International Management **& Economics**

Part 1

INTERNATIONAL BUSINESS
AN OVERVIEW

Case: Euro Disney

- 1992 debut – “Cultural Chernobyl”

- Why France?:
  government concessions, central location
  Popularity of french characters

- large number of adaptations

- Euro’s problems:
  The leisure habits of Europeans; competition
  The cost of visiting the park; U.S-French
  agricultural trade animosity

I - Introduction

- **International Business is all business transactions that involve two or more countries.**

- **International Business comprises a large and growing portion of the world’s total business.**

- **International Business usually takes place within a more diverse external environment.**

- **Why Companies Engage in International Business**

A) To Expand Sales: companie's sales are dependent on two factors: the consumers' interest in their product or services and the consumers' ability and willingness to buy them.

B) Acquire Resources: products, services, technology, and information

C) Diversify Sources of Sales and Supplies

D) Minimize Competitive Risk: companies move internationally for defensive reasons. Profits from one market can be used to expand operations in other markets.

Reasons for Recent International Business Growth

Expansion of Technology:

transportation, telecommunications;

Transportation and telecommunications costs are more conducive for international operations.

Liberalization of Cross-Border Movements:

goods, services, labour, Capital

Development of Supporting Institutional Arrangements: development by business and governments of institutions that enable us to effectively apply that technology.

Increase in Global Competition:

new products become global; Globalization of production

Modes of International Business

A - Merchandise Exports and Imports: visibles and invisibles

B - Performance of Services: fees; turnkey operations; management Contracts

C - Use of Assets: licensing agreements; royalties; franchising

D - Investments:

1) Foreign Direct Investment: gives the investor a controlling Interest in a foreign company. It gives access to:

- foreign markets
- foreign resources
- higher profits than exporting
- partial ownership

2) Portfolio Investment: stock in a company or loans to a company or country in the form of bonds, bills, or notes that the investor purchases.

E - Other Operational Definitions

- Strategic Alliances

F – MNCs, MNEs, TNCs, Global Company, Multidomestic Company

External Influences on International Business

Understanding a Company's Physical and Societal Environment Managers need a working knowledge of business operations, a working Knowledge of political sciences, law, anthropoly, sociology, economics, and geography.

Evolution of Strategy in the Internationalization Process

A) Patterns of Expansion: passive; external to internal handling of the business; limited to extensive modes of operations

B) Deepening mode of Commitment

C) Geographic Diversification (similar cultural background)

D) Leapfrogging of Expansion: companies are starting with a global focus.

The role of risk in International Management

Political risk and negotiation strategies

- Objectives
- Introduction
- Country analysis and political risk assessment
- Negotiation strategies
- Strategic management and political risk.

Objectives

- *Examine* the nature of political risk.
- *Understand* how to apply some of the tools and resources companies can use to measure and forecast political risk.
- *Discuss* some of the ways that firms manage risk.
- *Review* typical strategies and tactics used in negotiating agreements.

Introduction

- **Country risk analysis** examines the chances of non-market events (political, social and economic) causing financial, strategic or personnel losses to a firm following FDI in a specific country market.

Generic PEST framework

- The generic political, economic, social (or "socio-cultural") and technology **(PEST)** framework is used to:
  - map out particular competitive environments or investment contexts for firms at the regional or national level.
  - compare country conditions.
  - build future scenarios to understand short-term and long-term threats and opportunities.

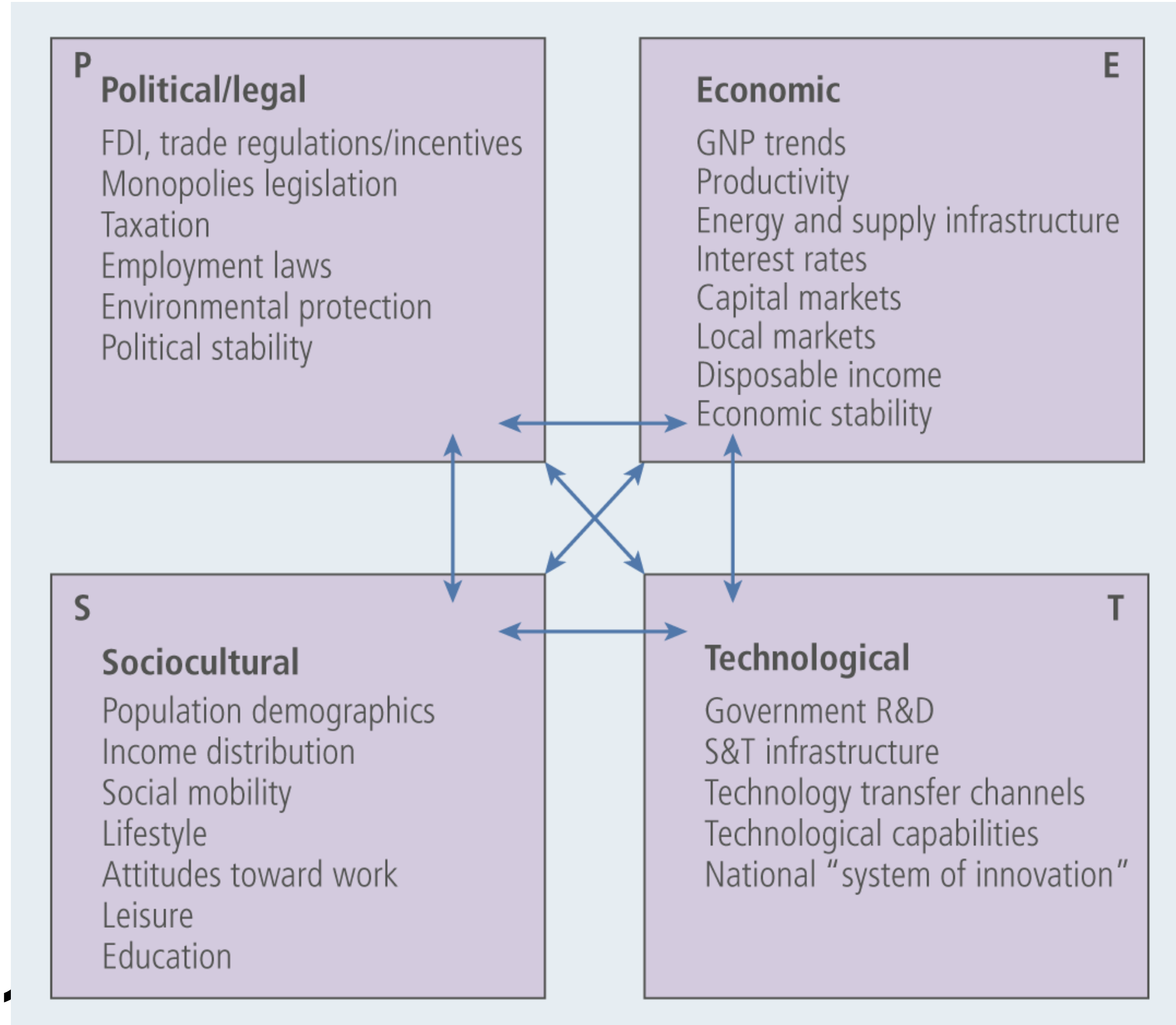

Figure
analysis

Desirable additions to the PEST framework

- In addition to the PEST framework, managers must add:
  - Depth of knowledge
    - risk assessments by political scientist and analysts
    - economic analysis
    - social analysis
  - Foresight
    - accurate scenario-building.

RISK

- This is the Chinese character for 'risk'. The first symbol is the symbol for "danger", while the second is the symbol for "opportunity".
- Risk is seen as danger and opportunity combined.

The nature of political risk

Levels of political risk

- **Macro political risk:** a risk that affects all foreign enterprises in the same way
- **Micro political risk:** a risk that affects selected sectors of the economy or specific foreign businesses.

Types of political risk

- **Legal-governmental risks** are potentially harmful to foreign businesses but are the product of, or permissible within, the existing political, economic and legislative system.
- **Non-legal or extra-governmental risks** lie outside the system and are a violation of existing laws.

	Legal/governmental	Non-legal/extra-governmental
Macro	Newly-elected government New overarching trade agreements General changes to policies or laws relating to foreign investors or investments	Coup or civil war Military attacks from other nations Internal terrorist attacks General corruption Mafia-type activities General property expropriation
Micro	Firm-specific legislation with adverse effects (e.g., export licenses, import duties, rules on profit repatriation) Subsidies or protection for competitors	Targeted attacks Firm-specific sabotage, extortion Theft or abuse of intellectual property rights Targeted or selective corruption

Figure 2 Types and levels of political risk

Sources of political risk	Groups that can generate political risk	Effects of political risk
Political philosophies that are changing or are in competition with each other	Current government and its various departments and agencies	Expropriation of assets (with or without compensation)
Changing economic conditions	Opposition groups in the government that are not in power but have political clout	Indigenization laws
Social unrest	Organized interest groups such as teachers, students, workers, retired persons, etc.	Restriction of operating freedom concerning, e.g., hiring policies and product manufacturing
Armed conflict or terrorism	Terrorist or anarchist groups operating in the country	Cancellation or revision of contracts
Rising nationalism	International organizations such as the World Bank or the United Nations	Damage to property and/or personnel from terrorism, riots, etc.
Impending or recent political independence	Foreign governments that have entered into international alliances with the country or that are supporting opposition to the government	Loss of financial freedom such as the ability to repatriate profits
Vested interests of local business groups		Increased taxes and other financial penalties
Competing religious groups		
Newly created international alliances		

Table 1: Political risk: sources, agents, and effects

Country analysis and political risk assessment

Risk assessment

- Forecasting political risk:
  - informal approaches for assessing risk
  - formal systematic procedures for assessing risk
    - ad hoc groups, standing committees
- Focus of assessment:
  - the political system in which the company will be doing business
  - the goods to be produced and the operations to be carried out

Quantifying risk vulnerability.

Quantifying risk vulnerability

- The political/legal, economic, sociocultural and technological environment of a foreign country has different implications depending on the type of international business that a firm is evaluating.
  - For example: export restrictions are more important if a firm is seeking to set up a plant to produce goods for exports than if the products are for the local market.

Weighted Country Risk Assessment Model			Country A			Country B		
		Selected Criteria	Risk (1 = High)	Importance (1 = Low)	Combined score (/25)	Risk (1 = High)	Importance (1 = Low)	Combined score (/25)
Political environment	1	Stability of the local political system	4	4	16	2	4	8
	2	Likelihood of internal conflict	5	4	20	2	4	8
	3	External threats to stability	3	3	9	3	3	9
	4	Harmful government intervention in the economic system	5	4	20	2	4	8
	5	Reliability of the country as a trading partner	3	4	12	3	4	12
	6	Policy continuity/predictability	4	5	20	2	5	10
	7	Stability of tax and tariff regime	5	4	20	3	4	12
	8	Effectiveness of public administration	4	3	12	3	3	9
	9	Prevalence of corruption	5	3	15	1	3	3
	10	Bureacratic delays	5	4	20	1	4	4
	11	Enforceability of contracts	4	4	16	2	4	8
	12	Corporate governance and ethics legislation	3	2	6	2	2	4
	13	Labor unions and labor relations	3	5	15	3	5	15
	14	Linguistic/ethnic/religious tensions	4	1	4	3	1	3
	15	Social stability	4	2	8	3	2	6

Table 2: The Weighted Country Risk Assessment Model

Weighted Country Risk Assessment Model			Country A			Country B		
		Selected Criteria	Risk (1 = High)	Importance (1 = Low)	Combined score (/25)	Risk (1 = High)	Importance (1 = Low)	Combined score (/25)
International economic environment	16	Import restrictions	2	4	8	2	4	8
	17	Export restrictions	3	5	15	3	5	15
	18	Attitudes toward foreign investors	4	3	12	3	3	9
	19	Respect for intellectual property rights (patents, brands)	4	4	16	1	4	4
	20	Restrictions on monetary transfers	3	5	15	3	5	15
	21	Revaluation of the currency during the last five years	3	2	6	2	2	4
	22	Balance of payments situation	4	2	8	4	2	8
Domestic economic environment	23	Per capita income	3	1	3	3	1	3
	24	Economic growth over the last five years	4	1	4	2	1	2
	25	Potential growth over the next three years	4	1	4	4	1	4
	26	Inflation over the past two years	3	3	9	2	3	6
	27	Accessibility of domestic capital markets to outsiders	4	4	16	4	4	16
	28	Availability of high-quality local labor force	4	5	20	4	5	20
	29	Availability of energy resources	4	4	16	4	4	16
	30	Infrastructure; transportation and communication systems	3	4	12	3	4	12
		TOTALS	113	100	377	79	100	261

Table 2 Continued