

 CENGAGE

International Business

Third Edition

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To our students:
past, present and future

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PREFACE TO THE 3rd EDITION

A EUROPEAN VIEW ON INTERNATIONAL BUSINESS

This book offers a European perspective on international business. In the age of globalization, isn't that a contradiction? Why did we set out to write a textbook specifically for you as students in Europe? There are five considerations why we have been writing this book:

- Students learn best from cases and examples that they can relate to. Thus we have developed a number of cases and examples specifically for this book that tell the experiences of European businesses. At the same time, we wish to broaden your horizon and equip you with an understanding of businesses in different parts of the world. As an international manager you will need to understand both the regional and global dimensions of business. Thus we also include a large number of cases and examples from all over the world.
- In Europe, international business (IB) is relevant for (almost) every business. Most textbooks in this field have been written primarily for US students and thus treat global business primarily as a phenomenon for big companies, with internationally operating entrepreneurs being an exception. That is understandable given the vast size of the domestic market of the USA. However, in Europe, where national markets are much smaller, even small- and medium-sized firms soon hit the limits of their domestic markets, and IB becomes a natural part of everything they do. Thus we relate much more to the needs and challenges faced by smaller firms, especially in Europe.
- Textbooks written by US authors typically draw primarily on scholarly work by US-based authors. However, there is important work by European scholars that is, in our view, not sufficiently appreciated in these textbooks. Thus we pay special attention to work by European scholars, for example the work by Hall and Soskice on varieties of capitalism (Chapter 2), by Hofstede and other European authors on culture and languages (Chapter 3), by Dunning, Buckley and Casson on the theory of foreign direct investment (Chapter 6), by Matten, Moon and others on corporate social responsibility (Chapter 10), by Nordic scholars in the tradition of Johansen and Vahlne on internationalization processes (Chapter 11), and by scholars across Europe on knowledge management and governance (Chapter 15) and on expatriate management (Chapter 16).
- European businesses deal with a variety of subtle differences when engaging in neighbouring countries as well as with big differences when going to, for example, China. This contrasts with US businesses for whom IB is a big strategic change from domestic operations (unless they go to Canada) and thus involves substantial differences. Thus we treat IB as a natural and integrated part of business activity but subject to a range of subtle differences when dealing with nearby yet still foreign institutions and businesses.

- European businesses do most of their IB elsewhere in Europe, where they operate within the institutional framework of the European Union (EU). Understanding this framework is thus essential. Therefore, we devote one entire chapter specifically to the institutional framework of the EU (Chapter 8), and we relate to the EU regulatory framework in later chapters of the book, for example EU competition policy in Chapters 13 and 14.

Of course, as an alternative to using an English-language ‘European’ textbook such as ours, instructors may consider adapting a textbook in local languages, for example in German or French. This approach has advantages – students may be more at ease with their own language, and examples are even more local. However, we would encourage instructors to adopt our textbook as a core or recommended reading because:

- Engaging in global business in most parts of the world requires competences in English, and the classroom is an ideal place to acquire and polish English language skills.
- An important aspect of building competences for IB is to put oneself in the position of a business partner or competitor in order to understand how they would handle a certain situation. Successful international managers are also able to critically reflect on the merits and demerits of their own country, its institutions and its businesses. The development of these capabilities requires looking ‘beyond the horizon’ of your national economy and engaging with individuals and businesses in other countries. Our European view encourages students to broaden their horizon beyond national boundaries.
- Both authors, being non-native speakers of English, remember how hard it was to start using English in a classroom setting. Thus we have written the text avoiding unnecessarily complex or colloquial expressions that may be inaccessible to students whose first language is not English.

OUR PERSPECTIVE AS AUTHORS

We, your authors, have studied, worked and taught global business throughout our careers. This personal experience and expertise gives us our foundation for writing this book and enables us to offer you diverse yet complementary perspectives on international business:

- We have conducted research ourselves on many of the issues discussed in this text. Mike Peng has investigated, for example, the institution-based view of business (Chapters 2 and 3), the resource-based view (Chapter 4) and strategies of global firms (Chapters 13 and 14). Klaus Meyer has also contributed to the institution-based view (Chapter 2) and investigated in particular foreign direct investment (Chapter 6) and foreign entry strategies (Chapters 11 and 12). This work has been published in leading scholarly journals in the field, such as the *Journal of International Business Studies*, *Strategic Management Journal* and *Journal of Management Studies*.
- In our research, we have investigated a wide range of different contexts, including in particular emerging economies. Mike Peng’s research has focused on contemporary China and other transition economies, while Klaus Meyer has studied businesses in Central and Eastern Europe as well as Asian economies such as China, Vietnam and Myanmar, and multinational firms from Germany, Denmark and the UK.

- We have taught at universities quite literally around the globe and thus learned from discussions with students offering a wide variety of perspectives and experiences. Mike Peng has taught at the University of Hawaii at Manoa, Ohio State University and University of Texas at Dallas (all USA), as well as at the Chinese University of Hong Kong and a number of universities in mainland China. Klaus Meyer has taught at Copenhagen Business School (Denmark), Hong Kong University of Science and Technology (Hong Kong), National Cheng-Chi University (Taiwan), as well as the University of Reading and the University of Bath (both UK). He recently also spent six years in Shanghai at China Europe International Business School; his first-hand experience of business in China is thus reflected in many cases.

PEDAGOGICAL FEATURES OF THIS BOOK

In designing this book, we have been guided by three main pedagogical ideas:

- 1 We want to provide a comprehensive yet solidly research-grounded overview of the field.
- 2 We want to facilitate learning of the essential concepts and analytical framework.
- 3 We want to stimulate students' own critical reflection and discussions that go beyond rote learning of the material presented in the text.

COMPREHENSIVE, RESEARCH-GROUNDED

International business is a very broad topic that integrates many scholarly disciplines. In selecting and presenting the material, we have been guided by two objectives: to integrate complex materials in an accessible style and to build on contemporary research. First, to provide a consistent structure that helps to analyze this complex subject, we organize the book around a unified framework that integrates all chapters. Given the wide range of topics in IB, many textbooks present the discipline item by item: 'This is how MNEs manage X.' Rarely do authors address: 'Why do MNEs manage X in this way?' More importantly, what are the big questions that the field is trying to address? Our framework suggests that IB can be united by one big question and two core perspectives. The big question is: 'What determines the success and failure of firms around the globe?' To address this question, we introduce two core perspectives: (1) an institution-based view and (2) a resource-based view. This framework presents an extension of our own research that investigates IB topics using these two perspectives. This focus on one big question and two core perspectives enables this book to analyze a variety of IB topics in a coherent fashion.

Second, this book engages leaders through an evidence-based approach. We have endeavoured to draw on the latest research, as opposed to the latest fads. The comprehensive yet research-grounded coverage is made possible by drawing on the most comprehensive range of the literature. Specifically, we have read and considered every article over the past twenty years in the *Journal of International Business Studies* and other leading IB and general management journals. In addition, we have consulted numerous specialty journals for specific chapters. As research for the book progressed, our respect and admiration for the diversity of insights of our field and the relevance of neighbouring disciplines grew substantially. The result is a

comprehensive set of evidence-based insights on IB. While citing every article is not possible, we cover work from a wide range of relevant scholars.

Furthermore, we provide evidence through contemporary examples that illustrate theoretical concepts in practice. These up-to-date examples are found all over the world, with an emphasis on European business. They not only encourage students to build bridges between theoretical frameworks and the contemporary world of business but also encourage them to find further examples in newspapers and magazines, such as *Financial Times* and *The Economist*. Many of the cases have been contributed by scholars from around the world, who have first-hand knowledge of the companies and contexts concerned, including Finland, Italy, France, Germany, the UK and the USA.

SUPPORTING LEARNING

The comprehensive nature of IB means that students of the subject have to engage with a wide range of concepts and frameworks based on current research. To facilitate the accessibility of this material, we use a clear, engaging, conversational style to tell the ‘story’. Relative to other books, our chapters are generally more lively. Moreover, we have introduced a number of features which aim to facilitate the learning of key concepts, facts and frameworks:

- We explicitly state **learning objectives** at the outset and in the margin throughout each chapter. These learning objectives are the basis for a brief **chapter summary** at the end of each chapter.
- An **Opening case** about a firm or country provides a taster of the issues from a real world perspective and a basis to reflect over issues introduced in the chapter.
- Engaging in international business requires knowledge of many concepts. We therefore state the definitions of key concepts as **margin notes** when they are first introduced, and we include a **Glossary** at the end of the book containing all key concepts in alphabetical order.
- **In Focus** boxes illustrate key concepts on the basis of shorter real world examples.
- So what? We conclude every chapter with **Implications for practice**, which clearly summarizes the key learning points from a *practical* standpoint in one or more tables.

CRITICAL REFLECTION AND DISCUSSION

The field of IB is subject to many debates, and many broader debates on globalization affect internationally operating MNEs. While it is important to ‘learn’ concepts and frameworks, we strongly believe that it is also important to critically engage with the ‘how’ and ‘why’ questions surrounding the field. It is debates that drive the field of practice and research forward. We therefore aim to encourage students to critically reflect over the material presented (we expect most students to find at least

one argument where they disagree with us) and to engage in cutting-edge debates. Several features aim to provoke discussion and critical reflections in each chapter:

- **Debates and extensions** section for *every* chapter (except Chapter 1, which is a big debate in itself).
- **Photo questions** challenge you to think about the consequences of the material presented. We use photos not only to illustrate the text but as a stimulus for developing your own ideas and arguments.
- **Recommended readings** provide a basis for further study, for example when you want to prepare a class assignment or a dissertation on a topic.
- **Critical discussion questions** at the end of each chapter provide a basis for group discussions or individual work on the issues in the chapter and their broader implications for society. Many of these questions concern ethical issues that have increasingly come to the forefront of public debates.
- **Closing cases** to each chapter provide the story of a specific company engaged in international business. Analysis of this case along with the questions provided will help gain deeper insights into the topic of the chapter and help to relate concepts to the real world of business.
- A set of **Integrative cases** provide further opportunities to deepen the study material and to discuss how firms may handle specific challenges they encounter in international business.

MOVING IN A FAST-CHANGING WORLD

In the eight years since the publication of the first edition of this textbook, the international economy has evolved in many ways. Some trends highlighted in our book, like the rise of emerging economies and heightened volatility, have accelerated. New phenomena, such as emerging economy MNEs and international arbitrage tribunals, gained prominence and thus deserve consideration in a broad-based textbook.

The main focus of our revisions has been on introducing new debate and extension sections on contemporary issues as well as new business cases, mostly researched by ourselves. For example, the eurozone and its crisis as well as Brexit are now extensively discussed in Chapter 8, supported by clarification of concepts such as the common market and extensive empirical data. Along with numerous updates on the global business environment, we also have used the opportunity to sharpen some of the conceptual frameworks and to incorporate recent research. For example, the discussion of mergers and acquisition in Chapter 14 has been substantially extended. Moreover, we are exploring the opportunities and challenges of modern technologies on IB, in particular in internet-enabled businesses. Thus, we included new cases such as *Airbnb* (Chapter 1), *Spotify* (Chapter 11) and *BMW* and *SSI Schaefer* (Integrative Cases).

These and other updated real world cases strengthen the bridge between theory and practice, making this textbook not only scholarly grounded, but – we hope – a foundation and stimulation for many international business careers.

Klaus Meyer
London, Ontario, May 2018

SCHOLARLY JOURNALS

Throughout this book, we make extensive reference to publications in scholarly journals. To report these references in an efficient way, we use abbreviations for management and economics journals such as *JIBS*, *AMJ*, *JMS* or *IBR*, as reported below. You will normally find these sources through your university library's databases, though a search through *Google Scholar* may also get you to the right place. When citing journals in other fields as well as newspapers and magazines, we report the full name (*Business Week*, *The Economist*). To trace newspaper articles, it is often easiest to go to these publications' own homepages and type the full title of the article in the search engine.

JOURNAL ACRONYMS

The most frequently cited journals are set in **bold**.

AE – *Applied Economics*; **AER** – *American Economic Review*; **AIM** – *Advances in International Marketing*; **AJS** – *American Journal of Sociology*; **AMA** – *Academy of Management Annals*; **AME** – *Academy of Management Executive*; **AMJ** – *Academy of Management Journal*; **AMLE** – *Academy of Management Learning & Education*; **AMR** – *Academy of Management Review*; **APJM** – *Asia Pacific Journal of Management*; **ASR** – *American Sociological Review*; **ASQ** – *Administrative Science Quarterly*; **ARS** – *Annual Review of Sociology*; **BEQ** – *Business Ethics Quarterly*; **BH** – *Business History*; **B&S** – *Business and Society*; **BSR** – *Business Strategy Review*; **CBR** – *China Business Review*; **CCM** – *Cross Cultural Management: An International Review*; **CES** – *Comparative Economic Studies*; **CJAS** – *Canadian Journal of Administrative Studies*; **CJE** – *Canadian Journal of Economics*; **CJWB** – *Columbia Journal of World Business*; **CMR** – *California Management Review*; **CPIB** – *Critical Perspectives in International Business*; **ECLR** – *European Competition Law Review*; **EER** – *European Economic Review*; **EJ** – *Economic Journal*; **EJE** – *European Journal of Education*; **EJLE** – *European Journal of Law and Economics*; **EJM** – *European Journal of Marketing*; **EJPE** – *European Journal of Political Economy*; **ELJ** – *European Law Journal*; **EMJ** – *European Management Journal*; **EMR** – *European Management Review*; **EoT** – *Economics of Transition*; **ETP** – *Entrepreneurship Theory and Practice*; **FA** – *Foreign Affairs*; **HBR** – *Harvard Business Review*; **HR** – *Human Relations*; **HRM** – *Human Resource Management*; **HRMR** – *Human Resource Management Review*; **IBR** – *International Business Review*; **ICC** – *Industrial and Corporate Change*; **IE** – *International Economy*; **IJCCR** – *International Journal of Cross-Cultural Management*; **IJHRM** – *International Journal of Human Resource Management*; **IJKM** – *International Journal of Knowledge Management*; **IJMR** – *International Journal of Management Reviews*; **IJPE** – *International Journal of Production Economics*; **IMR** – *International Marketing Review*; **IRLE** – *International Review of Law and Economics*; **JAMS** – *Journal of the Academy of Marketing Science*; **JAP** – *Journal of Applied Psychology*; **JB** – *Journal of Business*; **JBE** – *Journal of Business Ethics*; **JBF** – *Journal of Banking and Finance*; **JBR** – *Journal of Business Research*; **JBV** – *Journal of Business Venturing*; **JCMS** – *Journal of Common Market Studies*; **JCR** – *Journal of Consumer Research*; **JEBO** – *Journal of Economic Behavior and Organization*; **JEI** – *Journal of Economic Issues*;

JEL – *Journal of Economic Literature*; **JEP** – *Journal of Economic Perspectives*; **JEPP** – *Journal of European Public Policy*; **JES** – *Journal of Economic Surveys*; **JFE** – *Journal of Financial Economics*; **JHE** – *Journal of Health Economics*; **JIA** – *Journal of International Affairs*; **JIBS** – *Journal of International Business Studies*; **JID** – *Journal of International Development*; **JIE** – *Journal of International Economics*; **JIM** – *Journal of International Management*; **JKM** – *Journal of Knowledge Management*; **JLAS** – *Journal of Latin American Studies*; **JLEO** – *Journal of Law, Economics & Organization*; **JM** – *Journal of Management*; **JMG** – *Journal of Management and Governance*; **JMM** – *Journal of Marketing Management*; **JMS** – *Journal of Management Studies*; **JMR** – *Journal of Marketing Research*; **JOB** – *Journal of Organizational Behavior*; **JOM** – *Journal of Operations Management*; **JPA** – *Journal of Public Affairs*; **JPE** – *Journal of Political Economy*; **JSM** – *Journal of Strategic Management*; **JWB** – *Journal of World Business*; **JWT** – *Journal of World Trade*; **LODJ** – *Leadership and Organizational Development Journal*; **LRP** – *Long Range Planning*; **MBR** – *Multinational Business Review*; **MIR** – *Management International Review*; **MQ** – *McKinsey Quarterly*; **MS** – *Management Science*; **OBES** – *Oxford Bulletin of Economics and Statistics*; **OD** – *Organizational Dynamics*; **ODS** – *Oxford Development Studies*; **OEP** – *Oxford Economic Papers*; **OSc** – *Organization Science*; **OSt** – *Organization Studies*; **POM** – *Production and Operations Management*; **PoP** – *Perspectives on Politics*; **PSJ** – *Policy Studies Journal*; **QJE** – *Quarterly Journal of Economics*; **RDM** – *R&D Management*; **RES** – *Review of Economics and Statistics*; **RIE** – *Review of International Economics*; **RP** – *Research Policy*; **RWE** – *Review of World Economics*; **SC** – *Strategic Change*; **SJM** – *Scandinavian Journal of Management*; **SMJ** – *Strategic Management Journal*; **SMR** – *MIT Sloan Management Review*; **S&P** – *Society and Politics*; **TIBR** – *Thunderbird International Business Review*; **TNC** – *Transnational Corporations (United Nations)*; **WD** – *World Development*; **WE** – *World Economy*; **WTR** – *World Trade Review*.

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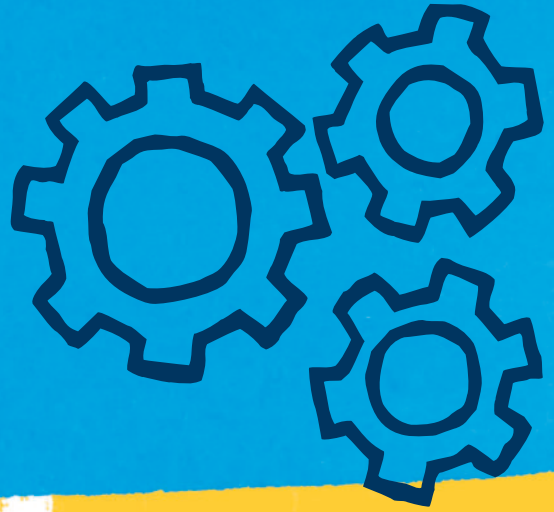
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PART ONE

FOUNDATIONS

- 1 Globalizing Business
- 2 Formal Institutions: Political, Economic and Legal Systems
- 3 Informal Institutions: Culture, Religion and Languages
- 4 Firm Resources: Competitiveness and Growth

CHAPTER ONE

GLOBALIZING BUSINESS



LEARNING OBJECTIVES

After studying this chapter, you should be able to

- 1 Explain the concept of international business (IB)
- 2 Articulate what you hope to learn by reading this book and taking this course
- 3 Identify one fundamental question and two core perspectives that provide a framework for studying this field
- 4 Participate in the debate on globalization with a reasonably balanced and realistic view
- 5 Summarize some basic trends in the global economy
- 6 Draw implications for action by integrating global and local knowledge



OPENING CASE

adidas: sales, suppliers and stakeholders around the world

On Shanghai's fashionable Huaihai Road, not far from the outlets of *Apple*, *Nike* and *Gucci*, a multi-storey store invites shoppers to try a brand hailing from a small town in Germany. In Herzogenaurach, the intense rivalry between *adidas* and *Puma* has propelled both

sports shoe manufacturers onto the international stage. *adidas* pulled ahead with innovative approaches to sport sponsorship, placing its three stripes on the sports kit of international competitors in many sports. After taking over US sports brand *Reebok* in 2005, *adidas* became the world's second largest provider of sports shoes and clothing (after *Nike*), while expanding into the much broader market of leisure clothing.



When Kasper Rørstad, a Dane, took over as CEO of this iconic German brand in 2016, *adidas* had a truly global footprint, with an equally strong presence on all continents. Western Europe was still the most important region accounting for 27.4% of sales, followed by North America with 17.7%. Yet about half of *adidas*' sales already came from emerging economies, including Greater China (15.6%), other Asia and Middle East (13.9%) and Latin America (9.0%). The success in China builds on two decades of brand building and a major marketing push ahead of the 2008 Olympics, featuring adverts associating *adidas* with the Chinese national team and its successes. In a highly competitive premium segment in China, global brands *Nike* and *adidas* have been challenged by local brands such as *Li Ning*. Yet, by focusing on innovation and product quality they sustained their popularity among increasingly affluent young urban people.

However, not only sales have become global; the value chain of the company also extends across the globe. In particular, the labour-intensive parts of shoes and clothing manufacturing have, since the 1980s, been moved to locations with low labour costs, often to independent suppliers. In 2018, *adidas* reported 783 primary suppliers around the world, many of which are based in emerging countries, led by China (151), Vietnam (79), Korea (74) and Indonesia (75). They were complemented by suppliers in advanced economies like the USA (77), Japan (32) and Germany (15).

With global supply chains labour relations have also become global, and consumers in Europe and North America take an active interest in where and how their shoes are made. The shoe and textile industry historically has a poor record on working conditions in its factories, especially in Asia. Therefore, *adidas* is continuously engaging with a wide range of stakeholders and developing its standards of engagement. These codes and processes cover a wide range of issues including forced labour, child labour, discrimination, wage and benefits, hours of work, collective bargaining, disciplinary practices, environmental requirements and community involvement. They are supported by auditing tools and procedures, some of which by independent third parties. Audit teams visit factories not only to monitor compliance but also to train the management in the use of the standards of engagement and to explain the likely benefits of higher standards for the business itself. The teams rate each factory on several criteria, and these compliance ratings – together with quality criteria – influence decisions on which suppliers to use. At the same time, *adidas* engages in a constructive dialogue to provide solutions to problems that occur and also to discontinue relationships with suppliers repeatedly found in violation of its standards. In the interests of transparency, since 2007, *adidas* has been publishing a full list of all its suppliers on its website, which is updated twice yearly, still a rare practice in the industry.

adidas is the founding member of the *Fair Labor Association* (FLA), which provides external, independent monitoring, complaints procedures and public reporting, and partnerships with other NGOs. For example, in Indonesia *adidas* acted as lead in an initiative to engage with the trade union movement, which established a framework agreement for trade union rights in the workplace. Employees can report violations of employment codes to independent monitors not only to a telephone hot line but also by SMS.

Over the years, the standards of engagement have led to improvements in business practices in supplier firms, especially in those firms that chose a proactive approach. An independent study found rising product quality, fewer accidents, lower staff turnover and rising productivity in a proactive supplier firm, while reluctant adoption of the code in another supplier firm led to inferior economic performance. Moreover, a track record of responsible supply chain management enhances the reputation of the brand globally.

But *adidas* cannot stand still. Fashions and user habits are constantly changing, as are best practices in the manufacturing of textiles and footwear. Online sales are becoming increasingly important, and *adidas* is not only developing its own phone app and an online supply chain but is also assessing its global network of traditional outlets. Also the manufacturing of shoes is changing. By 2017, *adidas* was building a 3-D printing plant that would produce shoes fully automatically in Germany, while one of its US suppliers, Tianyuan Garments, was experimenting with textile machines that could stitch together T-shirts completely automatically.

Sources: (1) S. Frenkel & D. Scott, 2002, *Compliance, Collaboration, and Codes of Labor Practice: The adidas Connection*, *CMR*, 45: 29–49; (2) L. Hartman, R. Wokutch & J. French, 2003, *adidas-Salomon*, in: L. Hartman, D. Arnold & R. Wokutch, eds, *Rising Above Sweatshops*, Westport, CT: Praeger, 191–248; (3) *The Economist*, 2017. Stitches in time, August 26; (4), *Handelsblatt*, 2018. Diese App ist für Adidas wichtiger als jeder Turnschuh, March 26; (5) www.adidas-group.com.

Were you surprised to learn how many people in different countries are involved with *adidas* – not just wearing their shoes and sports clothing but as labourers, NGOs or brand managers? Did you expect *adidas* to be so concerned what people think about its labour practices around the world? Did you realize that its marketing practices are adapted locally, even when referring to the same global brand? International business (IB) has become an integral part of many businesses – and products. Yet, managing IB activities – for example, coordinating multiple suppliers of components – is challenging even for experienced managers. This book is about these sorts of challenges faced by managers of firms operating around the globe. In particular, we will be exploring what determines the success and failure of firms engaged in IB.

EUROPEAN AND GLOBAL BUSINESS

International business (IB) is about (1) firms engaging in international (cross-border) economic activities and/or (2) the activity of doing business abroad. IB activities take many forms and involve many different actors. The most important actors in IB are known as **multinational enterprises (MNEs)**, defined as firms that engage in **foreign direct investment (FDI)** by directly investing in, controlling and managing value-added activities in other countries.¹ For example, *adidas*, an MNE, has undertaken many FDI projects, such as manufacturing plants in the UK or retail shops in China. In addition, it has a variety of relationships with other businesses (from suppliers to distributors), sports teams it sponsors and, last but not least, consumers. These others may not be MNEs themselves, but they engage in IB too. For example domestic firms actively compete and/or collaborate with foreign entrants. Understanding IB is thus also important for anyone facing foreign competitors.²

There are two key words in IB: international (I) and business (B). The I indicates that we will spend substantial time on analyzing the international environment of business, especially in Chapters 2, 3, 8 and 9. The B indicates why we study the

international business (IB)

(1) A firm that engages in international (cross-border) economic activities and/or (2) the action of doing business abroad.

LEARNING OBJECTIVE

- 1 Explain the concept of international business (IB)

multinational enterprise (MNE)

A firm that engages in foreign direct investments and operates in multiple countries.

foreign direct investment (FDI)

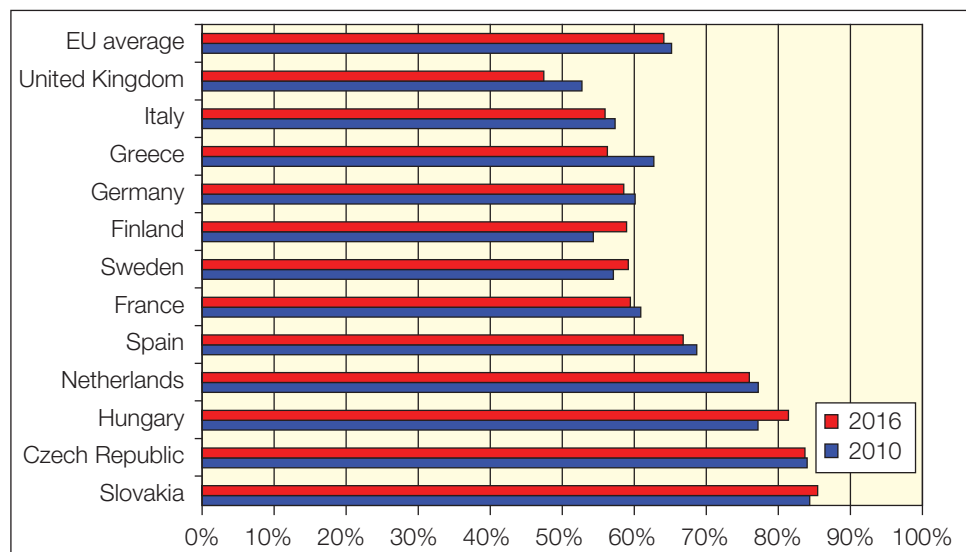
Investments in, controlling and managing value-added activities in other countries.

international environment: we want to know how and why it is important for business. It also indicates that we are not focused on one function, such as management, marketing or finance but on the overall picture of business.³ The dual focus on both the international environment and the firm is the essence of IB. Like economics and political science, we study the business environment, but we look at it from the perspective of firms and individuals engaged in business activities. Thus, IB is an integrative course that has the potential to provide you with an overall business perspective grounded in a global environment.

The international dimensions of business are increasingly important for all businesses, especially in Europe, because most national markets have opened to international competition. For example, suppliers of car parts need to be able and willing to cooperate with the car maker, for example *VW*, *Toyota* or *Fiat*, at multiple sites around the world if they want to sell to the brand. Moreover, with the creation of the common market in the European Union (EU), the definition of a home market is increasingly ambiguous. Especially in business-to-business markets, such as car parts, customers are often operating internationally, especially in Europe, such that competition in a single country would hardly be sustainable. Thus, it becomes difficult to tell what is international and what is domestic.

This book goes beyond traditional IB textbooks in two important ways. First, we focus on issues relevant to European businesses and managers. In Europe, domestic markets are smaller than, for example, in the USA and China. Hence, IB is an important aspect of business for almost all firms – large and small. Most of its business is conducted with neighbouring countries. For example, France and Germany are each other's main trading partners. For most European businesses, the EU member countries account for more than half of their international activities. Of the major nations, only British exporters sell less than half their overseas sales within the EU, while their Czech and Slovak counterparts sell over 83% within the EU in part because of their tight integration in pan-European supply chains in the car industry (see Figure 1.1). That is like working Monday to Friday on EU markets and Saturday on the rest of the world. Even the biggest MNEs do most of their business in their home region;⁴ truly global companies like *adidas* remain the exception rather than the rule.

Figure 1.1 Exports from EU member countries 2010 and 2016



Note: Share of intra-EU exports and imports in the countries' total exports in %.

Source: Authors' creation using data from Eurostat database, accessed January 2018.

Within their own region, however, businesses face different kinds of challenges than when expanding beyond their home region. Notably, they operate under the auspices of the EU and the rules that the EU has established for business (see Chapter 8). Moreover, in neighbouring countries, differences in institutions are relatively small, yet big enough to derail unsuspecting business people (Chapters 2 and 3). On the other hand, the rest of the world presents some of the most attractive (profitable) business opportunities and recently much larger growth potential. For example, *adidas* has been able to tap into both traditional Western European markets and fast growing Asian markets. Hence, as an IB executive, you need competence for both Europe and beyond.

This book aims to give you *both*, which distinguishes it from most English-language textbooks which are often written by leading scholars based in the USA and thus focus on issues of interest to Americans going international. Typically, these are large companies dealing in distant markets because the home market in the USA is so big. Thus our European focus implies that we are paying more attention than other textbooks to (1) business in nearby countries, (2) institutions of the EU, (3) small- and medium-sized enterprises (SMEs) and (4) research by European scholars on these issues.

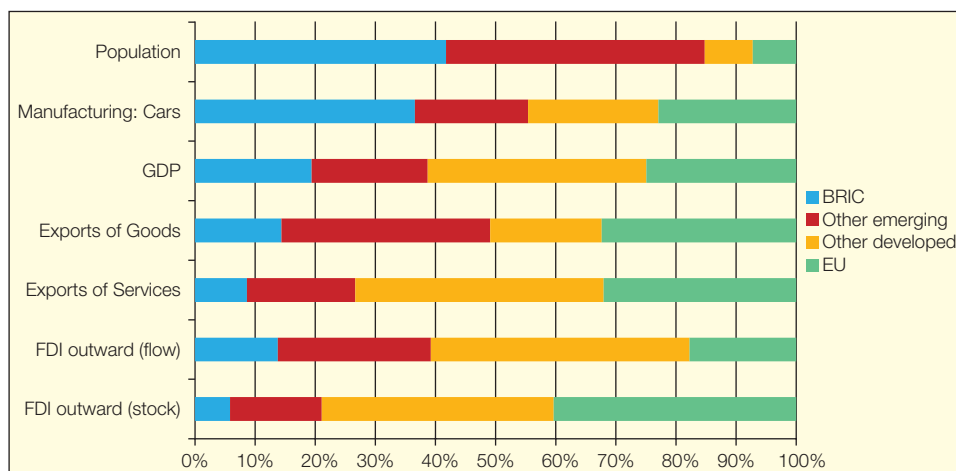
Second, this book is devoting extensive space to **emerging economies** (also known as **emerging markets**). These are economies that only recently established institutional frameworks that facilitate international trade and investment, typically with low- or middle-level incomes and above average economic growth.⁵ How important are emerging economies? Figure 1.2 provides some indications. The largest four emerging economies are indicated in blue: Brazil, Russia, India and China (also known as **BRIC**). About 85% of the people of the world live in an emerging market, but they collectively contribute only about 30% of global **gross domestic product (GDP)**, the most common measure of the economic power of an economy (In Focus 1.1). However, their participation in the global economy is rapidly increasing. For example, 55% of all cars are built in an emerging economy (25% in China alone). Together, emerging economies account for almost half of all goods exports and a quarter of all service exports. Their position in FDI is still small but rapidly increasing; note the much larger share in new FDI (FDI flow) in the year 2013 compared to the existing FDI operations (FDI stock). The rapid growth of some emerging economies is evident. Today's students – and tomorrow's business leaders – will find rich opportunities in emerging economies. This book will help you to recognize them.

emerging economies (emerging markets)
Economies that only recently established institutional frameworks that facilitate international trade and investment, typically with low- or middle-level income and above average economic growth.

BRIC
Brazil, Russia, India and China.

gross domestic product (GDP)
The sum of value added by resident firms, households and governments operating in an economy.

Figure 1.2 The contributions of emerging economies



Sources: Authors' creation using data extracted from (1) United Nations, 2014, *World Investment Report 2014*, New York and Geneva: UN; (2) World Bank, 2014, *World Development Indicators* database; (3) World Trade Organization, 2014, *WTO Statistics* database; (4) *The Economist*, 2014, *Pocket World in Figures*, London. All data refer to 2013.



IN FOCUS 1.1

Setting the terms straight

GDP, GNP, GNI, PPP – there is a bewildering variety of acronyms that are used to measure economic development. It is useful to set these terms straight before proceeding. Gross domestic product (GDP) is measured as the sum of value added by *resident* firms, households and government operating in an economy. For example, the value added by foreign-owned firms operating in Mexico would be counted as part of Mexico's GDP. However, the earnings of *non-resident* sources that are sent back to Mexico (such as earnings of Mexicans who do not live and work in Mexico and dividends received by Mexicans who own non-Mexican stocks) are not included in Mexico's GDP. One measure that captures this is **gross national product (GNP)**. More recently, the World Bank and other international organizations have used a new term, **gross national income (GNI)**, to supersede GNP. Conceptually, there is no difference between GNI and GNP. What exactly is GNI/GNP? It comprises GDP plus income from non-resident sources abroad.

While GDP, GNP and now GNI are often used as yardsticks of economic development, differences in cost of living make such a direct comparison less meaningful. In particular, the costs of living in emerging economies, especially services such as housing and haircuts, tend to be much lower than in developed economies. For example, €1 spent in Nairobi, Kenya can buy a lot more than €1 spent in Oslo, Norway. The **purchasing power parity (PPP)** exchange rate considers such differences. The PPP between

two countries is the rate at which the currency of one country needs to be converted into that of a second country to ensure that a given amount of the first country's currency will purchase the same volume of goods and services in the second country.

For example, according to the International Monetary Fund (IMF, see Chapter 9), the Swiss per capita GDP is US\$80 603 based on official (nominal) exchange rates – a lot *higher* than the US per capita GDP of US\$56 084. However, everything is more expensive in Switzerland. For example, a Big Mac costs US\$6.74 in Switzerland versus US\$5.30 in the USA. Thus, Switzerland's per capita GDP based on PPP is only US\$59 561 – only slightly higher than the US per capita GDP based on PPP, US\$56 084 (the IMF uses the USA as the benchmark in PPP calculations).

Overall, when we read statistics about GDP, GNP and GNI, always pay attention to whether these numbers are based on official exchange rates or PPP, which can make a huge difference. However, PPP values have been created to compare standards of living; they only weakly proxy the 'real' size of an economy. Also, be aware of intra-country variations in PPP. If you live as an expatriate in Manila or Shanghai, you will find many actual expenses to be quite similar to Europe: the cheap food or local transport does not meet the same quality and safety standards that most Europeans expect.

Sources: (1) *The Economist*, 2014, Calculating European GDP, August 23; (2) *The Economist*, 2017, The Big Mac index, July 13; (3) International Monetary Fund, 2016, *Report for selected countries and subjects (PPP valuation of country GDP)*, Washington: IMF.

WHY STUDY INTERNATIONAL BUSINESS?

LEARNING OBJECTIVE

- 2 Articulate what you hope to learn by reading this book and taking this course

International business is one of the most exciting, challenging and relevant subjects offered by business schools. In addition to the requirements of your degree programme, there are at least two compelling reasons you should study it.

First, for ambitious students who aspire to lead a business unit or an entire firm, expertise in IB is normally a prerequisite. It is increasingly difficult, if not impossible, to find top managers without significant international competences, even in

small- and medium-sized enterprises. Of course, eventually, hands-on global experience, not merely knowledge acquired from this course, will be required. However, mastery of the knowledge and demonstration of interest in IB during your education will set you apart as a candidate for fast-track career development that involves **expatriate assignments** – job assignments located abroad (see Chapter 16).

Thanks to globalization, low-skilled jobs not only command lower salaries but are also more vulnerable to international competition. However, top management capabilities, especially those that create connections across the world, are in demand. For example, if a factory in Europe is shut down and the MNE sets up a similar factory in China, only a few dozen people may keep their jobs. Yes, you guessed it: these jobs are top-level positions such as the chief executive, chief financial officer, factory directors and development engineers. They may be sent by the MNE as expats to China to lead operations there. To motivate their best people to take such challenging assignments, MNEs typically offer them a higher salary and extra perks during their stay. Knowledge of IB and the ability to contribute to discussions on global business issues are a foundation for becoming a sought after, globetrotting manager.

Second, even if you do not have aspirations to move around the world in your professional life, you may find yourself dealing with foreign-owned suppliers and buyers, competing with foreign-invested firms in your home market and perhaps even managing investments abroad. Very few companies in Europe are able to pursue their business without regular interaction across international borders. Moreover, you may also find yourself working for a foreign-owned firm if your domestic employer is acquired by a foreign MNE. Understanding how global business decisions are made may facilitate your own career in such MNEs. If there is a strategic rationale to downsize your unit, you would want to be able to figure this out and be the first one to talk to alternative employers. In other words, it is your career that is at stake. In this age of global competition, a good place to start is to study hard and do well in your IB course.

A UNIFIED FRAMEWORK

International business is a vast subject area. We draw on major social sciences, such as economics, geography, history, political science, psychology and sociology, as well as a number of business disciplines, such as finance and marketing. It is very easy to lose sight of the ‘forest’ while scrutinizing various ‘trees’ or even ‘branches’. The subject is not difficult, and most students find it to be fun. However, the number one student complaint (based on previous student feedback) is an overwhelming amount of information, which is also our number one complaint as your authors.

To address your possible complaint and make your learning more manageable (and ideally, more fun), we develop a unified framework as a consistent theme throughout this book (Figure 1.3). This will provide continuity to facilitate your learning. Specifically, we will focus on one fundamental question. This question acts to define a field and to orient the attention of students, practitioners and scholars in a certain direction. Our ‘big question’ is: What determines the success and failure of firms around the globe?⁶ To answer this question, we focus on two core perspectives throughout this book: (1) an institution-based view and (2) a resource-based view. The remainder of this section outlines why this is the case.

gross national product (GNP)

Gross domestic product plus income from non-resident sources abroad.

gross national income (GNI)

GDP plus income from non-resident sources abroad. GNI is the term used by the World Bank and other international organizations to supersede the term GNP.

purchasing power parity (PPP)

A conversion that determines the equivalent amount of goods and services different currencies can purchase. This conversion is usually used to capture the differences in cost of living in different countries.

expatriate assignment

A temporary job abroad with a multinational company.

LEARNING OBJECTIVE

- Identify one fundamental question and two core perspectives that provide a framework for studying this field