chapter

5

The Global Context of Business

After reading this chapter, you should be able to:

LO-1 Describe the rise of international business and identify the *major world marketplaces*.

LO-2 Explain how different forms of *competitive advantage, import–export balances, exchange rates*, and *foreign competition determine how countries* and businesses respond to the international environment.

LO-3 Discuss the factors involved in conducting business internationally and in selecting the *appropriate levels of international involvement and organizational structure*.

LO-4 Describe some of the ways in which *social, cultural, economic, legal, and political differences* act as barriers to international trade.

LO-5 Explain how *free trade agreements* assist world trade.

SCANLIFE

Tim Hortons USA: Exporting a Strategic Model Is No Easy Task

When you think of Tim Hortons, what images come to mind? Students typically use the following words: hockey, Timbits, maple, Canada, doughnuts, coffee, Sidney Crosby, inexpensive. Tim Hortons is very successful in Canada, and its doughnuts have become the Canadian equivalent of American apple pie or the Big Mac. The company has worked hard to create a warm, homegrown image in the minds of the Canadian consumer. Its low-cost/high-volume approach, its tremendous channel domination, and its unapologetic links to Canadian symbols are all sources of competitive advantage for Tim Hortons in Canada. According to the website, Tim Hortons is the fourth largest quick-service restaurant chain in North America. It is the largest in Canada with over 3000 stores. To put this figure into perspective, McDonald's has approximately 1400 stores in Canada. But can Tim Hortons successfully export its business model to the U.S.?

The Challenge

The first U.S. Tim Hortons opened in Buffalo, New York, in 1984, and there are now 563 stores in 12 northern U.S. states. Recently the company announced plans to open 300 new U.S. stores, and it now seems ready for a more concentrated push into the U.S. But what approach should be used? Should the same standardized approach that has worked in Canada be used or will the model have to be adapted for the U.S. market? For obvious reasons, Tim Hortons has not focused on hockey and Canadian symbols to sell

How Will This Help Me?

Whether you see yourself living abroad, working for a big company, or starting your own business, the global economy will affect you in some way. Exchange rates for different currencies and global markets for buying and selling affect everyone, regardless of their role or perspective. The material in this chapter will help you to (1) understand how global forces impact you as a *customer*, (2) understand how globalization affects you as an *employee*, and (3) assess how global opportunities and challenges can affect you as a business owner and as an *investor*.

its doughnuts and coffee in the U.S. It might try to replace hockey with baseball, but Dunkin' Donuts already has strong grassroots links to that sport. It could wrap itself in the U.S. flag, but that would leave it open to charges of being fake, and that approach might also confuse or upset Canadians who visit the U.S. Another problem: Tim Hortons cannot rely on a large marketing channel advantage in the United States. In Canada, there is one Tim Hortons for every 11 000 consumers, but this is not the case across the border. In the U.S., there are thousands of local coffee shops in addition to major players like Dunkin' Donuts, Starbucks, and even McDonald's (especially with its recent McCafé push). In the U.S., these companies have the sort of market penetration that Tim Hortons enjoys in Canada.

So, what can be done? Until now, Tim Hortons' central message in the United States has focused on value and freshness. This was not a very original idea, but at least it was an honest approach. Unfortunately, this hasn't differentiated Tim Hortons from its competitors. Something else is needed. But what? The company is now pursuing several strategies, including the acquisition of prime locations, co-branding, and going upscale.

Acquiring Prime Locations

In 2009, Tim Hortons opened its first outlets in New York City after reaching an agreement with a former Dunkin' Donuts franchisee who owned 12 prime locations in Manhattan and Brooklyn. This gave Tim Hortons a great opportunity to develop its brand and gain exposure in this key market because prime locations are difficult to find, especially in New York City. The fact that people were already accustomed to going to these particular locations for their coffee fix should also help. As a result of this deal, Tim Hortons has some much-needed exposure, including a location in Madison Square Garden.

Co-Branding

Also in 2009, Tim Hortons and Kahala Corporation, owner of the Cold Stone Creamery—an ice cream parlour franchise—announced a co-branding agreement that would see the development of up to 100 combined stores in the U.S. At the same time, approximately 60 outlets across Canada were converted to test this new co-branded format. This should help Tim Hortons to get noticed and to improve its competitive position in the U.S. market.

Going Upscale

In 2010, Tim Hortons announced that it was planning to create upscale café/bake shops with a different menu that would include pastries baked onsite. These new stores were scheduled to open in existing markets such as New York and Michigan. The announcement raised several new questions. Could a high-end Tim Hortons work? How would the company manage the traditional stores alongside the new outlets? Would there be a sub-brand created or would it eventually transform all U.S. locations? This strategy should help relieve some of the stress of the rising food costs that have recently been squeezing low-cost food providers like Tim Hortons. But can the company manage the brand and not confuse consumers? Time will tell.

Tim Hortons is taking a concept that has worked in Canada and is trying to make it work in a foreign market. In order to succeed, Tim Hortons must develop a clear strategy that U.S. consumers can identify with. That approach is what made the company successful in Canada. Succeeding in new markets is not easy!

The Contemporary Global Economy

The total volume of world trade today is immense—around \$8 trillion each year. As more firms engage in international business, the world economy is fast becoming a single interdependent system—a process called **globalization**. Even so, we often take for granted the diversity of goods and services available as a result of international trade. Your television set, your shoes, and even the roast lamb on your dinner table may all be **imports**—that is, products made or grown abroad but sold in Canada. At the same time, the success of many Canadian firms depends on **exports**—products made or grown domestically and shipped abroad.

GLOBALIZATION Process by which the world economy is becoming a single interdependent system.

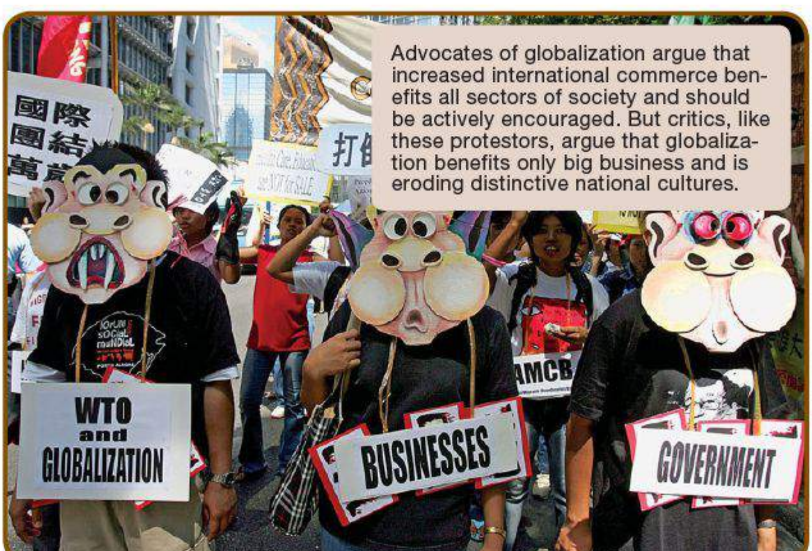
IMPORT Product made or grown abroad but sold domestically.

EXPORT Product made or grown domestically but shipped and sold abroad.

In early 2010, China officially passed Germany as the world's top merchandise exporter; this was a clear sign of the importance of international trade.[1] However, trade between nations can be traced back at least as far as 2000 BCE, when North African tribes took dates and clothing to Assyria and Babylonia in the Middle East and traded them for olive oil and spices. International business is nothing new. But international trade has become increasingly central to the fortunes of most nations of the world, as well as businesses. Whereas in the past many nations followed strict policies to protect domestic companies, today more and more countries are aggressively encouraging international trade. They are opening their borders to foreign businesses, offering incentives for their own domestic businesses to expand internationally, and making it easier for foreign firms to partner with local firms through various alliances.

Several forces have combined to spark and sustain globalization. For one thing, governments and businesses have simply become more aware of the benefits of globalization to their countries and stockholders. For another, new technologies have made international travel, communication, and commerce easier, faster, and cheaper than ever before. Overseas phone calls and seaborne shipping costs per tonne have both declined sharply over the last several decades. Likewise, transatlantic travel once required several days aboard a ship. Today, conventional transatlantic travel takes less than a day. The internet has also torn down barriers for large and small companies. Finally, there are competitive pressures: sometimes, a firm simply must enter foreign markets just to keep up with its competitors.

Globalization is not without its critics, who charge that it allows businesses to exploit workers in less developed countries and bypass domestic environmental and tax regulations. They also charge that globalization leads to the loss of cultural heritages and often benefits the rich more than the poor. As a result, many international gatherings of global economic leaders—including the G8 and G20 meetings in Toronto in 2010—have been marked by protests and demonstrations. But despite fears and apprehensions, globalization is part of our existence and there are some interesting trends emerging. A *Globe and Mail* article listed five key trends based on a report from McKinsey: (1) the economic centre of gravity will shift away from North America/Europe/Japan to Asia and Latin America, (2) the productivity imperative (improved productivity



Advocates of globalization argue that increased international commerce benefits all sectors of society and should be actively encouraged. But critics, like these protestors, argue that globalization benefits only big business and is eroding distinctive national cultures.

PER-CAPITA INCOME The average income per person of a country.

is essential to compete in the highly competitive marketplace), (3) the global grid (increasing complex global networks of people and capital), (4) environmental sustainability will take on even more importance, and (5) there will be increased controls on businesses and markets as governments try to cope with the financial crisis.[2]

LO-1 The Major World Marketplaces

The World Bank, an agency of the United Nations, uses **per-capita income**—average income per person—to make distinctions among countries. Its current classification method consists of four categories of countries:[3]

1. *High-income countries:* have an annual per-capita income greater than U.S. $11 906. They include Canada, the United States, most countries in Europe, Australia, New Zealand, Japan, South Korea, Kuwait, the United Arab Emirates, Israel, Singapore, and Oman.
2. *Upper middle-income countries:* have an annual per-capita income between U.S. $3856 and U.S. $11 905. This group includes Columbia, Peru, Lebanon, Hungary, Poland, Turkey, Mexico, Argentina, and South Africa.
3. *Low middle-income countries:* have an annual per-capita income between U.S. $976 and U.S. $3855. This group includes Côte d'Ivoire, Guatemala, Samoa, and Thailand.
4. *Low-income countries* (often called *developing countries*): have an annual per-capita income of U.S. $975 or less. Benin, Ethiopia, Haiti, and Vietnam are among the countries in this group. Due to low literacy rates, weak infrastructures, unstable governments, and related problems, these countries are less attractive for international business. For example, the East African nation of Somalia is plagued by drought, civil war, and starvation, and plays virtually no role in the world economy.

Geographic Clusters The world economy revolves around three major marketplaces: North America, Europe, and Asia. These clusters include relatively more of the upper-middle and high-income nations, but relatively few low- and low-middle-income countries. For instance, because Africa consists primarily of low- and low-middle-income countries, it is not generally seen as a major marketplace. The three geographic regions that do warrant this designation are home to most of the world's largest economies, biggest corporations, most influential financial markets, and highest-income consumers.

North America The United States dominates the North American business region. It is the single largest marketplace and still enjoys the most stable economy in the world. Canada also plays a major role in the global economy. Moreover, the United States and Canada are each other's largest trading partner. Many U.S. firms, such as General Motors and Procter & Gamble, have maintained successful Canadian operations for decades, and many Canadian firms, such as Research In Motion and Scotiabank, are also major international competitors.

Mexico has become a major manufacturing centre, especially along the U.S. border, where cheap labour and low transportation costs have encouraged many firms from the United States and other countries to build factories. The auto industry has been especially active, with Daimler, General Motors, Volkswagen, Nissan, and Ford all running large assembly plants in the region. Several major suppliers have also built facilities in the area. But Mexico's role as a low-cost manufacturing centre may be usurped by China as companies begin shifting production from Mexico to China.[4]

Europe Europe is often seen as two regions—Western and Eastern. Western Europe, dominated by Germany, the United Kingdom, France, Spain, and Italy, has long been a mature but fragmented marketplace. But the transformation of this region via the European Union (EU) (discussed later in this chapter) into an integrated economic system has further increased its importance. Major international firms, such as Unilever, Renault, Royal Dutch/Shell, Michelin, Siemens, and Nestlé, are headquartered in Western Europe.

E-commerce and technology have also become increasingly important in this region. There has been a surge in internet start-ups in southeastern England, the Netherlands, and the Scandinavian countries, and Ireland is now one of the world's largest exporters of software. Strasbourg, France, is a major centre for biotech start-ups; Barcelona, Spain, has many flourishing software and internet companies; and the Frankfurt region of Germany is dotted with both software and biotech start-ups.

Eastern Europe, once primarily Communist, has also gained importance, both as a marketplace and as a producer. Multinational corporations such as Nestlé, General Motors, and ABB Asea Brown Boveri have all set up operations in Poland. Ford, General Motors, Suzuki, and Volkswagen have all built new factories in Hungary. On the other hand, governmental instability has hampered development in Bulgaria, Albania, Romania, and other countries.

Pacific Asia Pacific Asia consists of Japan, China, Thailand, Malaysia, Singapore, Indonesia, South Korea, Taiwan, the Philippines, and Australia (which is technically not in Asia but is included because of proximity). Some experts still distinguish Hong Kong, though now part of China, as a part of the region, and others include Vietnam. Fuelled by strong entries in the automobile, electronics, and banking industries, the economies of these countries grew rapidly in the past three decades. A currency crisis in the late 1990s slowed growth in virtually every country of the region, but that crisis ran its course, and most of these countries, especially Japan and China, have since flourished.

As the trends indicate, Pacific Asia is a growing force in the world economy and a major source of competition for North American companies. The Japanese dominate the region, led by firms such as Toyota, Toshiba, and Nippon Steel. However, South Korea (with major manufacturers Samsung and Hyundai), Taiwan (with Chinese Petroleum and manufacturing for foreign firms), and Hong Kong (a major financial centre) are also successful players in the global economy. China, the world's most densely populated country, has emerged as an important market and now boasts the world's third-largest economy behind that of the United States and only slightly behind that of Japan.[5]

As in North America and Europe, technology is playing an increasingly important role in the future of this region. In some parts of Asia, however, the emergence of technology firms has been hampered by poorly developed electronic infrastructures, slower adoption of computers and information technology, and a higher percentage of lower-income consumers.

BRIC A term used to describe four important and powerful emerging markets in the business world: Brazil, Russia, India, and China.

The Rising Power of Emerging Markets: The Role of BRIC

BRIC is the term that is often used in international trade magazines and newspapers to describe the increasing importance of four specific nations in global trade: *B*razil, *R*ussia, *I*ndia, and *C*hina. The BRIC concept was first used by Goldman Sachs in 2001; since that time BRIC investment funds have become an important group for money managers and international analysts. These four nations have even begun to act like a unit, and an unofficial BRIC meeting took place in 2009.

The status of these four nations has risen in international trade for different reasons. Brazil is strong in commodities and agriculture, Russia is a powerful energy supplier, and China is a major hub of manufacturing activity. India has become a leading service provider at various levels ranging from basic customer service call centres to engineering solutions providers. The growth and quick market development of the consumer market in these four nations is also providing tremendous sales opportunities for foreign companies in many industries, including car manufacturing and high-end clothing brands.[6]

The old international trading patterns and activities are changing. Once upon a time, Western companies used less developed markets to acquire natural resources supplies and to carry out simple assembly tasks. But these four nations now demonstrate relationships that are much more complex. A clear signal of this shift was evident a couple of years ago, when Indian car maker Tata acquired

The growth in international commerce has led to the emergence of several major marketplaces. Much of the international commerce in these marketplaces, in turn, is managed from major cities. Traditional centres of international commerce include New York, London, Paris, Brussels, and Tokyo. In recent years, though, cities like Shanghai, Beijing, Hong Kong, Dubai, Vancouver, Bangalore, and Kuala Lumpur have taken on increased importance. For example, international business now defines the glittering skyline of Shanghai.

ABSOLUTE ADVANTAGE
The ability to produce something more efficiently than any other country.

COMPARATIVE ADVANTAGE
The ability to produce some products more efficiently than others.

NATIONAL COMPETITIVE ADVANTAGE
International competitive advantage stemming from a combination of factor conditions; demand conditions; related and supporting industries; and firm strategies, structures, and rivalries.

Jaguar and Land Rover from Ford. Earlier that year, Tata Steel bought the Anglo Dutch steel maker Corus Group LLC for US$12.1 billion. This was not quite business as usual.[7]

Of the four countries, Russia has encountered the most profound troubles in recent years. Some analysts have even called for the exclusion of Russia from this supergroup. Among the reasons cited were corruption and excessive levels of bureaucratic red tape. For example, in 10 years in the Russian market, IKEA had been able to open only 11 stores despite major efforts to expand. Frustrated by the red tape, IKEA put further investment in Russia on hold.[8]

While China, India, and Russia have had most of the attention, it is Brazil that is now at the front of the pack in terms of optimism and opportunity. In the first quarter of 2010, Brazil's economy expanded by an impressive 9 percent, which continued a positive trend despite the world economic crisis; the growth rate averaged 10 percent for the previous three quarters as well. This was based on positive domestic demand and high levels of investment. According to Transparency International, Brazil is the least corrupt of the four BRIC nations. Brazil's rich natural resources and momentum from World Cup 2014 should help propel it for years to come.[9]

While the BRIC nations have received a lot of publicity, there are tremendous opportunities and stories of development in many nations, including South Africa, Thailand, Indonesia, and Ukraine, to name just a few. A new world order is slowly emerging, and "old" economic powers like the U.S., Japan, Germany, and even Canada are going to have to adapt.

LO-2 Forms of Competitive Advantage

No country can produce all the goods and services that its people need. Thus, countries tend to export products that they can produce better or less expensively than other countries. The proceeds are then used to import products that they cannot produce effectively. However, this general principle does not fully explain why nations export and import. Such decisions hinge partly on the kind of advantages a particular country may enjoy regarding its abilities to create and/or sell various products and resources.[10] Traditionally, economists have focused on *absolute* and *comparative advantage* to explain international trade. But because this approach focuses narrowly on such factors as natural resources and labour costs, the more contemporary view of *national competitive advantage* has emerged.

Absolute Advantage

An **absolute advantage** exists when a country can produce something more cheaply and/or of higher quality than any other country. Saudi oil, Brazilian coffee beans, and Canadian timber approximate absolute advantage, but examples of true absolute advantage are rare. In reality, "absolute" advantages are always relative. For example, most experts say that the vineyards of France produce the finest wines in the world. But the growing wine businesses in California and Ontario attest to the fact that producers there can also produce very good values in wine—wines that are perhaps almost as good as French wines and that also are available in more varieties and at lower prices.

Comparative Advantage

A country has a **comparative advantage** in goods that it can produce more efficiently or better than other goods. For example, if businesses in a given country can make computers more efficiently than they can make automobiles, that nation's firms have a comparative advantage in computer manufacturing. Canada has a comparative advantage in farming (because of fertile land and a temperate climate), while South Korea has a comparative advantage in electronics manufacturing (because of efficient operations and cheap labour). As a result, Canadian firms export grain to South Korea and import electronic equipment from South Korea. All countries have a comparative advantage in *some* products, but no country has a comparative advantage in *all* products. Developed countries tend to have a comparative advantage in making high-tech products, while developing countries tend to have a comparative advantage in making products that require lots of low-cost labour.

National Competitive Advantage

In recent years, a theory of national competitive advantage has become a more widely accepted model of why nations engage in international trade.[11] **National competitive advantage** derives from four conditions:

1. *Factor conditions* are the factors of production that we identified in Chapter 1.
2. Demand conditions *reflect a large domestic consumer base that promotes strong demand for innovative products.*

3 Related and supporting industries *include strong local or regional suppliers and/or industrial customers.*

4 *Strategies*, *structures*, and *rivalries* refer to firms and industries that stress cost reduction, product quality, higher productivity, and innovative new products.

When all of these conditions exist in an industry, the companies in that industry are motivated to be very innovative and to excel. This, in turn, increases the likelihood that they will engage in international business. Japan, for instance, has strong domestic demand for automobiles. Its automobile producers have well-developed supplier networks, and Japanese firms have competed intensely with each other for decades. This set of circumstances explains why Japanese automobile companies such as Toyota, Honda, Nissan, and Mazda are generally successful in foreign markets.

International competitiveness refers to the ability of a country to generate more wealth than its competitors in world markets. Each year, the World Economic Forum publishes a global competitiveness ranking. The ranking is based on both hard economic data and on a poll of business leaders in many countries. In 2009, the top three countries on the list were Switzerland, the United States, and Singapore. Canada ranked ninth. Canada's high taxes, regulated industries, relatively large bureaucracy, and overly conservative capital market structure were listed as reasons for a lower rating.[12]

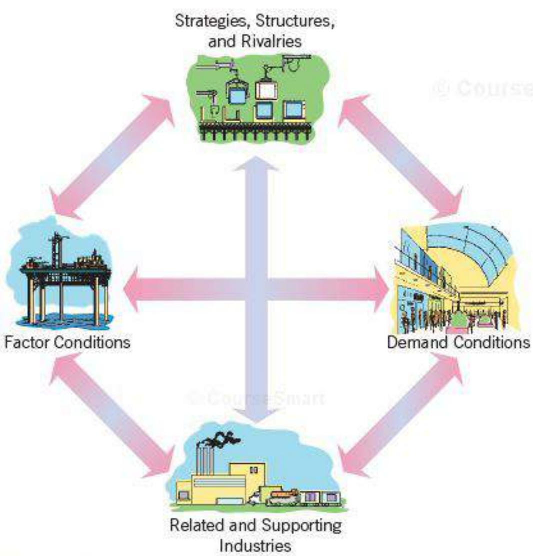


Figure 5.1
Attributes of national competitive advantage.

The Balance of Trade

A country's **balance of trade** is the difference in value between its total exports and its total imports. A country that exports more than it imports has a *favourable* balance of trade, or a **surplus**. A country that imports more than it exports has an *unfavourable* balance of trade, or a **deficit**. Canada has enjoyed a favourable balance of merchandise trade for many years, but in 2009, we had a trade deficit of $4.8 billion. The United States is by far the largest trading partner Canada has, and our overall trade balance has been generally favourable only because Canada exports so much more to the United States than it imports from it. But this is changing, partly due to the higher Canadian dollar. For years, economists had warned against Canada's dependence on the United States. Canada's nearly $47 billion surplus in 2008 turned into a deficit in large part because of a major decline in exports to the U.S. In addition, we import more from the countries of the European Union and Japan than we export to those countries, and we also import more than we export from all other countries as well (see Table 5.1).

INTERNATIONAL COMPETITIVENESS Competitive marketing of domestic products against foreign products.

BALANCE OF TRADE The economic value of all the products that a country exports minus the economic value of all the products it imports.

SURPLUS Situation in which a country exports more than it imports, creating a favourable balance of trade.

DEFICIT Situation in which a country's imports exceed its exports, creating a negative balance of trade.

BALANCE OF PAYMENTS Flow of all money into or out of a country.

The Balance of Payments

Even if a country has a favourable balance of trade, it can still have an unfavourable **balance of payments**. A country's balance of payments is the difference between money flowing into the country and money flowing out

Table 5.1 Canadian Exports to and Imports from Selected Countries, 2009

Country	Exports to (in billions of $)	Imports from (in billions of $)
United States	271.2	236.5
European Union	32.1	38.7
Japan	8.8	9.3
All others	57.4	89.6

EXCHANGE RATE Rate at which the currency of one nation can be exchanged for the currency of another nation.

EURO A common currency shared among most of the members of the European Union (excluding Denmark, Sweden, and the United Kingdom).

of the country as a result of trade and other transactions. An unfavourable balance means more money is flowing out than in. For Canada to have a favourable balance of payments for a given year, the total of our exports, foreign-tourist spending in this country, foreign investments here, and earnings from overseas investments must be greater than the total of our imports, Canadian-tourist spending overseas, our foreign aid grants, our military spending abroad, the investments made by Canadian firms abroad, and the earnings of foreigners from their investments in this country. Canada has had an unfavourable balance of payments for the last two decades, but it is slowly improving. In 1999, for example, $142 billion more flowed out of Canada than flowed in, but in 2009, that amount was $103 billion.[13]

Exchange Rates

An **exchange rate** is the rate at which the currency of one nation can be exchanged for another.[14] For example, if the exchange rate between Canadian dollars and British pounds is 1 to 1.55, this means that it costs $1.55 in Canadian dollars to "buy" one British pound. Alternatively, it would cost only 0.65 of a British pound to "buy" one Canadian dollar. This exchange rate means that 0.65 of a British pound and one Canadian dollar should have exactly the same purchasing power.

The value of one country's currency relative to that of another country varies with market conditions. For example, when many English citizens want to spend pounds to buy Canadian dollars (or goods), the value of the dollar relative to the pound increases, or becomes "stronger"; *demand* for the Canadian dollar is high. It is also "strong" when there is high demand for goods manufactured in Canada. Thus, the value of the Canadian dollar rises with the demand for Canadian goods. Exchange rates typically fluctuate by very small amounts on a daily basis. More significant variations usually occur over greater spans of time.

Fluctuation in exchange rates can have an important impact on the balance of trade. Suppose, for example, that you wanted to buy some English tea for 10 British pounds per box. At an exchange rate of 1.55 Canadian dollars to the British pound, a box will cost you $15.50 (10 pounds $\times$ 1.55 = 15.50). But what if the pound gets stronger? At an exchange rate of, say, 2.1 Canadian dollars to the pound, the same box of tea would cost you $21.00 (10 pounds $\times$ 2.1 = $21.00).

Changes in the exchange rate affect more than just the price of tea. If instead the Canadian dollar gets stronger in relation to the British pound, the prices of all Canadian-made products would rise in England and the prices of all English-made products would fall in Canada. As a result, the English would buy fewer Canadian-made products, and Canadians would spend more on English-made products. The result could conceivably be a Canadian trade deficit with England. This is why the recent increase in the value of the Canadian dollar has Canadian exporters very concerned.

One of the most significant developments in foreign exchange has been the introduction of the **euro**—a common currency among 16 members of the European Union (Denmark, Sweden, and the United Kingdom do not participate). The euro was officially introduced back in 2002. The Euro has quickly become as important as the U.S. dollar and the Japanese yen in international commerce. The euro has risen in value against the U.S. and Canadian dollars since its inception. It actually stood as high as $1.73 against the Canadian dollar in 2008; however, there was a sharp drop in the Euro currency in 2010—to $1.25. This raised fears about the stability of the Eurozone (see the Managing in Turbulent Times boxed feature entitled "The Crisis in Europe").

Exchange Rates and Competition Companies that conduct international operations must watch exchange-rate fluctuations closely because these changes affect overseas demand for their products and can be a major factor in international competition. In general, when the value of a country's domestic currency rises—becomes "stronger"—companies based there find it harder to export products to foreign markets and easier for foreign companies to enter local markets. It also makes it more cost-efficient for domestic companies to move production operations to lower-cost sites in foreign countries. When the value of a country's currency declines—becomes "weaker"—just the opposite patterns occur. Thus, as the value of a country's currency falls, its balance of trade should improve because domestic companies should experience a boost in exports. There should also be a corresponding decrease in the incentives for foreign companies to ship products into the domestic market.

A good case in point is the fluctuation in the Canadian dollar relative to the American dollar. About a decade ago, as we entered the new millennium, Canadians had grown accustomed to a weak dollar—in the 65–70 cent range against the U.S. dollar. The thought of a dollar at parity with the American dollar was almost unthinkable. Yet seven years later, on November 9, 2007, the dollar reached US$1.09, a level that had not been seen for decades. That movement and strength encouraged Canadians to cross

MANAGING IN TURBULENT TIMES

The Crisis in Europe: Let the Name Calling Begin

P-I-I-G-S! You would expect to hear this sort of language in an elementary school playground. Lately, however, this acronym is used by reporters to identify the primary sources of the economic crisis that threatens the European Union. The villains are *P*ortugal, *I*reland, *I*taly, *G*reece, and *S*pain.

Why are they villains? The governments of these countries have been spending far more money than they have been taking in. In 2010, most of the headlines focused on Greece as the leading culprit. This small European nation was particularly guilty of overspending and not living up to commitments it made when it entered the Eurozone. In 2009, Greece's annual deficit was 13 percent of GDP, which is far above the Eurozone's self-imposed limit of 3 percent. When an individual has too much debt and not enough income, bankruptcy is often the only solution. Default, the national equivalent, became a very real possibility for Greece. The country's financial situation had become very bad; partially because of U.S.-based Goldman Sachs' role as an enabler (it shielded some of Greece's debt with off-balance-sheet currency swaps).

But Greece was not alone. A key measure of economic stability is the debt-to-GDP ratio. A country's debt is the accumulation of all previous deficits (total obligations) and GDP measures total goods and services produced by a nation (which relates to its ability to pay). The PIIGS had the following ratios at the beginning of 2010: Greece 125 percent, Italy 117 percent, Portugal 85 percent, Ireland 83 percent, and Spain 66 percent. While Spain was in the best shape in terms of this particular ratio, its jobless rate stood at approximately 20 percent. These scary numbers raised many questions. How should the European Union deal with the problem nations? Should it allow Greece to default on its debt? If so, would that create a domino effect, with other nations following? Should the EU bail out Greece and reward its bad behaviour? Should the EU allow one of its nations to seek help from the International Monetary Fund (IMF)?

The initial reaction to the Greek crisis by the other EU countries was to say no to any sort of bailout or support. But for countries like Germany, that have large trade surpluses within the Eurozone, it was also in their interest to support the union and not risk its potential collapse. Pressure was therefore put on the Greek government to reduce its spending and to freeze the wages of government workers. But such actions will take time to have an effect, and in the meantime, the euro was taking a major hit on currency markets. The solidarity of the Eurozone was being severely tested for the first time. After months of debate, the European Union and the IMF stepped up with a EUR$750 billion support plan (EUR$500 from the EU and EUR$250 from the IMF). But this was not the end. The situation was dangerous for the union and had major implications for the world economy.

Critical Thinking Questions

1. Should the Eurozone partners allow one of their members to face the consequences of its economic problems on their own? Debate the pros and cons.
2. Should the Eurozone partners expel members from the EU who do not meet the financial criteria set out by the EU? Explain.

the U.S. border and purchase everything from clothing to cars. Over the next few years the dollar retreated a bit, but a new era was upon Canadians. In mid-2010, the dollar was once again flirting with parity.[15]

These dollar fluctuations have also had a huge impact on businesses. Canadian companies are finding it harder to compete internationally, since they can no longer rely on a cheap dollar to make their products more affordable across the border and abroad. But after the initial shock, companies are learning to cope. According to chairman and CEO of Clearwater Seafoods Income Fund, "The way you deal with the stronger Canadian dollar is to increase the efficiency of your operations."[16] Other companies, like Nova Scotia–based High Liner Foods, which buys most of its raw fish on the world markets in U.S. dollars, has seen a net benefit. The rise in the Canadian dollar helped the company increase profits by 40 percent in 2009.[17]

LO-3 International Business Management

Wherever a firm is located, its success depends largely on how well it is managed. International business is challenging because the basic management responsibilities—planning, organizing, leading, and controlling—are much more difficult to carry out when a business operates in several markets scattered around the globe. (We discuss the functions of management in Chapter 6.)

Managing means making decisions. In this section, we examine the three most basic decisions that a company's management must make when faced with the prospect of globalization. The first decision is whether to "go international" at all. Often that decision is made because a company feels it has to shift its production to a low-cost foreign country in order to remain competitive. Once that decision has been made, managers must decide on the company's level of international involvement and on the organizational structure that will best meet its global needs.

While Toyota markets five sport-utility vehicle models in Canada (manufacturing the RAV4 in Woodstock, Ontario, and exporting the other models to Canada), it sells only its two smallest ones at home in Japan, where crowded roads, narrow driveways, and scarce parking spaces make larger vehicles impractical.

"Going International"

The world economy is becoming globalized, and more and more firms are conducting international operations. As Figure 5.2 shows, several factors enter into the decision to go international. One overriding factor is the business climate in other nations. Even experienced firms have encountered cultural, legal, and economic roadblocks, as we shall see later in this chapter. In considering international expansion, a company should also consider at least two other questions: Is there a demand for its products abroad? If so, must those products be adapted for international consumption? As we saw in the opening case, these decisions can be quite complicated.

Gauging International Demand Products that are seen as vital in one country may be useless in another. Snowmobiles are popular for transportation and recreation in Canada and the northern United States, and they revolutionized reindeer herding in Lapland. But there would be no demand at all for this product in Central America. Although this is an extreme example, the point is quite basic to the decision to go international: namely, that foreign demand for a company's product may be greater than, the same as, or weaker than domestic demand. Even when there is demand, advertising may still need to be adjusted. For instance, in Canada, bicycles and small motorcycles are mainly used for recreation, but in many parts of Asia they are seen as transportation. Market research and/or the prior market entry of competitors may indicate whether there's an international demand for a firm's products. New Brunswick–based McCain Foods has worked hard to build market share in South Africa. It even developed single-sized portions of frozen vegetables to serve customers who do not have proper refrigeration. There are now 2000 McCain employees in South Africa serving eight African nations.[18]

Some products—like smart phones, Hollywood movies, and video games—are popular all over the world. Movies like *Avatar* and *Twilight* earn significant revenues in North America but generate even more revenues overseas.

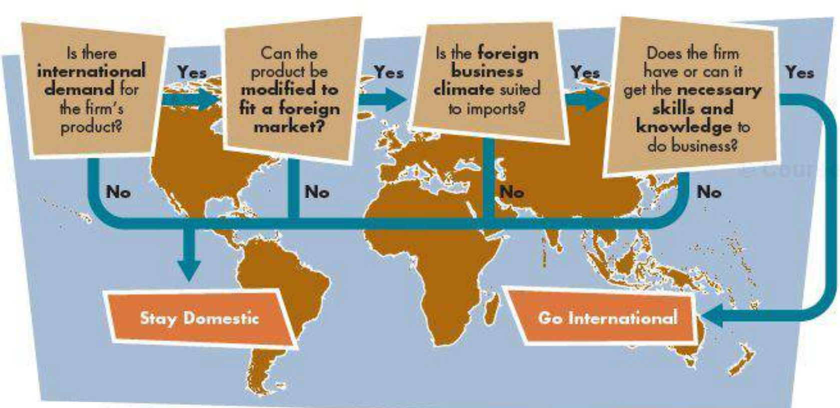


Figure 5.2
Going international.

Adapting to Customer Needs If there is international demand for its product, a firm must consider whether and how to adapt that product to meet the special demands and expectations of foreign customers. Movies, for example, have to be dubbed into foreign languages. Likewise, McDonald's restaurants sell wine in France, beer in Germany, and meatless sandwiches in India to accommodate local tastes and preferences. Ford products must have their steering wheels mounted on the right if they are to be sold in England and Japan. When Toyota launches upscale cars at home, it retains the Toyota nameplate; those same cars are sold under the Lexus nameplate in Canada because the firm has concluded that Canadian consumers will not pay a premium price for a "Toyota." BlackBerry smart phones may originate in Waterloo, Ontario, but Research In Motion has sold over 1.2 million smart phones in Indonesia; in Jakarta, a BlackBerry is an important symbol of success. To succeed in this market, RIM adapted its approach by creating prepaid scratch cards. This enables the consumer to pay a set amount for data and email service each week or month.[19] The boxed insert entitled "Epic Entrepreneurs" describes one company's experience in going international.

ENTREPRENEURSHIP AND NEW VENTURES

Epic Entrepreneurs: Have Camera, Will Travel

Help wanted: Dynamic and innovative company seeks staff who are adventurous, love to travel, and are willing to spend most of the year in some of the world's most exotic locations, many of them very warm! Sounds like a dream job, right? Well, while there's sure to be other mandatory criteria, jobseekers interested in working for EPIC Newsgroup Inc. must meet the above demands. EPIC was started in 2004 by two young Vancouverites, Sabrina Heinekey and Tiffany Steeves. While travelling on foreign assignment, the duo realized that many countries and their respective tourism boards, corporations, ministries, and so on were not using television as a promotional medium. They decided the gap was worth pursuing, and thus their agency was launched.

EPIC is a production and media placement company that creates segments for broadcast on various channels throughout Europe, North America, Africa, the Middle East, and Asia. Generally, each year Heinekey and Steeves select up to five countries that they believe have some form of potential for international interest (e.g., developing a brand, misconception of a brand, international mystique),and they prepare a thoroughly researched media package. As an example, EPIC produced a video for Jordan's tourism board. According to Steeves, "People often lump the Middle East together as a war-torn area. Well, Jordan isn't like that at all. It's a safe, peaceful country." So sometimes their work is to help countries reposition and/or realign themselves in the international marketplace. Many of EPIC's clients were previously working under the perception that television production as a form of media exposure was difficult and out of reach; EPIC provides a solution. However, in doing so, Heinekey and Steeves haven't always found the exotic, international locations easy to navigate themselves.

The pair learned early on that young women don't often play a role in the business environment of some countries. Heinekey and Steeves state, "In some countries, for example, we've had to disprove local attitudes towards working with two women. . . . " The cultural differences regarding television as an appropriate medium have also required that they "take potential clients through a learning process." What has been their guiding philosophy in navigating these unfamiliar waters? According to Heinekey, it's their sensitivity to cultural differences and their focus on professionalism and preparation that have helped open doors for them around the globe.

"We're really doing well," says Steeves. In 2007, the Business Development Bank of Canada (BDC) applauded their success and bestowed upon them the Young Entrepreneur Award for British Columbia. In 2008, *Chatelaine* magazine named the two co-founders in an issue that profiled "80 amazing women to watch." According to BDC president and CEO Jean-René Halde, "They took an interesting concept, developed a novel product, and turned it into a thriving global enterprise."

Critical Thinking Question

1. The decision to "go international" requires a high degree of analysis and examination of factors both internal and external to the business. Assess EPIC's form of competitive advantage, level of involvement in international business, and various barriers to international trade.

EXPORTER Firm that distributes and sells products to one or more foreign countries.

IMPORTER Firm that buys products in foreign markets and then imports them for resale in its home country.

INTERNATIONAL FIRM Firm that conducts a significant portion of its business in foreign countries.

MULTINATIONAL FIRM Firm that designs, produces, and markets products in many nations.

INDEPENDENT AGENT Foreign individual or organization that agrees to represent an exporter's interests.

LICENSING ARRANGEMENT Arrangement in which firms choose foreign individuals or organizations to manufacture or market their products in another country.

ROYALTIES Fees that an exporter receives for allowing a company in a foreign country to manufacture or market the exporter's products.

Levels of Involvement in International Business

After a firm decides to go international, it must decide on the level of its international involvement. Several options are available. At the most basic level, a firm may act as an *exporter* or *importer*, organize as an *international firm*, or operate as a *multinational firm*. Most of the world's largest industrial firms are multinationals.

Exporters and Importers An **exporter** is a firm that makes products in one country and then distributes and sells them in others. An **importer** buys products in foreign markets and then imports them for resale in its home country. Exporters and importers tend to conduct most of their business in their home nations. Both enterprises entail the lowest level of involvement in international operations and are excellent ways to learn the fine points of global business.

Exporting is not limited to multinationals. Small firms also export products and services. For example, Lingo Media Inc. is the largest supplier of English-language textbooks in China's primary school system. Now this Toronto-based company has created speak2me.cn, a learning solution website that uses voice recognition. The site was created to solve a major problem in China: there is a shortage of teachers who speak English properly. The company registered 1 million users on the site in the first year alone.[20]

International Firms As firms gain experience and success as exporters and importers, they may move to the next level of involvement. An **international firm** conducts a significant portion of its business abroad. International firms also maintain manufacturing facilities overseas but their primary focus remains on their domestic market.

Multinational Firms Most **multinational firms** do not ordinarily think of themselves as having domestic and international divisions. Instead, planning and decision making are geared toward global markets.[21] The locations of headquarters are almost irrelevant. Royal Dutch/Shell, Nestlé, IBM, and Ford are well-known multinationals.

The economic importance of multinational firms should not be underestimated. Consider, for example, the economic impact of the 500 largest multinational corporations. In 2009, Royal Dutch/Shell ranked number one in the Fortune Global 500 rankings with over 102 000 employees and US$458 billion in sales. Exxon was second with 105 000 employees and US$443 billion in sales. Walmart ranked third with US$405 billion in sales and 2.1 million employees (with 700 000 international employees in its 4000 international outlets). Multinationals employ millions of people; buy supplies, parts, equipment, and materials from thousands of other firms; and pay billions of dollars in taxes. Moreover, their activities and products affect the lives of hundreds of millions of consumers, competitors, and investors (sometimes not in a very positive way).[22] Organized protests against the activities of multinational corporations have become quite common.

International Organizational Structures

Different levels of involvement in international business require different kinds of organizational structure. For example, a structure that would help coordinate an exporter's activities would be inadequate for the activities of a multinational firm. In this section, we briefly consider the spectrum of international organizational strategies, including *independent agents*, *licensing arrangements*, *branch offices*, *strategic alliances*, and *foreign direct investment*.

Independent Agents An **independent agent** is a foreign individual or organization that agrees to represent an exporter's interests in foreign markets. Independent agents often act as sales representatives: they sell the exporter's products, collect payment, and ensure that customers are satisfied. Independent agents often represent several firms at once and usually do not specialize in a particular product or market. Levi Strauss uses agents to market clothing products in many small countries in Africa, Asia, and South America.

Licensing Arrangements Canadian companies seeking more substantial involvement in international business may opt for **licensing arrangements**. Firms give individuals or companies in a foreign country the exclusive right to manufacture or market their products in that area. In return, the exporter typically receives a fee plus ongoing payments called **royalties**.[23] Royalties are usually calculated as a percentage of the licence holder's sales. For example, Can-Eng Manufacturing, Canada's largest supplier of industrial furnaces, exports its furnaces under licensing arrangements with Japan, Brazil, Germany, Korea, Taiwan, and Mexico.

Franchising is a special form of licensing that is also very popular.[24] McDonald's and Pizza Hut franchise around the world. Similarly, Accor SA, a French hotel chain, franchises its Ibis, Sofitel, and Novotel hotels.

Branch Offices Instead of developing relationships with foreign companies or independent agents, a firm may simply send some of its own managers to overseas branch offices. A company has more direct control over branch managers than over agents or licence holders. **Branch offices** also give a company a more visible public presence in foreign countries. Potential customers tend to feel more secure when a business has branch offices in their country.

When a business operates branches, plants, or subsidiaries in several countries, it may assign one plant or subsidiary the responsibility for researching, developing, manufacturing, and marketing one product or line of products. This is known as **world product mandating**.

Strategic Alliances The concept of a strategic alliance was introduced in Chapter 2. In international business, it means that a company finds a partner in a foreign country where it would like to conduct business. Each party agrees to invest resources and capital in a new business or else to cooperate in some way for mutual benefit. This new business—the alliance—is then owned by the partners, which divide its profits. For example, Canadian publisher Lingo Media Inc. is involved in a strategic alliance with the state-owned People's Education Press, which is the market leader in providing textbooks to Chinese schools.[25]

The number of strategic alliances among major companies has increased significantly over the last decade and is likely to grow even more. In many countries, including Mexico, India, and China, laws make alliances virtually the only way to do business within their borders.[26]

In addition to easing the way into new markets, alliances give firms greater control over their foreign activities than independent agents and licensing arrangements. (All partners in an alliance retain some say in its decisions.) Perhaps most important, alliances allow firms to benefit from the knowledge and expertise of their foreign partners. In India, Walmart partnered with Bharti Enterprises to build 10–15 large cash-and-carry stores. Walmart wanted to capture a share of the booming retail market without angering the local mom-and-pop merchants and middlemen that dominate the industry.[27]

Foreign Direct Investment The term **foreign direct investment (FDI)** means buying or establishing tangible assets in another country.[28] For example, Dell recently built new assembly plants in Europe and Brazil, and Volkswagen built factories in Mexico and Brazil. The establishment of branch offices in foreign countries is also a type of foreign direct investment.

As we've seen, many Canadian firms export goods and services to foreign countries, and they also set up manufacturing operations in other countries. Bombardier recently landed a $4 billion deal in China, for the sale of 80 high-speed trains. This deal was made possible because of years of direct investments and a Bombardier/China joint venture group called Bombardier Sifang (Qingdao).[29] However, a debate has been going on for many years about how FDI by foreign firms in Canada affects Canadians. The **Foreign Investment Review Agency** was established in 1973 to ensure that FDI benefited Canadians. In 1985, FIRA became **Investment Canada** and the mandate was changed to focus on attracting foreign investment. Since the late 1980s, foreign ownership of Canadian industry has again been on the rise, and now stands at approximately 30 percent.[30]

Recently, foreign buyouts of major firms like Inco, Four Seasons Hotels, and Alcan have caused some Canadian business leaders to express renewed fears about FDI in Canada. A study by Secor Consulting concluded that Canada is the easiest country in the world for foreigners to come into and take over a business. It also found that only three countries in the world were net sellers of their companies: Canada, the United States, and Great Britain.[31] The most general concern is that foreign buyouts of Canadian firms will damage the economy because the head offices will move to foreign countries and major decisions will be made there, not in Canada.

Another concern is that foreign takeovers will mean large job losses. But a Statistics Canada study showed that between 1999 and 2005, foreign companies were responsible for creating *all* of the new head offices that were created in Canada and about two-thirds of the jobs in those new head offices.[32] Another survey of 150 senior Canadian executives showed that the issue of foreign ownership ranked low on their list of perceived economic challenges.[33] Many experts argue that placing limitations on foreign investment in Canada essentially shields companies from competition and makes them less efficient.[34] Table 5.2 lists the top 10 foreign-owned companies in Canada.

BRANCH OFFICE A location that an exporting firm establishes in a foreign country to sell its products more effectively.

WORLD PRODUCT MANDATING The assignment by a multinational of a product responsibility to a particular branch.

FOREIGN DIRECT INVESTMENT (FDI) Buying or establishing tangible assets in another country.

FOREIGN INVESTMENT REVIEW AGENCY (FIRA) Established in 1973 to screen new foreign direct investment in Canada; supposed to ensure that significant benefits accrued to Canada.

Table 5.2 Top 10 Foreign-Controlled Companies in Canada, 2009

Company	Annual Revenues (in billions of $)
1. Imperial Oil	21.3
2. Walmart Canada Corp.	17.5
3. Husky Energy Inc.	15.1
4. Novelis Inc.	11.5
5. Costco Wholesale Canada	10.9
6. Direct Energy Marketing Ltd.	10.8
7. Honda Canada Inc.	9.4
8. Ford Motor Co. of Canada	9.1
9. Ultramar Ltd.	7.3
10. Canada Safeway Ltd.	6.7

LO-4 Barriers to International Trade

Whether a business is selling to just a few foreign markets or is a true multinational, a number of differences between countries will affect its international operations. How a firm responds to and manages social, economic, and political issues will go a long way toward determining its success.

Social and Cultural Differences

Any firm involved in international business needs to understand something about the society and culture in the countries it plans to operate in. Unless a firm understands these cultural differences—either itself or by acquiring a partner that does—it will probably not be successful in its international business activities.

Some differences are relatively obvious. Language barriers can cause inappropriate naming of products. In addition, the physical stature of people in different countries can make a difference. For example, the Japanese and French are slimmer and shorter on average than Canadians, an important consideration for firms that intend to sell clothes in these markets. Differences in the average age of the local population can also have ramifications for product development and marketing. Countries with growing populations tend to have a high percentage of young people. Thus, electronics and fashionable clothing would likely do well. Countries with stable or declining populations tend to have more old people. Generic pharmaceuticals might be more successful in such markets.

In addition to such obvious differences, a wide range of subtle value differences can have an important impact. For example, many Europeans shop daily. To Canadians used to weekly trips to the supermarket, the European pattern may seem like a waste of time. But for Europeans, shopping is not just "buying food." It is also meeting friends, exchanging political views, gossiping, and socializing.

What implications does this kind of shopping have for firms selling in European markets? First, those who go shopping each day do not need the large refrigerators and freezers common in North America. Second, the large supermarkets one sees in Canada are not an appropriate retail outlet in Europe. Finally, the kinds of food Europeans buy differ from those Canadians buy. While in Canada prepared and frozen foods are important, Europeans often prefer to buy fresh ingredients to do their own food preparation "from scratch." These differences are gradually disappearing, however, so firms need to be on the lookout for future opportunities as they emerge.

Even more subtle behavioural differences that can influence business activity exist. For example, crossing your legs in a business meeting in Saudi Arabia is inappropriate, because showing the sole of your foot is viewed as an insult to the other people in the room. In Portugal, it is considered rude to discuss business during dinner, and in Taiwan, tapping your fingers on the table is a sign of appreciation for a meal. In China, don't give a businessman a green hat and don't wrap a gift in white or black (a green hat on a Chinese man is said to indicate that his wife is unfaithful, and black and white are associated with death). Deals can be lost based on inadvertent cultural insults. Knowledge of local dos and don'ts is important in international business activity. Do your homework.[35]

Economic Differences

Although cultural differences are often subtle, economic differences can be fairly pronounced. In dealing with economies like those of France and Sweden, firms must be aware of when—and to what extent—the government is involved in a given industry. The French government is heavily involved in all aspects of airplane design and manufacturing.

Similarly, a foreign firm doing business in a command economy must understand the unfamiliar relationship of government to business, including a host of idiosyncratic practices. General Motors, which entered a US$100 million joint venture to build pickup trucks in China, found itself faced with an economic system that favoured state-owned companies over foreign investors. So, while its Chinese suppliers passed on inflation-based price increases for steel and energy, GM could not in turn pass increases on to Chinese consumers. With subsidized state-owned automakers charging considerably less per truck, GM had no choice but to hold its own prices—and lose money on each sale. Despite such problems, however, not all companies have had entirely negative experiences. For example, when Motorola opened a factory in

China to manufacture communication devices, it involved Chinese technicians in the production process. Chinese designers and engineers played key roles in creating an operation that integrated manufacturing, sales, research, and development.

Legal and Political Differences

Legal and political differences are often closely linked to the structure of the economic systems in different countries. These issues include *tariffs* and *quotas, local-content laws,* and *business-practice laws.*

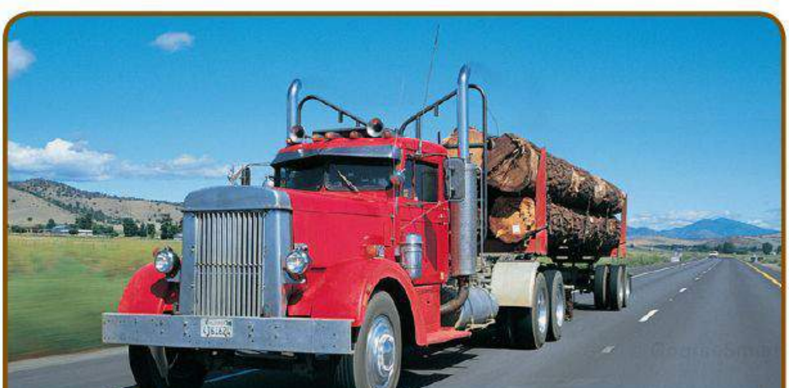
Quotas, Tariffs, and Subsidies Even free-market economies often use some form of quota and/or tariff that affects the prices and quantities of foreign-made products in those nations. A **quota** restricts the total number of certain products that can be imported into a country. It indirectly raises the prices of those imports by reducing their supply. The ultimate form of quota is an **embargo**: a government order forbidding exportation and/or importation of a particular product—or even all the products—of a particular country. For example, many countries control bacteria and disease by banning certain plants and agricultural products.

In contrast, a **tariff** is a tax charged on imported products. Tariffs directly affect the prices of products, effectively raising the price of imports to consumers, who must pay not only for the products but also for the tariff. Tariffs may take either of two forms. A **revenue tariff** is imposed strictly to raise money for the government. Most tariffs in effect today, however, are **protectionist tariffs** meant to discourage the import of a particular product. A few years ago, the Canadian government placed a 34.6 percent tariff on barbecues made in China after complaints were received that Chinese companies were unfairly subsidizing their production.[36]

Governments impose quotas and tariffs for a wide variety of reasons. For example, the U.S. government restricts the number of Japanese automobiles that can be imported into that country. Italy imposes high tariffs on imported electronic goods, thus making them more expensive. Canada also imposes tariffs on many imported goods.

Back in 2002, the U.S. Commerce Department imposed a 29 percent tariff on softwood lumber exported from Canada to the United States (84 percent of Canadian lumber is exported to the United States). Ottawa immediately appealed the decision under the provisions of both the North American Free Trade Agreement (NAFTA) and the World Trade Organization (WTO). During 2002 and 2003, both the WTO and NAFTA ruled against the United States on various points in the appeal and said that duties on Canadian lumber must be cut drastically. In spite of these rulings, the United States continued to impose the duties. The Canadian lumber industry paid over $5.3 billion in duties to the United States.[37] A tentative resolution was reached in 2006, when the United States agreed to pay back 78 percent of the duties imposed on Canadian lumber, on the condition that Canada agree that its share of the U.S. lumber market would be capped at 34 percent.[38] Several Canadian lumber companies said that they weren't happy with that, but an agreement was eventually reached that went into effect in October 2006.[39]

A **subsidy** is a government payment given to a domestic business to help it compete with foreign firms. Bombardier has received subsidies from both federal



The long-standing softwood lumber dispute between the United States and Canada hurt Canadian companies in the forestry industry. The dispute was settled in 2006, but much unhappiness is still evident, and critics have charged that the Conservative government caved in to American pressure.

QUOTA A restriction by one nation on the total number of products of a certain type that can be imported from another nation.

EMBARGO A government order forbidding exportation and/or importation of a particular product.

TARIFF A tax levied on imported products.

REVENUE TARIFF A tariff imposed solely to raise money for the government that imposes it.

PROTECTIONIST TARIFF A tariff imposed at least in part to discourage imports of a particular product.

SUBSIDY A government payment to help domestic business compete with foreign firms.

PROTECTIONISM Protecting domestic business at the expense of free market competition.

LOCAL-CONTENT LAWS Laws requiring that products sold in a particular country be at least partly made in that country.

and provincial governments. These funds and low-interest loans have helped the company compete and develop its major projects. Bombardier and its main rival, Brazil-based Embraer, have accused each other of receiving excessive unfair government support, which has led to disputes at the WTO. The end-of-chapter case addresses this dispute.

When the government of a country pays subsidies to one of its domestic companies or industries, this can have a negative effect on producers in other countries. For example, the WTO ruled that the U.S. government's subsidies to its cotton growers broke trade rules, depressed world cotton prices, and hurt Brazilian cotton producers.[40] These subsidies also hurt small cotton farmers in Africa because they caused highly productive U.S. farmers to produce a lot of cotton, which drove down the price African farmers received.[41] Canada's supply management system, which restricts imports and guarantees markets for producers of chickens, turkeys, eggs, and milk, could also come under fire since the WTO views the system as an unfair subsidy to producers.[42] More information about the WTO is available at the end of the chapter.

(This item omitted from WebBook edition)

Subsidies are designed to support domestic companies; however, in this free-trade era, governments are increasingly generous with foreign firms that can help develop local industries and provide local jobs. Warner Bros. is opening up a new studio to develop high-end video games in Montreal. Local talent, reputation, and knowledge were key factors in the decision, but government funding helped close the deal. The Quebec government provided $7.5 million to get the studio off the ground. Speed Racer is one of the games produced by Warner Bros. Interactive.

Protectionism—the practice of protecting domestic business at the expense of free market competition—has advocates and critics. Supporters argue that tariffs and quotas protect domestic firms and jobs. In particular, they protect new industries until they are able to compete internationally. Some claim they are necessary because other nations have such measures. Still others justify protectionism in the name of national security and argue that advanced technology should not be sold to potential enemies.

But opponents of protectionism are equally vocal. They note that protectionism reduces competition and drives up prices. They cite it as a cause of friction between nations. They maintain that while jobs in some industries would be lost if protectionism ceased, jobs in other industries would expand if all countries abolished tariffs and quotas.

Protectionism sometimes takes on almost comic proportions. Neither Europe nor the United States grows bananas, but both European and U.S. firms buy and sell bananas in foreign markets. Problems arose when the EU put a quota on bananas imported from Latin America—a market dominated by two U.S. firms, Chiquita and Dole—in order to help firms based in current and former European colonies in the Caribbean. The United States retaliated and imposed a 100 percent tariff on certain luxury products imported from Europe, including Louis Vuitton handbags, Scottish cashmere sweaters, and Parma ham.[43]

Local-Content Laws A country can affect how a foreign firm does business there by enacting **local-content laws** that require products sold in a particular country be at least partly made in that country. These laws typically mean that firms seeking to do business in a country must either invest directly or have a local joint-venture partner. In this way, some of the profits in a foreign country are shared with the people who live there. Many countries have local-content laws. In a fairly extreme case, Venezuela forbids the import of any product if a similar product is made in Venezuela. Back in 2005, Venezuela's president said he would cancel all mining licences and stop issuing new ones to foreign companies. This move was designed to protect the many small, local miners. Oil and gas licences held by foreign companies had already been cancelled.

These actions make foreign companies reluctant to invest in Venezuela.[44]

Local-content laws may even exist within a country; when they do, they act just like trade barriers. In Canada, for example, a low bid on a bridge in British Columbia was rejected because the company that made the bid was from Alberta. The job was given to a B.C. company. A window manufacturer from New Brunswick lost a contract in Nova Scotia despite having made the lowest bid, and the job went to a company in Nova Scotia.

The Agreement on Internal Trade (AIT) requires all 10 Canadian provinces to remove barriers to agricultural trade. But when Quebec—which has a strong dairy lobby—prohibited margarine coloured to look like butter, it was in violation of the agreement.[45] Unilever Canada Ltd. challenged the legality of the ban on coloured margarine in 2002, but it was not until 2008 that the province of Quebec repealed the law.[46] In another case, Prince Edward Island ignored a dispute panel ruling that stated P.E.I.'s milk import restrictions also violated the AIT.[47] A third case involves the question of who is allowed to audit the financial statements of public companies. At present, only chartered accountants (CAs) are allowed to do this in Quebec. This rule is being challenged by the certified general accountants (CGAs), who have auditing rights in most other provinces.[48] If provincial governments do not honour their obligations, the AIT will become meaningless.

Business-Practice Laws Many businesses entering new markets encounter problems in complying with stringent regulations and bureaucratic obstacles. Such practices are affected by the **business-practice laws** that host countries use to govern business practices within their jurisdictions. Walmart left Germany and South Korea because it did not effectively adapt to local tastes and was unable to achieve economies of scale.[49] In Germany, for example, Walmart had to stop refunding price differences on items sold for less by other stores because the practice is illegal in Germany. In an example closer to home, mixed martial arts UFC events have been held in Montreal, Vancouver, and the U.S., but until recently they were banned in Ontario.[50]

Paying bribes to government officials to get business is another problem area. The Canadian Corruption of Foreign Public Officials Act prohibits bribery of foreign officials, but as more Canadian companies do business abroad, they find themselves competing against companies that are not reluctant to pay bribes to get business. As a result, some Canadian companies are losing business.[51] In an attempt to create fairer competition among multinational companies, ministers from the Organisation for Economic Co-operation and Development (OECD) agreed in 1997 to criminalize bribery of foreign public officials.[52] Recently, four employees of the mining giant Rio Tinto pled guilty to bribery charges in China. Mr. Stern Hu, a top executive in charge of iron ore, was sentenced to 10 years in prison for accepting a bribe of US$146 000.[53]

Transparency International (TI), an organization devoted to stamping out global corruption, says that companies from Belgium and Canada are least likely to pay bribes to win business in foreign countries; Russian firms are most likely to pay bribes.[54] TI publishes a Corruption Perceptions Index, which ranks countries based on the amount of corruption that is perceived to exist, based on ratings by business people, academics, and risk analysts. The 2009 index showed that the least corrupt countries are New Zealand, Denmark, and Singapore, while the most corrupt countries are Myanmar, Afghanistan, and Somalia. Canada was tied for eighth least corrupt with Iceland and Australia, and the United States was nineteenth.[55]

BUSINESS-PRACTICE LAW Law or regulation governing business practices in given countries.

CARTEL Any association of producers whose purpose is to control supply of and prices for a given product.

DUMPING Selling a product for less abroad than in the producing nation.

Cartels and Dumping A **cartel** is an association of producers whose purpose is to control the supply and price of a commodity. The most famous cartel is the Organization of the Petroleum Exporting Countries (OPEC). It has given oil-producing countries considerable power in the last 25 years. At various times, other cartels have been evident in diamonds, shipping, and coffee. While nothing much can be done when governments form a cartel like OPEC, private-sector businesses can be prosecuted for doing so. In 2008 alone, the European Union imposed fines on importers of Dole and Del Monte bananas (who were fined US$95.5 million), on makers of car glass (fined $2 billion), and on makers of paraffin wax used in paper plates and cups (fined $1 billion).[56] Canada is involved in a potash cartel with Belarus and Russia (these three nations account for almost 80 percent of production); the price has quadrupled in just a few years.[57]

Many countries forbid **dumping**—selling a product abroad for less than the comparable price charged in the home country. Antidumping legislation typically defines dumping as occurring if products are being sold at prices less than fair value, or if the result unfairly harms domestic industry. Recently, the U.S. imposed duties of 10.36 to 15.78 percent on steel pipes produced in China. China denounced the U.S. protectionist approach.[58] However, the U.S. is not alone in its concerns; India has accused China of dumping products on the Indian market that it can't sell elsewhere.[59]

GENERAL AGREEMENT ON TARIFFS AND TRADE (GATT) International trade agreement to encourage the multilateral reduction or elimination of trade barriers.

WORLD TRADE ORGANIZATION (WTO) Organization through which member nations negotiate trading agreements and resolve disputes about trade policies and practices.

EUROPEAN UNION (EU) Agreement among major Western European nations to eliminate or make uniform most trade barriers affecting group members.

LO-5 Overcoming Barriers to Trade

Despite the barriers to trade described so far, international trade is flourishing. This is because both organizations and free-trade treaties exist to promote international trade. The most significant of these are the General Agreement on Tariffs and Trade (GATT), the World Trade Organization (WTO), the European Union (EU), and the North American Free Trade Agreement (NAFTA).

General Agreement on Tariffs and Trade (GATT)

Governments typically view exports as good (because they create jobs in the country) and imports as bad (because they cause job losses in the country). Because of this, governments may be tempted to erect trade barriers to discourage imports. But if every country does this, international trade is stifled. To overcome this tendency, the **General Agreement on Tariffs and Trade (GATT)**—which was often humorously referred to as the General Agreement to Talk and Talk—was signed after the Second World War. Its purpose was to reduce or eliminate trade barriers, such as tariffs and quotas. It did so by encouraging nations to protect domestic industries within agreed-upon limits and to engage in multilateral negotiations. While 92 countries signed GATT, not all complied with its rules. The United States was one of the worst offenders. A revision of GATT went into effect in 1994, but many issues remained unresolved—for example, the opening of foreign markets to most financial services.

World Trade Organization

On January 1, 1995, the **World Trade Organization (WTO)** came into existence as the successor to GATT. The 153 member countries are required to open markets to international trade, and the WTO is empowered to pursue three goals:

1. Promote trade by encouraging members to adopt fair trade practices.
2. Reduce trade barriers by promoting multilateral negotiations.
3. Establish fair procedures for resolving disputes among members.

The WTO is overseeing reductions in import duties on thousands of products that are traded between countries. Canada, the United States, and the European Union are founding members of the WTO.[60] Unlike GATT, the WTO's decisions are binding, and many people feared that it would make sweeping decisions and boss countries around. These fears were a bit overstated.[61] The WTO has served in its role as a ruling body but appeals can often drag on for years. For example, in 2010, Boeing won a ruling against Airbus because it received US$4.1 billion in loans from European governments while developing its A380 jets. Despite the ruling, there appears to be even more money being given to Airbus for development of the new A350. It has been five years since the case was first presented and it could be years before Boeing sees any rewards from the ruling.[62] The WTO also recently ruled against China and its practice of controlling access to distribution of films. China allows only 70 foreign films to be distributed in that country per year. The WTO ordered China to open distribution channels; this is seen as a big win for North American movie, music, and print distributors.[63]

The WTO has had significant trouble dealing with the issue of agricultural subsidies. Many attempts have been made during the last few years to resolve this problem (the so-called Doha Round of trade talks). The general idea was that developing countries would lower their tariffs on industrial goods, and European and American governments would lower subsidies on agricultural products. In 2008, however, these efforts collapsed, with negotiators from China and India blaming the United States, and negotiators from the United States blaming China and India.[64] In addition, WTO talks on trade liberalization have often been disrupted by protestors who resent the power of the WTO and who are concerned about what world trade is doing to both the environment and the developing countries.[65] Protestors include labour unions (which regard Third World imports as unfair), environmentalists (who are concerned about business activity harming the environment), social activists (who are concerned about poor working conditions in developing countries), and farmers (who are concerned about the effect of free trade on grain prices).

The European Union

Originally called the Common Market, the **European Union (EU)** initially included only the principal Western European nations like Italy, Germany, France, and the United Kingdom. But by 2010, 27 countries belonged to the EU (see Figure 5.3). Other countries are in the process of applying for membership, including Croatia and Turkey. The EU has eliminated most quotas and set uniform tariff levels on products imported and exported within its group. The EU is the largest free marketplace in the world and produces nearly one-quarter of total global wealth.[66]

The North American Free Trade Agreement

On January 1, 1994, the **North American Free Trade Agreement (NAFTA)** took effect. The objective of NAFTA was to create a free trade area for Canada, the United States, and Mexico. It eliminates trade barriers, promotes fair competition, and increases investment opportunities.

Surveys conducted during the early 1990s showed that the majority of Canadians were opposed to NAFTA. They feared that jobs would be lost to other countries or that Canada's sovereignty would be threatened, and that Canada would be flooded with products manufactured in Mexico, where wages are much lower. Supporters of NAFTA argued that the agreement would open up U.S. markets for Canadian products and thereby create more employment in Canada, that the agreement would not threaten Canada's sovereignty, and that NAFTA would create more employment possibilities for women.

Figure 5.3
The nations of the European Union.

NORTH AMERICAN FREE TRADE AGREEMENT (NAFTA) Agreement to gradually eliminate tariffs and other trade barriers among the United States, Canada, and Mexico.

What has actually happened since NAFTA took effect? A group of economists at the Canadian Economics Association concluded that free trade has not been as good for Canada as predicted by its supporters, nor as bad for Canada as predicted by its detractors.[67] Several specific effects are noticeable:

- NAFTA has created a much more active North American market.
- Direct foreign investment has increased in Canada.
- U.S. imports from (and exports to) Mexico have increased.
- Canada has become an exporting powerhouse.
- Trade between the United States and Canada has risen sharply, and Canada still enjoys a large trade surplus with the United States.

In the last few years, there is evidence that the benefits of NAFTA are slowly being eroded by ever-increasing delays at border crossings, caused mostly by heavy U.S. border security as a result of the terrorist attacks in 2001. Studies by the Conference Board of Canada and the Canadian and U.S. chambers of commerce show that companies are having difficulty taking advantage of the efficiencies of integrated supply chains because there are so many cross-border delays. Those delays are forcing companies to spend extra time and money just trying to ensure that their deliveries will get through to customers on time.[68] On the positive side, there is now an extensive Canadian presence in Mexico in everything from mining to auto parts to banking. For example, Scotiabank, the most international Canadian bank, has made great inroads in Mexico with over two million Mexican clients.[69]

Other Free Trade Agreements in the Americas

While NAFTA has been the most publicized trade agreement in the Americas, there has been a flurry of activity among other countries as well. On January 1, 1995, a free trade agreement known as Mercosur went into effect between Argentina, Brazil, Uruguay, and Paraguay. Venezuela was awaiting final approval to become the fifth member in 2010. Within the first decade of its existence, tariffs had been eliminated on 80 percent of the goods traded between the original members. Brazil has proposed enlarging Mercosur into a South American Free Trade Area (SAFTA), which might eventually negotiate with NAFTA to form an Americas Free Trade Area (AFTA).

Free Trade Agreements Elsewhere

Around the world, groups of nations are banding together to form regional trade associations for their own benefit. Some examples include

- the ASEAN Free Trade Area (see Figure 5.4)
- the Asia-Pacific Economic Cooperation (many nations of the Pacific Rim, as well as the United States, Canada, and Mexico)
- the Economic Community of Central African States (many nations in equatorial Africa)
- the Gulf Cooperation Council (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and United Arab Emirates

Figure 5.4
The nations of the Association of Southeast Asian Nations (ASEAN).

To improve your grade, visit the MyBusinessLab website at www.pearsoned.ca/mybusinesslab. This online homework and tutorial system allows you to test your understanding and generates a personalized study plan just for you. It provides you with study and practice tools directly related to this chapter's content. MyBusinessLab puts you in control of your own learning! Test yourself on the material for this chapter at www.pearsoned.ca/mybusinesslab.

Summary of Learning Objectives

1. **Describe the rise of international business and identify the *major world marketplaces*.** More and more business firms are engaged in international business. The global economy is characterized by a rapid growth in the exchange of information and trade in services. The three major marketplaces for international business are *North America*, *Europe*, and *Asia–Pacific*.

2. **Explain how different forms of *competitive advantage, import–export balances, exchange rates,* and *foreign competition* determine how countries and businesses respond to the international environment.** With an *absolute advantage*, a country engages in international trade because it can produce a good or service more efficiently than any other nation. Countries usually trade because they enjoy

comparative advantages; they can produce some items more efficiently than they can produce other items. A country that exports more than it imports has a *favourable balance of trade*, while a country that imports more than it exports has an *unfavourable balance of trade*. If the exchange rate decreases, our exports become less expensive for other countries, so they will buy more of what we produce. The reverse happens if the value of the Canadian dollar increases. Changes in the exchange rate therefore have a strong impact on our international competitiveness.

3. **Discuss the factors involved in conducting business internationally and in selecting the *appropriate levels of international involvement and international organizational structure*.** In deciding whether to do business internationally, a firm must determine whether a market for its product exists abroad and whether the firm has the skills and knowledge to manage such a business. Firms must also assess the business climates in other nations and the preferred level of international involvement: (1) *exporter* or *importer,* (2) *international firm,* or (3) *multinational firm.* The choice will influence the organizational structure of its international operations, specifically, its use of *independent agents, licensing arrangements, branch offices, strategic alliances,* and *direct investment.*
4. **Describe some of the ways in which *social, cultural, economic, legal, and political differences* act as barriers to international trade.** *Social* and *cultural differences* that can serve as barriers to trade include language, social values, and traditional buying patterns. Differences in economic systems may force businesses to establish close relationships with foreign governments before they are permitted to do business abroad. *Quotas, tariffs, subsidies,* and *local-content laws* offer protection to local industries. Differences in *business-practice laws* can make standard business practices in one nation illegal in another.
5. **Explain how *free trade agreements* assist world trade.** Several *trade agreements* have attempted to eliminate restrictions on free trade internationally. The *General Agreement on Tariffs and Trade (GATT)* was instituted to eliminate tariffs and other trade barriers among participating nations. The *European Union (EU)* has eliminated virtually all trade barriers among the 27 member nations. The *North American Free Trade Agreement (NAFTA)* eliminates many of the barriers to free trade among the United States, Canada, and Mexico.

Questions and Exercises

Questions for Analysis

1. Explain how the economic system of a country affects foreign firms interested in doing business there.
2. Assume that you are the manager of a small firm seeking to enter the international arena. What information would you need about the market that you're thinking of entering?
3. Do you think that a firm operating internationally is better advised to adopt a single standard of ethical conduct or to adapt to local conditions? Under what conditions might each approach be preferable?
4. Explain how it is possible for a country to have a positive balance of trade and a negative balance of payments.
5. Is NAFTA good or bad for Canada? Give supporting reasons for your answer.
6. The EU includes most of the Western European countries, but some (such as Switzerland) have chosen not to join. Why might that be? What are the implications for countries that do not join?

Application Exercises

7. Interview the manager of a local firm that does at least some business internationally. Identify reasons why the company decided to "go international," as well as the level of the firm's involvement and the organizational structure it uses for its international operations.
8. Select a familiar product. Using library references, learn something about the culture of India and identify the problems that might arise in trying to market this product to India's citizens.
9. What attributes of your province or region (cultural, geographical, economic, etc.) would be of interest to a foreign firm thinking about locating there? Visit provincial government sites and find resources that are available for businesses to help them invest in your province. Identify a company that has recently invested in your province. What reasons did it give for its decision?
10. Visit the website of a major global company such as Coca-Cola and enter some of its international sites. Make sure to choose countries from different parts of the world. What are some of the differences that you see in the websites? Identify some of the similar themes and report your findings.

TEAM EXERCISES

Building Your Business Skills

Putting Yourself in Your Place

Goal

To encourage students to apply global business strategies to a small-business situation.

Situation

Some people might say that Yolanda Lang is a bit too confident. Others might say that she needs confidence—and more—to succeed in the business she's chosen. But one thing is certain: Lang is determined to grow INDE, her handbag design company, into a global enterprise. At only 28 years of age, she has time on her side—if she makes the right business moves now.

These days, Lang spends most of her time in Milan, Italy. Backed by $50 000 of her parents' personal savings, she is trying to compete with Gucci, Fendi, and other high-end handbag makers. Her target market is women willing to spend $400 on a purse. Ironically, Lang was forced to set up shop in Italy because of the snobbishness of these customers, who buy high-end bags only if they're European-made. "Strangely enough," she muses, "I need to be in Europe to sell in North America."

To succeed, she must first find ways to keep production costs down—a tough task for a woman in a male-dominated business culture. Her fluent Italian is an advantage, but she's often forced to turn down inappropriate dinner invitations. She also has to figure out how to get her 22-bag collection into stores worldwide. Retailers are showing her bags in Italy and Japan, but she's had little luck in the United States. "I intend to be a global company," says Lang. The question is how to succeed first as a small business.

Method

Step 1 Join together with three or four other students to discuss the steps that Lang has taken so far to break into the U.S. retail market. These steps include:

- buying a mailing list of 5000 shoppers from high-end department store Neiman Marcus and selling directly to these customers; and
- linking with a manufacturer's representative to sell her line in major U.S. cities while she herself concentrates on Europe.

Step 2 Based on what you learned in this chapter, suggest other strategies that might help Lang grow her business. Working with group members, consider whether the following options would help or hurt Lang's business. Explain why a strategy is likely to work or likely to fail.

- Lang could relocate to the United States and sell abroad through an independent agent.
- Lang could relocate to the United States and set up a branch office in Italy.
- Lang could find a partner in Italy and form a strategic alliance that would allow her to build her business on both continents.

Step 3 Working alone, create a written marketing plan for INDE. What steps would you recommend that Lang take to reach her goal of becoming a global company? Compare your written response with those of other group members.

Follow-Up Questions

1. What are the most promising steps that Lang can take to grow her business? What are the least promising?
2. Lang thinks that her trouble breaking into the U.S. retail market stems from the fact that her company is unknown. How would this circumstance affect the strategies suggested in Steps 1 and 2?
3. When Lang deals with Italian manufacturers, she is a young, attractive woman in a man's world. Often, she must convince men that her purpose is business and nothing else. How should Lang handle personal invitations that get in the way of business? How can she say no while still maintaining business relationships? Why is it often difficult for women to do business in male-dominated cultures?
4. The American consulate has given Lang little business help because her products are made in Italy. Do you think the consulate's treatment of an American businessperson is fair or unfair? Explain your answer.
5. Do you think Lang's relocation to Italy will pay off? Why or why not?
6. With Lang's goals of creating a global company, can INDE continue to be a one-person operation?

Exercising Your Ethics

Weighing the Tradeoffs

The Situation

There is a small bank that is headquartered in western Canada. The firm is privately owned and all the managers own stock in the bank. The company's senior managers (and majority owners) have decided to sell the bank to a major international banking company within the next two to three years. But, the bank needs to trim its expenses in order to make it more attractive to a potential buyer.

The Dilemma

Because the bank corporation has been a locally owned and operated enterprise it has maintained a full slate of operations within the local market. For instance, its corporate offices, many banking outlets, and all of its support activities are housed locally. The latter category includes a large call centre—a staff of 30 people who handle most customer calls involving questions about their accounts.

There has been a growing trend in banking to outsource call centres to foreign countries (e.g., India). Such markets have an abundance of English-speaking employees, excellent technology, and low wages. One senior manager has argued that they should outsource the call centre immediately. This would enable the firm to lower its costs. When confronted with the prospect of cutting 30 jobs, the manager acknowledges that it will be tough but reasons that any buyer will eventually do the same.

Another vocal senior manager is opposed to this idea. This person argues that because the bank corporation was started locally and has strong ties to the local community, it should maintain its current operations until the bank is sold. He argues, if a new owner decides to cut jobs, "it will be on their conscience, not ours."

Team Activity

Assemble a group of four students and assign each group member to one of the following roles:

- Senior manager (majority owner) of the bank
- Call centre employee
- Bank customer
- Bank corporation investor

Action Steps

1. Before discussing the situation with your group, and from the perspective of your assigned role, decide whether the call centre should be outsourced immediately. Write down the reasons for your position.
2. Before discussing the situation with your group, and from the perspective of your assigned role, decide what underlying ethical issues, if any, there are in this situation. Write down the issues.
3. Gather your group together and reveal, in turn, each member's comments on whether the call centre should be outsourced immediately. Next, reveal the ethical issues listed by each member.
4. Appoint someone to record the main points of agreement and disagreement within the group. How do you explain the results? What accounts for any disagreement?
5. From an ethical standpoint, what does your group conclude is the most appropriate action for the bank to take in this situation?
6. Develop a group response to the following question: Can your team identify other solutions that might help satisfy both senior managers' views?

BUSINESS CASE 5

Bombardier's Global Strategy

Montreal-based Bombardier Inc. is a diversified Canadian company that specializes in transportation solutions, from commercial and business jets to rail transportation equipment and services. Bombardier was founded in 1942 to manufacture a now-classic Canadian product—tracked vehicles for transportation across snow-covered terrain. Many of the Bombardier snowmobiles that were manufactured decades ago can still be seen in various areas of Canada. One such half-track sits on the windswept shores of Yathkyed Lake in Nunavut, hundreds of kilometres from any town. It is a mute reminder of the important role Bombardier played in opening up Canada's remote North.

Bombardier's headquarters are in Montreal, but its employees also work in the United States, Mexico, Europe, and the Middle East. More than 90 percent of company revenues come from outside Canada. Bombardier's strategy is to achieve accelerated growth in foreign markets, so it is continually refining its strategy to find new business opportunities in global markets.

Bombardier has historically been very successful in the commercial airplane market with its regional jets, which seat 50–90 passengers. But competition is fierce. In the mid-1990s, Bombardier held two-thirds of the market; then Brazilian rival Embraer entered the market and became a strong competitor. In 2007, Embraer finally overtook Bombardier to become the market leader in regional jets. Along the way, Bombardier had complained to the World Trade Organization that the Brazilian government was unfairly subsidizing Embraer by giving it large sums of money. But the Canadian government was also giving loans to Bombardier's customers to help them purchase Bombardier's planes.

Irrespective of how the competitive wars in the regional jet market turn out, an inescapable fact is that the regional jet market is declining because airline companies want jets with longer ranges, lower operating costs, and wider cabins. Bombardier planners reasoned that if they did not develop a new jet, they would gradually be forced out of the commercial airplane business. In 2008, at the famous Farnborough International Airshow near London, England, the company announced that it would go ahead with its new transcontinental CSeries commercial jet, a plane that will seat 110–130 passengers and which is designed for transcontinental flights. The plane will be more fuel efficient than current models and much quieter due to technological improvements in the new engines. Bombardier also announced that Deutsche Lufthansa AG had signed a letter of intent (LOI) for 30 of the planes,

A photo of Bombardier's new CSeries plane. After getting an initial order from Lufthansa Bombardier began the process to produce its long awaited CSeries plane.

(Photo courtesy of Bombardier Inc. and used under license.)

as well as an option for 30 more. As of November 2010, Bombardier had recorded firm orders for 90 CSeries aircraft and options from Lufthansa, Lease Corporation International Group, and Republic Airways. Qatar Airways has also expressed strong interest in the plane.

The introduction of the CSeries aircraft means Bombardier will be going head to head with global giants Airbus and Boeing. That strategy is risky, but if it succeeds, it will mean huge sales revenues and profits for Bombardier. It will also mean that Canada is one of only three countries in the world that produce intercontinental commercial jet aircraft. Market research suggests that the market for commercial jets like the CSeries will be 5000–6000 units over the next 20 years, and Bombardier hopes to get 50 percent of that market. The price of each plane is about \$59 million, so if the company achieves its market share goal, it could receive approximately \$190 *billion* in revenues over the next 20 years.

That sounds impressive, but there are three areas of risk associated with Bombardier's strategy. First, there may (or may not) be competing products from other airplane manufacturers. Here, Bombardier may get lucky. There is little evidence that Airbus or Boeing is planning to develop a plane that will compete directly with the CSeries aircraft. That's because there are large order backlogs (four to five years) for both the Airbus A320 and the Boeing 737, and the companies are fully engaged trying to fill those orders. However, Embraer may be developing a jet to compete with the CSeries aircraft.

Second, there is some risk associated with Bombardier's alleged "cozy" relationship with the Canadian government. In the past, the federal government has loaned money to Bombardier's customers so they can purchase the planes and trains the company manufactures. But will the government decide to stop handing out money? When he was Opposition leader, Stephen Harper said he wanted to end this type of support to private-sector companies, but as prime minister he has now reversed his position. Industry Minister Jim Prentice says that Canada wants to maintain its position as a global supplier in the airplane business. The Liberal industry critic, Scott Brison, says the Canadian government doesn't have an industrial strategy and is just making ad hoc decisions based on which way the political winds are blowing. But given the uncertain economic times, it appears that government loans are likely to continue.

Third, there is a risk that Boeing, Airbus, and Embraer will argue at the World Trade Organization that Canada is illegally subsidizing Bombardier. There is a long and contentious history between Bombardier and Embraer about government subsidies, and each company has claimed at various times in the past that the other is being illegally subsidized by its government. The outcome of any legal action by other airplane manufacturers against Bombardier is very uncertain.

Bombardier's strategy also includes shifting some of the risk of the CSeries aircraft to suppliers and to government. The overall development cost and capital investment of the CSeries aircraft program are projected to total $3.4 billion, of which Bombardier is providing $2 billion, including $700 million in capital expenditures and $1.3 billion in non-recurring costs. The remaining $1.4 billion in CSeries aircraft program costs will be split between the government of Canada, the province of Quebec, the government of the United Kingdom (where the wings of the CSeries aircraft will be built), and suppliers. The various governments will be paid a royalty on each plane that is sold. The project will create 3500 high-paying jobs in Quebec and about 800 jobs in the United Kingdom.

Questions for Discussion

1. How does Bombardier's development of the CSeries aircraft highlight the challenges and opportunities of globalization?
2. What role will governments play in the success and failure of the CSeries aircraft? Identify the role of subsidies and debate the concept of free trade and protectionism as it relates to this case.
3. How does this case help demonstrate the important role of the WTO in the international business arena?
4. Do you think that Bombardier will be successful in its move to capture a share of this new growing market? Explain your answer. If yes, what are some of the long-term obstacles?

SCANLIFE

Part 1: The Contemporary Business World

Goal of the Exercise

In Chapter 4, we discussed how the starting point for virtually every new business is a *business plan*. Business plans describe the business strategy for any new business and demonstrate how that strategy will be implemented. One benefit of a business plan is that in preparing it, would-be entrepreneurs must develop their idea on paper and firm up their thinking about how to launch their business before investing time and money in it. In this exercise, you'll get started on creating your own business plan.

Exercise Background: Part 1 of the Business Plan

The starting point for any business plan is coming up with a "great idea." This might be a business that you've already considered setting up. If you don't have ideas for a business already, look around. What are some businesses that you come into contact with on a regular basis? Restaurants, childcare services, and specialty stores are a few examples you might consider. You may also wish to create a business that is connected with a talent or interest you have, such as crafts, cooking, or car repair. It's important that you create a company from scratch rather than use a company that already exists. You'll learn more if you use your own ideas.

Once you have your business idea, your next step is to create an "identity" for your business. This includes determining a name for your business and an idea of what your business will do. It also includes identifying the type of ownership your business will take, topics we discussed in Chapter 4. The first part of the plan also briefly looks at who your ideal customers are, as well as how your business will stand out from the crowd. Part 1 of the plan also looks at how the business will interact with the community and demonstrate social responsibility, topics we discussed in Chapter 3. Finally, almost all business plans today include a perspective on the impact of global business, which we discussed in Chapter 5.

Your Assignment

PEARSON mybusinesslab

Step 1

To complete this assignment, you first need to download the Business Plan Student Template file from the book's MyBusinessLab. This is a Microsoft Word file you can use to complete your business plan. For this assignment, you will fill in Part 1 of the plan.

Step 2

Once you have the Business Plan Student Template file, you can begin to answer the following questions in Part 1: The Contemporary Business World.

1. What is the name of your business?

   Hint: When you think of the name of your business, make sure that it captures the spirit of the business you're creating.

2. What will your business do?

   Hint: Imagine that you are explaining your idea to a family member or a friend. Keep your description to 30 words or fewer.

3. What form of business ownership (sole proprietorship, partnership, or corporation) will your business take? Why did you choose this form?

   Hint: For more information on types of business ownership, refer to the discussion in Chapter 4.

4. Briefly describe your ideal customer. What are they like in terms of age, income level, and so on?

   Hint: You don't have to give too much detail in this part of the plan; you'll provide more details about customers and marketing in later parts of the plan.

5. Why will customers choose to buy from your business instead of your competition?

Hint: In this section, describe what will be unique about your business. For example, is the product special, or will you offer the product at a lower price?

6. All businesses have to deal with ethical issues. One way to address these issues is to create a code of ethics. List three core principles your business will follow.

   Hint: To help you consider the ethical issues that your business might face, refer to the discussion in Chapter 3.

7. A business shows social responsibility by respecting all of its stakeholders. What steps will you take to create a socially responsible business?

   Hint: Refer to the discussion of social responsibility in Chapter 3. What steps can you take to be a "good citizen" in the community? Consider also how you may need to be socially responsible toward your customers and, if applicable, investors, employees, and suppliers.

8. Will you sell your product in another country? If so, what countries and why? What challenges will you face?

   Hint: To help you consider issues of global business, refer to Chapter 5. Consider how you will expand internationally (e.g., independent agent, licensing). Do you expect global competition for your product? What advantages will foreign competitors have?

Note: Once you have answered the questions, save your Word document. You'll be answering additional questions in later chapters.

Whistleblowers at the RCMP

In 2007, four members of the RCMP went public with charges of fraud, misrepresentation, corruption, and nepotism against the leadership of the RCMP. The most senior member of the group was Fraser Macaulay, a career Mountie who had worked his way up through the ranks to become a senior human resources officer. While it is very unusual for Mounties to talk publicly about fraud, nepotism, and other criminal allegations, Macaulay said he had tried to alert his bosses to problems at the RCMP, but that he was lied to, shunned, and eventually pushed out of his job for his whistleblowing activity. Macaulay recognized that his whitle-blowing would damage the RCMP's reputation, but he came forward because he felt that doing so would eventually make the organization a better place.

Macaulay alleged that a small group of top managers used the RCMP pension fund to hire people who were related to senior members of the force, but that these people did not actually do any pension fund work. The four Mounties who testified said that when they reported this unacceptable activity to senior management, they were stonewalled and punished.

When the allegations first emerged, an internal investigation was launched by the RCMP, but then cancelled by Commissioner Zaccardelli. The Ottawa city police then conducted their own investigation, but no formal charges were laid. The auditor general eventually confirmed much of what Macaulay alleged, but by that time he had been transferred to the Department of National Defence (DND), which was known among the RCMP as the "penalty box." He is certain that he was transferred because he had been looking into pension fund irregularities. He also received a reduced performance bonus from his boss, the assistant commissioner, Barbara George. He was told that happened because he didn't support the commissioner.

During his last conversation with Commissioner Zaccardelli, Macaulay was told "it was time to go." This was an emotional conversation and Macaulay felt terrible. He told Zaccardelli that he had never lied to the commissioner before, so why did Zaccardelli think he would start now? Zaccardelli called the accusations Macaulay was making "baseless" and said that the pension fund was not at risk. Macaulay pointed out that he never said that the pension fund was at risk, but that funds were being used in an unacceptable manner and relatives of top managers were being paid for work that was not pension-fund related. Macaulay says that now it's about accountability for decisions that top managers made.

After the public investigation, Macaulay was reinstated in his former job. His boss, Barbara George, was suspended from her job for allegedly misleading the parliamentary committee that was looking into the allegations. Commissioner Zaccardelli is no longer with the RCMP.

Video Resource: "RCMP Whistleblower," *The National* (April 2, 2007).

Questions for Discussion

1. Define ethics. Explain how this idea is relevant for the situation at the RCMP.
2. Briefly describe the four criteria that can be used when trying to make an ethical decision. Which of these criteria is most relevant in the RCMP situation described above? Why?
3. What is meant by the term "whistleblowing"? Why do whistleblowers so often get into trouble when they point out questionable organizational practices?
4. Using the three-step model proposed in Chapter 3, analyze this situation. What conclusions do you reach?

Mompreneurs

The term "mompreneur" is often used to describe women who are trying to take care of kids and run a business at the same time. But just being a mom and being in business doesn't make a woman a mompreneur. Rather, a mompreneur is a woman who starts a business *because* she is inspired by being a mother. Consider two stories.

Darlene Martin

Darlene Martin has been a skating instructor for 17 years, and while the money is great, the hours are awful and Darlene has not been able to spend as much time with her daughter as she would like. So, she has started a home-based business called Bijouxbead, making and selling expensive jewellery (prices range from $100 to $1000 per piece). As a mompreneur, she wants to be able to set her own hours, and she is hoping that Bijouxbead will also make big money.

So far, Darlene has spent $75 000 on her business, and her products are carried in three high-end stores. She also sells her products at invitation-only parties. She wants her business to break even this year, and to do that she must sell $45 000 worth of product in the next five weeks. So, she's planning a big jewellery show, and she has invited over 200 people. She checks out craft shows to see how other jewellers display their products, then stops in at the boutiques that are selling her products. The boutiques take a cut of up to 50 percent of sales revenue, but at the craft show she will keep all the profit.

On sale day, family and friends help Darlene with the set-up. She has just six hours to sell $45 000 worth of beads. The first visitors are skaters and their parents. Most other visitors are family and friends (her dentist comes as well). At the end of the day, Darlene has sold just $8500 worth of products. She is far short of her goal, and she realizes that she has to do things differently in order to be successful. She wants to get more publicity for her products in magazines like *Lou Lou* and *Flair*, and she hopes to have her jewellery worn by celebrities.

Sandra Wilson

When Sandra Wilson lost her job at Canadian Airlines in the 1990s, she decided to start a home-based business that would give her flexibility and some extra income. Since she had experienced difficulty in getting non-slip soft shoes for her son Robert, she decided to make a soft shoe out of leather. She named her company Robeez. In 1994, she went to the Vancouver Gift Show trade exhibition with 20 pairs of her new footwear. They were an instant hit. Sales in the first year of her business were $20 000, and doubled every year thereafter. By 2002, sales reached $2 million. A lot of celebrity moms now use her products. She says her business was built largely on word of mouth.

Robeez is the world's leading manufacturer of soft-soled leather footwear. It employs 450 people and sells a diverse product line in 6500 stores located in North America, Europe, Australia, and parts of Asia. In 2006, Sandra sold out to Stride Rite Corporation for $30 million. She can now enjoy the fruits of her labour. She is still with Stride Rite as a consultant, and she also meets with various mompreneurs once a month to help them.

Video Resource: "Mompreneurs," *Marketplace* (February 16, 2008).

Questions for Discussion

1. What are the advantages and disadvantages of being a mompreneur?
2. Why do you think that so much publicity is currently being given to mompreneurs? Why is so little publicity given to "dadpreneurs"?
3. Consider the following statement: *"Mompreneurs say they want to spend more time with their children, but many hours of hard work are required each day in order to make a new business successful. This means that mompreneurs will not actually be able to spend any more time with their children."* Do you agree or disagree with the statement? Explain your reasoning.