities and legal requirements.

Both franchising and licensing involve a royalty payment for the right to use a process or company name. Licensing usually involves a manufacturing process. Franchising commonly involves selling a product or service. Franchise agreements are popular with fast-food companies. McDonald's, Burger King, Wendy's, KFC, and Pizza Hut all have used franchising to increase their presence in foreign markets.

Joint Venture

Business partnerships can provide benefits to all parties involved. One type of global partnership is the joint venture. A **joint venture** is an agreement between two or more companies to share a business project.

The main benefit of a joint venture is the sharing of raw materials, shipping facilities, management activities, or production facilities. Concerns about this type of partnership include sharing of profits and not as much control because several companies are involved.

This arrangement is very popular for manufacturing. Joint ventures between Japanese and U.S. automobile manufacturers have been common. For example, the Ford Motor Company entered a joint venture with Mazda Motor Corporation. Ford used Mazda-produced parts for several of its cars. Mazda set up assembly plants for Ford Motor vehicles.

checkpoint >>

How does licensing differ from a franchise?



Cereal Partners Worldwide (CPW) is a joint venture between General Mills and Nestle to sell cereal in Latin America, Europe, the Middle East, and other areas of the world. General Mills brought popular products, such as Cheerios, Lucky Charms, and Trix, into the partnership. Nestle, well known all over the world, has a broad distribution system and is a well-known brand in most foreign countries.

INTERNATIONAL TRADE ORGANIZATIONS

International business activities can be very complex. As a result, several organizations have been created to help companies with global trade activities.

World Trade Organization

The World Trade Organization (WTO) was created in 1995 to promote trade around the world. With more than 150 member countries, WTO settles trade disputes and enforces free-trade agreements between its members. Other goals of WTO include the following.

- Lowering tariffs that discourage free trade
- Eliminating import quotas
- Reducing barriers for banks, insurance companies, and other financial services
- Assisting poor countries with economic growth

International Monetary Fund

The International Monetary Fund (IMF), with more than 150 member nations, helps to promote economic cooperation. It maintains an orderly system of world trade and exchange rates. The IMF was established in 1946 when the economic interdependence among nations was growing at a greater pace than ever before in history.

main idea

Describe activities of international trade organizations and agencies.

NETBookmark

The U.S. Department of Commerce and other federal government agencies provide extensive help to companies involved in exporting. Access the web site shown below and click on the link for Chapter 3. Review the various information sources available to exporters. Select one of the categories of services offered. Describe how companies that are starting or expanding their exporting activities could use the services.

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Before the International Monetary Fund was instituted, a country could often change the value of its legal tender to attract more foreign customers. As other countries lose business, they may impose trade restrictions or lower the value of their currency. As one nation tries to outdo another, a trade war may result. Today, cooperation among IMF nations makes trade wars less likely.

World Bank

The International Bank for Reconstruction and Development is

commonly called the *World Bank*. It was created in 1944 to provide loans for rebuilding after World War II. Today, the bank's key function is to give economic aid to less developed countries. These funds build communications systems, transportation networks, and energy plants.

The World Bank, with more than 180 member countries, has two main divisions: the International Development Association and the International Finance Corporation. The International Development Association (IDA) makes loans to help developing countries. The International Finance Corporation (IFC) provides capital and technical help to private businesses in nations with limited resources. The IFC promotes joint ventures between foreign companies and local companies to further capital investment in developing nations.

checkpoint >>

How does the International Monetary Fund assist countries?

3-3

Assessment

Xtra!
Study Tools

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Key Concepts

Determine the best answer.

- A company is planning to sell the rights to its brand name for use in other countries. This is an example of a
 - joint venture
 - trade agreement
 - franchise
 - licensing agreement
- The international organization that settles trade disagreements and enforces free-trade agreements is the
 - WTO
 - United Nations
 - IMF
 - World Bank

Make Academic Connections

- Economics** Visit a store or online site that sells toys, sporting goods, or other merchandise printed with logos or images belonging to other companies. List the information given that indicates a licensing agreement.
- Communication** Create a visual presentation (using software, photos, or a poster) that communicates the purpose of the International Monetary Fund or the World Bank.

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BUSINESS IMPROVING SOCIETY

The Hunger Site

Each day, more than 1,000 tons of edible food is thrown away in the United States. Elsewhere, several million people go hungry. Around the world, more than 20,000 people die every day from hunger-related causes. But what can one person do to solve this problem?

Tim Kunin and Greg Hesterberg decided to take action with The Hunger Site. On average, 220,000 people from around the world visit the web site each day to click the "Help Feed the Hungry" button.

Kunin and Hesterberg launched The Hunger Site in June 1999. The Hunger Site focuses the power of the Internet on a specific charitable cause: the elimination of world hunger. Since it started, more than 200 million visitors have given more than 300 million cups of staple food to the hungry all over the world. Site sponsors pay for the staple food, distributed to those in need by Mercy Corps and America's Second Harvest.

When visitors to The Hunger Site homepage click on the "Help Feed the Hungry" button, they view sponsor banner ads on the "Thank You" page. Money from banner advertising fees goes to the charity partners. Funds are divided among the organizations to help hungry people in more than 74 countries. Included are those in Africa, Asia, Eastern Europe, the Middle East, Latin America, and North America. Tim and Greg,

long-time friends and social activists, are committed to using this online effort to end world hunger.

Sponsors on The Hunger Site benefit in several ways. First, they are able to reach well-educated, upper-income consumers who are a desired target audience for many goods and services. Also, advertising on The Hunger Site creates good-will. Consumers usually appreciate a company's support of a cause they care about. Sponsorship builds customer loyalty. Research shows that at least three-fourths of adults are more likely to buy a product linked with a cause they care about. More than half would be willing to pay a higher price for the

product if it benefits a social cause in which they believe.

Think Critically

1. Locate another web site that promotes awareness of and attempts to solve a social issue or concern facing society today. Write a brief description of the web site, the issue, and the goals. Include your opinion about the likelihood of success.
2. Identify a social issue that is of interest to you and plan a web site that might be used to help raise awareness of the concern and lead to a solution.

REPRODUCED COURTESY OF THE HUNGER SITE

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CHAPTER 3 Assessment

Xtra! Quiz Prep
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Business Notes

3-1 INTERNATIONAL BUSINESS BASICS

1. Domestic business is the making, buying, and selling of goods and services within a country. International business refers to the business activities needed for creating, shipping, and selling goods and services across national borders.
2. A country is said to have an absolute advantage when it can produce a good or service at a lower cost than other countries. If a country specializes in the production of a good or service at which it is more efficient, it is said to have a comparative advantage.
3. Imports are items bought from other countries. Exports are goods and services sold to other countries. Nations do business with each other to increase the variety of goods and services available to their consumers.
4. Balance of trade is the difference between a country's exports and imports. The difference between a country's total payments to other countries and its total receipts from other countries is the balance of payments.
5. The exchange rate is the value of a currency in one country compared with the value of a currency in another country.
6. The value of global currencies is affected by three main factors: balance of payments, economic conditions, and political stability.

3-2 THE GLOBAL MARKETPLACE

7. The international business environment involves four main components: geography, cultural influences, economic development, and political and legal concerns.
8. Three formal barriers to international trade are quotas, tariffs, and embargoes. A quota is a limit set on the quantity of a product that may be imported or exported within a given period. A tariff is a tax placed on certain imported products. An embargo stops the import or export of a product completely.
9. Actions to encourage international trade include free-trade zones, free-trade agreements, and common markets.

3-3 INTERNATIONAL BUSINESS ORGANIZATIONS

10. Multinational companies conduct business activities in several countries and have management capable of doing business worldwide.
11. Common methods used for global business include licensing, franchising, and joint ventures.
12. The World Trade Organization was created to promote trade around the world. The International Monetary Fund helps to promote economic cooperation by maintaining a system of world trade and exchange rates. The World Bank provides economic assistance to less developed countries.

Communicate Business Concepts

1. Describe how an absolute advantage might affect a country's imports and exports.
2. Explain why it is difficult for a community or a nation to be completely independent.
3. How does international business contribute to a better standard of living for many people in various countries?
4. What are some attitudes and behaviors that might make it difficult for a foreign-based company to do business in the United States?
5. For the following situations, decide whether this is an example of an *informal* or *formal* trade barrier.
 - a. Law requiring that stores be closed on Sunday
 - b. Beliefs about not eating certain foods
 - c. Special tax on the sale of books
 - d. Required nutritional information on food packaging
 - e. Hiring family members when jobs are available in an organization

6. Describe situations in which a joint venture would benefit a company involved in international business.
7. A country sometimes uses high tariffs to protect its new and developing industries. What are two examples of new and developing industries either in the United States or in other countries? Do you think that such industries should be protected by high tariffs? If so, how long should they be protected?
8. Some people believe that the United States should place stiff controls on imports of goods that compete with U.S. businesses to prevent the "exporting of American jobs" to other countries. Give arguments for and against such a position.

Develop Your Business Language

Match the terms listed with the definitions.

9. Goods and services sold to another country.
10. A limit on the quantity of a product that may be imported and exported within a given period.
11. Government restrictions to reduce free trade.
12. An organization that conducts business in several countries.
13. The value of money of one country expressed in terms of the money of another country.
14. Goods and services bought from another country.
15. Stopping the importing or exporting of a certain product or service.
16. An agreement between two or more companies from different countries to share a business project.
17. The difference between a country's total exports and total imports of goods.
18. A tax that a government places on certain imported products.
19. The difference between a country's total payments to other countries and its total receipts from other countries.
20. A nation's transportation, communication, and utility systems.

KEY TERMS

- a. balance of payments
- b. balance of trade
- c. embargo
- d. exchange rate
- e. exports
- f. imports
- g. infrastructure
- h. joint venture
- i. multinational company (MNC)
- j. quota
- k. tariff
- l. trade barrier

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CHAPTER 3 ASSESSMENT

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Make Academic Connections

21. **GEOGRAPHY** Locate examples of multinational companies in different countries. Create a map showing where the companies are based and the other nations in which the companies operate.
22. **ECONOMICS** Go to the web site of an economic community (common market) or a regional trade organization. Make a list of the countries involved and describe some of the organization's activities.
23. **HISTORY** Conduct research on the history of money systems that have been used in other countries. Find examples of the use of a country's currency in another country.
24. **MUSIC** Very often, the music of a country reflects its history, culture, and religion. Find examples of music from other nations that reflect the past and current culture. What aspects of the music are distinctive to that country?
25. **METRIC CONVERSION** To make their exports suitable for use in other countries, U.S. manufacturers must produce goods that are measured in the metric system. For example, if a manufacturer wanted to export paint, which is sold in gallons in this country, it would probably export the paint in 4-liter cans (about 11.4 gallons). To what sizes would the items listed be converted for export to countries using the metric system? (See Appendix D.)
 - a. A quart bottle of liquid detergent
 - b. A 50-yard bolt of fabric
 - c. An automobile engine measured in cubic inches
 - d. A 12-inch ruler
 - e. A bathroom scale that measures in pounds
26. **TECHNOLOGY** Using a spreadsheet program, create a table and graph to report the changing value of the U.S. dollar compared with currencies of three other countries.
27. **MATH** Using the information in Figure 3-4 on page 58, determine how many U.S. dollars someone could buy for these amounts of currencies from other countries.
 - a. In Japan, 1,200 yen
 - b. In Canada, 5 Canadian dollars
 - c. In Saudi Arabia, 150 riyals
28. **CAREER PLANNING** Investigate what types of legal agreements a person would encounter when applying for a job to work for a multinational company in another country.

Linking School and Community

Visit a retail store in your community and select 10 clothing items you would like to own. Being careful not to damage the clothing, create a list of the items and indicate the countries in which these items were manufactured. Prepare a summary with the following information:

- Which countries are most often on your list?
- Are there several countries from the same geographic region?
- What are some possible similarities among these countries?
- What are possible economic advantages of these countries involved in clothing manufacturing?

Web Workout

Sold in more than 200 countries, Coca-Cola is one of the most recognized brand names in the world. A visit to the company's web site provides some insight into how the company has tailored its products and image to address cultural differences around the globe.

Think Critically

1. Locate a web site with information about the culture of a specific country. Write a paragraph describing an element of the culture that Coca-Cola might need to consider when doing business in that country.
2. Visit the web site of a company that produces another popular American product and locate information about its international operations. Write a paragraph summarizing content that demonstrates the company's sensitivity to the cultural differences of customers around the world. Illustrate your work with several images from the web site.

Decision-Making Strategies

Assume you have started a business that manufactures electric toasters that you want to sell to the people of China.

29. What are some potential difficulties that you might encounter when doing business in the Chinese market?
30. What actions could your company take to help improve your opportunities for success?

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Desktop Publishing Event

You and a partner have been hired to create, design, and produce a business publication using desktop publishing software. You have two hours of class time to prepare a newsletter that focuses attention on *International Business Basics*, *The Global Marketplace*, and *Organization for International Business*. Your team is allowed to use two computers, a scanner, and/or clip art. No other equipment may be used. The finished product may be submitted in black and white or in color on plain paper. Word division manuals and dictionaries may be used as reference materials. The second part of this competition includes a one-hour written objective test to determine your knowledge of desktop publishing; the score received on this portion of the event will equal 15 percent of the final event score.

PERFORMANCE INDICATORS EVALUATED

- Understand graphics, text creation, layout, creativity, and selection of appropriate fonts and type sizes for desktop publishing.

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- Prepare an interesting newsletter about international business.
- Incorporate graphics and layout that is pleasing to the reader.
- Incorporate correct punctuation, grammar, and sentence structure.
- Illustrate creativity throughout the publication.

For more detailed information about performance indicators, go to the FBLA web site.

Think Critically

- What is the difference between an average publication and a great publication?
- What strategies can be used to make a publication more reader-friendly?
- Who should be considered when producing a publication?
- Give two examples of items that are distracting on publications

<http://www.fbla-pbl.org/>

Portfolio Activity

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Access the web site shown here to find portfolio activities for this chapter. Use the activities to provide tangible evidence of your learning.

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