Ch 2 The nature and scope of International Business

Main contents:

- Definition of international business
- Scope of international business activities
- Trends in International Business
- International business versus domestic business
- The major carrier of international business: the MNCs
- An emerging phenomenon: International New Ventures
Definition of International Business

• International Business ----- any business activities that cross national boundaries, whether they be movement of goods, services, capital, or personnel; transfers of technology, information, or data, or even the supervision of employees.

• It gives special attention to the multinational enterprises.
Scope of International Business Activities

- International transactions in physical goods
  - mining, petroleum
  - agriculture
  - manufacturing

- International transactions in services
  - construction
  - hotel
  - tourism
  - business consulting
  - retailing, wholesaling
Scope of International Business Activities

- International Transactions in financial areas
  - commercial banking, investment banking
  - securities, insurance
- Communication media
  - telephone
  - magazines
  - books
  - movies
- Transaction in intangibles
  - technology
  - trademarks
Trends in international business (1)

Figure 6.2
Growth in World Exports, World GDP, and FDI, 1990–2001 (index = 100 in 1990)

## Trends in international business (2)

### Table 1.2: The Changing Demographics of World GDP and Trade

<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td>United States</td>
<td>40.3%</td>
<td>20.7</td>
<td>9.8%</td>
</tr>
<tr>
<td>Germany</td>
<td>9.7</td>
<td>4.2</td>
<td>8.9</td>
</tr>
<tr>
<td>France</td>
<td>6.3</td>
<td>3.1</td>
<td>4.3</td>
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<tr>
<td>Italy</td>
<td>3.4</td>
<td>2.7</td>
<td>3.5</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>6.5</td>
<td>3.2</td>
<td>4.6</td>
</tr>
<tr>
<td>Canada</td>
<td>3.0</td>
<td>1.9</td>
<td>3.1</td>
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<tr>
<td>Japan</td>
<td>5.5</td>
<td>6.5</td>
<td>5.0</td>
</tr>
<tr>
<td>China</td>
<td>NA</td>
<td>11.5</td>
<td>7.2</td>
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</tbody>
</table>

Sources: IMF, World Economic Outlook, April 2008. Data for 1963 are from N. Hood and J. Young, The Economics of the Multinational Enterprise (New York: Longman, 1973). The GDP data are based on purchasing power parity figures, which adjust the value of GDP to reflect the cost of living in various economies.
Trends in international business(3)

Figure 1.2
Percentage Share of Total FDI Stock, 1980–2006


Pro. Youzhen Zhao       FDU
Trends in international business (4)

FDI inflows, 1994-2002 (in US$ billion)


Pro. Youzhen Zhao    FDU
Trends in international business(5)

FDI Inflows, 1988–2007


Pro. Youzhen Zhao       FDU
Trends in international business(6)

Despite turmoil in the global economy, global foreign direct investment (FDI) inflows rose by 17 per cent in 2011, to US$1.5 trillion, surpassing their pre-crisis average, based on UNCTAD estimates (figure 1).

Figure 1. Global FDI flows, average 2005–2007 and 2007 to 2011
(Billions of US dollars)

Source: UNCTAD.
* Revised.
** Preliminary estimates.
Trends in international business(7)

Figure 2. UNCTAD’s global FDI quarterly index compared with global foreign portfolio investment index, first quarter 2007 to last quarter 2011
(Base 100: quarterly average of 2005)

Source: UNCTAD.
Notes: The Global FDI Quarterly Index is based on quarterly data of FDI inflows for 67 countries. The index has been calibrated so that the average of quarterly flows in 2005 is equivalent to 100. The similar index for global foreign portfolio investment is also based on quarterly data of portfolio investment inflows for the same 67 countries. This index has also been calibrated so that the average of quarterly flows in 2005 is equivalent to 100. Figures for the last quarter of 2011 are UNCTAD estimates.

Pro. Youzhen Zhao      FDU
Trends in international business(8)

Source: UNCTAD.
Note: Data for the last quarter of 2011 are preliminary.

Trends in international business (10)

**Figure 1.4**

- United States
- Japan
- United Kingdom
- France
- Germany
- Other

## World Trade (1)

### Table 1.1

<table>
<thead>
<tr>
<th>Country</th>
<th>1913</th>
<th>1950</th>
<th>1990</th>
<th>2006</th>
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<tbody>
<tr>
<td>France</td>
<td>21%</td>
<td>18%</td>
<td>5.9%</td>
<td>3.9%</td>
</tr>
<tr>
<td>Germany</td>
<td>20</td>
<td>26</td>
<td>5.9</td>
<td>3.9</td>
</tr>
<tr>
<td>Italy</td>
<td>18</td>
<td>25</td>
<td>5.9</td>
<td>3.9</td>
</tr>
<tr>
<td>Japan</td>
<td>30</td>
<td>—</td>
<td>5.3</td>
<td>2.3</td>
</tr>
<tr>
<td>Holland</td>
<td>5</td>
<td>11</td>
<td>5.9</td>
<td>3.9</td>
</tr>
<tr>
<td>Sweden</td>
<td>20</td>
<td>9</td>
<td>4.4</td>
<td>3.9</td>
</tr>
<tr>
<td>Great Britain</td>
<td>—</td>
<td>23</td>
<td>5.9</td>
<td>3.9</td>
</tr>
<tr>
<td>United States</td>
<td>44</td>
<td>14</td>
<td>4.8</td>
<td>3.2</td>
</tr>
</tbody>
</table>

Volume of world merchandise exports and gross domestic product, 2000-2009

Source: WTO, International Trade Statistics 2010

Pro. Youzhen Zhao    FDU
World exports of commercial services, Q1 2008–Q4 2009

Source: WTO, International Trade Statistics 2010

Pro. Youzhen Zhao  FDU
World Trade (4)

Leading economies of merchandise trade, 2009

Source: WTO, International Trade Statistics 2010
World Trade (5)

World merchandise trade development, 2007–2009

Source: WTO, International Trade Statistics 2010
## Growth in the volume of world merchandise exports and production, 2005-2010

<table>
<thead>
<tr>
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<th>2005-10</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
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<tbody>
<tr>
<td><strong>World merchandise exports</strong></td>
<td>3.5</td>
<td>2.5</td>
<td>-12.0</td>
<td>14.0</td>
</tr>
<tr>
<td><strong>Agricultural products</strong></td>
<td>3.5</td>
<td>2.5</td>
<td>-2.5</td>
<td>7.5</td>
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<tr>
<td><strong>Fuels and mining products</strong></td>
<td>1.5</td>
<td>1.0</td>
<td>-5.5</td>
<td>5.5</td>
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<tr>
<td><strong>Manufactures</strong></td>
<td>4.0</td>
<td>2.5</td>
<td>-15.0</td>
<td>18.0</td>
</tr>
<tr>
<td><strong>World merchandise production</strong></td>
<td>2.0</td>
<td>1.0</td>
<td>-2.5</td>
<td>4.0</td>
</tr>
<tr>
<td><strong>Agriculture</strong></td>
<td>2.0</td>
<td>3.5</td>
<td>0.5</td>
<td>0.0</td>
</tr>
<tr>
<td><strong>Mining</strong></td>
<td>0.5</td>
<td>1.5</td>
<td>-1.5</td>
<td>2.0</td>
</tr>
<tr>
<td><strong>Manufacturing</strong></td>
<td>2.5</td>
<td>0.0</td>
<td>-4.0</td>
<td>5.5</td>
</tr>
<tr>
<td><strong>World GDP</strong></td>
<td>2.0</td>
<td>1.5</td>
<td>-2.5</td>
<td>3.5</td>
</tr>
</tbody>
</table>

*Note: See the Metadata for the estimation of world aggregates of merchandise exports, production and GDP.*

Source: International Trade Statistics 2011, WTO
Discussion and Sharing

What is the different about international business versus domestic business? Anything special?
What is different about international business

- Multinational conflict (both inside and outside the corporation)
  - e.g. struggle for control (inside);
    - goals of company vs. host country (outside)
- Multinational environment (complex, dynamic, multi-dimensional)
  - e.g. Nanjing Automobile (Group) and Rover Carrefour in China, April 2008
- Management challenge (management mentality and practice)
  - e.g. Hua Li Group
- International risk (political risk, foreign exchange risk, etc.)
  (examples: next slides)
E.g. Foreign exchange risk


- About 1/3 of the exporting companies in Guangdong province will be closed due to reevaluation of RMB, new labor law, environmental protection, rising wages, materials and export tax refunding policy.

-------Mr. Tao Dong (陶冬)
Chief Economist of Credit Suisse First Boston

(textile, shoes, toys----low-end products ---industrial upgrading)

Source: China Business News    May 9, 2008
E.g. Political risk

Lenovo’s story in the States

• PCs --- threatening “national security”?  
• When the U.S. government institutions tried to buy computers from Lenovo, once again national security concern became a reason to say “no”!
Lenovo’s ownership structure as of 2/29/08

- Public shareholders 44.4%
- IBM 6.7%
- TPG Capital, General Atlantic LLC and Newbridge Capital LLC 6.5%
- Directors 0.6%
- Original Founders 14.6% (held indirectly through Legend Holdings Limited)
- **Chinese Academy of Sciences** 27.2% (held indirectly through Legend Holdings Limited)

(CAS's interest is entirely passive. It has never appointed any members of Lenovo's boards or any of its executives, nor has it directed Lenovo's strategy or its day to day management.)

Source: Jeffery Carlisle, Vice President, International Public Policy and government Affairs, Lenovo
<table>
<thead>
<tr>
<th></th>
<th>中海油</th>
<th>VS</th>
<th>雪佛龙</th>
</tr>
</thead>
<tbody>
<tr>
<td>每股价格</td>
<td>67美元</td>
<td>VS</td>
<td>63美元</td>
</tr>
<tr>
<td>合计出资</td>
<td>185亿美元</td>
<td>VS</td>
<td>170亿美元</td>
</tr>
<tr>
<td>出资方式</td>
<td>纯现金</td>
<td>VS</td>
<td>现金加股票</td>
</tr>
</tbody>
</table>

有利可图的竞争对手
The proposed US$ 2.2 billion acquisition of 3Com by Bain Capital LLC and China’s Huawei Technologies Co. sparked national-security concerns in Washington.

Under the terms of this deal, Huawei, founded by former army officer Ren Zhengfei 20 years ago, will get a 16.5% stake in 3 Com.

“There is a growing apprehension in the Congress about the proposed acquisition”----CFIUS (Committee on Foreign Investment in the United States) launched national security review in Jan.

Bain Capital cancelled its application of acquisition in Feb., 2008.
Chinaalco and Rio Tinto 2009

• On Feb. 12, 2009, a strategic collaboration agreement was signed between ChinaAlco and Rio Tinto that Chinaalco would input US$ 19.5 billion to Rio Tinto (12.3 billion to a JV and 7.2 billion to purchase convertible bonds). If it’s done, Chinaalco would have a 18% ownership of Rio Tinto.

• In June 2009, Rio Tinto cancelled this agreement by paying US$195 million “goodbye fee” to ChinaAlco.

• By this, Chinaalco had arranged US$21 billion fund-raising for this deal. And that prospective deal had been widely reported in Chinese media.
Huawei cancelled its application to acquire 3Leaf in 2011

- Huawei announced to acquire 3Leaf, a company in San Francisco Bay area, with 2 million US dollars, in May 2010
- It provided CFIUS with all the details of this deal in Nov. 2010
- 5 people of House of Representatives declared that this deal would threaten American computer network
- Huawei accepted CFIUS’s advice to cancel its application in Feb. 2011
What is different about international business

• More opportunities and choices
  (analysis from the perspective of value chain)

Analysis: better resource configuration

Examples:
  Transfer pricing
  Extending the life-span of products and technologies
The Multinational Corporation

• Definition

• MNCs have substantial direct investment in foreign countries, not just an export business. They should be engaged in the active management of these off-shore assets rather than simply holding them in a passive financial portfolio.

------ Christopher A. Bartlett
Harvard Business School
The Multinational Corporation

An enterprise whether of public, private, or mixed ownership

(a) comprising in two or more countries, regardless of the legal form and field of activity of those entities,

(b) which operates under a system of decision making permitting coherent policies and a common strategy through one or more decision making centers,

(c) in which the entities are so linked, by ownership or otherwise, that one or more of them may be able to exercise a significant influence over the activities of the others, and, in particular, to share knowledge, resources, and responsibilities with others.

----United Nations
The Multinational Corporation

• MNC is a very recent phenomenon, less than a century, and a vast majority have been developed in the post World War II years.

• Emergence of Services MNCs (Banking, insurance Corporation, Consulting, Accounting, Publication)

• Management integration of operations located in different countries as the key differentiating characteristic of MNC
The Multinational Corporations

• A key feature of the changing international business pattern.
  – International Mentality
  – Multinational Mentality
  – Global Mentality
  – Transnational Mentality
From domestic to global thinking: five generic mindset

-- Domestic mindset
-- International mindset
-- Multinational mindset
-- Global mindset
-- Transnational mindset
The Domestic mindset

• All reference points or experiences come from one single culture of business environment

• Limitation: in an interconnected economy, a high degree of isolation is clearly at risk
The International Mindset

The main role of overseas operations is to support the domestic parent company, so

• Products are developed for domestic market, only subsequently sold abroad
• Technology & knowledge are transferred from parent company to overseas operators
• Offshore manufacturing is as a means to protect home market
The Multinational mindset

*Emphasize the differences among national markets and operating environments,*

1. The MNC adopts more a flexible approach to overseas operation by modifying products, strategies & management practices country by country.
2. Subsidiaries are sensitive and responsive to local environment.
3. Managers of foreign operations tend to be highly independent entrepreneurs, often nationals of host country.
The Global Mindset

National tastes and preferences are more similar than different, so

• Creating products for a world market
• Manufacturing products on global scale in a few efficient plants
• Make and sell the same thing, the same way, everywhere
• More central coordination and control
Strategic capabilities of Transnational Corporations

Global efficiency

+ Multinational local responsiveness

+ Development and diffusion of worldwide knowledge
The Transnational Mindset

• More responsive to local needs while retaining global efficiency
• Resources and activities are dispersed but specialized
• Differentiated contributions by national units to integrated worldwide operation
• Knowledge developed jointly and shared worldwide
# Strategic Orientation of International, Multinational, Global and Transnational Companies

<table>
<thead>
<tr>
<th>Strategic Orientation</th>
<th>International</th>
<th>Multinational</th>
<th>Global</th>
<th>Transnational</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exploiting parent-company knowledge and capabilities through worldwide diffusion and adaptation</td>
<td>Building flexibility to respond to national differences through strong, resourceful, and entrepreneurial national operations</td>
<td>Building cost advantages through centralized, global-scale operations</td>
<td>Developing global efficiency, flexibility, and worldwide learning capability simultaneously</td>
<td></td>
</tr>
</tbody>
</table>
## Organizational Characteristics of the Multinational Corporations

<table>
<thead>
<tr>
<th>Organizational Characteristics</th>
<th>International</th>
<th>Multinational</th>
<th>Global</th>
<th>Transnational</th>
</tr>
</thead>
<tbody>
<tr>
<td>Configuration of assets and capabilities</td>
<td>Sources of core competencies centralized, others decentralized</td>
<td>Decentralized and nationally self-sufficient</td>
<td>Centralized and globally scaled</td>
<td>Dispersed, interdependent, and specialized</td>
</tr>
<tr>
<td>Role of overseas operations</td>
<td>Adapting and leveraging parent company competencies</td>
<td>Sensing and exploiting local opportunities</td>
<td>Implementing parent company strategies</td>
<td>Differentiated contributions by national units to integrated worldwide operation</td>
</tr>
<tr>
<td>Development and diffusion of Knowledge</td>
<td>Knowledge developed at the center and transferred to overseas units</td>
<td>Knowledge developed and retained within each unit</td>
<td>Knowledge developed and retained at center</td>
<td>Knowledge developed jointly and shared worldwide</td>
</tr>
</tbody>
</table>
International New Ventures

Origin:
• 2004 Decade Award Winning Article

“Toward a theory of international new venture”, by Benjamin Oviatt and Patricia McDougall (1994)

Journal of International Business Studies
A definition of INVs

• “We define an international new venture as
A business organization that, from inception, seeks to derive significant competitive advantage from the use of resources and the sale of outputs in multiple countries”.

-----Oviatt and McDougall( 1994)
### Theoretical perspectives

#### Geographic Scope

<table>
<thead>
<tr>
<th>Domestic</th>
<th>International</th>
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</thead>
<tbody>
<tr>
<td>Significant amounts of literature</td>
<td>Significant amounts of literature</td>
</tr>
<tr>
<td>significant amounts of literature</td>
<td></td>
</tr>
</tbody>
</table>

**Organization**
- new
- established

**Age**
- Domestic
- International
Types of International New Ventures

Coordination of Value Chain Activities

Number of Countries Involved

- Few Activities Coordinated across Countries (Primarily Logistics)
- Many Activities Coordinated across Countries

New International Market Makers

- Export/Import Start-up
- Multinational Trader
- Geographically Focused Start-up
- Global Start-up

Prof. Youzhen Zhao
FDU
Example: Shanghai San Wang

- Founded in Feb. 2005 by a Chinese Japanese and a Japanese company, manufacturing door seal of refrigerators
- Began to export in June 2005, with Hitachi as its main client
- Mitsubishi became the client from Sep. 2007
- Developed Chinese domestic market and began to produce for a JV between Taiwan and Japanese companies in March 2008
- Employees: 23 at the foundation; 87 at the end of 2008
More examples

- Aroma (candle….)
- Eral (clothes….)
- Lisi (plastic products….)
- Smal (small electric appliances….)
- YDH (auto parts)
Further thoughts of INVs

• Formation Process
• Main characteristics that distinguish them from domestic new ventures
• Competitive advantages of INVs

INVs’ development in China, in Italy? Difference?