

## UNIT 01

### GLOBAL MARKETING

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#### LESSON NO. 1: GLOBAL MARKETING: INTRODUCTION, SCOPE, BENEFITS, OBSTACLES AND PROTECTIONISM

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#### STRUCTURE

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- 1.2 Definitions of international and global marketing management
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#### 1.1 FROM INTERNATIONAL MARKETING TO GLOBAL MARKETING

The term global marketing has only been used for some ten years and began to assume widespread use in 1983 with the seminal article by Ted Levitt. Prior to that, international marketing or multinational marketing was the term used most often to describe international marketing activities. However, global marketing is not just a new term for an old phenomenon; there are real differences between international marketing and global marketing. In many ways global marketing is a subcategory

of international marketing with special importance in our present world. It has captured the attention of marketing academics and business practitioners alike and, as indicated by the title of our book, we attach considerable importance to this new type of international marketing. However, before we explain global marketing in greater detail, let us first look at the historical development of international marketing as a field and gain a better understanding of the phases through which it has passed.

### **1.1.1 Domestic marketing**

Marketing that is aimed at a single market, the firm's domestic market, is referred to as domestic marketing. In domestic marketing, the firm faces only one set of competitive, economic, and market issues and, essentially, must deal with only one set of customers, although the company may serve several segments in this one market. The marketing concepts that apply to domestic or single-country marketing are those we expect our readers are well versed in and will not be covered further in this book.

### **1.1.2 Export marketing**

The field of export marketing covers all those marketing activities involved when a firm markets its products outside its main (domestic) base of operation and when products are physically shipped from one market or country to another. Although the domestic marketing operation remains of primary importance, the major challenges of export marketing are the selection of appropriate markets or countries through marketing research, the determination of appropriate product modifications to meet the demand requirements of export markets, and the development of

export channels through which the company can market its products abroad. In this phase, the firm may concentrate mostly on the product modifications and run the export operations as a welcome and profitable by-product of its domestic strategy. Because the movement of goods across national borders is a major part of an exporting strategy, the required skills include knowledge of shipping and export documentation. Although export marketing probably represents the most traditional and least involved form of international marketing, it remains an important aspect for many firms. As a result, we have devoted chapter 18 exclusively to this topic.

### **1.1.3 International marketing**

When practising international marketing, a company goes beyond exporting and becomes much more directly involved in the local marketing environment within a given country or market. The international marketer is likely to have its own sales subsidiaries and will participate in and develop entire marketing strategies for foreign markets. At this point, the necessary adaptation to the firm's domestic marketing strategies becomes a main concern. Companies going international now will have to find out how they must adjust an entire marketing strategy, including how they sell, advertise, and distribute, in order to fit new market demands.

An important challenge for the international marketing phase of a firm becomes the need to understand the different environments the company needs to operate in. understanding different cultural, economic, and political environments becomes necessary for success. This is generally described as part of a company's internationalization process, whereby a firm becomes more experienced to operate in various foreign

markets. It is typical to find a considerable emphasis on the environmental component at this stage. Typically, much of the field of international marketing has been devoted to making the environment understandable and to assist managers in navigating through the differences. The development of the cultural/environmental approach to international marketing is an expression of this particular phase.

#### **1.1.4 Multinational marketing**

The focus on multinational marketing came as a result of the development of the multinational corporation. These companies are characterized by extensive development of assets abroad and operate in a number of foreign countries or markets as if they were local companies. Such development led to the creation of many domestic strategies, thus the name multidomestic strategy whereby a multinational firm competes with many strategies, each one tailored to a particular local market. The major challenge of the multinational marketer is to find the best possible adaptation of a complete marketing strategy to an individual country. This approach to international marketing leads to a maximum amount of localization and to a large variety of marketing strategies. The attempt of multinational corporations to appear 'local' wherever they compete, often results in the duplication of some key resources. The major benefits are the ability to completely tailor a marketing strategy to the local requirements.

#### **1.1.5 Multiregional marketing**

Given the diseconomies of scale of individualized marketing strategies, each tailored to a specific local environment, companies have begun to emphasize strategies for larger regions. These regional strategies

encompass a number of markets, such as Euro-strategies for Western Europe, and have come about as a result of regional economic and political integration. Such integration is apparent in North America, where the United States and Canada have signed a far-reaching trade pact and the inclusion of Mexico is discussed, or in the Pacific Rim, where a number of countries have made great progress in their economic development. Nowhere has the development been faster than in Europe through the impetus of Europe 1992, a series of political and economic measures aimed at total integration of the European Community. Companies considering regional strategies look to tie together operations in one region, rather than around the globe, the aim being increased efficiency. Many firms are presently working on such solutions, moving from many multidomestic strategies in Europe toward Pan-European strategies.

#### **1.1.6 Global Marketing**

Over the years, academics and international companies alike have become aware that opportunities for economies of scale and enhanced competitiveness are greater if they can manage to integrate and create marketing strategies on a global scale. A global marketing strategy involves the creation of a single strategy for a product, service, or company, for the entire global market, that encompasses many markets or countries simultaneously and is aimed at leveraging the commonalities across many markets. Rather than tailor a strategy perfectly to any individual market, the company aims at settling on one general strategy that will guide itself through the world market. The management challenge is to design marketing strategies that work well across many markets. It is driven not only by the fact that markets appear increasingly

similar in environmental and customer requirements, but, even more so, by the fact that large investments in technology, logistics, or other key functions force the companies to expand their market coverage.

Thus global marketing is the last stage in the development of the field of international marketing. While global marketers face their own unique challenges that stem from finding marketing strategies that fit many countries, the skills and concepts of the earlier stages are very important and continue to be needed. In fact, companies that take a global marketing approach will be good exporters because they will include some exporting in their strategies. Such firms will also have to be good at international marketing because designing one global strategy requires a sound understanding of the cultural, economic, and political environment of many countries. Furthermore, few global marketing strategies can exist without some local tailoring, which the hallmark of multinational is marketing. As a result, global marketing is but the last of a series of skills, all included under the broad concept of international marketing.

## **1.2 DEFINITIONS OF INTERNATIONAL AND GLOBAL MARKETING MANAGEMENT**

Although much conceptual work has been accomplished in global marketing, the use of the word global remained unclear among many marketing academics and executives. For many, global is just a new term or replacement term for international. Since, it does mean something new and different to us, we plan to make use of the term in a judicious way. For us, global marketing is a subset, albeit different and distinct, of international marketing. In general, we still use the term international more often to describe factors that relate to the entire field and to use

global mainly when it refers to the specific new phenomena in international marketing. The term global was selected because it indicates clearly that a significant portion of this text will deal specifically with new concepts and strategies without neglecting the standard concepts dealing with export, international, or multinational marketing.

Having examined the scope of international and global marketing, we are now able to define it more accurately. Any definition has to be built, however, on basic definitions of marketing and marketing management, with an added explanation of the international dimension. We understand marketing as the performance of business activities directing the flow of products and services from producer to consumer. A successful performance of the marketing function by a firm is contingent upon the adoption of the marketing concept, consisting of (a) a market focus, (b) a customer orientation, (c) an integrated marketing organization, and (d) customer satisfaction. Marketing management is the execution of a company's marketing operation. Management responsibilities consist of planning, organizing, and controlling the marketing program of the firm. To accomplish this job, marketing management is assigned decision-making authority over product strategy, communication strategy, distribution strategy, and pricing strategy. The combination of these four aspects of marketing is referred to as the marketing mix.

For international and global marketing management, the basic goals of marketing and the responsibilities described above remain unchanged. What is different is the execution of these activities in more than one country. Consequently, we define international marketing management as the performance of marketing activities across two or more countries.

### **1.3 MANAGEMENT ORIENTATION**

The form and substance of a company's response to global market opportunities depend greatly on management's assumptions or beliefs—both conscious and unconscious—about the nature of the world. The worldview of a company's personnel can be described as ethnocentric, polycentric, regiocentric, and geocentric. Management at a company with a prevailing ethnocentric orientation may consciously make a decision to move in the direction of geocentricism. The orientations are collectively known as the EPRG framework.

#### **1.3.1 Ethnocentric**

A person who assumes his or her home country is superior compared to the rest of the world is said to have an ethnocentric orientation. The ethnocentric orientation means company personnel see only similarities in markets and assume the products and practices that succeed in the home country will, due to their demonstrated superiority, be successful anywhere. At some companies, the ethnocentric orientation means that opportunities outside the home country are ignored. Such companies are sometimes called domestic companies. Ethnocentric companies that do conduct business outside the home country can be described as international companies; they adhere to the notion that the products that succeed in the home country are superior and, therefore, can be sold everywhere without adaptation.

In the ethnocentric, international company, foreign operations are viewed as being secondary or subordinate to domestic ones. An ethnocentric company operates under the assumption that “tried and true” headquarters knowledge and organizational capabilities can be applied in

other parts of the world. Although this can some-times work to a company's advantage, valuable managerial knowledge and experience in local markets may go unnoticed. For a manufacturing firm, ethnocentrism means foreign markets are viewed as a means of disposing of surplus domestic production. Plans for overseas markets are developed, utilizing policies and procedures identical to those employed at home. No systematic marketing research is conducted outside the home country, and no major modifications are made to products. Even if consumer needs or wants in international markets differ from those in the home country, those differences are ignored at headquarters.

Nissan's ethnocentric orientation was quite apparent during its first few years of exporting cars and trucks to the United States. Designed for mild Japanese winters, the vehicles were difficult to start in many parts of the United States during the cold winter months. In northern Japan, many car owners would put blankets over the hoods of their cars. Tokyo's assumption was that Americans would do the same thing. Until the 1980s, Eli Lilly and Company operated as an ethnocentric company in which activity outside the United States was tightly controlled by headquarters and focused on selling products originally developed for the U.S. market.

Fifty years ago, most business enterprises and especially those located in a large country like the United States could operate quite successfully with an ethnocentric orientation. Today, however, ethnocentrism is one of the biggest internal threats a company faces.

### **1.3.2 Polycentric**

The polycentric orientation is the opposite of ethnocentrism. The term polycentric describes management's often unconscious belief or assumption that each country in which a company does business is unique. This assumption lays the groundwork for each subsidiary to develop its own unique business and marketing strategies in order to succeed; the term multinational company is often used to describe such a structure. Until recently, Citicorp's financial services around the world operated on a polycentric basis. James Bailey, a Citicorp executive, offered this description of the company: "We were like a medieval state. There was the king and his court and they were in charge, right? No. It was the land barons who were in charge. The king and his court might declare this or that, but the land barons went and did their thing." Realizing that the financial services industry is globalizing, CEO John Reed is attempting to achieve a higher degree of integration between Citicorp's operating units. Like Jack Welch at GE, Reed is moving to instill a geocentric orientation throughout his company.

### **1.3.3 Regiocentric and Geocentric orientations**

In a company with a regiocentric orientation, management views regions as unique and seeks to develop an integrated regional strategy. For example, a U.S. company that focuses on the countries included in the North American Free Trade Agreement (NAFTA) the United States, Canada, and Mexico-has a regiocentric orientation. Similarly, a European company that focuses its attention on Europe is regiocentric. A company with a geocentric orientation views the entire world as a potential market and strives to develop integrated world market strategies. A company whose management has a regiocentric or

geocentric orientation is sometimes known as a global or transnational company.

The geocentric orientation represents a synthesis of ethnocentrism and polycentrism; it is a “worldview” that sees similarities and differences in markets and countries, and seeks to create a global strategy that is fully responsive to local needs and wants. A regiocentric manager might be said to have a worldview on a regional scale; the world outside the region of interest will be viewed with an ethnocentric or a polycentric orientation, or a combination of the two. Jack Welch’s quote at the beginning of this chapter that “globalization must be taken for granted” implies that at least some company managers must have a geocentric orientation. However, recent re-search suggests that many companies are seeking to strengthen their regional competitiveness rather than moving directly to develop global responses to changes in the competitive environment.

The ethnocentric company is centralized in its marketing management, the polycentric company is decentralized, and the regiocentric and geocentric companies are integrated on a regional and global scale, respectively. A crucial difference between the orientations is the underlying assumption for each. The ethnocentric orientation is based on a belief in home country superiority. The underlying assumption of the polycentric approach is that there are so many differences in cultural, economic, and marketing conditions in the world that it is impossible and futile to attempt to transfer experience across national boundaries.

#### **1.4 BENEFITS OF INTERNATIONAL MARKETING**

The importance of international marketing is neither understood nor appreciated by consumers though they are carrying out international marketing daily. Government officials, especially bureaucrats, seem to always point a negative aspect of international business. Many of their charges on international marketing are imaginary than real. Hence, it is essential that the benefits of international marketing be explicitly discussed. These benefits are

- (i) Endurance
- (ii) Progress of overseas markets
- (iii) Sales promotion
- (iv) Diversification
- (v) Inflation and wholesale price index
- (vi) Employment and placement VB.
- (vii) Standard of living style
- (viii) Understanding marketing process.

**(i) Endurance**

Every country is not as fortunate as America in terms of infrastructure, size, resources and opportunities. Hence, they must trade with other countries to survive. Similarly, every country is not as fortunate as India, which has abundant natural resources and a treasure of bio-diversity that it can survive within its resources even if there is a resource crunch. Even then it has to carry out trading with other countries to get oil and armaments for its own survival. Hong Kong cannot survive without food and water from China. The countries of Europe have had similar experience since most European nations are relatively small in size. Without a foreign market, European firms would not have sufficient economies of scale to allow them to be competitive with US firms.

Switzerland lacks natural resources, forcing it to depend on trade and adopt the geocentric perspective. Similarly, Japanese firms are dependent on raw material from other countries but they have better technical know-how as a result of which they are the world leaders in electronics and software industry.

**(ii) Progress of overseas markets**

Developing countries, in spite of a poor economy with serious marketing problems, are excellent markets. The US has found that India is the biggest market in the world for consumer and engineering products. According to a report prepared by the US Trade Representative US Congress, Latin America and Asia are experiencing the worst economic recession though they have potential in the world market.

The Conference Board's study of some 1500 companies found that US manufacturers, with factories or sales subsidiaries overseas, outperformed their counterparts during 1980s in terms of growth in 19 out of 20 major industrial groups and higher earnings in 17 out of 20 groups. American market cannot ignore the vast potential of the international market. The world market is four times larger than US market. In the case of Amway Corporation, a privately held US manufacturer of cosmetics, soaps, and vitamins, Japan represents a larger market than the US.

**(iii) Sales promotion**

Foreign markets constitute a large share of total business of many firms that have cultivated markets abroad. Many large US companies have done very well because of their overseas customers. IBM and Compaq

sell more computers abroad than at home. The case of Coca-Cola clearly emphasises the importance of overseas markets. Coca Cola is coming up with milk-based products as majority of Indians and Asians do not relish the taste of aerated drinks which are supposed to have caffeine which is addictive.

**(iv) Diversification**

In the international market, cyclical factors such as recession and seasonal factors such as climate affect the demand for most products. Due to these variables, there are sales fluctuations, which frequently be substantial enough to cause lay off of personnel. One way of diversifying a company's risk is to consider foreign markets as a solution for variable demands. For example, cold weather may depress demand for cold drink consumption. All countries do not enter the winter season at the same time and some of the countries are warm round the year.

**(v) Inflation and wholesale price index**

The best way to control inflation is to earn foreign exchange through exports. Imports can also be highly beneficial to a country because they constitute reserve capacity of the local economy. Without imports, there is no incentive for domestic firms to moderate their prices. The lack of imported product alternatives forces consumers to pay more, resulting in inflation and excessive profits for local firms. This development usually acts as a prelude to workers to demand higher wages, further exacerbating the problem of inflation. Import quotas imposed on Japanese automobiles in 1980s saved 46,200 US production jobs but at a cost of \$ 160 thousand per job per year. This huge cost was a result of the addition of \$ 400 to the prices of US cars and \$1000 to the prices of

Japanese imports. This windfall for Detroit resulted in record high profits for US automobiles.

**(vi) Employment and placements**

Tariff barriers and trade restrictions in certain countries had contributed significantly to the great depression of 1930 and have the potential to cause widespread unemployment again. Unrestricted trade, on the other hand, improves the world's GNP and enhances employment generally for all nations. With the liberalisation of economic policy, 1991, India has gained tremendously with the inflow of foreign direct investment as a result of which employment in the country has tremendously improved.

**(vii) Standard of living/style**

Trade affords countries and their citizen's a higher standard of living than is otherwise possible. Without trade, product shortages force people to pay more for less. Products taken for granted such as coffee and bananas may become unavailable overnight. Life in most of the countries will be more difficult were it not for the many strategic metals that must be imported. Trade also makes it easier for industries to specialise and gain access to raw materials, while at the same time fostering competition and efficiency.

**(viii) Marketing process**

International marketing should be considered a special case of domestic marketing. It has earlier been explained that there is very little difference between domestic and international marketing. Only thing is that the word multinational has been added in the international marketing process. Otherwise, the marketing mix is the same for both. With

improvements in information technology, the international markets have become easily accessible and the whole world has become a small global village.

## **1.5 SCOPE OF GLOBAL MARKETING**

The foundation for a successful international marketing programme is a sound understanding of the marketing discipline. Marketing is the process of focusing the resources and objectives of an organisation on environmental needs and opportunities. The first and the most fundamental fact about marketing is that it is a universal discipline. The marketing discipline is equally applicable from China to India, United States to Japan and Australia to Zanzibar. Marketing is a set of concepts, tools, theories, practices and procedures and experience.

Although the marketing discipline is universal markets and customers are quite differentiate. This means that marketing practices must vary from country to country. Each person is unique and each country is unique. This reality of differences means that we cannot always directly apply experience from one country to another. If the customers, competitors, channels of distribution and available media are different, it may be necessary to change our marketing plan.

The scope of international marketing is to have a borderless world like the multinational companies- Coca Cola, Pepsi, McDonald, Gillette and so on. Their products and body marketing mix elements are both international and local in nature. A central issue in international marketing is how to tailor the international marketing concept to fit a particular product or business

## **1.6 OBSTACLES TO INTERNATIONALIZATION**

Companies attempting to establish and maintain an international presence are likely to encounter obstacles to internationalization both from within the company and from outside. Such obstacles can be financial in nature: The Company might not have the finances to expand beyond national frontiers. Others are psychological: Fear of an unknown international environment or of local business practices may keep the company from international engagement. These two types of barriers, however, could equally affect the company's local expansion efforts:

Companies may not have the finances to expand beyond a small regional market, or they fear going into new markets where consumers may not be familiar with their products and hence may not respond to their marketing strategy.

Some obstacles are encountered only by firms in their process of internationalization-obstacles that they are unlikely to encounter in other expansion efforts. They are the self-reference criterion, government barriers, and international competition.

### **1.6.1 Self-Reference Criterion**

Of crucial importance to international operations is the ability of the firm, and especially of its marketing program, to adapt to the local business environment in order to serve the needs of local consumers and to address the requirements of local government, industry, and channels of distribution. An impediment to adaptation is the self-reference criterion, defined as individuals' conscious and unconscious reference to their own national culture, to home-country norms, values, as well as to

their knowledge and experience, in the process of making decisions in the host country.

“Cultural Influences on International Marketing’ illustrates a number of situations in which self reference can lead to a breakdown in communication between parties from different cultures. For example, an employee of a large multinational company from the United States conducting business in Japan who has been trained by career counsellors in the U.S. that looking one’s counterpart in the eyes conveys directness and honesty is likely to be perceived as abrasive and challenging. Similarly, if the same employee proceeds directly to transacting the business deal in Latin America or Southern Europe (instead of first interacting in a social setting in order to establish rapport), he/she would be perceived as arrogant, interested only in the bottom line, rather than in a long-term working relationship.

A first step to minimizing the impact of the self-reference criterion is selecting appropriate personnel for international assignments. Such employees are sensitive to others and have experience working in different environments. Second, it would be important to train expatriates to focus on and be sensitive to the local culture, rather than limit their personal interactions to own country nationals or to expatriates from countries with cultures that are similar to one’s own. In fact, an organization-level general orientation that instils and demonstrates sensitivity to international environments and openly spurns value judgments and national stereotyping should be instilled at the firm level.

### **1.6.2 Government Barriers**

Local governments, especially governments in developing countries, keep a tight control over international market entrants, permitting or denying access to international firms based on criteria that are deemed important for national industry and/or security considerations at a particular point in time. Among formal methods used by national governments to restrict or impede entrance of international firms in the local market are tariffs and barriers such as import quotas, or policies of restricting import license awards, foreign exchange restrictions, and local content requirements, among others. Member countries of the World Trade Organization, signatories of the General Agreement on Tariffs and Trade, or members of regional economic integration agreements such as NAFTA and the European Union find it very difficult to use tariffs as a means of restricting international expansion of companies in the countries' territories. Increasingly, they are using non-tariff barriers, such as cumbersome procedures for import paperwork processing, delays in granting licenses, or preference given to local service providers and product manufacturing for all contracting work.

### **1.6.3 International Competition**

Although competition can be a driver of internationalization, competitors can also erect barriers to new entrants in a market. They often do so by employing strategies such as blocking channels of distribution, binding retailers into exclusive agreements, slashing prices temporarily to prevent product adoption, or engaging in an advertising blitz that could hurt a company's initial sales in a market and cause it to retrench. With heavy competition from new and lesser, brands in Asia, Central and Eastern Europe, and North Africa and the Middle East, Marlboro has created a strong defensive strategy for its cigarettes: It slashed prices by as much as a third, and advertised heavily anywhere it was

legal, especially on billboards in the centre of different capital cities and towns in the provinces.

As an example, sales of Marlboro in South-Eastern Europe were hurt by various local competitors and, in particular, by a successful international brand, Assos from Greece. Assos was rapidly gaining a leading position in a number of markets in the region when Marlboro went on the offensive, limiting Assos's market share to a point where the company was forced to abandon many of its markets. Marlboro effectively put in question the international expansion of many new European and Asian brands, as well as new brands from the United States (it decimated, for instance, sales of new brands of American cigarettes created specifically for the Russian market).

## **1.7 PROTECTIONISM**

Protection of local markets from foreign companies constitutes an important mandate for national and local governments alike. Many political careers have been built and defended on market protection rhetoric. "We will not sell our country" has been a slogan of countries resisting foreign economic and political dominance in the past. Today, it is a slogan used against multinationals that are rapidly expanding, taking over emerging markets, and bringing with them a consumption culture perceived to go against local culture and traditions. These multinationals also are seen as eliminating small local producers and service providers, bankrupting formerly productive factories, and replacing abundant local labour with more efficient advanced technology, increasing local unemployment and disrupting political stability.

All actions by national and local governments aimed at protecting local markets from foreign competitor.

Some of the arguments for **protectionism** are indeed valid. The infant industry argument is aimed at protecting an emerging national industry from powerful international competitors, which could easily squeeze out a newcomer to the business merely with its brand name resonance and with pricing strategies that a new industry could not possibly sustain in the long term. The argument stressing the industrialization of developing countries also is valid for similar reasons. The national defence argument is regarded as justified in international trade forums and is widely accepted as a reasonable argument for protectionism.

There is also the argument for environmental protection and/or protection of natural resources and the need for maintaining standards to the benefit of all humankind; this line of arguments is also soundly reasoned. The problem with this defence of protectionism arises when the standards imposed are, in fact, simple protectionist arms that require foreign competition to go through excessive and unwarranted bureaucratic exercise, or when these requirements are imposed on international firms but not on local firms-or not to the same degree.

In general, it is believed that consumers pay the final price for the cost of strategies of protectionism. Arguments for protectionism ignore the economic advantages of free trade and the importance of adopting open market mechanisms for optimal long-term market performance. In fact, history has amply demonstrated that a government's right and authority to pick and choose winners among industries and firms could be corrupted and distorted by local influential firms, power-seeking politicians, and favour-seeking lobby groups. Politicians, particularly in the United States, favour trade barriers and vote for imposing them because such strategies appeal directly to the concerns of their constituencies regarding the possibility of losing their jobs. What these politicians do not consider is the subsequent retaliatory action of other

governments which will negatively affect the domestic economy, the higher consumer prices attributed to the tax imposed to subsidize the domestic industry, and higher prices attributed to the reduction in competition in the local market.

## **1.8 ARGUMENTS FOR PROTECTIONISM**

The following arguments most often advanced to justify the imposition of tariff and nontariff trade barriers or protectionism.

### **1.8.1 Protection of Markets with Excess Productive Capacity**

Markets that have excess productive capacity have committed significant resources to the production facilities. In the case of Central and Eastern Europe, for example, the standard for production during the central planning years under communism was represented by mammoth factories employing hundreds of thousands of workers, each charged with minuscule repetitive tasks under an elaborate division-of-labour program. The goal of such programs was both to ensure productivity and to assure a place of work to every individual, qualified or not. Such factories had, in addition to the workers, structures with directors and Para directors, all served by several secretaries whose specializations varied from typing to answering telephones, to making coffee, to taking care of the director's family's personal shopping.

After the fall of communism, the new factory owners (often foreign) quickly realized that they needed only a fraction of the workers for optimal production and proceeded to fire the rest, leading to regional unrest. Currently, remaining factories are protected from foreign buyouts and are managed locally. Often they are state-owned enterprises. National governments protect them from foreign investors. They also protect these enterprises by limiting the entrance of competing products, such as superior steel and higher-performance tractors, by

arguing that such restrictions are instituted to protect a market with excess productive capacity.

### **1.8.2 Employment Protection and Protection of Markets with Excess Labour**

Under the scenario presented in section (a) the markets of Central and Eastern Europe-especially those in the countries of the Former Soviet Union are now experiencing high levels of excess labour and underemployment, all of which lead to flares of social unrest. As a result, local politicians actively lobby against granting import licenses for products competing with locally produced goods that are established in the market. Arguments invoking employment protection are used to ensure that competing multinationals do not import products manufactured elsewhere that might drive local manufacturers out of business and create local unemployment. The argument also is used against multinationals that might purchase local plants and fire most of the redundant workers to create acceptable levels of profitability. A related argument, invoking the protection of markets with excess labour, is also used to prevent more efficient multinationals from taking over local businesses and streamlining local operations.

### **1.8.3 Infant Industry Arguments and Arguments Related to the Industrialization of Developing Countries**

The infant industry arguments and arguments related to the industrialization of developing countries are considered valid: Developing countries need to protect their markets from competitors from countries with an established industrial base. Foreign competitors would be able to offer higher quality products at lower costs and would undoubtedly undercut local

manufacturers attempting to break into the market. Foreign competition would present the greatest challenge to local industries in their infancy.

#### **1.8.4 Natural Resources Conservation and Protection of the Environment**

The resource conservation argument is considered to be valid in international trade organization forums, especially in light of worldwide shortages of raw materials. Similarly, a balance sometimes has to be struck between free trade and legitimate arguments such as those entering on environmental protection, but governments still need to find a way of agreeing when curbs on trade can be an acceptable way to pursue a greater good.

The problem with these two arguments arises when they are used arbitrarily, with a clear bias against international firms, either imposing the standards only on foreign firms or requiring them to meet higher standards than local firms.

#### **1.8.5 Protection of Consumers**

Protection of consumers is an often-echoed argument that ultimately favors local, over international, business. Standards that are rigidly applied against foreign businesses, quality controls that necessitate layers of costly bureaucracy, and arbitrary product origin requirements, among others, are invoked as a basis for this argument. Politicians in the European Union have argued that they were protecting consumers by imposing standards on imported beef: Listening to the unified voices of their constituencies and attempting to protect the local beef industry against the high-quality, cheap, corn-fed U.S. beef, the European Union banned its import, invoking the use of growth hormones in the United States. With cattle in many countries of the European Union plagued by mad-cow and/or hoof-and mouth disease, the primary option

available to European consumers is expensive Argentine beef. This is an unequivocal demonstration that consumer-protection gone-too-far is not necessarily in the interest of the consumer.

#### **1.8.6 National Defense Interests**

The national defence argument is also perceived as valid, and it is often invoked in international trade forums. Publications that attempt to destabilize the government, armament, and other similar products are often under an import ban. More recently, the national defence argument has been advocated by developing countries and/or by countries that attempt to control and restrict access of their population to Western influence. Such nations may perceive a threat in the unrestricted imports of information-based services through electronic channels; countries such as China, Singapore, and Saudi Arabia impose restrictions on and even ban ownership of satellite dishes, whereas other nations are attempting to control citizen access on the World Wide Web (WWW).

### **1.9 TOOLS OF GOVERNMENT PROTECTIONISM**

#### **1.9.1 Tariff and non-tariff barriers**

##### **(a) Tariffs**

Tariffs are any type of tax imposed on goods entering a particular country. Tariffs are imposed to

- Discourage imports of particular goods, such as consumer goods, which often are not considered essential in developing countries

- Penalize countries that are not politically aligned with the importing country, or countries that are imposing tariffs or non tariff restrictions on goods from the importing country
- Generate revenues for the importing country

In general, tariffs that are assessed by the United States are relatively low, less than 10 percent. Some developing countries set tariffs higher than 100 percent for products that compete with an infant industry. For example, countries attempting to develop their own automobile industry are likely to impose very high tariffs to all automobiles imported into the country.

#### **(b) Nontariff Barriers**

Nontariff barriers include all measures, other than traditional tariffs, that are used to distort international trade flows; they raise prices of both imports and import-competing goods and favor domestic over foreign supply sources by causing importers to charge higher prices and to restrict import volumes.

In the past twenty years, in an attempt to keep markets closed without going against the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization, governments have created new nontariff barriers, such as orderly market arrangements, voluntary import expansion, and voluntary export restraints, which limit market access for foreign businesses. Many countries have erected these nontariff barriers, but most are imposed by the United States, members of the European Union, and by other industrialized countries on exporting countries such as Japan, South Korea, and developing countries. Other, more traditional, nontariff barriers include quotas, currency controls, and standards-such as environmental, quality, performance, and health standards, which are expensive to provide and to evaluate. Boycotts, embargoes,

and sanctions are the most severe barriers to trade that are imposed usually to punish a company or a national government.

Nontariff barriers are constantly evolving: They are in a continuous process of refinement, aimed at avoiding scrutiny from the World Trade Organization or other trade organizations. Although the most frequently encountered nontariff barriers are described here, it is important to note that new variants of the barriers described are continuously emerging in the global trade arena.

### **1.9.2 Import Quotas and Orderly Market Arrangements**

Import quotas specify a maximum quantity (unit limit) or a value (usually specified in the national currency) of a product that may be imported during a specified period. Quotas are administered either on a global first-come, first-served basis or on a bilateral basis to restrict shipments from a specific supply source such as the Multifiber Arrangement.

The Multifiber Arrangement was initiated as a temporary measure in 1974 (but lasted 21 years). Its articulated goals were to expand trade, to reduce barriers to trade, and to initiate a progressive liberalization of world trade in textile products, while ensuring the orderly and equitable development of this trade and avoiding disruptive effects in individual markets and on individual lines of production in both importing and exporting countries. In reality, this was an orderly market arrangement, an intricate process of establishing quotas in the textile and apparel industries, initiated by the United States and Europe, whose textile operations were moving to Asia to take advantage of cheaper labor. The Multifiber Arrangement was nullified under the Uruguay Round of the General Agreement on Tariffs and Trade in 1995 but has since been replaced by very similar nontariff barriers.

### **1.9.3 Nonautomatic Import Licenses**

Nonautomatic import licenses are issued on a discretionary basis and are used to restrict imports of a given product. Licensing requirements can restrict the volume of imports, as do quotas, or they can be used to impose on the exporter or importer specific conditions that will result in fewer imports. It should be mentioned that the World Trade Organization presently requires member countries to ensure transparency of the import-license granting process; they are asked to do so by publicizing information concerning administration of restrictions, by listing information regarding the licenses granted over the most recent period, and, where practicable, by providing additional import statistics of the products concerned.

### **1.9.4 Automatic Import Licenses**

Automatic import licenses are granted freely to importing companies. Automatic licenses are used by the importing country's government for the purpose of import surveillance: The licenses have the potential to discourage import surges, they place additional administrative and financial burdens on the importer, and they may also raise costs by delaying product shipments.

### **1.9.5 Voluntary Import Expansion (VIE)**

Under a voluntary import expansion (VIE), a country agrees to open its markets to imports. Voluntary import expansions increase foreign access to a domestic market, while increasing competition and reducing prices. Voluntary import expansions are not voluntary at all: A country agrees to import products as a result of pressure from another country. An example of voluntary import expansion is Japan's decision to avert U.S.-imposed trade sanctions by importing U.S. semi-conductors.

### **1.9.6 Voluntary Export Restraints (VER)**

Voluntary export restraints (VERs) are self-imposed quotas and constitute a barrier to trade often used in the 1980s to protect local industries. The United States, for example, used voluntary export restraints to protect local steel and automobile industries. Voluntary export restraints are agreed upon by the importing country and the exporting country. A country that is subject to voluntary export restraints limits the quantity of products it exports to another, primarily because it attempts, by doing so, to avoid more severe, future mandatory import restrictions. Voluntary export quotas are still used today even though they have been banned by the Uruguay Round of the General Agreement on Tariffs and Trade (and now by the World Trade Organization) since 1999. The United States is imposing them informally, for example, for Japanese steel imports; this protection mechanism has been used since 1969 in the long history of trade protection of the U.S. steel industry.

### **1.9.7 Price Controls: Increasing Prices of Imports**

Price controls have a direct effect on a product mix aimed at a particular market. Increasing the price of imports to match minimum prices of domestic offerings is one such strategy that is frequently used for both products and for retailers. For example, Japan uses such controls to ensure that locally produced rice is not at a disadvantage relative to rice imports from the United States, which are of equally high quality but are sold at much lower prices. In this instance, the prices of imports are held artificially high so that local consumers would not discriminate in favour of U.S. competitors. Similarly, Wal-Mart and other discounters and category specialists in the European Union are constantly scrutinized and often pressured by local authorities to raise prices; EU governments charge that these international retailers price products below cost to drive out smaller competitors.

**Price Controls: Antidumping and Countervailing Duty Actions**

Antidumping and countervailing duty actions were designed to counter unfair competition, such as predatory pricing. Dumping refers to selling below fair value to undermine competitors' charging the market price and/or to get rid of excess inventory-with the same outcome, of undermining competition. When used as price controls, antidumping measures involve initiating investigations to determine whether imports are sold below fair value, imposing duties to offset dumping, as well as adopting other measures to counter the effects of dumping. Countervailing measures include investigations to determine whether imports are sold below fair prices as a result of foreign subsidies; such determination is usually followed by duties that are imposed to offset this practice and measures taken to offset effects of subsidies.

To the detriment of international trade, such measures have become protectionist tools that are used to intimidate importers and restrict trade. The European Union has been under scrutiny recently for excessive use of antidumping investigations. Such investigations probing into antidumping activity and countervailing duty investigations are focused on a specific product from a particular supply source, and thus they are frequently referred to as "made-to-measure" protectionist devices.

#### **1.9.8 Price Controls: Paratariff Measures**

Paratariff measures are charges that increase the costs of imports in a manner similar to tariffs. Such measures include allowing an initial number of product units to enter, the country duty-free and charging tariffs to subsequent shipments in excess of this quota; they also include advance import deposits, additional import charges, seasonal tariffs, and customs charges. The United States uses many of these paratariff measures to discourage shipment of certain agricultural products from developing countries.

### **1.9.9 Standards**

Standards as barriers to trade are frequently used as barriers to imports, primarily imposed by highly industrialized countries. Problematic are standards that are especially strict, such as those imposed by the European Union against hormone-fed U.S. beef and bio-engineered corn and soybeans on safety grounds. Standards that discriminate against foreign firms in particular, or that simply create more bureaucratic hurdles for importing firms, act as nontariff barriers to trade.

On the positive side, excessive standards could and often do help local and international industry alike, by deterring gray markets. For example, the United States has very strict environmental and manufacturing standards for automobiles. Importing an automobile that is not specifically designed according to U.S. specifications is very costly: One has to use expensive automobile conversion services and obtain the appropriate Department of Transportation authorization to use the vehicle.

### **1.9.10 Local Content Requirements and Foreign Ownership: Percentage Requirements**

Governments of many emerging market economies mandate that a certain percentage of the products imported are locally produced: They mandate a local content requirement. Manipulating and/ or assembling the product on the territory of the importing country-usually in a foreign trade zone can often meet this requirement. China, for example, has always presented a challenge to importing firms. Multinational firms often join with Chinese partners and agents to either package or manufacture enough of the product to have it qualify based on local content requirements; firms often do tricky calculations on local services and part values to meet such local content edicts.

In addition to the traditional local content requirements, there are other forms of favouring local contribution and labour. For example, governments often impose regulations to protect local carriers for passenger and freight transportation. An example would be restricting foreign airlines landing rights or ability to pick up passengers at an intermediate stop ("third freedom" rights); this requirement favours national airlines operating on international routes.

Foreign ownership restrictions also are widely used. Some ownership restrictions refer to the percentage ownership in a business—for example, requiring 51 percent or more of a joint venture to be owned by a national firm. Other restrictions are even more stringent and discriminatory in favour of nationals. The history of Indonesia's automobile industry is a case in point. Initially, the industry was in the hands of Indonesians from the military ranks or senior officials; as the "New Order" was instituted, the industry went into the hands of the ruling Suharto family and of the large Chinese conglomerates, creating a powerful lobbyist that was able to ban imports of motor vehicles until 1993, when the ban was replaced by tariffs in the range of 175 to 275 percent.<sup>20</sup>

It should be mentioned that service industries in particular are subjected to regulations that invoke foreign ownership restrictions. Creative strategies that employ an ambiguous legal environment are used to block entry of international service providers or to place them at a disadvantage relative to local competitors.

#### **1.9.11 Boycott**

A boycott is usually initiated as the result of an action group calling for a ban on consumption of all goods associated with a particular company and/or country. Often, boycotts target a company that is representative, or even synonymous, with its country of origin. For example, when the uprising in the

West Bank and Gaza erupted, Coke sales in neighbouring Egypt and Jordan were hit by local boycott calls. McDonald's restaurants were the target of French protesters, who were against tariffs imposed by the United States on European Union countries. Exxon-owned Esso has been the target of a high-profile boycott campaign by groups angered at its support of the U.S. government's rejection of the Kyoto climate change pact.

### **1.9.12 Embargoes and Sanctions**

Embargoes and sanctions are imposed by a country (or a number of countries) against another country. An embargo prohibits all business deals with the country that is the target of the embargo, often affecting businesses from third countries that do business with both the country (or countries) imposing the embargo and the country under embargo. The embargo could be limited to a particular product and/or to particular circumstances. For example, "smart sanctions" have been imposed by the United States and the United Kingdom on Iraq's oil exports, modifying the oil embargo against Iraq to allow for use of oil revenues aimed at humanitarian purposes. Liberia is presently experiencing an arms embargo imposed by the United Nations Security Council as a punishment for its support of Sierra Leone's Revolutionary United Front.

The United States has imposed, for decades, a full embargo against Cuba. The embargo covers any commercial and non-commercial relationship with Cuba, and it even prohibits visits to the country by U.S. citizens, with some exceptions. Furthermore, multinational companies from other countries doing business in the United States are prohibited, under the embargo, from engaging in any business deals with Cuba. Unfortunately for the United States, this strategy does not appear to reach its goal-punishing Fidel Castro, Cuba's president since the onset of the embargo, and his communist regime, by derailing its economy. On the contrary, Cuba is reaching out to the world by

transforming itself into a hub for information technology, one where U.S. companies may be at a disadvantage relative to competition in the future.

Finally, a form of no retaliatory embargo exists: It is imposed when imports into a country that has established quotas for a particular product exceed those quotas.

### **1.9.13 Currency and Capital Flow Controls**

Strategies involving currency and capital flow controls are used in economies that are under tight government control and/or that are experiencing hard-currency shortages. In the case of capital flow, countries use arguments of self-determination to ensure that regions in the country are uniformly developed or that there would not be a capital flight from the country. Such strategies affect international businesses in that they restrict market -dictated activity in the name of protectionism.

Governments use currency flow restrictions primarily to influence the stability of the national currency. Such restrictions, however, directly affect the flow of imports into the country, by giving priority to desirable goods and restricting the import of less desirable goods and services. Among the currency controls used by governments are the following:

- Blocked currency
- Differential exchange rates
- Foreign exchange permits

### **1.9.14 Blocked Currency**

A country using a blocked currency strategy does not allow importers to exchange local currency for the seller's currency. This strategy can be used as a political weapon, to create obstacles for international business attempting to enter the country. More often, however, the strategy is used because the country is experiencing acute balance-of-payments difficulties. Firms fortunately have at their disposal counter trade strategies to address this type of barrier. Under a typical scenario, the exporter sells goods in exchange for local currency and uses the proceeds to purchase local goods for sale abroad; U.S. companies in the past often-bought goods from Mexico and from Eastern Europe with local currency to address this barrier.

Another method that firms can use to bypass blocked exchange rates entails using unofficial (and, from the perspective of the importing country, illegal) exchange offices. Such offices exist both abroad and in the importing country; however, they offer unfavourable exchange rates and expose the company to the risk of government action against it.

#### **1.9.15 Differential Exchange Rates**

Two types of differential exchange rates can be used. The first, which is government imposed, refers to a strategy the government uses to promote imports of desirable and necessary goods, such as armament and petrol, and to discourage imports of less desirable and necessary goods, such as consumer goods and services, entertainment, and the like. Offering a less favourable exchange rate for international products and services reflects a government strategy that ultimately increases the cost of this second category of products to the final consumer and discourages its purchase.

A second type of differential exchange rate is favourable to the international firm importing products into this market. In this situation, a

difference exists between the black market exchange rate and the official government exchange rate, with the black market rate being higher than the government rate. The rate difference is a reflection of economic distortion: A high black market exchange rate can signal a likely depreciation of the local currency, or foreign exchange rationing by the government, or both. A large difference between the government and the free exchange rate can also be interpreted as a tax on exports and a subsidy on imports, stimulating the diversion of resources from the official to the black market sector.

#### **1.9.16 Foreign Exchange Permits**

Countries attempting to control foreign exchange often require the use of foreign exchange permits. Such permits are typically provided by the Central Bank. They also give priority to imports of goods that are in the national interest and delay access to foreign exchange for products that are not deemed essential. An exchange permit can also stipulate differential exchange rates. Most countries that experience a shortage of hard currency require foreign exchange permits. China and countries in Sub-Saharan Africa currently require such permits. In the past, Latin American and Eastern European countries relied heavily on the use of foreign exchange permits for imports.

#### **1.10 SELF-ASSESSMENT QUESTIONS**

1. How and why does global marketing differ from domestic marketing?
2. Explain the scope of global marketing.
3. Why is the task of the global marketer more complex and difficult than that of the domestic marketer?

4. Distinguish among ethnocentricity, polycentricity and egocentricity.
5. Distinguish among domestic marketing, foreign marketing, international marketing, multinational marketing and global marketing.

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**LESSON NO. 2:     INTERNATIONAL MONETARY FUND  
(IMF) AND WORLD TRADE ORGANISATION (WTO)**

**STRUCTURE**

- 2.1     International Monetary Fund (IMF)
  - 2.1.1     Origin of International Monetary Fund (IMF)
  - 2.1.2     Functions of IMF
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- 2.2     World Trade Organisation (WTO)
  - 2.2.1     Trade without discrimination
  - 2.2.2     Objectives of WTO
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- 2.3     Self-assessment questions

## **2.1 INTERNATIONAL MONETARY FUND (IMF)**

### **2.1.1 Origin of International Monetary Fund (IMF)**

Even before the Second World War ended, monetary experts in the U.S.A. and the U.K. began planning to solve the monetary problems likely to be faced after the war. Known after their authors as the Keynes Plan and the White Plan, both sets of proposals were subjected to intensive discussion and furnished the basis for the Bretton Woods Conference, which decided to set up the two organizations, the IMF and the IBRD. The creation of the Fund represents a major effort at international monetary co-operation. Its main objectives are:

1. To promote exchange stability and orderly exchange arrangements and to avoid competitive devaluation.
2. To help re-establish multilateral system of trade and payments and to eliminate foreign exchange restrictions.
3. To provide for international adjustment, superior to deflation, by making available increased international reserves.
4. To facilitate the expansion and balanced growth of international trade.

### **2.1.2 Functions of IMF**

The basic functions of IMF are:

1. To lay down ground rules for the conduct of international finance.

2. To provide short and medium-term assistance for overcoming short-term balance of payments deficits.
3. Creation and distribution of reserves in the form of SDRs.

The fund has 182 member-countries, accounting for about 80 per cent of the total world production and 90 per cent of the world trade. Members' quotas in the Fund amount to approximately SDR 212 billion (April, 1999). Quotas are used to determine (i) the voting power of members, (ii) their contribution to the Fund's resources, (iii) their access to these resources, and (iv) their share in the allocation of SDRs. India's quota in the Fund is SDR 4,158.2 million.

### **2.1.3 Main features of the international monetary system as it existed upto 1973**

1. Par value system: The exchange value of a member's currency was fixed in terms of gold. Since the price of gold was officially fixed at U.S. \$ 35 per ounce, it also meant that par values were fixed in terms of dollar. Dollar was used as the intervention currency as at that time dollar was as good as gold. In fact, members preferred to keep dollars in reserve, in as much as dollars earned interest while gold reserves did not.
2. Change in par value: In order to achieve short-term balance of payments equilibrium, members could borrow funds from the international Monetary Fund. If the IMF help did not serve the purpose, the IMF was required. If the proposed change was greater than 10 per cent, it could be allowed provided (i) there was a fundamental disequilibrium, and (ii) devaluation would be

the right remedy for solving the fundamental disequilibrium. Fundamental disequilibrium was nowhere defined, but experience has shown that severe depression abroad with prolonged unemployment at home and cases of structural disequilibrium could be taken as cases of fundamental disequilibrium.

3. Exchange control was not permitted on current transactions except (i) when a member's currency was under massive attack, and (ii) when the Fund declared some currency as scarce. Members could use exchange control so far as the use of that currency was concerned.

#### **2.1.4 Changes made after 1973**

1. A member can peg its currency to (i) either a single major currency, or (ii) a basket of currencies, or (iii) allow it to float independently, or (iv) adjust it to a set of indicators. Thus, there is a complete departure from the par value system. It is, however, subject to surveillance by the fund.
2. A reduction in the role of gold in the International Monetary System. There is now no statutory price for gold. In fact, one-third of the gold stock with the IMF was disposed of to create a Trust Fund to be used to provide additional balance of payments support on concessional terms to 59 eligible developing members. S.D.R. is now the unit of account for Fund's transactions.

#### **2.1.5 Assistance provided by the fund**

Ordinarily, a fund member subscribes its quota in the Fund by paying 25 per cent in reserve assets and 75 per cent in its own currency. When a member draws on the Fund's resources, it purchases the currencies of other member-countries or SDRs with its own currency, leading to a rise in Fund's holdings of the member's currency. The borrowing member must buy back its own currency within a specified period with SDRs or currencies specified by the fund. The Fund's financial resources are made available to its members through a variety of policies, which differ mainly in the type of balance of payments need they address and in the degree of conditionality attached to them. The rules governing access to the use of the Fund's general resources apply uniformly to all members.

For any purchase, a member is required to represent to the fund that the desired purchase is needed because of its balance of payments or reserve position or developments in its reserves.

Access to Fund resources is determined in relation to a member's quota. The annual access limit is 100 per cent of quota and the cumulative access limit is 300 per cent of quota.

**(i) Regular facilities**

**Reserve Tranche.** A member has a reserve tranche position if the IMF's holdings of its currency in the General Resources Account, excluding those holdings that reflect the member's use of IMF resources, are less than its 'quota', that is, the amount a member pays to belong to the IMF, which is based on a complex formula that generally reflects the size of the country's economy in the world economy. A member may draw up to the full amount of its reserve tranche position at any time, subject only to the member's representation of a balance of payments need. A reserve tranche drawing does not constitute a use

of IMF credit and is not subject to charges or to an expectation or obligation to repurchase.

**Credit tranches:** IMF credit is subject to different conditions and phasing, depending on whether it is made available in the first credit 'tranche' (segment) of 25 per cent of a member's quota or in the upper credit tranches (any segment above 25 per cent of quota). For drawings in the first credit tranche, members must demonstrate reasonable efforts to overcome their balance of payments difficulties.

Upper credit tranche drawings are made in installments, or phased, and are released when performance targets are met. Such drawings are normally associated with Stand-By or Extended Arrangements, which typically seek to resolve balance of payments difficulties and to support structural policy reforms where appropriate. Performance criteria and periodic reviews are used to assess policy implementation.

**Stand-By Arrangements:** Stand-By Arrangements give members the right to draw up to a specified amount of IMF resources during a prescribed period. Drawings are normally phased on a quarterly basis, with their release conditional upon meeting performance criteria and the completion of periodic reviews. Performance criteria generally cover bank credit, government or public sector borrowing, trade and payments restrictions, and international reserve levels. These criteria allow both the member and the IMF to assess progress and may signal the need for further corrective policies. Stand-By Arrangements typically range from 12 to 18 months (although they can extend up to three years). Repayments are made within 3 ¼ to 5 years of each drawing.

**Extended fund facility (EFF):** The EFF provides assistance for members' adjustment programs over longer periods and with generally larger amounts of

financing than under Stand-By Arrangement. Extended Arrangements, which normally run for three years (and can be extended for a fourth), are designed to rectify balance of payments difficulties stemming largely from structural problems that require a longer period of adjustment.

A member requesting an Extended Arrangement outlines its objectives and policies for the period of the arrangement and presents a detailed statement each year of the policies and measures to be pursued over the next 12 months. The phasing and performance criteria are comparable to those under Stand-By Arrangements; although phasing on a semiannual basis is possible Repayments are made within 4 ½ to 10 years of each drawing.

**(ii) Concessional facility**

Enhanced structural adjustment facility (ESAF): This facility, established by the Executive Board in 1987 and extended and enlarged in February 1994, is the principal means by which the IMF provides financial support, in the form of highly concessional loans, to low-income member countries facing protracted balance of payments problems.

At the same time the ESAF was extended and enlarged, no new resources were made available for its precursor—the Structural Adjustment Facility (SAF), which had been established in 1986. The end of 1995 disbursed all remaining SAF resources. The objectives and primary features of the SAF were similar to those of the current ESAF, but programs supported under ESAF Arrangements are more ambitious with regard to macroeconomic policy and structural reform measures.

ESAF resources are intended to support strong medium-term structural adjustment programs. Eligible members seeking ESAF resources must develop,

with the assistance of the staffs of the IMF and the World Bank, a policy framework paper (PEP) for a three-year adjustment program. The PEP, which is updated annually, describes the authorities' economic objectives, macroeconomic and structural policies during the three-year period, and associated external financing needs and major sources of financing. The PEP, which is a document of the national authorities, is intended to ensure a consistent framework for economic policies and to attract financial and technical assistance in support of the adjustment program.

Adjustment measures under ESAF-supported programs are expected to strengthen substantially a country's balance of payments position and foster growth during the three-year period. Monitoring under ESAF Arrangements is conducted through quarterly financial and structural benchmarks. In addition, semiannual performance criteria are set for key quantitative and structural targets. ESAF loans are disbursed semiannually, initially upon approval of an annual arrangement and subsequently based on the observance of performance criteria and after completion of a midterm review. ESAF loans are repaid in 10 equal semiannual installments, beginning 5 ½ years and ending 10 years after the date of disbursement. The interest rate on ESAF loans is 0.5 per cent a year.

### **(iii) Special facilities**

Compensatory and contingency financing facility (CCFF): The compensatory element of the CCFF provides timely financing to members experiencing a temporary shortfall in export earnings or excess in cereal import costs, attributable to factors largely beyond the member's control. Particularly commodity exporters have used this element of the facility. The contingency element helps members with IMF arrangements keep their adjustment programs on track when faced with unexpected, adverse external shocks. The affected variables could include export earnings, import prices, and international interest

rates; workers' remittances and tourism receipts may also be covered if they are a significant component of the member's current account.

**Buffer stock financing facility (BSFF):** Under this facility, the IMF helps finance a member's contribution to approved international buffer stocks if the member demonstrates a balance of payments need. No drawings have been made under this facility since January 1984.

**Supplemental reserve facility (SRF):** The IMF established the supplemental reserve facility in reaction to the unprecedented level of demand for IMF resources during the recent Asian crisis. The facility provides financing to members experiencing exceptional balance of payments difficulties owing to a large short-term need resulting from a sudden and disruptive loss of market confidence reflected in pressure on the capital account and the member's reserves. Its use requires a reasonable expectation that the implementation of strong adjustment policies and adequate financing will result in an early correction of such difficulties. Access under the SRF is not subject to the usual access limits but is based on the financing needs of the member, its capacity of repay, the strength of its program, and its record of past use of IMF resources and cooperation with the IMF. Financing is committed for up to 1 year, and repurchases are expected to be made within 1 to 1 ½ years, and must be made within 2 to 2 ½ years, from the date of each purchase. For the first year, the rate of charge on SRF financing is subject to a surcharge of 300 basis points above the usual rate of charge on other IMF loans; the surcharge then increases by 50 basis points every six months until it reaches 500 basis points.

**Contingent credit lines (CCL):** In April 1999, the Board agreed to provide Contingent Credit Lines for a two-year period. Like the Supplemental Reserve Facility, the CCL is designed to provide short-term financing to help members overcome expectational balance of payments problems arising from a

sudden and disruptive loss of market confidence. A key difference is that the SRF is for use by members already in the midst of a crisis, whereas the CCL is a preventive measure solely for members concerned with their potential vulnerability to contagion but not facing a crisis at the time of the commitment. In addition, the eligibility criteria confine potential candidates for a CCL to those members implementing policies considered unlikely to give rise to a need to use IMF resources; whose economic performance— and progress in adhering to relevant internationally accepted standards— has been assessed positively by the IMF in the latest Article IV consultation and thereafter; and who have constructive relations with private sector creditors with a view to facilitating appropriate private sector involvement. Resources committed under a CCL can be activated only if the Board determined that the exceptional balance of payments financing needs faced by a member have arisen owing to contagion—that is, circumstances largely beyond the member's control stemming primarily from adverse developments in international capital markets consequent upon developments in other countries.

The CCL is not subject to general IMF access limits, but commitments under the CCL are expected to range from 300 per cent to 500 per cent of the member's quota. The maturity of and rate of charge on CCL resources are the same as for SRF resources.

**(iv) Other forms of financial assistance**

Support for currency stabilization funds: The IMF decided in 1995 to provide financial support for the establishment of currency stabilization funds to bolster confidence in countries' exchange-rate-based stabilization strategies—preferably an exchange rate peg with relatively narrow margins or a preannounce crawl. The countries' economic policies would have to be sufficiently tight that inflation would be compatible with the targeted exchange

rate anchor, so that little use of the currency stabilization fund for exchange market intervention would be expected. So far, the IMF has not actually provided this type of assistance.

**Emergency financing mechanism (FEM):** The EFM comprises a set of procedures that allow for quick Board approval of IMF financial support while ensuring sufficient conditionality. It is to be used in rare circumstances representing or threatening a crisis in a member's external accounts and requiring an immediate IMF response. The EFM was established in September 1995 and was used in 1997 for the Philippines, Thailand, Indonesia, and Korea, and in 1998 for Russia.

**Emergency Assistance:** The IMF also provides emergency financial assistance to a member facing balance of payments difficulties caused by a natural disaster. The assistance is available through outright purchases, usually limited to 25 per cent of quota, provided that the member is cooperating with the IMF to find a solution to its balance of payments problem. In most cases, this assistance has been followed by an arrangement with the IMF under one of its regular facilities.

In 1995, the policy on emergency assistance was expanded to cover countries in post conflict situations. This assistance may be provided when the member's institutional or administrative capacity has been disrupted by conflict but still has sufficient capacity for planning and policy implementation and a demonstrated commitment on the part of the authorities; there is an urgent balance of payments need; and IMF support could be catalytic and is part of a concerted international effort. Conditions for emergency assistance include a statement of economic policies, a quantified macroeconomic framework to the extent possible, and a statement of the authorities' intention to move as soon as possible to an upper credit tranche Stand-By or Extended Arrangement or to an

ESAF Arrangement. The conditionality is tailored to the individual country situation and to rebuilding the country's administrative and institutional capacity.

To conclude, it may be said that the use of Fund's resources enables member-countries to get necessary foreign exchange resources in times of difficulties and thus ensures better planning of import requirements both for domestic use and export production. The limits regarding the use of the IMF facilities may be exceeded in exceptional cases.

#### **2.1.6 Special drawing rights (SDRs)**

SDR is an international reserve asset created by the Fund as supplement to the existing reserve assets. As any assets do not back SDRs, they are also known as paper gold. They were first allocated to all member-countries of the IMF in 1970-72 on the basis of the then existing quotas, total allocation being SDR 9.3 billion. To strengthen the resources of the Fund, SDR allocations were again made in 1979-81 to the extent of 12.12 billion. The total allocations now amount to SDR 21.42 billion.

In 1970, the value of an SDR was equal to US \$ 1, which was maintained till July, 1974 when it was decided to value the SDR on the basis of a basket of 16 currencies. From January 1, 1999, the amount of currency units in the SDR valuation basket and the weight of each to be used to calculate the amount of each of these currencies in the basket will be as follows:

US Dollar	0.5821	39 per cent
Euro (Germany)	0.2280	21 per cent
Japanese Yen	27.2000	18 per cent
Euro (France)	0.1239	11 per cent
pound	0.1050	11 per cent

The IMF calculates the value of SDR in US Dollar terms daily. On February 15, 2000 one SDR was equal to US \$ 1.35.

Due to the sharp depreciation in the value of the US dollar, SDR has now emerged as a standard of value. It is the unit of account for Fund's transactions. It is also finding increasing acceptance as a unit of account for private contracts and international treaties and for use by many international and regional organizations.

Members designated by the Fund are obliged to accept SDRs upto the point when their holdings of SDRs increase to 3 times their allocation. There is an important reason why members are willing to accept SDRs— they earn an interest determined weekly on the excess of their holdings over the original allocations. The Fund has prescribed 14 institutions as other holders of SDRs. Other holders' can acquire and use SDRs in transactions and operations by agreement with participants and other holders under the same terms and conditions as participants. They cannot, however, receive allocations of SDRs.

Countries having a deficit can utilise their SDRs upto 85 per cent of their holdings for (i) obtaining foreign currency, (ii) to redeem balances of their own currencies held by other member-countries, and (iii) to meet their obligations to the Fund, viz., and repayment of interest charges. Countries having less SDRs than allocated would have to pay interest (determined weekly by the Fund).

SDRs may now be freely transferred, by agreement between participants, in transactions and operations that include purchases and sales of SDRs. SDR have also been used as a currency peg.

The question of fresh allocation of SDRs is very often pressed by developing countries on the following grounds: (i) international liquidity

constraints prevent a general expansion in world trade and production, (ii) a new issue of SDRs will provide adequate resources to the countries in debt to maintain imports and provide further impetus to the growth of world trade, and (iii) developing countries are not in a position to borrow at commercial terms. However, the degree of required support for a fresh SDR allocation is still lacking.

## **2.2 WORLD TRADE ORGANISATION (WTO)**

The World Trade Organization (WTO) was established on 1<sup>st</sup> January 1995. Governments had concluded the Uruguay Round negotiations on 15th December 1993 and ministers had given their political backing to the results by signing the Final Act at a meeting in Marrakech, Morocco, in April 1994. The 'Marrakech Declaration' of 15th April 1994, affirmed that the results of the Uruguay Round would strengthen the world economy and lead to more trade, investment, employment and income growth throughout the world. The WTO is the embodiment of the Uruguay Round results and the successor to the General Agreement on Tariffs and Trade (GATT). The WTO has a larger membership than GATT (145 by the end of March 2002). India is one of the founder members of the WTO.

### **2.2.1 Trade without discrimination**

The main principle that guided the erstwhile GATT and directs the present incumbent, WTO, is to promote trade without discrimination. For almost 50 years, key provisions of GATT outlawed discrimination among members and between imported and domestically produced merchandise. According to Article I, the famous "most favored nation" (MFN) clause, members are bound to grant to the products of other members treatment no less favorable than that accorded to the products of any other country. A second form of non-discrimination

known as “national treatment” requires that once goods have entered a market, they must be treated no less favorably than the equivalent domestically produced goods. This is Article III of the GATT apart from the revised GATT (known as “GATT 1994”), several other WTO agreements contain important provisions relating to MFN and the national treatment. Intellectual property protection by WTO members provides for MFN and national treatment. The General Agreement Trade in Services (GATS) requires members to offer MFN treatment to services and service suppliers of other members pre-shipment inspection; trade related investment measures and the application of sanitary and phytosanitary measures.

WTO, contrary to popular belief, is not a “free trade” institution. It permits tariffs and other forms of protection but only in limited circumstances. It is a system of rules dedicated to open, fair and undistorted competition.

### **2.2.2 Objectives of WTO**

In its preamble, the agreement establishing the World Trade Organization reiterates the objectives of GATT. These are: raising standards of living and incomes, ensuring full employment, expanding production and trade and optimal use of the world’s resources. The preamble extends these objectives to services and makes them more precise.

- It introduces the idea of “sustainable development” in relation to the optimal use of the world’s resources, and the need to protect and preserve the environment in a manner consistent with various levels of national economic development.

- It recognizes that there is a need for positive efforts to ensure that developing countries, and especially the least developed among them, secure a better share of the growth in international trade.

### **2.2.3 Functions of WTO**

The agreement establishing WTO provides that it should perform the following four functions:

- First, it shall facilitate the implementation, administration and operation of the Uruguay Round legal instruments and of any new agreements that may be negotiated in the future.
- Second, it shall provide a forum for further negotiations among member countries on matters covered by the agreements as-well as on new issues falling within its mandate.
- Third, it shall be responsible for the settlement of differences and disputes among its member countries.
- Fourth, it shall be responsible for carrying out periodic reviews of the trade policies of its member countries.

### **2.2.4 Most favoured nations status**

According to WTO, all the signatory countries are given the most favoured nations (MFN) status so that these countries have market access to each others, trading areas. India has already given a most favoured nation status to Pakistan; however, Pakistan has not so far reciprocated. India, in any case, is not going to suffer because of the acrimonious attitude of Pakistan.

### **2.2.5 The WTO structure**

Its highest authority—the Ministerial Conference— dominates the structure of the WTO. This body is composed of representatives of all WTO members. It meets at least every two years and is empowered to make decisions on all matters under any of the multilateral trade agreements.

The day-to-day work of the WTO is entrusted to a number of subsidiary bodies, principally, the General Council, also composed of all WTO members, which is required to report to the Ministerial Conference. The General Council also convenes in two particular forms- as the Dispute Settlement Body and the Trade Policy Review Body. The former oversees the dispute settlement procedure and the latter conduct regular reviews of trade policies of individual WTO members.

The General Council delegates' responsibility to three other bodies, namely the Councils for Trade in Goods; Trade in Services and Trade-Related Aspects of Intellectual Property Rights (TRIPS). The Council of Goods oversees the implementation and functioning of all the agreements covering trade in goods, though many such agreements have their own specific overseeing bodies. The latter two Councils have responsibility for their respective WTO agreements and may establish their own subsidiary bodies as necessary.

The Ministerial Conference reports to the General Council which delegates' responsibility to three other bodies as mentioned above. The Committee on Trade and Development is concerned with issues relating to the developing countries and especially to the "least developed" along them. The Committee on Balance of Payments is responsible for consultations among WTO members and countries, which resort to trade and restrictive measures in order to cope with their balance of payments difficulties. Finally, a Committee on Budget, Finance and Administration deals with issues relating to WTO's financing and budget. Each of the plurilateral agreements of the WTO- those on

civil aircraft, government procurement, dairy products and bovine meat-establish their own management bodies, which are required to report to the General Council.

#### **2.2.6 The WTO secretariat and budget**

The WTO Secretariat is located in Geneva. It has 148 members and is headed by its Director General, Supachai Panitchpakdi, and four deputy directors. Its responsibilities include the servicing of WTO delegate bodies with respect to negotiations and the implementation of agreements. It has a particular responsibility to provide technical support to developing countries, and especially the least developed countries. WTO economists and statisticians provide trade performance and trade policy analyses while its legal staff assists in the resolution of trade disputes involving the interpretation of WTO rules and precedents. Other secretariat work is concerned with accession negotiations for new members and providing advice to governments considering membership.

The WTO budget is around US \$83 million (105 million Swiss Francs) with individual contributions calculated based on shares in the total trade conducted by WTO members. Part of the WTO budget also goes to the International Trade Centre.

#### **2.2.7 Norms for joining WTO**

Most WTO members were previously GATT members who signed the Final Act of the Uruguay Round and concluded their market access negotiations on goods and services by the Marrakech meeting in 1994. A few countries, which joined the GATT later, in 1994, signed the Final Act and concluded negotiations on their goods and services schedules, and became WTO members. Other countries that had participated in the Uruguay Round negotiations

concluded their domestic ratification procedures only during the course of 1995 and became members thereafter.

Aside from these arrangements, which relate to “original” WTO membership, any other state or customs territory having full autonomy in the conduct of its trade policies may accede to the WTO on terms agreed with WTO members.

In the first stage of the accession procedures, the applicant government is required to provide the WTO with a memorandum covering all aspects of its trade and economic policies having a bearing on WTO agreements. This memorandum becomes the basis for a detailed examination of the accession request in a working party.

Alongside the working party’s efforts, the applicant government engages in bilateral negotiations with interested members’ governments to establish its concessions and commitments on goods and its commitments on services. This bilateral process, among other things, determines the specific benefits for WTO members in permitting the applicant to accede. Once both, the examination of the applicant’s trade regime and market access negotiations, are complete the working party draws up basic terms of accession.

Finally, the results of the working party’s deliberations contained in its report, a draft protocol of accession, and the agreed schedules resulting from the bilateral negotiations are presented to the General Council or the Ministerial Conference for adoption. If a two-thirds majority of WTO members vote in favour, the applicant is free to sign the protocol and to accede to the Organization; when necessary, after ratification in its national parliament or legislature.

The General Council convenes, as appropriate, to discharge the responsibilities of the Dispute Settlement Understanding as well as of the Trade Policy Review Body. These bodies may have their own chairman and establish rules of procedure, as they feel necessary, for the fulfillment of these responsibilities.

The bodies provided under the plurilateral trade agreements carry out the functions assigned to them under those agreements and operate within the institutional framework of the WTO. These bodies keep the General Council informed of their activities on a regular basis.

### **2.2.8 Agreements of the WTO**

There are 28 agreements that had been signed in the Uruguay Round of the GATT, 1994. The details of these agreements are given below:

#### **A. Trade in Goods**

- General Agreement on Tariffs and Trade 1994 (GATT, 1994)  
Associate Agreements

1) Agreement on Implementation of Article VII of GATT 1994

(Customs Valuation)

- 2) Agreement on Pre-shipment Inspection (PSI)
- 3) Agreement on Technical Barriers to Trade (TBT)
- 4) Agreement on the Application of Sanitary and Phytosanitary Measures (SPS)
- 5) Agreement on Import Licensing Procedures
- 6) Agreement on Safeguards

- 7) Agreement on Subsidies and Countervailing Measures (SCM)
  - 8) Agreement on Implementation of Article VI of GATT 1994 (Anti-dumping) (ADP)
  - 9) Agreement on Trade-Related Investment Measures (TRIMS)
  - 10) Agreement on Textiles and Clothing (ATC)
  - 11) Agreement on Agriculture
  - 12) Agreement on Rules of Origin
- Understanding and Decisions
    - 1) Understanding on Balance of Payments Provisions of GATT 1994
    - 2) Decisions Regarding Cases where Customs Administrations have Reasons to Doubt the Truth or Accuracy of the Declared Value (Decision on Shifting the Burden of Proof)
    - 3) Understanding on the Interpretation of Article XVII of GATT 1994 (State trading enterprises)
    - 4) Understanding on Rules and Procedures Governing the Settlement of Disputes
    - 5) Understanding on the Interpretation of Article II: 1(b) of GATT 1994 (Binding of Tariff Concessions)
    - 6) Decision on Trade and Environment
    - 7) Trade Policy Review Mechanism

## **B. Trade in Services**

- General Agreement on Trade in Services (GATS)

### **C. Intellectual Property Rights (IPRs)**

- Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) Plurilateral Trade Agreements
- Agreement on Trade in Civil Aircraft
- Agreement on Government Procurement
- International Dairy Agreement
- International Bovine Meat Agreement

### **2.3 SELF ASSESSMENT QUESTIONS**

1. Describe the functions and main features of international monetary fund.
2. Write a detail note on Special Drawing Rights (SDR).
3. Write detail note on Assistance provided by IMF.
4. What are the main functions and objectives of WTO? Also right short note on most favoured trade nations status.
5. Write a detail note on agreements of WTO.

## **LESSON NO. 3: LIBERALIZATION OF SERVICE INDUSTRIES: GATS, TRIMS AND TRIPS**

### **STRUCTURE**

- 3.1 Introduction
- 3.2 The Background to The WTO Negotiations
- 3.3 Current Scenario of GATS
- 3.4 TRIMS
- 3.5 TRIPS
- 3.6 The Private Sector
- 3.7 Views of EU and US Governments
- 3.8 Developing Countries
- 3.9 The Regulators
- 3.10 Summary
- 3.11 Questions for Discussion

### **OBJECTIVES**

The motive of the lesson is to know the background to the WTO Negotiations, current scenario of GATS, TRIPS, TRIMS, the private sector, views of EU and US Governments, developing countries and the regulators towards the service industries.

#### **3.1 INTRODUCTION**

Negotiations under way at the World Trade Organisation in Geneva will address, and perhaps to a significant extent reshape, the

regulatory framework for financial and other services around the world. As they seek to reduce barriers to market access, those engaged in these talks are inevitably drawing lines between acceptable and unacceptable domestic regulation. Key constituencies are watching closely to see, and influence, where the lines will fall. Among the eager onlookers are private sector companies from, for instance, banking, insurance, securities and asset management, as well as national regulators and outside critics. Much of the debate in the WTO turns on the issue of whether there are general principles of regulation to which all can sign up. Here there are differences between developed and developing countries, and, to a degree that is becoming increasingly obvious, between the European Union and the United States. It is highly desirable that private sector views should be made known to Governments and regulators. To this end, there have been useful discussions between private sector representatives on both sides of the Atlantic. This article offers some analysis of the different positions taken both in the public and private sectors, and puts forward some suggestions on how, in due course, differences could be bridged.

### **3.2 THE BACKGROUND TO THE WTO NEGOTIATIONS**

For most of the past fifty years international trade negotiations focused on trade in goods. However, the complex set of negotiations - the so-called Uruguay Round - which concluded in 1994 and created the World Trade Organisation also, and for the first time, covered trade in services. One of the agreements to emerge from the Uruguay Round, and to be administered by the WTO, is the General Agreement on Trade in Services, or GATS. The GATS Agreement was basically a framework agreement establishing general principles for WTO negotiations on

services, itself a useful achievement. On financial services, as on most other services, member Governments were in many cases willing to undertake not to add to the restrictions faced by foreign suppliers. They did not commit themselves to dismantle these restrictions to any significant degree. The aim of the new negotiations is achieve significant liberalisation. That is in the interests of the big financial service exporters like the EU and US, whose markets are already largely open and who would gain from improved overseas access. It is no less in the interests of countries around the world whose markets are more protected but whose economic future depends on access to high quality financial and other services. The existing GATS provisions on domestic regulation

Among the important principles enshrined in the GATS Agreement are those related to domestic regulation. Articles III and VI of GATS effectively provide a blueprint for reconciling liberalisation and regulation. Regulations affecting trade in services have to be published. They must be administered in a reasonable, objective and impartial manner. Applicants to provide services which Governments have agreed to liberalise must be given an answer within a reasonable period. Administrative decisions must be subject to review. These and other provisions are designed to ensure that liberalisation is not frustrated by regulatory failings.

At the same time the need for proper prudential regulation is specifically acknowledged in the GATS annex on financial services. This came to be known as the “prudential carve-out”, and was introduced to meet the concerns of regulators. So the existing GATS Agreement reflects a balance which many Governments can accept. On the one hand, there are good economic arguments for promoting quality and

efficiency in financial services by opening up to foreign competition. On the other, market imperfections, and particularly the disparity between suppliers' and customers' knowledge of the financial soundness of suppliers, requires proper prudential regulation going beyond normal anti-trust restraints on market abuse.

### **3.3 CURRENT SCENARIO OF GATS**

Why then has the domestic regulation of services become an issue for debate, and sometimes controversial debate, at the WTO? This is because GATS Article VI.4 calls on the WTO Council for Trade in Services, "with a view to ensuring that measures relating to qualification requirements and procedures, technical standards and licensing requirements do not constitute unnecessary barriers to trade in services", to develop disciplines to ensure that such requirements are based on objective and transparent criteria, and are not more burdensome than necessary to ensure the quality of the service.

In terms of process, the task of debating and elaborating these disciplines falls to the WTO Working Party on Domestic Regulation, created in April 1999 for this purpose. It is due to complete its work by the conclusion of the present Round of WTO negotiations, which has been fixed for January 2005. So far the Working Party has made little progress. It has tried to work out how broadly similar disciplines could be applied to all services sectors. But the issues are not easy; and the Working Party can hardly be expected to move swiftly when significant differences persist among member Governments. It is therefore worth looking at the attitudes of the different key players in the debate on regulation which will be running over the coming months. This debate

involves Governments in developed and developing countries, the private sector, regulators, and outside critics, notably in NGOs.

### **3.4 AGREEMENT ON TRADE-RELATED INVESTMENT MEASURES**

Members, considering that Ministers agreed in the Punta del Este Declaration that "Following an examination of the operation of GATT Articles related to the trade restrictive and distorting effects of investment measures, negotiations should elaborate, as appropriate, further provisions that may be necessary to avoid such adverse effects on trade"; Desiring to promote the expansion and progressive liberalisation of world trade and to facilitate investment across international frontiers so as to increase the economic growth of all trading partners, particularly developing country Members, while ensuring free competition; Taking into account the particular trade, development and financial needs of developing country Members, particularly those of the least-developed country Members; Recognizing that certain investment measures can cause trade-restrictive and distorting effects; Hereby agree as follows:

#### **Article 1: Coverage**

This Agreement applies to investment measures related to trade in goods only (referred to in this Agreement as "TRIMs").

#### **Article 2: National Treatment and Quantitative Restrictions**

1. Without prejudice to other rights and obligations under GATT 1994, no Member shall apply any TRIM that is inconsistent with the provisions of Article III or Article XI of GATT 1994.

2. An illustrative list of TRIMs that are inconsistent with the obligation of national treatment provided for in paragraph 4 of Article III of GATT 1994 and the obligation of general elimination of quantitative restrictions provided for in paragraph 1 of Article XI of GATT 1994 is contained in the Annex to this Agreement.

### **Article 3: Exceptions**

All exceptions under GATT 1994 shall apply, as appropriate, to the provisions of this Agreement.

### **Article 4: Developing Country Members**

A developing country Member shall be free to deviate temporarily from the provisions of Article 2 to the extent and in such a manner as Article XVIII of GATT 1994, the Understanding on the Balance-of-Payments Provisions of GATT 1994, and the Declaration on Trade Measures Taken for Balance-of-Payments Purposes adopted on 28 November 1979 (BISD 26S/205-209) permit the Member to deviate from the provisions of Articles III and XI of GATT 1994.

### **Article 5 : Notification and Transitional Arrangements**

1. Members, within 90 days of the date of entry into force of the WTO Agreement, shall notify the Council for Trade in Goods of all TRIMs they are applying that are not in conformity with the

provisions of this Agreement. Such TRIMs of general or specific application shall be notified, along with their principal features.<sup>1</sup>

2. Each Member shall eliminate all TRIMs which are notified under paragraph 1 within two years of the date of entry into force of the WTO Agreement in the case of a developed country Member, within five years in the case of a developing country Member, and within seven years in the case of a least-developed country Member.
3. On request, the Council for Trade in Goods may extend the transition period for the elimination of TRIMs notified under paragraph 1 for a developing country Member, including a least-developed country Member, which demonstrates particular difficulties in implementing the provisions of this Agreement. In considering such a request, the Council for Trade in Goods shall take into account the individual development, financial and trade needs of the Member in question.
4. During the transition period, a Member shall not modify the terms of any TRIM which it notifies under paragraph 1 from those prevailing at the date of entry into force of the WTO Agreement so as to increase the degree of inconsistency with the provisions of Article 2. TRIMs introduced less than 180 days before the date of entry into force of the WTO Agreement shall

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<sup>1</sup> In the case of TRIMs applied under discretionary authority, each specific application shall be notified. Information that would prejudice the legitimate commercial interests of particular enterprises need not be disclosed.

not benefit from the transitional arrangements provided in paragraph 2.

5. Notwithstanding the provisions of Article 2, a Member, in order not to disadvantage established enterprises which are subject to a TRIM notified under paragraph 1, may apply during the transition period the same TRIM to a new investment (i) where the products of such investment are like products to those of the established enterprises, and (ii) where necessary to avoid distorting the conditions of competition between the new investment and the established enterprises. Any TRIM so applied to a new investment shall be notified to the Council for Trade in Goods. The terms of such a TRIM shall be equivalent in their competitive effect to those applicable to the established enterprises, and it shall be terminated at the same time.

#### **Article 6: Transparency**

1. Members reaffirm, with respect to TRIMs, their commitment to obligations on transparency and notification in Article X of GATT 1994, in the undertaking on "Notification" contained in the Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance adopted on 28 November 1979 and in the Ministerial Decision on Notification Procedures adopted on 15 April 1994.
2. Each Member shall notify the Secretariat of the publications in which TRIMs may be found, including those applied by regional and local governments and authorities within their territories.

3. Each Member shall accord sympathetic consideration to requests for information, and afford adequate opportunity for consultation, on any matter arising from this Agreement raised by another Member. In conformity with Article X of GATT 1994 no Member is required to disclose information the disclosure of which would impede law enforcement or otherwise be contrary to the public interest or would prejudice the legitimate commercial interests of particular enterprises, public or private.

**Article 7: Committee on Trade-Related Investment Measures**

1. A Committee on Trade-Related Investment Measures (referred to in this Agreement as the "Committee") is hereby established, and shall be open to all Members. The Committee shall elect its own Chairman and Vice-Chairman, and shall meet not less than once a year and otherwise at the request of any Member.
2. The Committee shall carry out responsibilities assigned to it by the Council for Trade in Goods and shall afford Members the opportunity to consult on any matters relating to the operation and implementation of this Agreement.
3. The Committee shall monitor the operation and implementation of this Agreement and shall report thereon annually to the Council for Trade in Goods.

**Article 8: Consultation and Dispute Settlement**

The provisions of Articles XXII and XXIII of GATT 1994, as elaborated and applied by the Dispute Settlement Understanding, shall

apply to consultations and the settlement of disputes under this Agreement.

#### **Article 9: Review by the Council for Trade in Goods**

Not later than five years after the date of entry into force of the WTO Agreement, the Council for Trade in Goods shall review the operation of this Agreement and, as appropriate, propose to the Ministerial Conference amendments to its text. In the course of this review, the Council for Trade in Goods shall consider whether the Agreement should be complemented with provisions on investment policy and competition policy.

### **3.5 AGREEMENT ON TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS (TRIPS)**

#### **GENERAL PROVISIONS AND BASIC PRINCIPLES**

##### **Article 1: Nature and Scope of Obligations**

1. Members shall give effect to the provisions of this Agreement. Members may, but shall not be obliged to, implement in their law more extensive protection than is required by this Agreement, provided that such protection does not contravene the provisions of this Agreement. Members shall be free to determine the appropriate method of implementing the provisions of this Agreement within their own legal system and practice.
2. For the purposes of this Agreement, the term "intellectual property" refers to all categories of intellectual property that are the subject of Sections 1 through 7 of Part II.

3. Members shall accord the treatment provided for in this Agreement to the nationals of other Members.<sup>2</sup> In respect of the relevant intellectual property right, the nationals of other Members shall be understood as those natural or legal persons that would meet the criteria for eligibility for protection provided for in the Paris Convention (1967), the Berne Convention (1971), the Rome Convention and the Treaty on Intellectual Property in Respect of Integrated Circuits, were all Members of the WTO members of those conventions.<sup>3</sup> Any Member availing itself of the possibilities provided in paragraph 3 of Article 5 or paragraph 2 of Article 6 of the Rome Convention shall make a notification as foreseen in those provisions to the Council for Trade-Related Aspects of Intellectual Property Rights (the "Council for TRIPS").

## **Article 2: Intellectual Property Conventions**

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<sup>2</sup> When "nationals" are referred to in this Agreement, they shall be deemed, in the case of a separate customs territory Member of the WTO, to mean persons, natural or legal, who are domiciled or who have a real and effective industrial or commercial establishment in that customs territory.

<sup>3</sup> In this Agreement, "Paris Convention" refers to the Paris Convention for the Protection of Industrial Property; "Paris Convention (1967)" refers to the Stockholm Act of this Convention of 14 July 1967. "Berne Convention" refers to the Berne Convention for the Protection of Literary and Artistic Works; "Berne Convention (1971)" refers to the Paris Act of this Convention of 24 July 1971. "Rome Convention" refers to the International Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organizations, adopted at Rome on 26 October 1961. "Treaty on Intellectual Property in Respect of Integrated Circuits" (IPIC Treaty) refers to the Treaty on Intellectual Property in Respect of Integrated Circuits, adopted at Washington on 26 May 1989. "WTO Agreement" refers to the Agreement Establishing the WTO.

1. In respect of Parts II, III and IV of this Agreement, Members shall comply with Articles 1 through 12, and Article 19, of the Paris Convention (1967).
2. Nothing in Parts I to IV of this Agreement shall derogate from existing obligations that Members may have to each other under the Paris Convention, the Berne Convention, the Rome Convention and the Treaty on Intellectual Property in Respect of Integrated Circuits.

### **Article 3: National Treatment**

1. Each Member shall accord to the nationals of other Members treatment no less favourable than that it accords to its own nationals with regard to the protection<sup>4</sup> of intellectual property, subject to the exceptions already provided in, respectively, the Paris Convention (1967), the Berne Convention (1971), the Rome Convention or the Treaty on Intellectual Property in Respect of Integrated Circuits. In respect of performers, producers of phonograms and broadcasting organizations, this obligation only applies in respect of the rights provided under this Agreement. Any Member availing itself of the possibilities provided in Article 6 of the Berne Convention (1971) or paragraph 1(b) of Article 16 of the Rome Convention shall make a notification as foreseen in those provisions to the Council for TRIPS.

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<sup>4</sup> For the purposes of Articles 3 and 4, "protection" shall include matters affecting the availability, acquisition, scope, maintenance and enforcement of intellectual property rights as well as those matters affecting the use of intellectual property rights specifically addressed in this Agreement.

2. Members may avail themselves of the exceptions permitted under paragraph 1 in relation to judicial and administrative procedures, including the designation of an address for service or the appointment of an agent within the jurisdiction of a Member, only where such exceptions are necessary to secure compliance with laws and regulations which are not inconsistent with the provisions of this Agreement and where such practices are not applied in a manner which would constitute a disguised restriction on trade.

#### **Article 4: Most-Favoured-Nation Treatment**

With regard to the protection of intellectual property, any advantage, favour, privilege or immunity granted by a Member to the nationals of any other country shall be accorded immediately and unconditionally to the nationals of all other Members. Exempted from this obligation are any advantages, favour, privilege or immunity accorded by a Member:

- (a) deriving from international agreements on judicial assistance or law enforcement of a general nature and not particularly confined to the protection of intellectual property;
- (b) granted in accordance with the provisions of the Berne Convention (1971) or the Rome Convention authorizing that the treatment accorded be a function not of national treatment but of the treatment accorded in another country;

- (c) in respect of the rights of performers, producers of phonograms and broadcasting organizations not provided under this Agreement;
- (d) deriving from international agreements related to the protection of intellectual property which entered into force prior to the entry into force of the WTO Agreement, provided that such agreements are notified to the Council for TRIPS and do not constitute an arbitrary or unjustifiable discrimination against nationals of other Members.

#### **Article 5: Multilateral Agreements on Acquisition or Maintenance of Protection**

The obligations under Articles 3 and 4 do not apply to procedures provided in multilateral agreements concluded under the auspices of WIPO relating to the acquisition or maintenance of intellectual property rights.

#### **Article 6: Exhaustion**

For the purposes of dispute settlement under this Agreement, subject to the provisions of Articles 3 and 4 nothing in this Agreement shall be used to address the issue of the exhaustion of intellectual property rights.

#### **Article 7: Objectives**

The protection and enforcement of intellectual property rights should contribute to the promotion of technological innovation and to the transfer and dissemination of technology, to the mutual advantage of

producers and users of technological knowledge and in a manner conducive to social and economic welfare, and to a balance of rights and obligations.

#### **Article 8: Principles**

1. Members may, in formulating or amending their laws and regulations, adopt measures necessary to protect public health and nutrition, and to promote the public interest in sectors of vital importance to their socio-economic and technological development, provided that such measures are consistent with the provisions of this Agreement.
2. Appropriate measures, provided that they are consistent with the provisions of this Agreement, may be needed to prevent the abuse of intellectual property rights by right holders or the resort to practices which unreasonably restrain trade or adversely affect the international transfer of technology.

#### **3.6 THE PRIVATE SECTOR**

For some years now there have been regular contacts between the financial service industries in Europe, North America and East Asia over WTO services issues, with a view to establishing common ground and putting shared recommendations to Governments. A good current example of this work is the insurance model schedule, which insurance associations from the EU, the US, Canada and Japan have drawn up together and are jointly recommending to their Governments. The authors of this schedule see it as a framework of insurance regulation

which will both promote competition in the market place and sound solvency-based regulation.

However, private sector views on regulatory issues are not always identical. Some sections of the US financial services community, perhaps influenced by the views of their own regulatory authorities, are more cautious than their European counterparts in drawing up new disciplines under GATS Article VI.4. These differences are best seen in the debate which is emerging at a Government level.

### **3.6 VIEWS OF EU AND US GOVERNMENTS**

It is common ground across the North Atlantic that regulatory requirements applied to services should be objective and transparent. But hitherto the US have been reluctant to go beyond transparency into criteria based on necessity and proportionality, to reflect the Article VI.4 provision that requirements should be “no more burdensome than necessary to ensure the quality of the service”. The EU by contrast has argued that the criteria should relate to necessity and proportionality as well as transparency, although they have not yet elaborated these ideas in any great detail.

### **3.7 DEVELOPING COUNTRIES**

There are now more than 140 member countries of the WTO. In some of the smaller and poorer countries, regulatory systems, where they exist, are fairly basic. A number of Governments of developing countries have expressed resistance to new regulatory disciplines, mainly on the grounds that they do not have the skilled staff to administer them and that existing WTO commitments are more than they can readily cope

with. There may also be an element of bargaining, since developing countries know that services are a high priority for the US and EU.

### **3.8 THE REGULATORS**

It is difficult to attribute to regulators around the world a single view on what is or should be in the GATS agreement. The existing provisions, couched as they are in very broad terms, should cause them no great difficulty, although there are worries about how the powerful dispute settlement procedures of the WTO might be applied to breaches of WTO rules on domestic regulation. Understandably, perhaps, regulators have been mainly concerned with international agreements in their own fields (the Basel Accord, IOSCO, IAIS). Some of them may not yet have grappled with the fact that they are bound by the WTO agreements, particularly the GATS, and that their Governments are committed in the WTO to efforts to work out, and get agreed internationally, regulatory disciplines for service industries.

There are of course good reasons for such disciplines, and for preventing obscure or unnecessary regulation from impeding the growth of trade in services. But there is plenty of scope for misunderstanding or worse between trade negotiators and regulators, and the two need to stay close together as the work goes forward. Equally, there should be contact between the regulators and those in the financial services industry who take an interest in WTO matters. In the United Kingdom, for example, a senior representative of the Financial Services Authority sits on the private sector committee (the Liberalisation of Trade in Services, or LOTIS, committee) which pulls together views from the City of London and UK financial services.

### **3.9 THE OUTSIDE CRITICS**

Several NGOs advocating third world development concerns have been critical of GATS, and not least of the provisions on regulation. They argue that GATS does, or may, deny developing countries the ability to regulate in their own best interests, and to control foreign service suppliers and investors. These criticisms seem misconceived. Not only does GATS encourage prudential regulation, but it permits any member country to exclude Foreign Service suppliers or to admit them subject to conditions. It is difficult to argue that it is against the interests of developing countries that regulation should be transparent, or no more burdensome, or restrictive of trade, than necessary to secure its objectives. It is certainly not in the interests of Foreign Service suppliers to operate in a weak or badly-run regulatory environment. Conversely, the presence of foreign service suppliers familiar with an efficient regulatory environment should serve to strengthen the hand of local regulators who are still learning the ropes.

### **3.10 SOLUTION IN SERVICE INDUSTRIES**

The WTO debate on domestic regulation will not be concluded quickly. Any solution will need to respect the central concerns of the main players. The regulators will need to be convinced that international agreements reached in the WTO will not weaken their ability to put in place and implement necessary prudential regulation at home. The private sector will want to be sure that opportunities to export and invest abroad will not be frustrated by obscure or unnecessary regulation which is in fact protectionism in disguise. Developing countries will expect understanding of the need for sequencing, to cater for the practical limits on their ability to staff and finance new disciplines to be applied across

all service sectors. The EU and the US, with the backing of their respective service industries, will need to find ways of reconciling their differences over the Article VI.4 mandate, possibly by a combination of regulatory principles which apply across all service sectors with other principles which will apply to certain sectors alone.

### **3.11 SUMMARY**

These are not impossible tasks, given the amount of common ground, both intellectual and practical, which already exists. But they have, understandably, been low on the agenda of Governments and financial regulators who have faced more immediate issues, political and economic, in the last couple of years. This is the moment for a fresh impetus and for trade negotiators and regulators to work together on a coherent solution to be in place by mid-2004, ahead of the deadline for the conclusion of the GATS negotiations in early 2005.

### **3.12 QUESTIONS FOR DISCUSSION**

- 1 Explain the background to the WTO negotiations.
2. Explain the current scenario of GATS in India.
3. What are the views of EU and US Governments regarding GATS?
4. What are the regulations for developing countries regarding GATS?
5. Explain the provisions of TRIPS.
6. Explain the provisions of TRIMS.

## LESSON NO. 4: WORLD BANK

### STRUCTURE

- 4.1 Introduction
- 4.2 International Development Association
- 4.3 International Finance Corporation
- 4.4 [Multilateral Investment Guarantee Agency](#)
- 4.5 International Centre for Settlement of Investment Disputes
- 4.6 Summary
- 4.7 Questions for Discussion

### OBJECTIVES

After studying the lesson, you should be able to understand the working, structure of different international financing agencies like World Bank, International Development Association, International Finance Corporation, [Multilateral Investment Guarantee Agency](#), and International Centre for Settlement of Investment Disputes.

#### 4.1 INTRODUCTION

Conceived during World War II at Bretton Woods, New Hampshire, the World Bank initially helped rebuild Europe after the war. Its first loan of \$250 million was to France in 1947 for post-war reconstruction. Reconstruction has remained an important focus of the Bank's work, given the natural disasters, humanitarian emergencies, and

post conflict rehabilitation needs that affect developing and transition economies. Today's Bank, however, has sharpened its focus on poverty reduction as the overarching goal of all its work. It once had a homogeneous staff of engineers and financial analysts, based solely in Washington, D.C. Today, it has a multidisciplinary and diverse staff including economists, public policy experts, sectoral experts, and social scientists. 40 percent of staff are now based in country offices.

The Bank itself is bigger, broader, and far more complex. It has become a Group, encompassing five closely associated development institutions: the [International Bank for Reconstruction and Development](#) (IBRD), the [International Development Association](#) (IDA), the [International Finance Corporation](#) (IFC), the [Multilateral Investment Guarantee Agency](#) (MIGA), and the [International Centre for Settlement of Investment Disputes](#) (ICSID).

## **4.2 INTERNATIONAL DEVELOPMENT ASSOCIATION**

The International Development Association (IDA) is the part of the World Bank that helps the earth's poorest countries reduce poverty by providing interest-free loans and some grants for programs aimed at boosting economic growth and improving living conditions. IDA funds help these countries deal with the complex challenges they face in striving to meet the Millennium Development Goals. They must, for example, respond to the competitive pressures as well as the opportunities of globalization; arrest the spread of HIV/AIDS; and prevent conflict or deal with its aftermath.

### **4.2.1 IDA's Mission**

The International Development Association (IDA) is the part of the World Bank that helps the earth's poorest countries reduce poverty by providing interest-free loans and grants for programs aimed at boosting economic growth and improving living conditions. IDA funds help these countries deal with the complex challenges they face in striving to meet the Millennium Development Goals. They must, for example, respond to the competitive pressures as well as the opportunities of globalization; arrest the spread of HIV/AIDS; and prevent conflict or deal with its aftermath. IDA's long-term, no-interest loans pay for programs that build the policies, institutions, infrastructure and human capital needed for equitable and environmentally sustainable development. IDA's goal is to reduce inequalities both across and within countries by allowing more people to participate in the mainstream economy, reducing poverty and promoting more equal access to the opportunities created by economic growth.

#### **4.2.2 IDA's History**

The International Bank for Reconstruction and Development (IBRD), better known as the World Bank, was established in 1944 to help Europe recover from the devastation of World War II. The success of that enterprise led the Bank, within a few years, to turn its attention to the developing countries. By the 1950s, it became clear that the poorest developing countries needed softer terms than those that could be offered by the Bank, so they could afford to borrow the capital they needed to grow. With the United States taking the initiative, a group of the Bank's member countries decided to set up an agency that could lend to the poorest countries on the most favourable terms possible. They called the agency the "International Development Association." Its founders saw

IDA as a way for the "haves" of the world to help the "have-nots." But they also wanted IDA to be run with the discipline of a bank. For this reason, US President Dwight D. Eisenhower proposed, and other countries agreed, that IDA should be part of the World Bank (IBRD).

IDA's [Articles of Agreement](#) became effective in 1960. The first IDA loans, known as credits, were approved in 1961 to Chile, Honduras, India and Sudan. IBRD and IDA are run on the same lines. They share the same staff and headquarters, report to the same president and evaluate projects with the same rigorous standards. But IDA and IBRD draw on different resources for their lending, and because IDA's loans are deeply concessional, IDA's resources must be periodically replenished (see "IDA Funding" below). A country must be a member of IBRD before it can join IDA; 165 countries are IDA members.

#### **4.2.3 IDA's Borrowers**

IDA lends to those [countries](#) that had an income in 2005 of less than \$1,025 per person and lack the financial ability to borrow from IBRD. Some "blend borrower" countries like India and Indonesia are eligible for IDA loans because of their low per person incomes but are also eligible for IBRD loans because they are financially creditworthy. Eighty-one countries are currently eligible to borrow from IDA. Together these countries are home to 2.5 billion people, half of the total population of the developing world. Most of these people, an estimated 1.5 billion, survive on incomes of \$2 or less a day.

#### **4.2.4 IDA Lending**

IDA credits have maturities of 20, 35 or 40 years with a 10-year grace period before repayments of principal begins. IDA funds are [allocated to the borrowing countries](#) in relation to their income levels and record of success in managing their economies and their ongoing IDA projects. There is no interest charge, but credits do carry a small service charge, currently 0.75 percent on funds paid out. See the [terms of IDA lending](#). In fiscal year 2005 (which ended June 30, 2005), IDA commitments totaled \$8.7 billion. New commitments in FY05 comprised 160 new operations in 64 countries. Forty-five percent of new commitments went to Sub Saharan Africa, 33 percent to South Asia, 12 percent to East Asia and the Pacific, 6 percent to Eastern Europe and Central Asia (ECA), and the remainder to poor countries in North Africa and in Latin America. The leading IDA borrowers in FY05 are listed in Table 4.1.

Since 1960, IDA has lent \$161 billion to 108 countries. Annual lending figures have increased steadily and averaged about \$8.4 billion over the last three years. Most loans address basic needs, such as primary education, basic health services, and clean water and sanitation. IDA also funds projects that safeguard the environment, improve conditions for private business, build infrastructure, and support reforms to liberalize countries' economies and strengthen their institutions. All these projects pave the way toward economic growth, job creation, higher incomes and better living conditions.

**Table 4.1: Top Ten IDA Borrowers in Financial Year 2005**

Top Ten IDA Borrowers	\$ million
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India	1 138
Vietnam	6 99
Bangladesh	6 00
Pakistan	5 00
Ethiopia	4 50
Ghana	3 64
Tanzania	3 56
Nigeria	3 30
Uganda	3 28
Afghanistan	2 85

#### 4.2.5 IDA Funding

While the IBRD raises most of its funds on the world's financial markets, IDA is funded largely by contributions from the governments of the richer member countries. Additional funds come from IBRD's income and from borrowers' repayments of earlier IDA credits.

See the [list of cumulative contributions](#) to IDA Replenishments and donor shares of total contributions. Donors get together every three years to replenish IDA funds. Donor contributions account for more than half of the US\$33 billion in the [IDA14 replenishment](#), which finances projects over the three-year period ending June 30, 2008. The United States, the United Kingdom, Japan, Germany, France, Italy and Canada made the largest pledges to IDA14, but less wealthy nations also contribute to IDA. Turkey and Korea, for example, once IDA borrowers, are now donors. Countries currently eligible to borrow from IBRD (but not from IDA) –Brazil, Czech Republic, Hungary, Mexico, Poland, Russia, the Slovak Republic, and South Africa – are also IDA14 donors. Other contributors include Australia, Austria, Barbados, Belgium, Denmark, Finland, Greece, Iceland, Ireland, Israel, Kuwait, Luxembourg, Netherlands, New Zealand, Norway, Portugal, Saudi Arabia, Singapore, Slovenia, Spain, Sweden, Switzerland and Venezuela.

To increase openness and help ensure that IDA's policies are responsive to country needs and circumstances, representatives from each IDA region were invited to take part in the IDA13 and IDA14 replenishment negotiations. The number of borrower representatives was expanded – to a total of nine – during the IDA14 replenishment negotiations. In both IDA13 and IDA14, background policy papers were

publicly released, as well as drafts of the replenishment reports prior to their finalization.

#### **4.2.6 IDA's Role in Reducing Poverty**

IDA helps to reduce poverty by collaborating with other development partners, as well as through its own programs. IDA has learned from experience that development programs are most successful when the borrower country – not just the government, but non-governmental organizations (NGOs) and other of civil society – acquires a sense of ownership of the programs through deep involvement in their design and execution. The borrower country now leads in preparing the Poverty Reduction Strategy (PRS) that establishes priorities for IDA support. In each country, IDA works with local development partners to ensure that the PRS is carried out in a coherent way and that IDA focuses on areas where it has comparative advantage. In IDA13, IDA targeted human-development projects in areas like education, health, social safety nets, water supply and sanitation (36%); law, justice and public administration (23%); industry (18%); infrastructure (14%), and agriculture and rural development (8%).

#### **4.2.7 IDA's Performance**

In India, the National AIDS Control project supported training of 52,500 physicians and 60 percent of nursing staff in HIV/AIDS management topics. In Yemen, the Taiz Flood Disaster Prevention and Municipal Development project prevented serious damage from the 1996 floods, benefiting 21,000 households directly and over half a million people indirectly. In Africa, more than 5 million textbooks (mostly locally developed and produced) were supplied to primary schools. In

Asia, over 6,700 health care facilities were constructed or upgraded, then equipped and staffed to provide basic health care to rural populations. The social investment fund projects in Latin America reached some 9.5 million beneficiaries. Activities supported by these projects generated almost a million person-months of employment.

IDA emphasizes broad-based growth, including:

- (i) Sound economic policies, rural development, private business and sustainable environmental practices,
- (ii) Investment in people, in education and health, especially in the struggle against HIV/AIDS, malaria and TB,
- (iii) Expansion of borrower capacity to provide basic services and ensure accountability for public resources,
- (iv) Recovery from civil strife, armed conflict and natural disaster, and
- (v) Promotion of trade and regional integration

IDA carries out analytical studies to build the knowledge base that allows intelligent design of policies to reduce poverty. IDA also advises governments on ways to broaden the base of economic growth and protect the poor from economic shocks.

The one billion children who live in countries that receive funds from IDA are the main beneficiaries of IDA-backed investments in basic health, primary education, literacy and clean water. IDA is now the single largest source of donor funds for basic social services in the poorest countries. IDA also coordinates donor assistance to provide relief for poor countries that cannot manage their debt-service burden.

Globalization – the increasing integration of world markets and societies – has allowed China, India and many other developing countries to achieve faster growth through expanded foreign direct investments and access to export markets. IDA is re-invigorating its work in trade to assist the poorest and most marginalized countries to limit adverse disruptions from globalization and to enhance net benefits from it. IDA's work in this area emphasizes measures to improve the investment climate; enhance regional integration, particularly in Africa; strengthen competitiveness; remove barriers to the markets of industrial countries; and forge partnerships that enable acquisition of appropriate skills and infrastructure.

#### **4.3 INTERNATIONAL FINANCE CORPORATION**

The world was a different place when the International Finance Corporation (IFC) was established in 1956. No one spoke of emerging markets. There was no worldwide trend toward privatization, no communications revolution, no globalized economy. World population was less than half of what it is today. The economies of poor countries were still in very early stages of development, lacking the human resources, physical infrastructure and sound institutions needed to raise incomes and improve living standards. The responsibility for development was almost universally assigned to the public sector. Private sector investment in developing countries was small, and not much thought was given to increasing it. It was into this environment that IFC was born.

For several years officials of the World Bank had been supporting the creation of a new and different entity to complement their own. The Bank had been founded to finance post-World War II

reconstruction and development projects by lending money to member governments, and had been doing so effectively. Yet in its initial years, some senior staff had seen the need for creating a related institution to spur greater private sector investment in poor countries.

Major international corporations and commercial financial institutions at the time showed relatively little interest in working in Africa, Asia, Latin America or the Middle East. Entrepreneurs in these regions had few domestic sources of capital to draw upon and even less from abroad. They needed a catalyst.

At the 1944 Bretton Woods Conference that led to the creation of the Bank and the International Monetary Fund, initial proposals for this kind of support had been made—and rejected. These proposals would have given the Bank the ability to meet some of these goals by lending to private companies without government guarantees. Then, in the late 1940s, the concept was greatly refined by Bank President Eugene R. Black and his Vice President, former U.S. banker and General Foods Corporation executive Robert L. Garner.

Garner was an ardent believer in the role of private enterprise. Addressing the Inaugural Meeting of IFC's Board of Governors on November 15, 1956, he said, "I believe deeply that the most dynamic force in producing a better life for people, and a more worthy life, comes from the initiative of the individual—the opportunity to create, to produce, to achieve for himself and his family—each to the best of his individual talents. And this is the essence of the system of competitive private enterprise—20th century model—as it has been developed by the most enlightened and successful business concerns. It holds the promise of rewards according to what the individual accomplishes. It is based on

the concept that it will benefit most its owners and managers if it best satisfies its customers; if it promotes the legitimate interests of its employees; if in all regards it acts as a good citizen of the community. It is moved by the desire to earn a profit—a most respectable and important motive, so long as profit comes from providing useful and desirable goods and services. It is my belief that the best services and the best profits result from a competitive system wherein skill and efficiency get their just reward."

Garner worked with his assistant Richard Demuth and others to create a new private sector investment arm affiliated with the Bank, rather than having it lend directly from its own resources to the private sector. This new multilateral entity, at first internally termed the International Development Corporation, would be owned by governments but act like a corporation and be equally comfortable interacting with the public and private sectors. It would lend money, take equity positions and provide the technical expertise in appraising private investment proposals in developing countries, as the Bank was doing for public sector projects. It also would work alongside private investors, assuming equal commercial risks. In the process of removing some of the major barriers to new private investment in developing countries, it would encourage the domestic capital formation needed to create jobs, increase foreign exchange earnings and tax revenues, and transfer knowledge and technology from north to south.

The idea received its first official backing in the March 1951 report of a U.S. development policy advisory board headed by Nelson Rockefeller. This panel conceived of a package to add considerable value to the Bank's own product by encouraging the growth of

productive private enterprises that would contribute many key components to development. One such component, Garner wrote, was entrepreneurship "that elusive combination of imagination to see an opportunity and to mobilize the necessary resources to seize it." Another was the mobilization of new capital from private investors willing to take substantial risks in return for potentially large rewards. Others included job creation, new labor skills, management capacity and technological advances. In the process business owners in developing countries would "successfully transmute machines, labor and capital into a dynamic going concern, producing at a competitive cost goods of a quality that the market will accept." Garner actively marketed the concept. After the 1952 presidential elections, the United States reduced its support for the idea, eventually endorsing a modified proposal two years later that left IFC to start business with no equity investment powers (this provision was changed in 1961). Other nations then came aboard, and the Bank drafted the formal Articles of Agreement in 1955.

#### **4.3.1 IFC's Articles of Agreement**

The IFC Articles of Agreement came into force on July 20, 1956, when the requisite number of at least 30 member countries subscribing at least \$75 million to IFC's capital was attained. The initial total authorized capital was \$100 million. The first thirty-one member countries as of July 20, 1956 were: Iceland, Canada, Ecuador, United States, Egypt, Australia, Mexico, Costa Rica, Ethiopia, Peru, Dominican Republic, United Kingdom, Panama, Ceylon, Haiti, Guatemala, Nicaragua, Bolivia, Honduras, India, El Salvador, Pakistan, Jordan, Sweden, Norway, Japan, Denmark, Finland, Colombia, Germany and

France. On that date the capital subscriptions amounted to \$78,366,000. IFC's Articles of Agreement enshrined three critical principles. The founders insisted that IFC adopt a business principle, taking on the full commercial risks of its investments, accepting no government guarantees and earning a profit from its operations; be an honest broker, using its unique abilities as a corporation owned by governments to "bring together investment opportunities, domestic and private capital, and experienced management," and; play a catalytic role, investing only in projects for which "sufficient private capital is not available on reasonable terms."

#### **4.3.2 IFC Launched**

Robert L. Garner was appointed President of IFC by its Board of Directors on July 24, 1956. He holds the distinction of being the only person to hold the position of President of IFC without also being President of the World Bank. All of Garner's successors have been titled "Executive Vice President", with the President of the Bank being President of IFC also. Garner opened IFC's inaugural press conference the next day by saying that IFC was the first inter-governmental organization, which had as its main objective the promotion of private enterprise. He believed private enterprise to be the most effective and dynamic force for economic development. IFC would benefit not only the underdeveloped but also the industrial countries. There was increasing interest in overseas investment and expansion on the part of established companies in the developed countries. Private enterprise was the only weapon the free world possessed which the communists did not. That was one of the reasons, Garner said, why he welcomed the

establishment of this new organization, after several years of preparation.

#### **4.3.3 IFC Staff**

Garner appointed John G. Beevor to be Vice President of IFC, Richard H. Demuth, who had done much to foster the establishment of IFC, to be Assistant to the President, and Davidson Sommers to be General Counsel. Beevor had been engaged in preparatory work on the organization of IFC since March 1956, when he was released from his position as Managing Director of the Commonwealth Development Finance Company Limited of London to join the staff of the Bank. Demuth was Director of the Bank's Technical Assistance and Liaison Staff, and Sommers was the Bank's General Counsel. Both Demuth and Sommers had been associated with the Bank since 1946, and would continue to hold their positions in the Bank while serving in IFC. The Treasurer, Secretary, Director of Administration and Director of Information of the Bank were appointed to the same positions in IFC. Apart from its management, IFC's own staff consisted at the outset of an Engineering Adviser, with one assistant, and of eight operations officers, of six different nationalities. IFC also had its own administrative assistants.

#### **4.3.4 Initial Inquiries**

IFC received a large number and variety of inquiries and proposals with reference to possible investments in many of its member countries. As was inevitable with a new type of international financial organization, many inquiries were based on a misunderstanding of its purpose, which is to use its funds for investment in private enterprises, and not to finance transactions such as export credits, installment sales, ship mortgages, and the like. Other inquiries involving commercial or agricultural projects were declined in

view of IFC's policy to confine its activities, in the earlier years, to the field of industrial enterprise, which includes processing of agricultural products and mining. A number of investment proposals, which at first appeared promising, showed, after investigation, weaknesses of various types making them unsuitable for IFC financing. On the other hand, several proposals on which considerable work was done were postponed or withdrawn by the sponsors for various reasons. Some decided to do the entire financing them; some secured financing from other sources. A few were withdrawn because of inability to agree on financial terms.

#### **4.3.5 First Operations**

On June 20, 1957, IFC reached agreement for a \$2 million investment in Siemens do Brasil Companhia de Electricidade. This investment, together with the equivalent of \$8.5 million being invested by Siemens of Germany, was to be used to expand the plant facilities and business of Siemens do Brasil for the manufacture of electric generating equipment, switchgear, transformers, large motors and accessories for utility and industrial application as well as telephone equipment. This was the first integrated plant for manufacture of such a broad range of heavy electrical apparatus in Brazil.

On August 13, 1957, IFC reached agreement for an investment equivalent to \$600,000 in Engranesy Productos Industriales, S.A., a Mexican company owned by Mexican and American stockholders. The investment would help to expand the plant facilities and business for the manufacture and sale of a variety of industrial products and components, to include the addition of machine tooling for the manufacture of automotive and other mechanical parts, a forge shop, and an electric steel furnace.

#### **4.4      MULTILATERAL      INVESTMENT      GUARANTEE** **AGENCY**

As a member of the World Bank Group, MIGA's mission is to promote foreign direct investment (FDI) into developing countries to help support economic growth, reduce poverty, and improve people's lives. The development needs today are stark. Nearly 28 percent of the world's population—1.7 billion people live on less than a dollar a day. Billions of people live without access to safe drinking water or sewage treatment. Children can't attend school because there's no electricity to light classrooms in some countries, and no roads to get to school in others. The list goes on. Developing country governments cannot shoulder the burden—financially or technically—of addressing these needs alone. Foreign direct investors can play a critical role in reducing poverty, by building roads, for example, providing clean water and electricity, and above all, providing jobs. By taking on these tasks, the private sector can help economies grow and avert the need for governments to use funds better spent on acute social needs, while taking advantage of the opportunity to make profitable investments.

##### **4.4.1    MIGA and FDI**

Concerns about investment environments and perceptions of political risk often inhibit foreign direct investment, with the majority of flows going to just a handful of countries and leaving the world's poorest economies largely ignored. MIGA addresses these concerns by providing three key services: [political risk insurance](#) for foreign investments in developing countries, [technical assistance](#) to improve investment climates and promote investment opportunities in developing countries, and [dispute mediation](#) services, to remove possible obstacles to future

investment. MIGA's operational strategy plays to our foremost strength in the marketplace—attracting investors and private insurers into difficult operating environments.

The agency's strategy focuses on specific areas where we can make the greatest difference:

Infrastructure development is an important priority for MIGA, given the estimated need for \$230 billion a year solely for new investment to deal with the rapidly growing urban centers and underserved rural populations in developing countries.

Frontier markets—high-risk and/or low-income countries and markets—represent both a challenge and an opportunity for the agency. These markets typically have the most need and stand to benefit the most from foreign investment, but are not well served by the private market.

Investment into conflict-affected countries is another operational priority for the agency. While these countries tend to attract considerable donor goodwill once conflict ends, aid flows eventually start to decline, making private investment critical for reconstruction and growth. With many investors wary of potential risks, political risk insurance becomes essential to moving investments forward.

South-South investments (investments between developing countries) are contributing a greater proportion of FDI flows. But the private insurance market in these countries is not always sufficiently developed and national export credit agencies often lack the ability and capacity to offer political risk insurance.

MIGA offers comparative advantages in all of these areas—from our unique package of products and ability to restore the business community's confidence, to our ongoing collaboration with the public and private insurance market to increase the amount of insurance available to investors.

#### **4.4.2 Confidence, Security, and Credibility**

MIGA gives private investors the confidence and comfort they need to make sustainable investments in developing countries. As part of the World Bank Group, and having as our shareholders both host countries and investor countries, MIGA brings security and credibility to an investment that is unmatched. Our presence in a potential investment can literally transform a "no-go" into a "go." We act as a potent deterrent against government actions that may adversely affect investments. And even if disputes do arise, our leverage with host governments frequently enables us to resolve differences to the mutual satisfaction of all parties.

#### **4.4.3 Market Leader**

MIGA is a leader when it comes to assessing and managing political risks, developing new products and services, and finding innovative ways to meet client needs. But we don't stop there. We also provide expert advice to help countries attract and retain quality foreign investment, and a host of online services to make sure investors know about business opportunities in our developing member countries.

#### **4.4.4 Complex Deals**

MIGA can be the difference between make or break, by providing that all-critical lynchpin that enables a [complex transaction](#) to go ahead. MIGA offers innovative coverage of the nontraditional sub-

sovereign risks that often accompany water and other infrastructure projects. We can also cover interest rate hedging instruments, as we did for a power project in Vietnam, as well as provide capital markets guarantees, which we recently did for residential mortgage-backed securities in Latvia.

#### **4.4.5 Private Market**

MIGA complements the activities of other investment insurers and works with partners through its [coinsurance](#) and [reinsurance](#) programs. By doing so, we are able to expand the capacity of the political risk insurance industry to insure investments, as well as to encourage private sector insurers into transactions they would not have otherwise undertaken.

#### **4.4.6 Our Development Impact and Priorities**

Since its inception in 1988, MIGA has issued nearly 800 guarantees worth more than \$14.7 billion for projects in 91 developing countries. MIGA is committed to promoting socially, economically, and environmentally sustainable projects that are above all, developmentally responsible. They have widespread benefits, for example, generating jobs and taxes, and transferring skills and know-how. Local communities often receive significant secondary benefits through improved infrastructure. Projects encourage similar local investments and spur the growth of local businesses. We ensure that projects are aligned with World Bank Group country assistance strategies, and integrate the best environmental, social, and governance practices into our work.

MIGA specializes in facilitating investments in high-risk, low-income countries—such as in [Africa](#) and conflict-affected areas—which account for 42 percent of our portfolio. By partnering with the World Bank and others, MIGA is able to leverage finance for guarantee trust funds in these difficult or frontier markets. The agency also focuses on supporting complex infrastructure projects and promoting investments between developing countries.

MIGA's [technical assistance](#) services also play an integral role in catalyzing foreign direct investment by helping developing countries define and implement strategies to promote investment. MIGA develops and deploys tools and technologies to support the spread of information on investment opportunities. Thousands of users take advantage of our suite of online investment [information services](#), which complement country-based capacity-building work.

The agency uses its legal services to further smooth possible impediments to investment. Through its [dispute mediation program](#), MIGA helps governments and investors resolve their differences, and ultimately improve the country's investment climate.

#### 4.5 INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

On a number of occasions in the past, the World Bank as an institution and the President of the Bank in his personal capacity have assisted in mediation or conciliation of investment disputes between governments and private foreign investors. The creation of the International Centre for Settlement of Investment Disputes (ICSID) in

1966 was in part intended to relieve the President and the staff of the burden of becoming involved in such disputes. But the Bank's overriding consideration in creating ICSID was the belief that an institution specially designed to facilitate the settlement of investment disputes between governments and foreign investors could help to promote increased flows of international investment.

ICSID was established under the [Convention on the Settlement of Investment Disputes between States and Nationals of Other States](#) (the Convention) which came into force on October 14, 1966. ICSID has an Administrative Council and a Secretariat. The Administrative Council is chaired by the World Bank's President and consists of one representative of each State which has ratified the Convention. Annual meetings of the Council are held in conjunction with the joint Bank/Fund annual meetings.

ICSID is an autonomous international organization. However, it has close links with the World Bank. All of ICSID's members are also members of the Bank. Unless a government makes a contrary designation, its Governor for the Bank sits ex officio on ICSID's Administrative Council. The expenses of the ICSID Secretariat are financed out of the Bank's budget, although the costs of individual proceedings are borne by the parties involved.

Pursuant to the Convention, ICSID provides facilities for the conciliation and arbitration of disputes between member countries and investors who qualify as nationals of other member countries. Recourse to ICSID conciliation and arbitration is entirely voluntary. However, once the parties have consented to arbitration under the ICSID Convention, neither can unilaterally withdraw its consent. Moreover all

[ICSID Contracting States](#) whether or not parties to the dispute, are required by the Convention to recognize and enforce ICSID arbitral awards.

Besides providing facilities for conciliation and arbitration under the ICSID Convention, the Centre has since 1978 had a set of [Additional Facility Rules](#) authorizing the ICSID Secretariat to administer certain types of proceedings between States and foreign nationals, which fall outside the scope of the Convention. These include conciliation and arbitration proceedings where either the State party or the home State of the foreign national is not a member of ICSID. Additional Facility conciliation and arbitration are also available for cases where the dispute is not an investment dispute provided it relates to a transaction which has "features that distinguishes it from an ordinary commercial transaction." The Additional Facility Rules further allow ICSID to administer a type of proceedings not provided for in the Convention, namely fact-finding proceedings to which any State and foreign national may have recourse if they wish to institute an inquiry "to examine and report on facts."

A third activity of ICSID in the field of the settlement of disputes has consisted in the Secretary-General of ICSID accepting to act as the appointing authority of arbitrators for ad hoc (i.e., non-institutional) arbitration proceedings. This is most commonly done in the context of arrangements for arbitration under the Arbitration Rules of the [United Nations Commission on International Trade Law \(UNCITRAL\)](#), which are specially designed for ad hoc proceedings.

Provisions on ICSID arbitration are commonly found in investment contracts between governments of member countries and investors from other member countries. Advance consents by

governments to submit investment disputes to ICSID arbitration can also be found in about twenty investment laws and in over 900 [bilateral investment treaties](#). Arbitration under the auspices of ICSID is similarly one of the main mechanisms for the settlement of investment disputes under four recent multilateral trade and investment treaties (the North American Free Trade Agreement, the Energy Charter Treaty, the Cartagena Free Trade Agreement and the Colonia Investment Protocol of Mercosur).

Under the ICSID Convention, ICSID proceedings need not be held at the Centre's headquarters in Washington, D.C. The parties to an ICSID proceeding are free to agree to conduct their proceeding at any other place. The ICSID Convention contains provisions that facilitate advance stipulations for such other venues when the place chosen is the seat of an institution with which the Centre has an arrangement for this purpose. ICSID has to date entered in such arrangements with the [Permanent Court of Arbitration](#) at The Hague, the Regional Arbitration Centres of the Asian-African Legal Consultative Committee at Cairo and Kuala Lumpur, the [Australian Centre for International Commercial Arbitration](#) at Melbourne, the [Australian Commercial Disputes Centre](#) at Sydney, the [Singapore International Arbitration Centre](#), the GCC Commercial Arbitration Centre at Bahrain and the [German Institution of Arbitration](#) (DIS). These arrangements have proved their usefulness in many ICSID cases and have helped to promote cooperation between ICSID and these institutions in several other respects.

The number of [cases](#) submitted to the Centre has increased significantly in recent years. These include cases brought under the ICSID Convention and cases brought under the ICSID Additional

Facility Rules. In addition to its dispute settlement activities, ICSID carries out advisory and research activities relevant to its objectives and has a number of [publications](#). The Centre collaborates with other [World Bank Group](#) units in meeting requests by governments for advice on investment and arbitration law. The publications of the Centre include multi-volume collections of [Investment Laws of the World](#) and of [Investment Treaties](#), which are periodically updated by ICSID staff. Since April 1986, the Centre has published a semi-annual law journal entitled [ICSID Review-Foreign Investment Law Journal](#). The journal was recently rated as one of the top 20 international and comparative law journals in the United States.

Since 1983, the Centre has also co-sponsored, with the [American Arbitration Association](#) (AAA) and the [International Chamber of Commerce](#) (ICC) International Court of Arbitration, colloquia on topics of current interest in the area of international arbitration.

#### **4.6 SUMMARY**

The World Bank is a vital source of financial and technical assistance to developing countries around the world. Basically it is not a bank in the common sense. It is made up of two unique development institutions owned by 184 member countries; the International Bank for Reconstruction and Development (IBRD) and the [International Development Association \(IDA\)](#). Each institution plays a different but supportive role in our mission of global poverty reduction and the improvement of living standards. The IBRD focuses on middle income and creditworthy poor countries, while IDA focuses on the poorest countries in the world. It provides low-interest loans, interest-free credit and grants to developing countries for education, health, infrastructure,

communications and many other purposes.

#### **4.7 QUESTIONS FOR DISCUSSION**

1. Define World Bank and its role at international level.
2. What do you mean by International Development Association?  
Explain its functioning.
3. Explain the structure and role of International Finance Corporation.
4. Discuss the [Multilateral Investment Guarantee Agency](#) and International Centre for Settlement of Investment Disputes as the part of World Bank.

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## UNIT II

<b>LESSON</b>	<b>1</b> <b>INTERNATIONAL MARKETING ENVIRONMENT</b>
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### LESSON OUTLINE

- International marketing environment
- Risks involved in international marketing
- Economic environment
- Political and legal environment
- Cultural environment
- Tariff barriers
- Non-tariff barriers
- Summary

### LEARNING OBJECTIVES

*After reading this lesson  
you should be able to:*

- Various factors constituting international business environment
- Risks involved in international marketing
- Meaning and importance of analysis of international business environment
- Effects of various tariff and non-tariff barriers on international business

Liberalisation, privatisation and dynamic business activities taking place all over the world have lured many business firms to undertake international marketing activities. Even some national companies are merging to gain strength to enter into international marketing as no country or business enterprise can be sheltered from the winds of change and global competition. Therefore, the business

organisations, in order to cope up with these challenges, have to adapt and adjust accordingly.

When a business firm crosses its national frontiers to market its products or services, it is called 'International Marketing'. Thus, international marketing is the performance of business activities of a business firm in one or more countries other than its country of origin.

According to Terpstra, "International marketing can be defined as marketing carried across national boundaries."<sup>1</sup>

According to Cateora, "International Marketing is the performance of business activities that direct the flow of a company's goods and services to consumers or users in more than one nation for a profit."<sup>2</sup>

According to Ramaswami and Namakumari, "International Marketing involves all the activities that form part of domestic marketing. An enterprise engaged in international marketing has to correctly identify, assess and interpret the needs of the overseas customers and carry out integrated marketing to satisfy those needs."<sup>3</sup>

From the gist of these various definitions, it may be made out that the basic functions of international marketing as well as domestic marketing are the same but there are some specific characteristics that are unique in international marketing.

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<sup>1</sup>. Terpstra Vern, "International Marketing", Holt, Reinhart and Winston, 1977, p. 4.

<sup>2</sup>. Cateora Phillip R., "International Marketing", McGraw Hill, Irwin, 1997, p. 6.

<sup>3</sup>. Ramaswami V.S. and Namakumari, S., "Marketing Management: Planning, Implementation and Control", Macmillan India Ltd., New Delhi, 2004, p. 667.

## **INTERNATIONAL MARKETING ENVIRONMENT**

As international marketing involves in marketing across a firm's national boundaries, it has to confront with varying legal, political, cultural and sociological dimensions, which add many complexities to the task of marketing activities of the firm.

As international marketing management is the undertaking of the marketing management activities and functions keeping in mind as how to meet best the requirements of the customers of the countries to be served, this requires a detailed analysis of the likings and disliking of the customers, the prevailing product classes and standards etc. Thus, international marketing environment possess some new challenges in addition to the domestic marketing management challenges.

### ***MOTIVATION FOR INTERNATIONAL MARKETING***

The business firms enter into international marketing only when they perceive some factors, which motivate them to do so. If there exists no motivational factors for a firm to enter into international marketing, the firm would rather prefer to remain domestic.

According to Kotler and Keller, "Most companies would prefer to remain domestic if their domestic market were large enough. Managers would not need to learn other languages and laws, deal with volatile currencies, face political and legal uncertainties or redesign their products to suit different customer needs and expectations. Business would be easier and safer. Yet

several factors are drawing more and more companies into the international arena”<sup>8</sup>

From the above definition, it can be made out that it is not only the size of the domestic market which motivates the business firms to go in for international market, but, besides this, there are some other factors also which create attractions for international marketing.

There could be one or more of the following reasons which may influence a business firm's decisions to go in for international marketing.

1. **Higher profit margins for exports:** If the profit margins for exports are higher than in domestic sales, the firm may be attracted to export its produce than selling domestically.
2. **Under-utilisation of Capacity:** If the domestic sales are not sufficient enough to make the fullest utilisation of the installed production capacity of the firm, then these firms seek export orders in order to fully utilize their production capacity.
3. **Economies of Scale:** Sometimes, business firms also undertake exports to attain economies of scale of production, as the additional production required for exports will result into division of fixed costs over more number of units. Thus, this will bring in the economies of scale, as the cost per piece will reduce.
4. **Reduction of dependence on one market:** International marketing is also undertaken in order to lower down the risk involved while, marketing only domestically. Because in the domestic market, the demand may fall on account of local competition or some other factors. The foreign markets sales may reduce these risks.

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<sup>8</sup>. Kotler Phillip and Keller Kevin L., “Marketing Management”, Pearson Education, Pte. Ltd., Delhi, 2006, p. 617.

5. **Export obligation for obtaining imported inputs:** Sometimes, the government may impose export obligation on the firms, which want to import some inputs of production. This is done in order to attain balance of payments.
6. **Business Expansion:** Some firms undertake to exporting as an opportunity for business expansion as this way, the firms can expand their business and thus find new markets and hence more profits.

### **RISKS INVOLVED IN INTERNATIONAL MARKETING**

Despite of the various advantages or motivations for entering into international marketing, there are some business risks also which are associated with it due to the variations of business environmental factors from country to country. The firms must also weigh these risks before deciding for going in for international marketing.

According to Ramakumari and Namakumari, “The difference between domestic and international marketing is essentially environmental and cultural in character. And cultural diversity continues despite the world getting closer. Modern communication and transport systems have, no doubt, brought the nations of the world closer, but the cultural differences continue. So, understanding the cultural variances and nuances, and responding to them in a manner and style that is appealing to the foreign buyer becomes the crucial task. It is not enough if the international marketer communicates in the buyer’s language. Language is only one aspect of culture. A nation’s history, its social

and religious heritage, the value system of its people, the code of conduct handed down through generations – all these are components of a nation's culture. Moreover, culture is not a static entity. It undergoes a continuous evolution. So, sizing up the cultural dynamics of the different markets of the world is quite a difficult exercise. And that explains the difficulty of international marketing<sup>10</sup>.

The various types of risks involved in international marketing can be divided into the following categories:

- (a) Business Environmental Factors,
- (b) Foreign Exchange Regulations and Rates,
- (c) Tariff and Non-tariff barriers,
- (d) Balance of Payment conditions.

In this chapter the various types of risks relating only to business environmental factors have been discussed:

### **International Marketing Environmental Factors**

Each nation has its own culture, value, customs, attitudes, faiths, habits, taboos, languages, social organisations, classes and ethnic groups. Each of these elements varies from country to country. These various factors affect

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<sup>10</sup>. Ramaswami V.S. and Namakumari, S., "Marketing Management: Planning, Implementation and Control", Macmillan India Ltd., New Delhi, 2004, p. 668.

the life styles and the consumption patterns of its citizens. Therefore, the marketers, while designing their strategies for international marketing must take care of their needs, wants, requirements, tastes and preferences while entering into negotiations with them and doing business abroad.

There are the following three types of environmental risks involved in international marketing:

- (i) Economic Environment
- (ii) Political and Legal Environment
- (iii) Cultural Environment

**(i) Economic Environment**

Economic environment is filled with various factors like general economic conditions, market conditions, industrial structure, competitors and nature of competition; economic system, fiscal and monetary policies, financial facilities and constraints, level of economic development.

These various factors of the economic environment pose risks for many firms wishing to enter into international marketing, as they may not have adequate information and knowledge about these various factors.

**(ii) Political and Legal Environment**

Political environment includes political atmosphere and stability, political parties and their philosophies, government administration and policies concerning business and international policies of the government. Legal environment includes various types of laws. Therefore the various

factors relating to political as well as legal environment both have direct and immediate impact on marketing and seller-buyer relationships.

The marketing managers must take these political and legal factors into consideration. Particularly, the aspects to be considered are the political stability of the host country, their attitude toward foreign business firms and investments, importance of the company's product to the host nation, monetary regulations, currency convertibility, custom clearance procedures, price controls, efficiency of administrative system, nature of procedures concerned with imports, legal laws and restrictions pertaining to marketing mix decisions etc.

### **(iii) Cultural Environment**

Various nations differ among themselves on the basis of the prevailing cultural environment, which has an important bearing on the various consumption and marketing activities.

According to Louis, "Cultural environment refers to the traditions, Laws, rules and beliefs"<sup>11</sup>.

The international marketing offer must suit and fit the foreign customers' culture. The marketing programmes for international marketing must be developed keeping in mind the cultural environment of the import country.

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<sup>11</sup> . Louis Allen A., "Management and Organisation", Macstraw Hill, New York, 1958, p. 118.

The cultural differences pose a great challenge for the marketer and necessary adjustments must be made to cope with the cultural pattern of the buyers.

### **Tariff Barriers**

Tariff barriers are also a major factor of international marketing environment. Tariff barriers imposed by various nations demotivate the exports and imports of the items on which these countries impose some sort of tariffs or duties.

A tariff or duty may be levied either according to the value of the goods or according to its weight or quantity. The former type of duties is known as ad-valorem duty and the later is a specific duty. An ad-valorem duty is charged as a fixed percentage of the imported/exported article.

The various types of tariff barriers have been discussed below.

- a) **Export duties:** Export duties are imposed on those items, which are scarce in the exporting country itself or in order to provide exhaustible natural resources for domestic industries. Certain countries levy export duties to collect funds for defraying the expenses of export promotion activities. Sometimes the duties are levied to charge higher prices from foreigners for the commodities, which are in short supply.
- b) **Import duties:** One of the important purposes of import duties is to obtain revenue for the public treasury. Tariffs are also very popular for

protecting domestic industries from foreign competition. The protection of domestic industries is very essential for the development of a country. Domestic industries may also require protection against the aggressive and unfair practices of foreign competitors. In recent years, tariffs are often employed to restrict imports with a view to correcting disequilibrium in the balance of payments.

In order to achieve uniformity amongst countries as to customs duties and other levies, products have been grouped into various categories, depending upon the material of which they are made. The nomenclature system has been worked out by an international committee of experts under the aegis of the Customs Co-operation Council. This classification of goods adopted by them came to be known as the Brussels Tariff Nomenclature (BTN), which is presently being followed by a number of countries when they impose customs duties for imported goods.

- c) ***Transit duties:*** Transit duties were very common during the period of mercantilism and in the early nineteenth century. At that time, transportation was very slow and costly. The use of the shortest route, therefore, was very important. Countries situated in a favourable geographical position fully exploited their position and levied heavy transit duties on the merchandise passing through their territories. Progress in the field of transportation during the nineteenth century robbed transit duties of their earlier profitability and decreased the incentive for their maintenance. Another important factor, which led to the elimination of transit duties, is the desire among nations for international economic co-operation. The burden of transit duties is

borne either by the consumers in the importing country or by the producers in the exporting country, depending upon the conditions of demand and supply in the two countries. Transit duties, like other duties, have a tendency to restrict the volume of world trade.

- d) ***Anti-dumping duties:*** Dumping is the practice of selling goods abroad at a price below their normal price (or even below their marginal cost). The purpose of this may be to maintain a stable or oligopolistic domestic market structure by disposing of temporary surpluses abroad, or as a means of disrupting the domestic market of a foreign competitor. Anti-dumping duty is levied when the selling price of an important product is lower than the normally prevailing domestic price. To meet a situation of this nature whenever it arises, most countries, under their own legislation, have the power to impose anti-dumping duties on the ground of injury to their domestic industries. Anti dumping duties normally take the form of additional import duties and charges.
- e) ***Countervailing duties:*** Countervailing duties are levied in the same way as anti-dumping duties, and the explanation for their levy is generally the charge that imports from a specified country are directly or indirectly subsidised. The amount of countervailing duty normally corresponds to the amount of the subsidy. The intention of this levy is to neutralise the benefit of export subsidy given by the exporting country to its exporters.

### **Non-Tariff Barriers**

A non-tariff barrier is any measure other than a tariff that raises an obstacle to the free flow of goods in the overseas market. Non-tariff barriers are normally erected in the form of prior import deposits, import quota/licensing, foreign exchange regulations, exchange formalities, government

procurements, state trading, health and safety measures, canalisation of trade, preferential arrangements, trading blocks, technical and administrative regulations, economic and political wards.

A government to protect its domestic market or to avoid the balance of payment conditions to go unfavourable generally imposes non-tariff barriers.

- i) ***Prior Import Deposits:*** Some countries impose a condition that importers in their countries should deposit money upto 100 percent of the value of their imports in advance with any specified authority, normally their Central Bank. Such deposits are generally for a specific period; and whenever any country introduces such a policy, its government ensures that the required amount has been deposited before the issue of an import licence.
- ii) ***Quantitative Restrictions Through Quota Licence System:*** Quantitative restrictions are normally imposed in the form of quotas and import licences, or a combination of both. Quotas are generally global, bilateral or historical, and are based on imports during the previous period. These are often more selective than tariffs and tend to be adjusted more frequently. Under this system, the importing country specifies the quantities of a commodity that would be allowed to import from various countries. The fixation of quotas depends on the relationship of the importing country with the supplier of the commodity.
- iii) ***Foreign Exchange Regulations:*** Exchange control methods have been widely used by a number of countries to regulate imports, and are usually adopted by most of the developing nations who experience an

unfavourable balance of payments. Under this scheme, the importer has to ensure that adequate foreign exchange is available for import of goods by obtaining a clearance from the exchange control authorities prior to the concluding of a contract with the supplier.

- iv) ***Consular Formalities:*** A number of importing countries demand that consular documents – such as certified invoices, import certificates, etc. – must necessarily accompany the shipping documents. Sometimes, they even insist that such consular documents should be drawn in the languages of the importing countries. The fees payable for such documentation are often quite high, sometimes up to 3 percent of the f.o.b. value of a product. Heavy penalties are levied by importing countries if there are any errors in documentation.
- v) ***Technical and Administrative Regulations:*** These regulations are in respect of physio-sanitary and veterinary regulations, technical visas, food and drugs regulation—often in the language of the importing country. Administrative regulations take the shape of technical standards, e.g., of electrical goods, machinery, etc. and the countries practising such regulations insist that the exporters should strictly adhere to the same standards laid down by them. In the case of pharmaceutical products, the importing countries normally specify the pharmacopoeic standards that should be satisfied before their import is permitted. Such specifications exclude the import of commodities, which, though of good quality do not conform to standards that have been laid down. Often, documentation formalities relating to technical and administrative regulations are difficult and time-consuming, and even a minor error or omission may result in the holding up of goods by the customs authorities of the importing country. These technical and administrative regulatory measures impede the free flow of internal trade to a large extent.

- vi) ***Health and Safety Regulations:*** Many countries impose strict health and safety regulations on the import or sale of products, particularly food products. Regulations based on environmental considerations are becoming increasingly. A specific duty is a fixed sum of money charged upon each unit of the commodity imported. Some times specific and Ad Valorem duties are simultaneously levied on a commodity. A duty in which both these forms of duties are combined is generally known as the compound or mixed tariff.

**(d) Balance of Payment Conditions**

Some times if the balance of payment conditions of country goes unfavourable, in order to control it, the government imposes some restrictions on the import of some items. This may result into unfavourable conditions for the exporters in these markets.

Balance of payment and balance of trade are discussed side by side in order to understand the basis differences between the two.

Balance of trade describes the difference between merchandise exports and merchandise imports of a country. If the volume of merchandise exports exceeds imports then it is favourable balance of trade otherwise unfavourable balance of trade.

Favourable balance of trade is not necessarily a symptom of prosperity. Balance of trade represents only one of the various components of foreign transactions.

Balance of payment of a country has been defined as systematic record of all economic transaction between the residents of reporting country with the rest of the countries of global. Balance of payment is very wide term and it includes both visible and invisible transactions. The payment made for merchandise imports and receipts for merchandise exports, loans to and investments in foreign countries and enterprises, foreign investments in domestic enterprises, borrowings from foreign countries, tourists' expenditures of the citizens of reporting country made abroad and that made by foreign tourists in the reporting country. Money paid to the foreign carriers and receipts for carrying foreign goods, Insurance premiums, cable and telephone payment made to foreign agencies and received from the foreign countries by these agencies of the reporting countries, commission and exchange charges received by the banks of the reporting country, and paid to the foreign country's banks. Besides the above, balance of payment includes all the other expenses made by the citizens of the reporting country in foreign land.

The two sides of the balance of payment must always balance. If a country has more receipts than expenditure, it is called to have positive balance of payment and if has to make more payments than receivables then it is

negative balance of payment. Balance of payment is considered to be the economic barometer of a country's health. Balance of payment can also be used to evaluate a country's international solvency and to determine the appropriateness of the external value of its currency.

There are two types of transactions viz. autonomous and induced. The autonomous transactions take place as a matter of routine and if there is a deficient i.e. (positive or negative balance of payment) then the same is adjusted by induced transactions of compensatory transactions. The example of compensatory transaction is official borrowings, grant, received from abroad and changes in the country's foreign exchange reserves.

#### SUMMARY

International marketing is the performance of business activities that direct the flow of a goods and services to consumers or users at one or more foreign countries. The basic functions of international marketing as well as domestic marketing are the same but there are some specific characteristics, which are unique in international marketing.

When a company operates in a large number of countries by making necessary adaptations or adjustments to its products and the various other components of the marketing mix, it tends to become a global company.

The business firms enter into international marketing when they perceive some factors, which motivate them to do so. If there are no motivations for a firm to enter into international marketing then the firm rather prefers to remain domestic.

The various factors, which may motivate the business firm to enter into international marketing are: higher profit margin for exports, under utilisation of capacity, economies of scale, reduction of dependence on one market, export obligation for obtaining imported inputs and business expansion.

Despite of various advantages of international marketing, there are many risks also which are mainly due to varying business environment among the different countries of the globe. These risks relate to business

environment factors, foreign exchange regulation and rates, various tariff and non-tariffs barriers and balance of payments conditions etc. The firm must weigh these various risks before deciding for going in for international marketing.

#### REVIEW QUESTIONS

1. What do you understand by international marketing environment? Discuss its and importance.
2. What are the various risks involved in international marketing?
3. Discuss the various environmental factors which affect the international marketing.
4. What are tariff barriers? How they effect international marketing operations.
5. What are non-tariff barriers? How they effect international marketing operations.
6. What do you understand by the term balance of payment?
7. How balance of payment effect international marketing of a country?
8. Discuss in detail the various motivational factors for a firm for entering into international marketing.
9. Discuss the various factors which business firms should take utmost care of while undertaking international marketing operations.
10. Define international marketing environment. Distinguish between the marketing environment for domestic marketing and international marketing.

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## UNIT II

<b>LESSON</b>	<b>2</b> <b>POLITICAL AND LEGAL SYSTEMS</b>
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### LESSON OUTLINE

- Political environment
- Political risks
- Managing political risks
- The legal environment
- International marketing and legal systems
- Legal issues in international marketing
- Summary

### LEARNING OBJECTIVES

*After reading this lesson  
you should be able to:*

- Meaning and importance of political environment
- To understand the various political risks
- To learn about the prevailing legal systems in the world
- To understand the importance of the legal issues for international marketing management

The global environment of business continues to pose new challenges for managers. Today businesses are pursuing a variety of international business activities (not just exporting and direct investment) in order to achieve a complex set of motives. The global marketplace is becoming increasingly crowded by a constant flow of new entrants from new countries. Managers are busily forming international partnerships in search of synergistic alliances in procurement, distribution, marketing, and technology.

These dynamic elements of the global marketplace are compelling firms to rethink their organizational structures, business processes, and market positioning. The more alert managements turn to market research and intelligence for staying abreast of customer and product markets. Many are searching for best practices, and they benchmark against the very best in their industry globally. In an era of substantial outsourcing and collaborations, managers are also sharpening their interorganizational partnering skills.

There are several stages through which a firm may go as it becomes increasingly involved across borders. A purely domestic firm focuses only on its home market, has no current ambitions of expanding abroad, and does not perceive any significant competitive threat from abroad. Such a firm may eventually get some orders from abroad, which is seen either as an irritation (for small orders, there may be a great deal of effort and cost involved in obtaining relatively modest revenue) or as "icing on the cake." As the firm begins to export more, it enters the export stage, where little effort is made to market the product abroad, although an increasing number of foreign orders are filled. Such firms which are involved in international marketing are suggested to various types of legal and political systems which pose many opportunities as well as threats.

All firms entering international business start with just exporting and later on reach to the international stage. As certain country markets begin to appear especially attractive with more foreign orders originating there, the firm may go into countries on an ad hoc basis—that is, each country may be entered sequentially, but with relatively little learning and marketing efforts being shared across countries. In the multi-national stage, some efficiency is pursued by standardizing across a region (e.g., Central America, West Africa, or Northern Europe). Finally, in the global stage, the focus centers on the entire

World market, with decisions made optimize the product's position across markets—the home country is no longer the center of the product. An example of a truly global company is Coca Cola.

The various political and legal systems and environment confronted by the multinational market firms has been discussed below:

### **The Political Environment**

An international business entity is a guest of the host country and, therefore, the host country reserves the right of not only allowing it access but also of expropriating it. It also can influence the scale and dimensions of the operations through its policies. Political risk is thus the vulnerability of returns of a project to the political acts of a sovereign government.

While the economic and financial environments are of critical importance to the MNC, the political environment and the prevailing legal systems also influence most international business activities. Almost from the beginning of multinational business operations, MNCs have been regarded as threats to national sovereignty, and while the zenith of this outlook probably occurred in the 1970s, it is still alive and flourishing in the 1990s. Naturally, different ideologies will be reflected in different economic systems, with the People's Republic of China and the USA being at opposite ends of the spectrum. While the number of centrally planned economies has shrunk rapidly following the massive political changes in Eastern Europe, a new factor may be the rise of the fundamentalist Moslem

approach to state management of the political and economic environments.

Another facet of the political environment, which has come to the fore in recent years, has been the involvement of governments in different areas of business. For example, in virtually every industrialized country the government controls the postal services and the railways. During the 1980s, however, there has been a boom in privatization, particularly in telecommunications, energy, steel and shipbuilding.

Finally, the force of nationalism can never be ignored. While this was relatively dormant during the period 1975-86, it has become a very potent factor in Europe, with a significant number of former Soviet client states regaining sovereignty. Perhaps as a result, nationalism has also raised its profile within the EC affecting, for example, Catalonia, Brittany, Belgium (Flemings and Walloons), Scotland and the Basque Country.

### **Political Risks**

The principal concept used by international businessmen in appraising the political environment is known as political risk. This expresses itself through government-inspired events and actions that impact on the international companies working within a particular state. Political risk can be defined as: 'the risk of loss of assets,

earning power, or managerial control due to events or actions that are politically based or politically motivated’.

The immediate association of political risk is with developing countries in terms of nationalization and expropriation of assets, but it is also present in industrialized countries, as the following examples may demonstrate:

- The election of conservative Prime Minister Thatcher in the United Kingdom in 1979.
- The election of socialist President Mitterrand in France in 1981.
- The accession of Portugal and Spain to the EC in 1986.
- The accession of Portugal and Spain to the EC in 1986.
- The reunification of Germany in 1990.
- The great mass of political decisions by member states upon which the whole concept of the Single European Market (1992) rests.

Perhaps the most difficult political risk assessment the MNC must make is when it contemplates its initial entry into a particular country. Daniels and Radebaugh (1986) suggest a simple check-list for the primary appraisal:

1. What is the political structure of the country?
2. Under what type of economic system does the country operate?

3. Is my industry in the public or private sector?
4. If it is in the public sector, does the government also allow private competition in that sector?
5. If it is in the private sector, is there any tendency to move it toward public ownership?
6. Does the government view foreign capital as being in competition or in partnership with public or local private enterprises?
7. In what ways does the government control the nature and extent of private enterprise?
8. How much of a contribution is the private sector expected to make in helping the government formulate overall economic objectives?

If the situation is especially complex, or if the new foreign investment is very large, most MNCs would move beyond such a simple assessment and call on the assistance of specialist political risk assessment consultants, most of whom have had extensive previous experience working with or within government or international bodies like the UN or the World Bank.

## **Assessing Political Risks**

It has been observed that international managers when entering new markets recognize the existence of political risk but refuse to give it the required significance. This is more so because although the existence of political risk has been widely accepted, the definition of political risk does not explain whether such risk is country specific or firm specific. Here the discussion entails assessment of both country specific risk and firm specific risk.

### **Country Specific Risks**

Country specific risk refers to risk arising out of doing business with a specific country.

- What is the current political system in existence?
- What is the stability and permanency of government policy?
- What are the encouragements the business firms will receive as a result of political activity?

### **Firm Specific Risk**

Although business units undertake country risk assessment they have realized that political risk does not manifest itself equally among various firms. This is the major assumption underlying country risk assessment. It has been observed that sometimes firms in the same country receive differential treatment.

It is commonly believed that firm specific political risk arises because of the following:

- size and visibility
- product handled
- attitude of the company.

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## **Management of Political Risk**

The insecurity arising out of political risk especially, risk of loss of investment and information, in foreign lands can be minimized through proper management of political risk. Political risk management process can be undertaken either before the investment is made or after the investment is made. The former refers to pre-investment planning whereas the latter refers to post-investment planning.

### **Pre-investment Planning**

Under the pre-investment planning for political risk management, four options are available to the international marketer. They are:

- Avoidance
- Insurance
- Negotiating the Environment
- Structuring the Investment

### **The Legal Environment**

The legal environment within which MNCs have to conduct operations could be regarded as a subset of the political environment, as the two are completely intertwined. However, the legal factors are put in a separate section here to emphasize their importance.

Unfortunately for MNCs, they do not work within a single, unified international legal environment; on the contrary, an MNC faces a different legal context in every country within which it operates. These codes are usually put in place by governments in an attempt to control the amount, rate and impact of both outward and inward investment.

- *Industrial intellectual property rights*: this includes all aspects of trade names, trade secrets, copyrights and patents. As business has become progressively internationalized, so MNCs and their home governments have brought pressure to bear – particularly, but not solely, on developing countries – to bring regulations into line with those of the industrialized countries. In industries like pharmaceuticals, MNCs often refuse to set up manufacturing or R&D facilities in countries with insufficient safeguards in this sphere.
- *Trade obstacles*: this includes tariffs and quotas, which are usually clearly laid down by regulations, and other less well-defined factors. A good example here is product labeling where the requirements are not only legal, but also culture-bound; for instance, foreign companies trading in France must produce all labels, warranties, instructions, etc. in French. Also, in the pharmaceutical industry, safety and efficacy regulations show a bewildering variety from one country to another, with no individual country's standards being acceptable in another.

- *Product liability*: this has been a boom area for the legal profession in many industrialized countries in the last ten years, though this is hardly surprising when the long list of product manufacturing problems is considered. Again, the pharmaceutical industry could be quoted as a case in point, although the most spectacularly disastrous example must be the Bhopal incident. In 1984, an explosion occurred at Union Carbide's plant at Bhopal in India, as a result of which poisonous emissions killed over 2,000 people. As a result; not only were Indian regulations tightened up, but also there was a wave of environmental legislation throughout the industrialized world.
- *Monopoly and restrictive trades practices*: this type of legislation is common throughout the developed world. US regulations are regarded as tightest, followed by Germany, However, unlike other areas of legislation, there is a move towards uniformity here, with the EC taking the lead in the approach to the Single European Market.

### **Home-Country Legislation**

This includes all legislation passed in a particular country to regulate the activities of MNCs based in that country while operating overseas. The best-known example is the US Foreign Corrupt Practices Act, which was passed following a number of highly publicized bribery cases in the 1970s involving American

multinationals. It forbids US firms giving bribes or any other questionable payments anywhere in the world as these are regarded as 'ethically repugnant' (President Carter's words) and bad for the international reputation of American business.

### **International Marketing and the Legal Systems**

Every business operates within the jurisdiction of legal system. The legal system is an inevitable component of the environment within which a business operates. The commercial law existing within any country influences not only each and every variable of marketing mix but also the environment within which a business operates. This has a direct bearing on the management of global marketing plan. Thus for example, the advertising laws in West Germany are so strict that it is best advised for the international marketer to get himself good legal counsel before framing his advertising strategy in West Germany. In fact all over Europe, there exists different set of laws preventing promotion of products through price discounting. These laws are based on the premise that such practices differentiate buyers. This example reflects the influence on only one of the variable of marketing mix. Laws may exist for other variables of marketing mix viz. product, price, and place. Thus monitoring the legal environment is also essential. International business came out with an article indicating areas where

management should consider the laws before framing their strategy.

They include watching out for rules regarding:

- Retail price maintenance
- Product quality
- Packaging
- After sales commitment
- Price controls
- Property rights, which include immovable property and patent & trade, mark regulations.
- Cancellation of agreements

### **The Development and Scope of International Law**

The domestic marketer is aware of the jurisdiction of the legal system and the bearing it has on his activities. But when he crosses national frontiers to market or produce his product in a host country; the problem of legal system arises on two counts. They are:

- a) Every country has its own legal system.
- b) The legal systems of the world are not harmonized and are in fact based on contradicting political philosophers.

The legal system that exists in different countries of the world are antecedents of one of the two legal philosophies. They are common law and code law philosophies.

### **Legal Issues in International Marketing**

The field of international law is wide and cannot be dealt with fully here. However, certain issues like entering into contract, the method at seeking recourse, protecting property rights, tax laws, and foreign exchange are some of the major issues facing the international marketer. These issues can be illustrated as under:

The decision to market product across the national frontier imply that agreements have to be entered into with parties on the other side. For this legal counsels advice on contract act as it exists in the foreign land is absolutely essential.

Not only must the marketer be aware of laws regarding contract, and termination of contracts but he must also be aware of the legal formalities that he is subjecting himself to. Thus as per Coelso Doctrine a person desirous of doing business in Latin America must agree to subject himself as a national. This has important bearings for an executive doing business with Latin American countries. The entry decision may be influenced to a great extent by such laws as they exist in that country.

A marketer must also be aware of and monitor laws regarding product quality, packaging, price control, retail price maintenance, after sales service. If it he wishes to continue his marketing efforts in that country.

## **SUMMARY**

Although a firm regards it as an economic entity it is drawn and affected by political developments. It therefore becomes necessary for the firm, particularly an international firm to monitor not only the domestic but also the international political environment. Since the international business firm operates in a host country and as a guest of that country, it becomes particularly important for it to monitor the developments taking place in the domestic political environment of the host country.

The three main concerns facing any international business entity are political stability, the government's orientation and nationalism.

While political stability is necessary for a business entity, it is particularly important for an international marketing firm because they reflect the success or failure of any business concern, for political stability is often associated with stability of economic policies. The other concerns facing international business are orientation of the government and nationalism. The orientation of the government can very often reveal whether international marketing can survive in that country or not. Nationalism also influences this variable because the business entity has to exist and operate within that country. These concerns, through their impact, give rise to political risks.

The legal systems in different countries of the world are by no means identical. This difference between code law and common law puts the international marketing firms into various types of legal complications.

A marketer must also be aware of and monitor laws regarding product quality, packaging, price control, and retail price maintenance and after sales service etc.

### **IMPORTANT QUESTIONS**

1. What do you understand by the term 'Political Environment'?
2. Discuss the importance of political environment for international marketing management.
3. What are the various types of political risks for international marketing? How a business firm can assess the political risks?
4. How political risks can be managed?
5. Define and elaborate term, 'Legal Environment'.
6. Discuss the international marketing and legal systems.
7. Discuss the development and scope of international law.
8. Discuss the various legal issues relating to international marketing.
9. Discuss the various political risks which are firm specific.
10. Briefly summarise the various issues concerning international marketing on account of political and legal environment.

## UNIT II

<b>LESSON</b>	<b>3</b> <b>MULTILATERAL AND GEOGRAPHICAL GROUPINGS</b>
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### LESSON OUTLINE

- Patterns of Multilateral and Geographical Groupings
- Regional Co-operative Groups
- Free Trade Area
- Customs Union
- Common Market
- Political Union
- Major Multilateral and Geographical Economic Groups
- Conflict between Multilateralism and Regionalism
- Summary

### LEARNING OBJECTIVES

*After reading this lesson  
you should be able to:*

- The rationale of cross border trade and forms of economic groupings.
- Patterns of regional economic groups for cross border trade.
- Major forms of multilateral and geographical economic groups.
- Major Geographical and Multilateral groups of the world.
- Conflict between multilateralism and regionalism.

Among the important global trends today is the evolution of the multinational market region – those groups of countries that seek mutual economic benefit from reducing intraregional trade and tariff barriers. Organizational form varies widely among market regions, but the universal orientation of such multinational cooperation is economic benefit for the participants. Political and social benefits sometimes accrue, but the dominant motive for affiliation is economic, as countries, all over the world, now look for economic alliances to expand their access to free markets.

Regional economic cooperative agreements have been around since the end of World War II. The most successful has been the European Community (EC), the world's largest multinational market region and foremost example of economic cooperation.

Multilateral and Geographical market groups form large markets that provide potentially significant market opportunities for international business. When it became apparent that the EC was to achieve its long-term goal of a single European market, a renewed interest in economic cooperation was sparked. The European Economic Area (EEA), a 17-country alliance between the European Union (EU) and members of EFTA (European Free Trade Area), became the world's largest single unified market. Canada, the United States, and Mexico entered into a free-trade agreement to form NAFTA (North American Free Trade Agreement). Many countries in Latin America, Asia, Eastern Europe, and elsewhere are either planning some form of economic cooperation or have entered into such agreements. With the dissolution of the USSR (Soviet Union) and the independence of Eastern European countries, linkages among the independent states and republics are also forming. The Commonwealth of Independent States (CIS) is an initial attempt at realignment into an economic union of some of the Newly Independent States (NIS)-former republics of the USSR.

The growing trend of economic cooperation is increasing concerns about the effect of such cooperation on global competition. Governments and businesses are concerned that the EEA, NAFTA, and other cooperative regional groups have become regional trading blocs without trade restrictions internally but with borders protected from outsiders.

### **Patterns of Geographical and Multilateral Groupings**

Many countries of the world started forming some multilateral market groups which are mainly based on their geographic locations. These groups took several forms, varying significantly in the degree of cooperation, dependence, and inter relationship among participating nations. There are five fundamental groupings for regional economic integration ranging from regional cooperation for development, which requires the least amount of integration, to the ultimate integration of political union.

**Regional Cooperation Groups:** The most basic economic integration and cooperation is the regional cooperation for development (RCD). In the RCD arrangement, governments agree to participate jointly to develop basic industries beneficial to each economy. Each country makes an advance commitment to participate in the financing of a new joint venture and to purchase a specified share of the output of the venture. An example is the project between Colombia and Venezuela to build a hydroelectric generating plant on the Orinoco River. They shared jointly in construction costs and they share the electricity produced.

**Free-Trade Area (FTA):** A free-trade area requires more cooperation and integration than the regional cooperation of groups. It is an agreement among two or more countries to reduce or eliminate customs duties and nontariff trade barriers among partner countries while members maintain individual tariff schedules for external countries.

The FTA consists of a number of countries within which trade is free in the sense that customs duties are not levied at the frontier on trade but in practice it is limited to specified products with specified exceptions.

Essentially, an FTA provides its members with a mass market without barriers that impede the flow of goods and services. The United States has free-trade agreements with Canada and Mexico (NAFTA) and separately with Israel.

The seven-nation European Free Trade Association (EFTA), among the better-known free-trade areas, still exists although five of its members also belong to the EEA.

**Customs Union:** A customs union represents the next stage in economic cooperation like FTA, there are no internal tariff barriers on intra-union trade. The customs union is a logical stage of cooperation in the transition from an FTA to a common market. The European Community was a customs union before becoming a common market. Customs unions exist between France and Monaco, Italy and San Marino, and Switzerland and Liechtenstein.

**Common Market:** Common market is the succeeding stage of economic integration. A common market agreement eliminates all tariffs and other restrictions on internal trade, adopts a set of common external tariffs, and removes all restriction on the free flow of capital and labor among member nations. Thus a common market is a common marketplace for goods as well as for services (including labor) and for capital. It is a unified economy and lacks only political unity to become a political union.

The European Economic Community (EEC) is the most successful experiment so far as a common market is concerned. The Treaty of Rome (which established the European Economic Community) called for common external tariffs and the gradual elimination of intra-market tariffs, quotas, and other trade barriers. The treaty also called for elimination of restrictions on the movement of services, labor, and capital; prohibition of cartels; coordinated monetary and fiscal policies; common agricultural policies; use of common investment funds for regional industrial development; and similar rules for wage and welfare payments.

Latin America boasts two common markets, the Central American Common Market (CACM) and the Andean Common Market. Both have roughly similar goals and seek eventual full economic integration.

**Political Union:** Political union is the most fully integrated form of regional cooperation. It involves complete political and economic integration; it may be voluntary or enforced. The most notable enforced political union was the Council for Mutual Economic Assistance (COMECON), a centrally controlled group of countries organized by the USSR. With the dissolution of the USSR and the independence of Eastern Europe, COMECON was disbanded.

The Commonwealth of Nations is a voluntary organization providing for the loosest possible relationship that can be classified as economic integration. The British Commonwealth is comprised of Britain and countries formerly part of the British Empire. Its members recognize the British Monarch as their symbolic head although Britain has no political authority over the Commonwealth. Its member states had received preferential tariffs when trading with Great Britain but, when Britain joined the European Community, all preferential tariffs were abandoned. The Commonwealth can best be described as the weakest of political unions and is mostly based on economic history and a sense of tradition. Heads of state meet every three years to discuss trade and political issues they jointly face, and compliance with any decisions or directives issued is voluntary. Two new political unions have come into existence in this decade, the Commonwealth of Independent States (CIS), made up of the republics of the former USSR, and the European Union (EU).

The European Union was created when the 12 nations of the European community ratified the Maastricht Treaty. The members committed themselves economic and political integration. The treaty allows for the free movement of goods, persons, services, and capital throughout the member

states; a common currency; common foreign and security policies, including defense; a common justice system; and cooperation between police and other authorities on crime, terrorism, and immigration issues. However, not all the provisions of the treaty have been universally accepted. The dismantling of border controls to permit passport-free movement between countries, for example, has been implemented by only 7 out of 15 EU member states.

## **MAJOR MULTILATERAL AND GEOGRAPHICAL GROUPING**

### **European Union (EU)**

The *most* successful regional economic grouping so far has been the EU. The *EU*, earlier known as European Common Market, was formed as a result of the Rome Treaty signed in 1957 and came into existence on January 1, 1958. The basic objective was to accelerate economic growth and promote stability within the member-countries through free movement of trade as the initial step. The original members were: Belgium, France, Germany, Italy, Luxembourg and Netherlands. Subsequently, the U.K., Ireland, Denmark, Spain, Greece and Portugal joined the ECM. (It later changed its name to European Economic Community and it became European Union on January 1, 1993.) Austria, Finland and Sweden have joined the Union with effect from January 1995.

The *EU*, after 1992, is the largest, most developed consumer market in the world with a population of 370 million, as against a population of 261 million in the USA and 125 million in Japan. The per capita income varies from \$ 11,030 for Portugal which is the lowest to \$ 42,930 for Luxembourg which is the highest. The Union also accounts for about 40 per cent of world trade. The somewhat disconcerting fact for the non-EU countries is that an

increasing proportion *of* the trade is being accounted for by the intra-group trade.

The Treaty *of* Rome, 1957 which established the grouping, envisaged establishment *of* a common market comprising all the member-countries, where people, goods, services and capital could move freely. There have been no intra tariffs from 1968 when a customs union was formed. But it still falls short of being a single market; for example, in financial services, technical standards and mutual recognition of professional qualifications.

In February 1986, the twelve member-countries signed the Single European Act, whose objective was to create a market without borders on January 1, 1993. This involved, among other measures, elimination of technical and tax barriers as well as various types of national trade protection measures then being administered by the member-countries.

The EU has negotiated various types of trade agreements and co-operation agreements with a very large number of countries. The European Union is linked by bilateral free-trade agreements to the countries in Central and Eastern Europe, a group of which are linked by CEFTA, while another group is linked by the Baltic Free- Trade Area. The EU is negotiating second-generation bilateral free-trade agreements based on a reciprocal exchange of preferences with partners in the Mediterranean and North Africa, as part of the process of establishing a Euro-Med free trade area by 2010. The EU also concluded a free-trade agreement with South Africa and with Mexico which entered into force in 2000. The EU has also proceeded with discussions with the Gulf Cooperation Council (GCC). India has also signed a trade and economic co-operation agreement with the EU. This provides for mutual co-operation in economic, agricultural and industrial development in addition to preferential trade

### **European Free Trade Area (EFTA)**

The EFTA was formed at the same time as the EEC, almost as a counter-measure. The UK, Portugal, Ireland and Denmark left it to join the EEC. Austria, Finland and Sweden left it to join the EEC with effect from January 1, 1995. The EFTA now continues with Iceland, Liechtenstein, Norway and Switzerland.

The EEC and EFTA have formed a European Trading Area where trade in industrial products is free of all tariffs. The EFTA is pursuing free trade, agreements with extra-regional trade partners notably with Canada and Mexico.

### **North American Free Trade Area (NAFTA)**

The goal of NAFTA, the world's largest free trade area, is to eliminate barriers to trade and investment between the three countries, the U.S.A., Canada and Mexico. The implementation of NAFTA on January 1, 1994, brought the immediate elimination of tariffs on more than one half of U.S. imports from Mexico and more than one third of U.S. exports to Mexico. Within 10 years of implementation of the agreement, all U.S.-Mexico tariffs should be eliminated except for some U.S. agricultural exports to Mexico that will be phased out in 15 years. Most U.S.-Canada trade is already duty free. NAFTA also seeks to eliminate non-tariff trade barriers.

The NAFTA agreement commits all parties to end restrictions on NAFTA-member foreign investors, provide a high-level of intellectual property rights protection, liberalize trade in services, and establish dispute settlement mechanisms to be used among the three partners. NAFTA has side agreements

on environmental and labour standards making it the first U.S. trade accord to be formally linked to such commitments.

### **Southern Common Market (SCM)**

The Southern Common Market, best known by its Spanish acronym MERCOSUR was established in 1991 and is the largest of the regional grouping. Argentina, Brazil, Paraguay and Uruguay are members. Chile and Bolivia are associate-members. MERCOSUR was established with the objective of encouraging economic integration among member states by means of the free flow of goods and services. A common market among members which removed tariffs from 85 per cent of intra-regional trade, went into effect on January 1, 1995.

### **The Andean Community (AC)**

The Andean community was established 1996 as a successor to the Andean Group which had its origins in the 1969 Cartagena Agreement also known as the Andean Pact. The Andean community's members are Bolivia, Colombia, Ecuador, Peru and Venezuela. Panama has observer status. Chile a founding member of the Andean pact withdrew in 1976. The Andean Group's original intent was to increase trade among the members and to devise joint industrial programmes for industries such as petrochemicals, Metalworking and Automobiles. There was also an effort to launch a new common currency.

### **Central American Common Market (CACM)**

The Central American Common Market was founded in 1960 under the General Treaty of Central American Integration. CACM's members are Costa Rica, Guatemala, El Salvador, Honduras, and Nicaragua. The General Treaty's original intent was to create a free trade area among the central

American countries while establishing a common tariff with nonmember countries. In late 1993, the CACM country presidents and the president of Panama signed a protocol to the 1960 treaty pledging themselves to the full economic integration of the region.

### **Caribbean Community and Common Market (CARICOM)**

CARICOM was founded in 1973 and succeeded the Caribbean Free Trade Association (CARTFTA) established in 1968.

CARICOM'S 14 members included 13 former British territories and Suriname. The members are: Antigua and Barbuda, the Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, Montserrat, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, and Trinidad and Tobago. The British Virgin Islands and the Turks and Caicos Islands are associate members. CARICOM's objectives are the economic integration of the members through a common market, coordination of the foreign policies of member states and functional cooperation especially in areas of social and human development. CARICOM maintains a common external tariff with exceptions.

### **Association of South East Asian Nations (ASEAN)**

This is an important regional economic grouping which is emerging as a major force in world trade. It was formed in 1967 but started making progress only in 1970s. Its members are Brunei, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam. The first step towards economic integration was through partial liberalisation of trade in select range of products. The other important step was to identify several

regional projects which would cater to the requirements of all the member-countries. Each country will have one regional project.

ASEAN has developed a Common Effective Preferential Tariffs (CEPT) plan to reduce tariffs systematically for manufactured and processed products, leading to an ASEAN free trade area in 15 years.

Intra -ASEAN trade has so far covered only a small percentage of total trade of the group. Intra-group trade stood at \$ 24 billion in 1990 as against the group's total trade turnover of \$ 265 billion. ASEAN has decided to invite as 'guest country' both China and India.

### **Global System of Trade Preferences among Developing Countries (GSTP)**

The Agreement establishing the Global System of Trade Preferences (GSTP) 'among developing countries was signed on 13th April, 1988 at Belgrade" following conclusion of the First Round of Negotiations. The Agreement was '(signed by 48 developing countries, which exchanged concessions in the course, of that Round. The Agreement came into force from 19th April, 1989 and 40 \countries including India have ratified it so far.

The GSTP established a framework for the exchange of trade concessions among the members of the Group of 77. It provides a mechanism for negotiations in successive stages for establishing trade preferences with a view to promo~ trade and economic co-operation among developing countries. It lays down rules, principles and procedures for conduct of negotiations and for implementation of the result of the negotiations. The coverage of the GSTP extends to arrangements in the area of tariffs, non-tariff measures, direct trade measures including medium and long-term contracts and sectoral agreements.

One of the basic principles of the Agreement on GSTP is that it is to be negotiated step by step, improved and extended in successive stages. Accordingly, the Ministerial Meeting on GSTP held in Teheran on 21st November, 1991 adopted the Teheran Declaration on the launching of the Second Round of GSTP negotiations. The aim of the Second Round is to facilitate the process of accession to the GSTP Agreement and to carry forward the exchange of trade concessions.

### **South Asian Preferential Trading Arrangement (SAPTA)**

The Agreement establishing the SAARC Preferential Trading Arrangement (SAPTA) was signed on 11th April, 1993 at the Seventh SAARC Summit held in Dhaka, and the SAPTA came into effect on December 7, 1995. The Agreement establishes a framework for the exchange of trade concessions among the Member States of SAARC. It lays down rules, principles and procedures for the conduct of negotiations and for implementation of the results of the negotiations. The coverage of SAPTA extends to arrangements in the areas of tariffs, para-tariffs, non-tariff measures and direct trade measures. The Agreement is, however, limited to merchandise trade and excludes services from its scope.

In the first round of SAPTA negotiations, India offered import tariff concessions on 106 items whereas the number of items on which the other SAARC countries offered concessions is as follows: Pakistan 35; Sri Lanka 31; Maldives 17; Nepal 14; Bangladesh 12 and Bhutan 11. Further, the tariff concessions offered by India in respect of most items go up to 50 per cent whereas the range of concessions offered by the other countries is 5 to 15 per cent.

The Second Round of SAPTA Negotiations resulted in exchange of tariff concessions of 1972 tariff lines. Out of this, India has offered concessions on 911 tariff lines and received concessions on 456 tariff lines at the six digit level. The Third Round of Negotiations is to be completed soon. The ultimate objective is to establish a Free Trade Area in the region (SAFTA) by 2001 A.D.

### **Bangkok Agreement**

The First Agreement on Trade Negotiations among Developing Member- Countries of ESCAP, popularly known as the Bangkok Agreement, was signed on 31st July, 1975 in Bangkok. Bangladesh, Republic of Korea, Sri Lanka and India are members of the Agreement. The Agreement provides for liberalisation of both tariff and non-tariff barriers in *inter se* trade among participating countries. At present, the operation of the Agreement is limited to tariff concessions only. The Agreement envisages special concessions to least developed countries. The Agreement could not generate the anticipated trade flows on account of limited membership and product coverage. The product coverage increased considerably as a result of the Second Round of Negotiations which concluded in May 1990. In addition, Papua New Guinea has acceded to the agreement. Afghanistan and China have also expressed their interest in joining the Bangkok Agreement but they have yet to initiate the process.

### **Asia-Pacific Economic Cooperation (APEC)**

Formed in 1989 as an informal dialogue group With limited Participation. APEC has become a *forum for negotiations to* achieve the goal of *freer* trade and investment in the Asia-Pacific region.

APEC has 18 members: Australia. Brunei, Canada. Chile. China. Hong Kong. Indonesia, Japan. South Korea. Malaysia. Mexico, New Zealand, Papua New Guinea, Philippines, Singapore, Taiwan, Thailand and the United States.

In Indonesia in 1994, the APEC leaders agreed via their Bogor Declaration "to achieve free and open trade and investment in the region" by firm dates - 2010 *for* the industrial economies that make up 85 per cent of APEC trade and 2020 *for* the rest. This is potentially the most sweeping trade agreement in history, committing half the world economy *to* eliminate all barriers *to* exchange among themselves. In addition, APEC has consistently pledged *to* promote further liberalization *of* the global trading system under its doctrine of open regionalism.

### **CONFLICT BETWEEN MULTILATERALISM AND REGIONALISM**

Both GATT and WTO accommodated regional arrangements. The major argument for regionalism has been that smaller group of countries would find it easier to move towards integration than in a much wider multilateral system. However, as the groupings become larger, this argument tends to lose validity. Many of the new regional arrangements contain countries as diverse in outlook, economic size and level of development as any countries in the multilateral system. Thus the fact remains that regional and geographical arrangements are an exception to the MFN principle which is the essence of the WTO rules.

### **Conclusion**

The formation of the various economic groupings on account of attaining multilateral benefits, the groupings have led to the change in the complexion of the entire world market place significantly. These international business firms and multinational groups spell opportunity in bold letters through access to greatly enlarged markets with reduced or abolished country-by-country tariff barriers and restrictions. Production, financing, labor, and marketing decisions are affected by the remapping of the world into market groups.

As goals of the EEA and NAFTA are reached, new marketing opportunities are created; so are new problems. World competition will intensify as businesses become stronger and more experienced in dealing with large market groups. European and non-European multinationals are preparing to deal with the changes in competition in a fully integrated Europe. In an integrated Europe, U.S. multinationals may have an initial advantage over expanded European firms because U.S. businesses are more experienced in marketing to large, diverse markets and are accustomed to looking at Europe as one market. The advantage, however, is only temporary as mergers, acquisitions, and joint ventures consolidate operations of European firms in anticipation of the benefits of a single European market. International managers will still be confronted by individual national markets with the same problems of language, customs, and instability, even though they are packaged under the umbrella of a common market.

### **Summary**

The globalization of markets, the restructuring of Eastern Europe into independent market-driven economies, the dissolution of the Soviet Union into independent states, the worldwide trend toward economic cooperation, and enhanced global competition make it important that market potential be viewed in the context of regions of the world rather than country by country. Formal

economic cooperation agreements such as the EC are the most notable examples of multilateral and geographical economic groups.

Multilateral and economic cooperative agreements have been around since the end of World War II. These economic groupings give rise to many benefits to the member countries which are multilateral in nature and scope.

Geographical and multilateral market groups take several forms, varying significantly in degree of cooperative, dependence and their relationship among participating nations.

There are five fundamental groups for multilateral and geographical integration. The various possible multilateral and geographical groupings are: regional cooperation groups, free trade area, customs union, common market and political union. The major multilateral and geographical groupings in the world are: European union (EU), European Free Trade Area (EFTA), North American Free Trade Area (NEFTA), Southern Common Market (SCM), The Andean Community (AC), Central American Common Market (CACM), Caribbean Community and Common Market (CARICOM), Association of South East Asian Nations (ASEAN), Global System of Trade Preferences among Developing Countries (GSTP) and South Asian Preferential Trading Arrangement (SAPTA) and the Bank of Agreement of Asia Pacific Economic Cooperation (APEC).

Among the important global trends today is the evolution of the multinational market region – the groups of countries that seek mutual economic benefit from reducing intraregional trade and tariff barriers.

Multinational market groups form large markets that provide potentially significant market opportunities for international business.

Multinational market groups take several forms, varying significantly in the degree of cooperation, dependence, and interrelationship among participating nations.

### **Important Questions**

1. Discuss the significance of formation of multilateral and geographical groupings.
2. Discuss the various forms of multilateral and geographical groupings in the world for cross border trade.
3. Is it possible to form a political union? Comment.
4. Discuss the major multinational and geographical economic groups in the world.
5. What is GSTP? Discuss its importance and significance to the member countries.
6. What are the reasons for conflict between multilateralism and regionalism?
7. Discuss the various trade benefits to the countries forming ASEAN.
8. Distinguish between the formation and scope of EU, EFTA and NAFTA.
9. Discuss in detail the formation of Central Asian Common market.
10. Discuss the importance of various regional groupings in the present era formation of WTO.

## UNIT II

<b>LESSON</b>	<b>4 CULTURE AND BUSINESS CUSTOMS</b>
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### LESSON OUTLINE

- Marketing environment
- International marketing environment
- Social cultural factors
- Culture
- Cultural dynamism
- Elements of Culture
- Business customs
- Host country culture
- Coping international cultural differences
- Cultural Adaptation
- Summary

### LEARNING OBJECTIVES

*After reading this lesson you should be able to:*

- International marketing environment
- Various elements of culture
- Importance of

business customs of  
host country for  
international  
marketing  
management

- The importance of culture for international marketing
- The cultural dynamism
- Need and importance of adaptation of culture for international marketing
- Aids for coping international cultural differences

## MARKETING ENVIRONMENT

Every business is run in a given set of environment, which constitutes of various factors some of which are internal to the business while some others are external. It is a proven truth that the success of a business, to a great extent, depends on its ability to foresee the environmental changes and to modify its business strategies appropriately. It is also true that only those businesses survive for long, which keep pace with the changing environment.

A business is an open system and marketing functions performed by a business are a sub-system of its overall business system. As the business, being an open system has a continuous interface with the external environment,

which in turn affects its overall functioning in general and its marketing functions in particular.

The marketing environment of a business consists of several factors some of which are controllable by it while some others are non-controllable. Further, out of the various components of the environment, some factors may be internal to the business organization while some others may be external to it. All these types of the constituents of the environment are dynamic in nature, which interact with one another and also the business organizations. To some extent the business organisations also affect the environment. The businesses have to adjust their activities in tune with the changes in the components of the environment. Thus, a constant monitoring of the environment is necessary for a business to draw plans for its adaptation to the environmental forces. These forces of the business environment cause both threats as well as opportunities for it.

### **International Marketing Environment**

The environment to a business varies from time to time and country to country. All the business functions are directly related to the existing environment in which it operates. The marketing activities are the most affected ones due to the changes in environmental conditions in the various different countries operation.

The business firms must adapt to the changing conditions of the environment for their long run survival, as those firms, which do not keep pace with the changes in the environment are surely to fail – sooner or later. Thus the marketing management of a business rests squarely on the knowledge of the marketing environment. It has to know where the environment is heading, what

trends are emerging therein and how a marketing firm should respond to the changes in the environment.

The international marketing environment constitutes a number of forces, which are all dynamic in nature, though the degree varies amongst them. The marketers have to upgrade their policies and tune up their marketing programmes in accordance with the trends in the marketing environment.

Various authors have many varying factors to be considered important for inclusion in the list constituting the components of the marketing environment.

According to Kotler and Keller, “Within the rapidly changing global picture, marketers must monitor six major environmental forces: demographic, economic, social-cultural, natural technological and political legal.”<sup>1</sup>

According to Chhabra and Grover, “Marketing environment may be broadly classified into economic and non-economic. Economic environment comprises economic system, structure and quality of economic development, fiscal, industrial and foreign trade policies, factor endowment, economic planning and international economic relations. Non-economic environment comprises social, demographic, political, legal, cultural and educational factors.”<sup>2</sup>

According to Ramaswami and Namakumari, “Marketing environment involves of mega environment that is specific to the given business.

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1. Kotler Phillip and Keller K.L., “Marketing Management”, Pearson Education Pte. Ltd., Delhi, 2006, p.92.
  2. Chhabra T.N. and Grover S.K., “Marketing Management”, Dhanpat Rai and Co. (Pvt.) Ltd., New Delhi, 1998, p.1.53.

Mega environment covers the political, the demographic, and the socio-cultural and economic environment. It also includes the legal environment and the government policies. The environment specific to the given business includes such aspects as structure of the industry, nature of competition and factors relating to customers and demand”.<sup>3</sup>

According to Saxena, “A systematic approach to environmental analysis and diagnosis involves understanding of the forces namely socio-economic, competition, technology, government policies and suppliers”.<sup>4</sup>

The various experts have included various terms to define the important components of the international marketing environment but on synthesizing the views of all these experts, we can conclude that the forces in the environment which have a considerable influence on the marketing functions and decisions can be divided into the following three categories:

- a) Economic
- b) Non-economic
- c) Physical / Natural

Each of the above three types of the forces act and interact with each other. In other words the economic factors have non-economic implications and non-economic factors have economic implications and both of these are also influenced and influence the factors prevalent in the physical environment.

## **SOCIO-CULTURAL FACTORS**

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- 3. Ramaswamy V.S. and Namakumari V., “Marketing Management – Planning, Implementation and Control”, Macmillan India Ltd., New Delhi, 2002, p.27.
  - 4. Sexena Rajan, “Marketing Management”, Tata McGraw Hill Publishing Company Limited, New Delhi, 2002, p.51.

For international marketing, the modern business thinking advocates the business to take on the responsibility for serving or safeguarding socio-cultural interests as one of its important objectives as the business owes its existence to the society served and is itself deeply influenced by the society's social institutions.

The international socio-cultural environment constitutes factors like family background, caste, structure, customs, conventions, values and attitudes, the cultures and subcultures and the knowledge levels and the belief system of the people. These factors influence the international market demand level for many products as their consumption decisions depend upon people's attitudes, beliefs, customs, social norms and social cultural values etc.

The business firm engaged in international need to understand people's views about the consumption of a good or service and rest of the marketing decisions should be based on it.

OVERALL IT CAN BE CONCLUDED THAT THE SOCIO-CULTURAL FABRIC IS AN IMPORTANT ENVIRONMENTAL FACTOR THAT SHOULD BE ANALYSED WHILE FORMULATING THE INTERNATIONAL MARKETING STRATEGIES. THE COST OF IGNORING IT COULD BE VERY HIGH.

#### **Culture**

Culture can be regarded as the sum total of attitudes, beliefs and lifestyles of the citizens of a country. Thus, the international manager must be aware of attitudes toward material culture, work and achievement, time, change, authority, family, decision-making, and risk. Since this description includes a vast number of intangible factors, it should come as no surprise that the cultural environment of international business gives MNC managers so many problems.

The prevailing culture and practiced business customs at a place are one of the very important dimensions of international marketing. These influence all aspects of consumer behaviour ones are pervasive in all marketing activities in product design, packaging, pricing, promotion, distribution and communication etc. The marketers wishing to expand than operation cross borders, operations must be fullyfamiliar with the cultural dimensions of the consumer their and also about the prevalent business customers as these ---- as significant implications for trade.

Cultural dimension is one of the important dimensions of international marketing environment, other dimensions being political, economic, legal, technological, geographic etc. These influences all aspects of consumer behaviour and is pervasive in all marketing activities in product design, packaging, pricing, promotion, distribution, communication and the like. Since the scope of marketing concept is to satisfy consumer needs, it is quite clear that the marketer must be fully familiar with the cultural dimensions of consumer behaviour in target markets and must understand their implications for specific marketing functions.

### ***Cultural Dynamics***

Man uses the media of culture in adapting to the physical, biological, psychological, social, anthropological, and historical components of human existence. Each culture evolves its own modes and norms to solve problems created by man's existence in society. Accidental solutions were found for some problems; inventions and innovations have provided solutions to other problems. But more commonly a society found answers to most of its problems through direct or indirect interaction with and borrowing from other cultures. Inter-cultural borrowing is a significant phenomenon of cultural dynamics. What a culture adopts from another culture becomes adapted to its needs in course of time and once the adaptation becomes assimilated, it is passed on as cultural heritage of that society. In other words, culture is a living and dynamic phenomenon which keeps on constantly interacting with other culture and passes through the continuing process of adopting, adapting and assimilating.

A significant characteristic of human society is that the culture is passed on to succeeding generations which constantly build upon and expand the inherited culture, from which man learns a wide range of behaviour that is of relevance to marketing.

### ***Elements of Culture***

Culture includes all facets of life. In order to obtain a total picture of a culture it is necessary to investigate every possible side of it. For facilitating an accurate study of culture, the anthropologists have evolved a “cultural scheme” which embodies all the various elements of culture. The main elements included within the meaning of the term ‘culture’ are:

1. Material Culture
  - Technology
  - Economics
2. Social Institutions
  - Social organization
  - Education
  - Political structures
3. Man and the Universe
  - Belief systems
4. Aesthetics
  - Graphic and plastic arts
  - Folklore
  - Music, drama and the dance
5. Language

These five broad dimensions of culture embrace all the major aspects of man's social heritage. They serve as a framework for the analysis of

cultural ramifications. The foreign marketer may find such 'cultural scheme' as a useful instrument in assessing the potential and intricacies of a foreign market. Each of these elements of culture has some influence on the marketing process and they differ from culture to culture. It is therefore necessary to study the implications of these differences in analyzing specific foreign markets.

A brief analysis of the elements of the 'cultural scheme' of a society will illustrate the variety of ways in which culture and marketing are interlinked.

### **Business Customs**

Business customs are as much a cultural element of a society as is the language. Culture not only establishes the criteria for day-to-day business behavior but also forms general patterns of attitude and motivation. Executives are to some extent captives of their cultural heritages and cannot totally escape language, heritage, political and family ties, or religious backgrounds.

As culture and business customs play a very significant role for the success of a business firm engaged in international marketing, these firms must adopt some measures to adapt the required changes.

One report notes that Japanese culture, permeated by Shinto precepts, is not something apart from business but determines its very essence. Thus, the many business and trade problems between Japan and the U.S. reflect the widespread ignorance of Japanese culture by American businesspeople. Although international business managers may take on the trappings and

appearances of the business behaviour of another country, their basic frame of references is most likely to be that of their own people.

As host countries have come to resent the 'cultural imperialism' of so many MNCs, so these companies have come to realize, particularly in the last ten years, the critical importance of this area. Culture is all-pervasive, and represents a dilemma for both operating and strategic management. It is a truism of strategic management that any strategy which runs counter to the corporate culture is certain to fail. The same is true of an international strategy which runs counter to a national or regional culture, but the results of failure will become apparent even more quickly. The broad prescription for MNC managers is to avoid insensitivity toward, or ignorance of, the aspects of local culture which will have most influence on commercial success in any particular country. This requires a high level of cultural awareness and a sufficient degree of cultural empathy; at the operational level, it also demands a significant level of cultural training for expatriate managers before a new posting.

Finance and accounting is the functional area least involved; cultural considerations are most important in marketing, with human resource management coming a close second. The question of language is crucial, and arouses great sensitivity in many countries. While there is a trend toward the acceptance of English as the universal business 'language, MNC managers should be aware that such a presumption causes great offence in for example, France. Non-verbal communication also holds its pitfalls, with different elements having different intrinsic meanings; this includes the use of eye contact, touching, personal appearance, relative position between people having a discussion, bodily postures, distance apart, and non-verbal aspects of speech like accents and tones.

### **Host-Country Culture**

Host-country religion also has a fundamental part to play, with each major religion having an impact on the overall attitude to business. The so-called 'Protestant work ethic' is a noticeable feature of Christianity; however, not only is this rather obviously shared by Roman Catholics, but it also finds a resonance in Confucianism. MNCs operating in Islamic countries have to be keenly aware that Moslems pray at five specific times during the day, and that there must be no requirement to work during these intervals. The concept of the (extremely) extended family is important to Hindus, -and includes support of all family members in the business world; thus, MNC managers have" to be extra sensitive to the problems of pay, promotion, discipline and dismissal, Buddhists lay little stress on material wealth, and so are much' less susceptible to western methods of motivating the workforce. Animism is probably the oldest religion and is widespread in Africa and Latin America. The Animist puts all problems down to the action of evil spirits which must be exorcized; this can cause some odd situations for the expatriate production manager who has to cope with the Animist response to defective quality, machine breakdowns, and industrial accidents.

### **Coping International Cultural Differences**

Asheghian and Ebrahimi (1990) give a useful check-list for the MNC managers as an aid to coping with international differences in culture:

1. Be culturally prepared: forewarned is forearmed.
2. Learn the local language and its non-verbal elements.
3. Mix with host nationals, including socially.
4. Be creative and experimental without fear of failure.
5. Be culturally sensitive; do not stereotype or criticize.
6. Recognize complexities in the host culture.
7. Perceive yourself as a culture bearer and ambassador.

8. Be patient, understanding and accepting of your hosts.
9. Be most realistic in your expectations.

Accept the challenge of intercultural experiences.

A lack of empathy for and knowledge of foreign business practices can create insurmountable barriers to successful business relations. Some businesses plot their strategies with the idea that counterparts of other business cultures are similar to their own and are moved by similar interests, motivations, and goals – that they “are just like us”. Even though they may be just like us in some respects, many differences exist and that can lead to frustration, miscommunication, and, ultimately, failed business opportunities if they are not understood and responded to properly.

Knowledge of the business culture, management attitudes, and business methods existing in a country and a willingness to accommodate the differences are important to success in an international market. Unless marketers remain flexible in their own attitudes by accepting differences in basic patterns of thinking, local business tempo, religious practices, political structure, and family loyalty, they are hampered, if not prevented, from reaching satisfactory conclusions to business transactions. In such situations, obstacles take many forms, but it is not unusual to have one negotiator’s business proposition accepted over another’s simply because “that one understands us”.

### **Cultural Adaptation**

Adaptation is a key concept in international marketing and willingness to adapt is a crucial attitude. Adaptation, or at least accommodation, is required on small matters as well as large ones. In fact, the small, seemingly

insignificant situations are often the most crucial. More than tolerance of an alien culture is required. There is a need for affirmative acceptance, that is, open tolerance of the concept “different but equal”. Through such affirmative acceptance, adaptation becomes easier because empathy for another’s point of view naturally leads to ideas for meeting cultural differences.

As a guide to adaptation, there are 10 basic criteria that all who wish to deal with individuals, firms, or authorities in foreign countries should be able to meet. They are (1) open tolerance, (2) flexibility, (3) humility, (4) justice/fairness, (5) adjustability to varying tempos, (6) curiosity/interest, (7) knowledge of the country, (8) liking for others, (9) ability to command respect, and (10) ability to integrate oneself into the environment.

### **Summary**

Culture can be defined as a “sum total of man’s knowledge, beliefs, art, morals, laws customs and any other capabilities and habits acquired by him as a member of the society”. It is the distinctive way of life of a group of people, their complete design for living. Culture, thus, refers to man’s entire social heritage – a distinctive life-style of a society and its total value system which is intricately related to the consumption pattern of the people.

Business customs are as much a cultural element of a society as is the language. Culture not only establishes the criteria for day-to-day business behavior but also forms general patterns of attitude and motivation. Executives are to some extent captives of their cultural heritages and cannot totally escape language, heritage, political and family ties, or religious backgrounds.

As host countries have come to resent the 'cultural imperialism' of so many MNCs, so these companies have come to realize, particularly in the last ten years, the critical importance of this area. Culture is all-pervasive, and represents a dilemma for both operating and strategic management. It is a truism of strategic management that any strategy which runs counter to the corporate culture is certain to fail. The same is true of an international strategy which runs counter to a national or regional culture, but the results of failure will become apparent even more quickly. The broad prescription for MNC managers is to avoid insensitivity toward, or ignorance of, the aspects of local culture which will have most influence on commercial success in any particular country. This requires a high level of cultural awareness and a sufficient degree of cultural empathy; at the operational level, it also demands a significant level of cultural training for expatriate managers before a new posting.

### **Important Questions**

1. What is international marketing environment? Discuss the main constituents of international marketing environment.
2. Discuss the socio-culture factors important for international marketing management.
3. Define culture. Discuss its importance for international marketing.
4. What do you understand by the term, 'Cultural Dynamism'? Discuss the various elements of cultural dynamism.
5. What do you understand by the term, 'Cultural Adaptation'? Discuss.
6. Discuss the various means for coping cultural differences for international marketing.
7. How culture and business customs influence international marketing?
8. What do you understand by the term 'Business Customs'?

9. Discuss the need and importance of adaptation of business customs of host country for the firms engaged in international marketing.
10. How the religion of host country can effect the business of an international marketing firms.

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## UNIT II

<b>LESSON</b>	<b>5 ECONOMIC AND FINANCIAL DIMENSIONS</b>
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### LESSON OUTLINE

- Economic Environment
- Economic System
- Government Policies
- Structural Anatomy
- Market Conditions
- Factor Endowment
- Financial Environment
- The Foreign Exchange Market
- The Money Market
- The Long-term Capital Market
- International Monetary Fund
- IBRD
- International Development Association
- International Financial Corporation

### LEARNING OBJECTIVES

*After reading this lesson you should be able to:*

- The various factors which constitute the economic environment of a country
- The role of

government in  
influencing the  
international  
marketing  
management  
Functions

- The various constituents of financial environment for international marketing
- The money market and long-term capital market
- Various international financial institutions

## **ECONOMIC ENVIRONMENT**

The various constituents of the economic environment affecting international marketing management functions and decisions of business firms include:

- i) Economic system
- ii) Government policies
- iii) Structural autonomy
- iv) Market conditions
- v) Factor endowment

## **ECONOMIC SYSTEM**

There are three types of economic systems existing in the world. These are (i) centrally planned economies or communist system, (ii) market driven economies or free economies called market driven economies and (iii) mixed economies.

In case of a centrally planned economy, all the means of production are strictly controlled by the state and the role of private firms is bare minimum. In such type of economies, the firms from can not make their own decisions and the firms from other countries cannot directly export goods or services directly.

In case of capitalist economies there is a greater freedom to marketing firms for domestic operations and also for exports and imports subject to the confinement to the laws and procedures.

In case of mixed economies, there are restrictions on some of the businesses, which the state takes up to itself or those, which are of strategic importance. Thus in such types of economies there is lesser freedom as compared to the capitalistic economies.

## **GOVERNMENT POLICIES**

The ideology of the party, which forms the government in a country, its various decisions and its various policies related to business, greatly affects the marketing environment of the business firms operating there.

If a government has a liberal export import policy and allows exports and imports without much restriction then the business and thus the marketing activities will flourish there but the same will not happen where the

Ex-im policy poses many restrictions. Similarly if excise duties are reduced on the production of a consumer product, there is will be move demand for the same and the market size for this product will increase.

Industrial policies relate to licensing policies for manufacturing or service industry. If the government has liberal licensing policy then its business and service sector will grow faster and there will be more marketing activities.

Public policy or social policy intersects the field of marketing when public policy makers believe that government intervention in the process or outcome of marketing exchanges will benefit society as a whole.

Consumers all over the world have become more and more aware of their due rights and have become consequently very demanding and choosy as for the Indian firms; the foreign buyers have started now to look for the ISI, ISO, AGMARK, and FPO trademarks on the products. These trademarks give the consumers a legal guarantee of the quality of the products bearing them. They also help in protecting the consumers against unfair trade practices.

In order to influence the marketing decisions of companies, the role of Government has assumed one or a combination of the following:

- Participative
- Institutional
- Commercial
- Legislative

## **1. PARTICIPATIVE**

By taking marketing activities by its own self, the government entails active participation in the country's marketing operations. Major forms of the state participation may be:-

- (a) To stabilize prices and protect consumers the government may undertake supply of certain product e.g. In India, Food Corporation of India and Cotton Corporation of India in order to stabilize prices and protect consumers.
- (b) Promotion or discouraging consumption of certain commodities e.g. G.O.I. promotes the sale of family planning devices through its own purchases and mass-consumption campaigns.
- (c) Infrastructural facilities on preferential basis e.g. in India Railways extend preferential treatment for dairy products and food items.

Thus by about governments extend a lot of influence on the marketing decisions of the companies.

## **2. INSTITUTIONAL**

The governments set up their own institutions for protecting consumers e.g. in India the government has set up National Consumer Service (NCS and the National Co-operative Federation etc.).

## **3. COMMERCIAL**

Another reason to which government's influence on marketing decision may be attributed is the need to regulate the commercial relations amongst the country's citizens. The government does so by legislating and enforcing relevant laws.

## **4. LEGISLATIVE**

Laws of the land play a decisive role in shaping the marketing and consumption activities in a state. The countries pass various laws to influence the trade and marketing activities in their countries. For example, in India, there are various laws, which influence the marketing decisions of the firms. Some important ones prevailing in India have been listed below:

1. Indian Contract Act, 1872 (i) Gen and (ii) Agency Relationship.
2. Indian Sales of Goods Act 1930
1. MRTP Act, 1969
2. The Companies Act 1956
3. The Patents Act 1970
4. Essential Commodities Act, 1956
5. Prevention of Food Adulteration Act, 1954.
6. Drugs and Medical Remedies (Objectionable Ads), Act, 1954.
7. Sales Promotion Employees (Conditions of Service) Act, 1976.

Overall it may be said that government can influence various marketing activities of business by its intervention in the form of framing some policies governing business, passing some legislations and even sometimes by taking up some of the commercial activities of its own.

The monetary and the various other policies of the government also affect the progress and development of business.

## **STRUCTURAL ANATOMY**

An economy consists of various sectors like agriculture, production, service etc. The structural anatomy means the composition of these sectors in the structure of the economy. According to Chhabra and Grover, "The structural anatomy comprises the structure of national output, the occupational

distribution of labour-force employed, capital formation composition and trade compositions etc.”<sup>1</sup>

The environment for international marketing activities gets a boost if there is an equal level of development of these various sectors of the economy and the imbalances among their development hampers the marketing functions of the other sectors.

### **MARKET CONDITIONS**

The factors prevailing in a market also greatly influence the marketing decisions of a business. The market conditions where there are a large number of buyers and there is a rising pattern of demand for a product, these factors create opportunities for the marketers of such products. On the contrary when there is recession in the market and product demand is declining, these market forces are not favorable for the marketers of such products.

### **FACTOR ENDOWMENT**

The availability and the supply condition of the various factors of production (men, money, materials and machinery) effect many marketing decisions of the affected firms. The market locations, where the factors of input for the production of a product are available cheaply and easily, will be at an advantageous position than the other locations where there is the scarcity of such factors. Thus the variance in the degree of the supply of factors of input also has a direct bearing on the economic environment and through this on the business and particularly marketing.

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1. Chhabra, T.N. and Grover, S.K., “Marketing Management”, Dhanpat Rai and Co. Pvt. Ltd., New Delhi, 1998, p. 1.60.

So, overall it can be summed up that the various economic factors affect the marketing functions of a business though there may be variations in their level of affect. Further, in the economic arena, marketers need to focus on income distribution and levels of savings, debt and credit availability and the working of the various financial institutions.

## **FINANCIAL ENVIRONMENT**

The international financial scene has undergone a sea change in the two decades. The major development in International Finance can be summarized under the following markets constituting the International Financial System.

### **The Foreign Exchange Market**

Since the advent of generalized floating in 1973, the currency rates in the Foreign Exchange Market are determined by the forces of demand and supply under the present arrangement. This causes a tremendous variability in the exchange rates of major currencies on day-to-day basis. This enhanced variability has proved to be a major problem both for the policy-makers at national level as well as the corporate manager.

A great deal of time has to be devoted in managing foreign currency risks, and the cost of buying a cover to protect against foreign currency fluctuations has to be incorporated in normally international business transactions. On the other hand, however, variability in exchange rates has opened up profit opportunities for the speculators who take positions in a currency as well as the arbiters who take advantage of the differences in rates in various markets at a given point of time. An arbiter buys a particular currency in

a market where it is cheaper and sells the same currency (same amount) in another market where the rate is slightly higher and makes the profit in the process: This has forced the foreign exchange markets continuously buy and sell different currencies with a view to make profit. The developments in information technology have also helped the spatially dispersed markets to come closer. The foreign exchange market happens to be the largest market where transactions worth \$500-700 billion take place everyday.

There are a lot of new hedging products such as forward rates, currency options, currency futures, and roll over covers etc. which have become available in the recent times.

### **The Money Market**

The world money markets have seen a mushroom growth in various short-term financing and treasury products. The forward exchange market acts as a bridge between the exchange market and the money market.

In the International money market, funds in any currency are traded outside the regulations governing domestic markets in that currency. For instance, when the US dollar deposits are traded outside the banking regulations governing domestic US dollar deposits, this type of transaction is the core of the so-called Eurodollar market. When speaking of all the currencies traded in foreign markets one usually refers to them as Euro-currency markets.

The Euro-currency markets have witnessed a tremendous increase in the volume of transactions during the current decade. The deregularization of these markets have been a major feature in the past. The availability of short-term financing products such as the commercial paper has increased the access of corporate borrowers in these markets. Also, due to the

tremendous flexibility available in these markets, it is possible to totally separate the financial aspect of a project from its investment aspect by accessing the short-term money markets. Since there are no regulations governing these markets, the borrowing costs tend to be slightly lower than in the domestic markets. Similarly, the depositor is also offered a slightly higher return than what he would be carrying to the domestic markets. The products in these markets are of short-term nature because the interest rates and currency values fluctuate on a continuous basis.

### **The Long-term Capital Markets**

If one wishes to raise long-term capital from under natural markets, one can today choose from the array of instruments that are available for this purpose. These include the syndicated Loans, Bonds, Equity Issues, and the derivative products. While the syndicated loan markets are accessible by an ordinary corporate borrower, the Bond and the equity markets are meant only for the top class corporate clients. These bond markets offer cost advantage to the syndicate loans to the borrower. To the investor also, they offer a slightly higher rate of return and liquidity as they are often bearer bonds. If a bond a multicurrency one, then it automatically provides protection against currency fluctuations.

Access to international equity markets helps a company to take advantage of international portfolio diversification and minimize the overall risks of its operation. Also, the cost of funds may turn out to be lower by accessing gamut of the segmented markets.

To summarize the trends in all the three markets, it is worth nothing the following:

1. Financial risk management has become the major issue today due to the fact that currencies and interest rates fluctuate continuously in the foreign exchange and international money markets. This increases the cost of international operation as a company needs to buy a cover against these fluctuations.
2. International integration of various markets has increased the access for funds by a company, also the cost of funds to same extent.
3. Increase in volume of transactions, and going deregulation of various markets have developed healthy competition in these markets, thereby bringing down the margins of intermediaries.
4. Due to the availability of various linking and hedging products the three major markets today seem to overlap with each other a great deal.

### **International Monetary Fund (IMF)**

The IMF was established on 27<sup>th</sup> December 1945 as an independent international organization and began operations on 1<sup>st</sup> March 1947. The capital resources of the Fund comprise SDRs and currencies that the members pay under quotas calculated for them when they join the Fund. The fund headquarters is located in Washington DC with offices in Paris and Geneva.

The objectives of the bank are to promote international monetary co-operation, the expansion of international trade and exchange rate stability; to assist in the removal of exchange restrictions and establishment of a multilateral system of payments; and to alleviate any serious disequilibrium in members' international balance of payments by making the financial resources of the Fund available to them, usually subject to conditions to ensure the revolving nature of the fund resources.

Each member of the fund undertakes a broad obligation to collaborate with the Fund and other members to ensure the existence of orderly exchange arrangements and to promote a system of stable exchange rates. In addition, members are subject to certain obligations relating to domestic and external policies that can affect the balance of payments and the exchange rate. The fund makes its resources available, under proper safeguards, to its members to meet short-term or medium-term payment difficulties.

### **International Bank for Reconstruction and Development (IBRD)**

IBRD was conceived at the Bretton Woods Conference in July 1944 and began its operations in June 1946. It has its headquarters at Washington DC and is also known as 'World Bank'. The Bank's purpose is to provide funds and technical assistance to facilitate economic development in its poorer member countries.

The bank obtains its funds from capital paid in by member countries; sales of its own securities; sale of parts of its loan; repayments and net earnings.

The bank furnishes a wide variety of technical assistance. It acts as executing agency for a number of pre-investment surveys financed by the UN Development Programme. The Bank helps member countries to identify and prepare projects for the development of agriculture, education and water supply by drawing an expertise of the FAO, WHO, UNIDO, and UNESCO through its co-operative agreements with these organizations.

### **International Development Association (IDA)**

IDA is a lending agency which came into existence on 24<sup>th</sup> September 1960. Administered by the World Bank, IDA is open to all members of the Bank.

IDA concentrates its assistance on those countries with an annual per capital GNP of less than \$481 (1987 rates). Its resources consist mostly of subscriptions, general replenishments from its more industrialized and developed members, special contributions, and transfer from the net earnings of the Bank. IDA credits are made to Governments only.

### **International Finance Corporation (IFC)**

The Corporation, an affiliate of the World Bank, was established in July 1956. IFC supplements the activities of the World Bank by encouraging the growth of productive in the form of subscription to the share capital of privately owned companies, or long-term loans or both. The corporation will help finance new ventures and assist established enterprises to expand, improve or diversify. It also provides a variety of advisory services to public and private sector clients.

### **Summary**

International trade is concerned the relationship with output, income and expenditure.

In the great majority of cases, economic factors are the most influential subset that the international manager has to consider in his analysis of the remote environment.

Economic parameters are even more significant in dealing with international markets, because the MNC manager is trying to evaluate many and varied national and regional economies. These are likely to exhibit a number of different themes, including the different rates of economic growth, improving or deteriorating balance of payment, various fiscal approaches, with governments increasing or decreasing the levels of spending and taxation, a wide spectrum of monetary policies, where monetary stability and the increase or decrease in money supply are strategic elements in any government's armory and the stage a country is at in the never-stationary business cycle – boom, depressions, recession, recovery, and back to prosperity again.

Thus it could be argued that these factors are even more important in international markets than they are at home; in taking its business activities overseas, the MNC faces the problem of assessing and understanding many economies whose characteristics are likely to prove highly divergent.

There are a number of economic indicators which the individual MNC is required to scrutinize carefully before entering a market; in turn, even the largest of international markets is likely to show marked change in these indicators as a result of substantial inward investment activity by MNCs. These economic indicators include the gross national product (GNP), GNP per capita, the rate of private (as opposed to public/governmental) investment, the level of personal consumption (especially that made out of discretionary income), variations in unit labour costs, and the distribution of incomes as measured by total disposable income per household or disposable income per capita.

The breakdown of the gold standard during the inter-war years resulted in a period of unstable exchange rates, inadequate world activity and protectionism. The Bretton Woods Agreement, signed in 1945, was intended to provide the basis for a new world economic order, with a liberal yet stable

system of trade evolving. The two fundamental institutions created by the Agreement were the International Monetary Fund (IMF) and the Bank of Reconstruction and Development (World Bank). The latter is purely a lending institution and its main concern is for the economic development of the Third World, although it is now becoming involved in the economic restructuring of eastern Europe. The IMF was set up to monitor the economic policies of its member countries, to extend them credit when in temporary difficulties with balance of payments, and to allow changes in the rates of exchange when a permanent imbalance is seen to have developed. While the Bretton Woods framework had no direct linkage with MNCs, yet these organizations have had to work within the international financial environment set up by the Agreement.

At a regional level, the European Monetary System (EMS) has been developed by the twelve member states of the EC in an effort to bind their currencies together more tightly so that fluctuations between them are reduced to an acceptable minimum; this increases the efficiency of internal trade within the EC by lowering the overall transaction costs, and is therefore very attractive to MNCs. In addition, the effort to develop the European Currency Unit (ECU) as a single denominator for intra-EC trade is likely to magnify these beneficial factors. In fact, the EMS has become one of the main driving forces for economic integration of a very high degree within the EC; in turn, this is likely to increase the pressures for further political integration, a trend which may not be quite so attractive to MNCs.

When considering individual foreign countries, MNCs will obviously be influenced by different tax regimes, and minimization of global tax payouts by declaring foreign profits in appropriate countries is a very worthwhile activity. An international firm can also achieve a formidable competitive advantage by borrowing funds in countries with low interest rates

and investing these funds in other parts of its global network, including the home country.

### **Important Questions**

1. Discuss the various constituents of the economic environment which affects international marketing management functions.
2. How the government policies of the host country can influence the functioning of a business firm engaged in international marketing.
3. What do you understand by the term, 'Structural Autonomy'? How this affects international marketing?
4. Discuss the various constituents of the prevalent financial environment in the global markets.
5. Discuss the terms international money market and long-terms capital markets.
6. Discuss in detail the functioning of IMF.
7. Discuss in detail the objectives and functions of international development association (IDA).
8. Discuss the various economic systems prevalent in the world. How these can affect international marketing functions?
9. Discuss the importance of government policies of the host country for international marketing.
10. Discuss the role, importance and significance of foreign exchange market for international market management.

### **UNIT-III**

#### **ASSESSING INTERNATIONAL MARKET OPPORTUNITIES**

Whether an organization markets its goods and services domestically or internationally, the definition of marketing still applies. However, the scope of marketing is broadened when the organization decides to sell across international boundaries, this being primarily due to the numerous other dimensions which the organization has to account for. For example, the organization's language of business may be "English", but it may have to do business in the "French language". This not only requires a translation facility, but the French cultural conditions have to be accounted for as well. Doing business "the French way" may be different from doing it "the English way". This is particularly true when doing business with the Japanese.

It is recognized that in the "postmodern" era of marketing, even the assumptions and long standing tenants of marketing like the concepts of "consumer needs", "consumer sovereignty", "target markets" and "product/market processes" are being challenged. The emphasis is towards the emergence of the "customizing consumer", that is, the customer who takes elements of the market offerings and moulds a customized consumption experience out of these. Even further, post modernism, posts that the consumer who is the consumed, the ultimate marketable image, is also becoming liberated from the sole role of a consumer and is becoming a producer. This reveals itself in the desire for the consumer to become part of the marketing process and to experience immersion into "thematic settings" rather than merely to encounter products. So in consuming food products for example, it becomes not just a case of satisfying hunger needs, but also can be rendered as an image - producing act. In the post modern market place the product does not project images, it fills

images. This is true in some foodstuffs. The consumption of "designer water" or "slimming foods" is a statement of a self image, not just a product consuming act. Acceptance of postmodern marketing affects discussions of products, pricing, advertising, distribution and planning. However, given the fact that this textbook is primarily written with developing economies in mind, where the environmental conditions, consumer sophistication and systems are not such that allow a quantum leap to postmodernism, it is intended to mention the concept in passing. Further discussion on the topic is available in the accompanying list of readings. When organizations develop into global marketing organizations, they usually evolve into this from a relatively small export base. Some firms never get any further than the exporting stage. Marketing overseas can, therefore, be anywhere on a continuum of "foreign" to "global". It is well to note at this stage that the words "international", "multinational" or "global" are now rather outdated descriptions. In fact "global" has replaced the other terms to all intents and purposes. "Foreign" marketing means marketing in an environment different from the home base, its basic form being "exporting". Over time, this may evolve into an operating market rather than a foreign market. One such example is the Preferential Trade Area (PTA) in Eastern and Southern Africa where involved countries can trade inter-regionally under certain common modalities.

### **Marketing research**

Marketing research is traditionally defined as the systematic gathering, recording, and analyzing of data to provide information useful in marketing decision making. While the research processes and methods are basically the same whether applied in Columbus, Ohio, or Colombo, Sri Lanka, international marketing research involves two additional complications. First, information must be communicated across cultural boundaries. That is, executives in Chicago must be able to "translate" their research questions into terms that

consumers in Guangzhou, China, can understand. Then the Chinese answers must be put into terms (i.e., reports and data summaries) that American managers can comprehend. Fortunately, there are often internal staff and research agencies that are quite experienced in these kinds of cross-cultural communication tasks. Second, the environments within which the research tools are applied are often different in foreign markets. Rather than acquire new and exotic methods of research, the international marketing researcher must develop the ability for imaginative and deft application of tried and tested techniques in sometimes totally strange milieus. The mechanical problems of implementing foreign marketing research often vary from country to country. Within a foreign environment, the frequently differing emphases on the kinds of information needed, the often limited variety of appropriate tools and techniques available, and the difficulty of implementing the research process constitute the challenges facing most international marketing researchers.

### **Breadth and Scope of International Marketing Research**

The basic difference between domestic and foreign market research is the broader scope needed for foreign research. Research can be divided into three types based on information needs: (1) general information about the country, area, and/or market; (2) information necessary to forecast future marketing requirements by anticipating social, economic, consumer, and industry trends within specific markets or countries; and (3) specific market information used to make product, promotion, distribution, and price decisions and to develop marketing plans. In domestic operations, most emphasis is placed on the third type, gathering specific market information, because the other data are often available from secondary sources. A country's political stability, cultural attributes, and geographical characteristics are some of the kinds of information not ordinarily gathered by domestic company marketing research departments

but which are required for a sound assessment of a foreign market. This broader scope of international marketing research is reflected in Unisys Corporation's planning steps, which call for collecting and assessing the following types of information:

1. Economic: General data on growth of the economy, inflation, business cycle trends, and the like; profitability analysis for the division's products; specific industry economic studies; analysis of overseas economies; and key economic indicators for the United States and major foreign countries.
2. Sociological and political climate: A general non economic review of conditions affecting the division's business. In addition to the more obvious subjects, it also covers ecology, safety, leisure time, and their potential impact on the division's business.
3. Overview of market conditions: A detailed analysis of market conditions the division faces, by market segment, including international.
4. Summary of the technological environment: A summary of the "state of the art" technology as it relates to the division's business, carefully broken down by product segments.
5. Competitive situation: A review of competitors' sales revenues, methods of market segmentation, products, and apparent strategies on an international scope.

Such in-depth information is necessary for sound marketing decisions. For the domestic marketer, most such information has been acquired after years of experience with a single market, but in foreign markets this information must be gathered for each new market. There is a basic difference between information ideally needed and that which is collectible and/or used. Many firms engaged in foreign marketing do not make decisions with the benefit of the information listed. Cost, time, and the human elements are critical variables.

Some firms have neither the appreciation for information nor adequate time or money for implementation of research. As a firm becomes more committed to foreign marketing and the cost of possible failure increases, however, greater emphasis is placed on research. Consequently, a global firm is or should be engaged in the most sophisticated and exhaustive kinds of research activities.

### **The Research Process**

A marketing research study is always a compromise dictated by limits of time, cost, and the present state of the art. The researcher must strive for the most accurate and reliable information within existing constraints. A key to successful research is a systematic and orderly approach to the collection and analysis of data. Whether a research program is conducted in New York or New Delhi, the research process should follow these steps:

1. Define the research problem and establish research objectives.
2. Determine the sources of information to fulfill the research objectives.
3. Consider the costs and benefits of the research effort.
4. Gather the relevant data from secondary and/or primary sources.
5. Analyze, interpret, and summarize the results.
6. Effectively communicate the results to decision makers.

Although the steps in a research program are similar for all countries, variations and problems in implementation occur because of differences in cultural and economic development. While the problems of research in England or Canada may be similar to those in the United States, research in Germany, South Africa, or Mexico may offer a multitude of different and difficult distinctions. These distinctions become apparent with the first step in the research process—formulation of the problem. Subsequent text sections illustrate some frequently encountered difficulties facing the international marketing researcher.

### **Defining the Problem and Establishing Research Objectives**

The research process should begin with a definition of the research problem and the establishment of specific research objectives. The major difficulty here is converting a series of often ambiguous business problems into tightly drawn and achievable research objectives. In this initial stage, researchers often embark on the research process with only a vague grasp of the total problem. This first, most crucial step in research is more critical in foreign markets because an unfamiliar environment tends to cloud problem definition. Researchers either fail to anticipate the influence of the local culture on the problem or fail to identify the self-reference criterion (SRC) and so treat the problem definition as if it were in the researcher's home environment. In assessing some foreign business failures it is apparent that research was conducted, but the questions asked were more appropriate for the U.S. market than for the foreign one. For example, all of Disney's years of research and experience in keeping people happy standing in long lines could not help them anticipate the scope of the problems they would run into at Euro Disney. The firm's experience had been that the relatively homogeneous clientele at both the American parks and Tokyo Disneyland were cooperative and orderly when it came to queuing up. Actually, so are most British and Germans. But the rules about queuing in other countries such as Spain and Italy are apparently quite different, creating the potential for a new kind of intra-European "warfare" in the lines. Understanding and managing this multinational customer service problem has required new ways of thinking. Isolating the SRC and asking the right questions are crucial steps in the problem formulation stage.

Other difficulties in foreign research stem from failure to establish problem limits broad enough to include all relevant variables. Information on a far greater range of factors is necessary to offset the unfamiliar cultural

background of the foreign market. Consider proposed research about consumption patterns and attitudes toward hot milk-based drinks. In the United Kingdom, hot milk-based drinks are considered to have sleep-inducing, restful, and relaxing properties and are traditionally consumed prior to bedtime. People in Thailand, however, drink the same hot milk-based drinks in the morning on the way to work and see them as being invigorating, energy-giving, and stimulating. If one's only experience is the United States, the picture is further clouded since hot milk-based drinks are frequently associated with cold weather, either in the morning or the evening, or for different reasons each time of day. The market researcher must be certain the problem definition is sufficiently broad to cover the whole range of response possibilities and not be clouded by his or her self-reference criterion.

Once the problem is adequately defined and research objectives established, the researcher must determine the availability of the information needed. If the data are available—that is, if they have been collected already by some other agency—the researcher should then consult these secondary data sources.

### **Problems of Availability and Use of Secondary Data**

The breadth of many foreign marketing research studies and the marketer's lack of familiarity with a country's basic socioeconomic and cultural patterns result in considerable demand for information like that generally available from secondary sources in the United States. The U.S. government provides comprehensive statistics for the United States; periodic censuses of U.S. population, housing, business, and agriculture are conducted and, in some cases, have been taken for over 100 years. Commercial sources, trade

associations, management groups, and state and local governments also provide the researcher with additional sources of detailed U.S. market information.

Unfortunately, the quantity and quality of marketing-related data available on the United States is unmatched in other countries. The data available on and in Japan is a close second, and several European countries do a good job of data collection and reporting them. Indeed, on some dimensions the quality of data collected in these latter countries can actually exceed that in the U.S. However, in many countries substantial data collection has been initiated only recently. Through the continuing efforts of organizations such as the United Nations and the Organization for Economic Cooperation and Development (OECD) improvements are being made worldwide. The problems of availability, reliability, comparability of data, and validating secondary data are described below.

### **Availability of Data**

Much of the secondary data an American marketer is accustomed to having about United States markets is just not available for many countries. Detailed data on the numbers of wholesalers, retailers, manufacturers, and facilitating services, for example, are unavailable for many parts of the world, as are data on population and income. Most countries simply do not have governmental agencies that collect on a regular basis the kinds of secondary data readily available in the United States. If such information is important, the marketer must initiate the research or rely on private sources of data.

### **Reliability of Data**

Available data may not have the level of reliability necessary for confident decision making for many reasons. Official statistics are sometimes

too optimistic, reflecting national pride rather than practical reality, while tax structures and fear of the tax collector often adversely affect data. Although not unique to them, less-developed countries are particularly prone to being both overly optimistic and unreliable in reporting relevant economic data about their countries. China's National Statistics Enforcement Office recently acknowledged that it had uncovered about 60,000 instances of false statistical reports since beginning a crackdown on false data reporting several months earlier. Seeking advantages or hiding failures, local officials, factory managers, rural enterprises, and others filed fake numbers on everything from production levels to birthrates. For example, a petrochemical plant reported one year's output to be \$20 million, 50 percent higher than its actual output of \$13.4 million. Finally, if you believe the statistics, Chinese in Hong Kong are the world-champion consumers of fresh oranges—64 pounds per year per person, twice as much as Americans. However, apparently about half of all the oranges imported into Hong Kong, some \$30 million worth, actually find their way into Greater China, where U.S. oranges are (wink, wink) illegal. Willful errors in the reporting of marketing data are not uncommon in the most industrialized countries, either. Often print media circulation figures are purposely overestimated even in OECD countries.<sup>5</sup> The European Community (EC) tax policies can affect the accuracy of reported data also. Production statistics are frequently inaccurate because these countries collect taxes on domestic sales. Thus, some companies shave their production statistics a bit to match the sales reported to tax authorities. Conversely, foreign trade statistics may be blown up slightly because each country in the EU grants some form of export subsidy. Knowledge of such "adjusted reporting" is critical for a marketer who relies on secondary data for forecasting or estimating market demand.

### **Comparability of Data**

Comparability of available data is the third shortcoming faced by foreign marketers. In the United States, current sources of reliable and valid estimates of socioeconomic factors and business indicators are readily available. In other countries, especially those less developed, data can be many years out of date as well as having been collected on an infrequent and unpredictable schedule. Naturally, the rapid change in socioeconomic features being experienced in many of these countries makes the problem of currency a vital one. Further, even though many countries are now gathering reliable data, there are generally no historical series with which to compare the current information. A related problem is the manner in which data are collected and reported. Too frequently, data are reported in different categories or in categories much too broad to be of specific value. The term supermarket, for example, has a variety of meanings around the world. In Japan a supermarket is quite different from its American counterpart. Japanese supermarkets usually occupy two-or three-story structures; they sell foodstuffs, daily necessities, and clothing on respective floors. Some even sell furniture, electric home appliances, stationery, and sporting goods, and have a restaurant. General merchandise stores, shopping centers, and department stores are different from stores of the same name in the United States. Furthermore, data from different countries are often not comparable. One report on the problems of comparing European cross-border retail store audit data states, "Some define the market one way, others another; some define price categories one way, and others another. Even within the same research agency, auditing periods are defined differently in different countries." As a result, audit data are largely not comparable.

### **Validating Secondary Data**

The shortcomings discussed here should be considered when using any source of information. Many countries have similarly high

standards of collection and preparation of data generally found in the United States, but secondary data from any source, including the United States, must be checked and interpreted carefully. As a practical matter, the following questions should be asked to effectively judge the reliability of secondary data sources:

1. Who collected the data? Would there be any reason for purposely misrepresenting the facts?
2. For what purposes were the data collected?
3. How were the data collected? (methodology)
4. Are the data internally consistent and logical in light of known data sources or market factors?

Checking the consistency of one set of secondary data with other data of known validity is an effective and often-used way of judging validity. For example, a researcher might check the sale of baby products with the number of women of childbearing age and with birthrates, or the number of patient beds in hospitals with the sale of related hospital equipment. Such correlations can also be useful in estimating demand and forecasting sales. In general, the availability and accuracy of recorded secondary data increase as the level of economic development increases. There are exceptions; India is at a lower level of economic development than many countries but has accurate and relatively complete government-collected data. Fortunately, interest in collecting quality statistical data rises as countries realize the value of extensive and accurate national statistics for orderly economic growth. This interest to improve the quality of national statistics has resulted in remarkable improvement in the availability of data over the last 20 years. However, where no data are available, or the secondary data sources are inadequate, it is necessary to begin the collection of primary data.

### **Gathering Primary Data: Quantitative and Qualitative Research**

If, after seeking all reasonable secondary data sources, research questions are still not adequately answered, the market researcher must collect primary data—that is, data collected specifically for the particular research project at hand. The researcher may question the firm's sales force, distributors, middlemen, and/or customers to get appropriate market information. In most primary data collection, the researcher questions respondents to determine what they think about some topic or how they might behave under certain conditions. Marketing research methods can be grouped into two basic types: quantitative and qualitative research. In both methods, the marketer is interested in gaining knowledge about the market. In quantitative research, usually a large number of respondents are asked to reply either verbally or in writing to structured questions using a specific response format (such as yes/no) or to select a response from a set of choices. Questions are designed to get specific responses to aspects of the respondents' behavior, intentions, attitudes, motives, and demographic characteristics. Quantitative research provides the marketer with responses that can be presented with precise estimations. The structured responses received in a survey can be summarized in percentages, averages, or other statistics. For example, 76 percent of the respondents prefer product A over product B, and so on. Survey research is generally associated with quantitative research, and the typical instrument used is the questionnaire administered by personal interview, mail, telephone, and most recently over the Internet. Scientific studies often are conducted by engineers and chemists in product-testing laboratories around the world. There, product designs and formulas are developed and tested in consumer usage situations. Often those results are integrated with consumer opinions gathered in concurrent survey studies. One of the best examples of this kind of marketing research comes from Tokyo. You may not know it, but the Japanese are the world champions of bathroom and toilet technology. Their biggest company in that industry, Toto, has spent millions

of dollars in developing and testing consumer products. "Thousands of people have collected data [using survey techniques] on the best features of a toilet, and at the company's 'human engineering laboratory,' volunteers sit in a Toto bathtub with electrodes strapped to their skulls, to measure brain waves and 'the effects of bathing on the human body.'" <sup>7</sup> Toto is now introducing one of its high-tech (actually low-tech compared to what they offer in Japan) toilets in the U.S. market. It's a \$600 seat, lid, and control panel that attaches to the regular American bowl. It features a heated seat and deodorizing fan. In qualitative research, if questions are asked they are almost always open-ended and/or in-depth, and unstructured responses that reflect the person's thoughts and feelings on the subject are sought after. Direct observation of consumers in choice or product usage situations is another important qualitative approach to marketing research. One researcher spent two months observing birthing practices in American and Japanese hospitals to gain insights into the export of health care services. Nissan Motors Corp. has sent a researcher to live with an American family (renting a room in their house for six weeks) to directly observe how Americans use their cars. Qualitative research seeks to interpret what the "people in the sample are like, their outlooks, their feelings, the dynamic interplay of their feelings and ideas, their attitudes and opinions, and their resulting actions." The most often-used form of qualitative questioning is the focus group interview. However, oftentimes in-depth interviewing of individuals can be just as effective while consuming fewer resources. Qualitative research is used in international marketing research to formulate and define a problem more clearly and to determine relevant questions to be examined in subsequent research. It is also used where interest is centered on gaining an understanding of a market, rather than quantifying relevant aspects. For example, a small group of key executives at Solar Turbines International, a division of Caterpillar Tractor Co., called on key customers at their offices around the world. They discussed in great

depth with both financial managers and production engineers potential applications and the demand for a new size of gas-turbine engine the company was considering developing. The data and insights gained during the interviews to a large degree confirmed the validity of the positive demand forecasts produced internally through macroeconomic modeling. The multi-million-dollar project was then implemented. Additionally, during the discussions new product features were suggested by the customer personnel that proved most useful in the development efforts. Qualitative research is also helpful in revealing the impact of socio cultural factors on behavior patterns and in developing research hypotheses that can be tested in subsequent studies designed to quantify the concepts and relevant relationships uncovered in qualitative data collection. Procter & Gamble has been one of the pioneers of this type of research—the company has systematically gathered consumer feedback for some 70 years.<sup>11</sup> It was the first company to conduct in-depth consumer research in China. In 1994 P&G began working with the Chinese Ministry of Health to develop dental hygiene programs and has now reached over one million children in 28 cities. The company will soon offer Crest toothpaste in two flavors and toothbrushes in four colors to Chinese consumers.<sup>12</sup> Procter & Gamble also conducts research with washing-machine manufacturers to develop the best products given the evolving technology in the home-appliance industry.<sup>13</sup> The details of Procter & Gamble's integration of qualitative and quantitative marketing research efforts in Egypt provide a good case in point: For years Procter & Gamble had marketed Ariel Low Suds brand laundry detergent to the 5 percent of homes in the Egyptian market that had automatic washing machines. P&G planned to expand its presence in the Egyptian market, and commissioned a study to: (1) identify the most lucrative opportunities in the Egyptian laundry market; and (2) develop the right concept, product, price, brand name, package, and advertising copy once the decision was made to pursue a segment of the laundry market.

The "Habits and Practices" study, P&G's name for this phase, consisted of home visits and discussion groups (qualitative research) to understand how the Egyptian housewife did her laundry. The company wanted to know her likes, dislikes, and habits (the company's knowledge of laundry practices in Egypt had been limited to automatic washing machines). From this study, it was determined that the Egyptian consumer goes through a very laborious washing process to achieve the desired results. Among the 95 percent of homes that washed in a non automatic washing machine or by hand, the process consisted of soaking, boiling, bleaching, and washing each load several times. Several products were used in the process; bar soaps or flakes were added to the main wash, along with liquid bleach and bluing to enhance the cleaning performance of the poor quality of locally produced powders. These findings highlighted the potential for a high-performing detergent that would accomplish everything that currently required several products. The decision was made to proceed with the development and introduction of a superior-performing high-suds granular detergent. Once the basic product concept (i.e., one product instead of several to do laundry) was decided on, the company needed to determine the best components for a marketing mix to introduce the new product. The company went back to focus groups to assess reactions to different brand names (the choices were Ariel, already in the market as a low-suds detergent for automatic washers, and Tide, which had been marketed in Egypt in the 1960s and 1970s), to get ideas about the appeal and relevant wording for promotions, and to test various price ranges, package design, and size. Information derived from focus group encounters helped the company eliminate ideas with low consumer appeal and to focus on those that triggered the most interest. Further, the groups helped refine advertising and promotion wording to ensure clarity of communication through the use of everyday consumer language. At the end of this stage, the company had well-defined ideas garnered from several focus groups, but did not have a "feel" for the rest of the people in the

target market. Would they respond the same way the focus groups had? To answer this question, the company proceeded to the next step, a research program to validate the relative appeal of the concepts generated from focus groups with a survey (quantitative research) of a large sample from the target market. Additionally, brand name, price, size, and the product's intended benefits were tested in large sample surveys. Information gathered in the final surveys provided the company with the specific information used to develop a marketing program that led to a successful product introduction and brand recognition for Ariel throughout Egypt. Often times the combination of qualitative and quantitative research proves quite useful, as in the example of P&G's research on Ariel or as demonstrated in other industrial and business-to-business marketing settings. In one study the number of personal referrals used in buying legal, banking, and insurance services in Japan was found to be much greater than in the United States. The various comments made by the executives during the personal interviews in both countries proved invaluable in interpreting the quantitative results, suggesting implications for managers and providing ideas for further research. Likewise, the comments of sales managers in Tokyo during in-depth interviews helped researchers understand why individual financial incentives were found not to work with Japanese sales representatives. As we shall see later in this chapter, using either research method in international marketing research is subject to a number of difficulties brought about by the diversity of cultures and languages encountered.

### **Problems of Gathering Primary Data**

The problems of collecting primary data in foreign countries are different only in degree from those encountered in the United States. Assuming the research problem is well defined and the objectives are properly formulated, the success of primary research hinges on the ability of the researcher to get correct and truthful information that addresses the research

objectives. Most problems in collecting primary data in international marketing research stem from cultural differences among countries, and range from the inability of respondents to communicate their opinions to inadequacies in questionnaire translation.

### **Ability to Communicate Opinions**

The ability to express attitudes and opinions about a product or concept depends on the respondent's ability to recognize the usefulness and value of such a product or concept. It is difficult for a person to formulate needs, attitudes, and opinions about goods whose use may not be understood, that are not in common use within the community, or that have never been available. For example, it may be impossible for someone who has never had the benefits of an office computer to express accurate feelings or provide any reasonable information about purchase intentions, likes, or dislikes concerning a new computer software package. The more complex the concepts, the more difficult it is to design research that will help the respondent communicate meaningful opinions and reactions. Under these circumstances, the creative capabilities of the international marketing researcher are challenged. No company has had more experience in trying to understand consumers with communication limitations than Gerber. Babies may be their business, but babies often can't talk, much less fill out a questionnaire. Over the years Gerber has found that talking to and observing both infants and their mothers are important in marketing research. In one study Gerber found that breast-fed babies adapted to solid food more quickly than bottle-fed babies because breast milk changes flavor depending on what the mother has eaten. For example, infants were found to suck longer and harder if their mother had recently eaten garlic. In another study, weaning practices were studied around the world. Indian babies were offered lentils served on a finger. Some Nigerian children got fermented sorghum, fed by the grandmother through the funnel of

her hand. In some parts of-tropical Asia mothers "food-kissed" pre chewed vegetables into their babies' mouths. All this research helps the company decide which products are appropriate for which markets. For example, the Vegetable and Rabbit Meat and the Freeze-Dried Sardines and Rice flavors popular in Poland and Japan, respectively, most likely won't make it to American store shelves.

### **Willingness to Respond**

Cultural differences offer the best explanation for the unwillingness or the inability of many to respond to research surveys. The role of the male, the suitability of personal gender-based inquiries, and other gender-related issues can affect willingness to respond. In some countries, the husband not only earns the money but also dictates exactly how it is to be spent. Because the husband controls the spending, it is he, not the wife, who should be questioned to determine preferences and demand for many consumer goods. In some countries, women would never consent to be interviewed by a male or a stranger. A French Canadian woman does not like to be questioned and is likely to be reticent in her responses. In some societies, a man would certainly consider it beneath his dignity to discuss shaving habits or brand preference in personal clothing with anyone—most emphatically not a female interviewer. Anyone asking questions about any topic from which tax assessment could be inferred is immediately suspected of being a tax agent. Citizens of many countries do not feel the same legal and moral obligations to pay their taxes as do U.S. citizens. So, tax evasion is an accepted practice for many and a source of pride for the more adept. Where such an attitude exists, taxes are often seemingly arbitrarily assessed by the government, which results in much incomplete or misleading information being reported. One of the problems revealed by the government of India in a recent population census was the underreporting of tenants by landlords trying to hide the actual number of people living in houses and flats. The landlords had

been subletting accommodations illegally and were concealing their activities from the tax department.

In the United States, publicly held corporations are compelled by the Securities and Exchange Commission (SEC) to disclose certain operating figures on a periodic basis. In many European countries, however, such information is seldom if ever released and then most reluctantly. Attempts to enlist the cooperation of merchants in setting up an in-store study of shelf inventory and sales information ran into strong resistance because of suspicions and a tradition of competitive secrecy. The resistance was overcome by the researcher's willingness to approach the problem step-by-step. As the retailer gained confidence in the researcher and realized the value of the data gathered, more and more requested information was provided. Besides the reluctance of businesses to respond to surveys, local politicians in underdeveloped countries may interfere with studies in the belief that they could be subversive and must be stopped or hindered. A few moments with local politicians can prevent days of delay. Although such cultural differences may make survey research more difficult to conduct, it is possible<sup>^</sup> In some communities, locally prominent people could open otherwise closed doors; in other situations, professional people and local students have been used as interviewers because of their knowledge of the market. Less direct measurement techniques and nontraditional data analysis methods may also be more appropriate. In one study, Japanese supermarket buyers rated the nationality of brands (foreign or domestic) as relatively unimportant in making stocking decisions when asked directly; however, when an indirect, paired-comparison questioning technique was used, brand nationality proved to be the most important factor.

### **Sampling in Field Surveys**

The greatest problem of sampling stems from the lack of adequate demographic data and available lists from which to draw meaningful samples. If current, reliable lists are not available, sampling becomes more complex and generally less reliable. In many countries, telephone directories cross-index street directories, census tract and block data, and detailed social and economic characteristics of the population being studied are not available on a current basis, if at all. The researcher has to estimate characteristics and population parameters, sometimes with little basic data on which to build an accurate estimate. To add to the confusion, in some South American, Mexican, and Asian cities, street maps are unavailable, and in some Asian metropolitan areas, streets are not identified nor are houses numbered. In contrast, one of the positive aspects of research in Japan and Taiwan is the availability and accuracy of census data on individuals. In these countries, when a household moves it is required to submit up-to-date information to a centralized government agency before it can use communal services such as water, gas, electricity, and education. The effectiveness of various methods of communication (mail, telephone, and personal interview) in surveys is limited. In many countries, telephone ownership is extremely low, making telephone surveys virtually worthless unless the survey is intended to cover only the wealthy. In Sri Lanka, fewer than 10 percent of the residents—only the wealthy—have telephones. Even if the respondent has a telephone, the researcher may still not be able to complete a call. The adequacy of sampling techniques is also affected by a lack of detailed social and economic information. Without an age breakdown, for example, the researcher can never be certain of a representative sample requiring an age criterion because there is no basis of comparison with the age distribution in the sample. A lack of detailed information, however, does not prevent the use of sampling; it simply makes it more difficult. In place of probability techniques, many researchers in such situations rely on convenience samples taken in

marketplaces and other public gathering places. McDonald's recently got into trouble over sampling issues. The company was involved in a dispute in South Africa over the rights to its brand name in that fast-emerging market. Part of the company's claim revolved around the recall of the McDonald's name among South Africans. In the two surveys the company conducted and provided as proof in the proceedings, the majority of those sampled had heard the company name and could recognize the logo. However, the Supreme Court judge hearing the case took a dim view of the evidence because the surveys were conducted in "posh, white" suburbs when 76 percent of the South African population is black. Based in part on these sampling errors, the judge threw out McDonald's case. Inadequate mailing lists and poor postal service can also be problems for the market researcher using mail to conduct research. In Nicaragua, delays of weeks in delivery are not unusual, and expected returns are lowered considerably because a letter can be mailed only at a post office. In addition to the potentially poor mail service within countries, the extended length of time required for delivery and return when a mail survey is conducted from another country further hampers the use of mail surveys. Although airmail reduces this time drastically, it also increases costs considerably. The kinds of problems encountered in drawing a random sample include:

- No officially recognized census of population.
- No other listings that can serve as sampling frames.
- Incomplete and out-of-date telephone directories.
- No accurate maps of population centers. Thus, no cluster (area) samples can be made.

While all the conditions described do not exist in all countries, they illustrate why the collection of primary data requires creative applications of research techniques when firms expand into many foreign markets.

### **Language and Comprehension**

The most universal survey research problem in foreign countries is the language barrier. Differences in idiom and the difficulty of exact translation create problems in eliciting the specific information desired and in interpreting the respondents' answers. Equivalent concepts may not exist in all languages. Family, for example, has different connotations in different countries. In the United States, it generally means only the parents and children. In Italy and many Latin countries it could mean the parents, children, grandparents, uncles, aunts, cousins, and so forth. The meaning of names for family members can have different meanings depending on the context within which they are used. In the Italian culture, aunt and uncle are different for the maternal and paternal sides of the family. The concept of affection is a universal idea but the manner in which it is manifest in each culture may differ. Kissing, an expression of affection in the West is alien to many Eastern cultures and even taboo in some.

Literacy poses yet another problem. In some less-developed countries with low literacy rates, written questionnaires are completely useless. Within countries, too, the problem of dialects and different languages can make a national questionnaire survey impractical. In India, there are 14 official languages and considerably more unofficial ones. One researcher has used pictures of products as stimuli and pictures of faces as response criterion in a study of eastern German brand preferences to avoid some of the difficulties associated with language differences and literacy in international research. Furthermore a researcher cannot assume that a translation into one language will suffice in all areas where that language is spoken. Such was the case when one of the authors was in Mexico and requested a translation of the word outlet, as in retail outlet, to be used in Venezuela. It was read by Venezuelans to mean an electrical outlet, an outlet of a river into an ocean, and

the passageway into a patio. Needless to say, the responses were useless-although interesting. Thus, it will always be necessary for a native speaker of the target country's language to take the "final cut" in any translated material. All marketing communications, including research questionnaires, must be written perfectly. If not, consumers and customers will not respond with accuracy, or even at all. The obvious solution of having questionnaires prepared or reviewed by a native speaker of the language of the country is frequently overlooked. Even excellent companies like American Airlines bring errors into their measurement of customer satisfaction by using the exact same questionnaire in Spanish for their surveys of passengers on routes to Spain and Mexico. To a Spaniard orange juice is "zumo de naranja"; a Mexican would order "jugo de naranja." These apparently subtle differences are no such things to Spanish speakers. In another case, a German respondent was asked the number of washers (washing machines) produced in Germany for a particular year; the reply reflected the production of the flat metal disk. Marketers use three different techniques, back translation, parallel translation, and decentering, to help ferret out translation errors ahead of time.

- **Back Translation.** In back translation the questionnaire is translated from one language to another, and then a second party translates it back into the original. This process pinpoints misinterpretations and misunderstandings before they reach the public. A soft-drink company wanted to use a very successful Australian advertising theme, "Baby, its cold inside," in Hong Kong. They had the theme translated from English into Cantonese by one translator and then retranslated by another from Cantonese into English, where the statement came out, "Small Mosquito, on the inside it is very cold." Although "small mosquito" is the colloquial expression for small child in Hong Kong, the intended meaning was lost in translation.

- **Parallel Translation.** Back translations may not always ensure an accurate translation because of commonly used idioms in both languages. Parallel translation is used to overcome this problem. In this process, more than two translators are used for the back translation; the results are compared, differences discussed, and the most appropriate translation selected.

- **Decentering.** A third alternative, known as decentering, is a hybrid of back translation. It is a successive iteration process of translation and retranslations of a questionnaire, each time by a different translator. For example, an English version is translated into French and then translated back to English by a different translator. The two English versions are compared and where there are differences, the original English version is modified and the process is repeated. If there are still differences between the two English versions, the original English version of the second iteration is modified and the process of translation and back translation is repeated. The process continues to be repeated until an English version can be translated into French and back translated, by a different translator, into the same English. In this process, wording of the original instrument undergoes a change, and the version that is finally used and its translation have equally comprehensive and equivalent terminologies in both languages. Regardless of the procedure used, proper translation and perfect use of the local language in a questionnaire are of critical importance to successful research design. Because of cultural and national differences, confusion can just as well be the problem of the researcher as of the respondent. The question itself may not be properly worded in the English version, or English slang or abbreviated words are often translated with a different or ambiguous meaning. Such was the case mentioned above with the word outlet for retail outlet. The problem was not with the translation as much as it was of the term used in the question to be translated. In writing questions for translation, it is important that precise terms, not colloquialisms or slang, are

used in the original to be translated. One classic misunderstanding which occurred in a Reader's Digest study of consumer behavior in Western Europe resulted in a report that France and Germany consumed more spaghetti than did Italy. This rather curious and erroneous finding resulted from questions that asked about purchases of "packaged and branded spaghetti." Italians buy their spaghetti in bulk; the French and Germans buy branded and packaged spaghetti. Since the Italians buy little branded or packaged spaghetti, the results underreported spaghetti purchases by Italians. Had the goal of the research been to determine how much branded and packaged spaghetti was purchased, the results would have been correct. However, because the goal was to know about total spaghetti consumption, the data were incorrect. Researchers must always verify that they are asking the right question. Finally, some of the problems of cross-cultural marketing research can be addressed after data have been collected. For example, we know that consumers in some countries such as Japan tend to respond to rating scales more conservatively than Americans. That is, on a 1 to 7 scale anchored by "extremely satisfied" and "extremely dissatisfied," Japanese may tend to answer more toward the middle (more 3s and 5s), while Americans' responses may tend toward the extremes (more 1s and 7s). Such a response bias can be managed through statistical standardization procedures to maximize comparability. Some translation problems can also be detected and mitigated post hoc through other statistical approaches as well.

### **Multicultural Research: A Special Problem**

As companies become global marketers and seek to standardize various parts of the marketing mix across several countries, multicultural studies become more important. A company needs to determine to what extent adaptation of the marketing mix is appropriate. Thus, market characteristics across diverse cultures must be compared for similarities and differences before a company

proceeds with standardization on any aspect of marketing strategy. The research difficulties discussed thus far have addressed problems of conducting research within a culture. When engaging in multicultural studies, many of these same problems further complicate the difficulty of cross-cultural comparisons. Multicultural research involves dealing with countries that have different languages, economies, social structures, behavior, and attitude patterns. When designing multicultural studies, it is essential that these differences be taken into account. An important point to keep in mind, when designing research is to be applied across culture is to ensure comparability and equivalency of results. Different methods may have varying reliabilities in different countries. It is essential that these differences be taken into account in the design of a multicultural survey. Such differences may mean that different research methods should be applied in individual countries. In some cases the entire research design may have to be different between countries to maximize the comparability of the results. For example, Japanese, compared to American businesspeople, tend not to respond to mail surveys. This problem was handled in two recent studies by using alternative methods of questionnaire distribution and collection in Japan. In one study, attitudes of retail buyers regarding pioneer brands were sought. In the U.S. setting a sample was drawn from a national list of supermarket buyers and questionnaires were distributed and collected by mail. Alternatively, in Japan questionnaires were distributed through contact people at 16 major supermarket chains and then returned by mail directly to the Japanese researchers.<sup>23</sup> The second study sought to compare the job satisfaction of American and Japanese sales representatives. The questionnaires were delivered and collected via the company mail system for the U.S. firm. For the Japanese firm, participants in a sales training program were asked to complete the questionnaires during the program. While the authors of both studies suggest that the use of different methods of data collection in comparative studies does

threaten the quality of the results, the approaches taken were the best (only) practical methods of conducting the research. The adaptations necessary to complete these cross-national studies serve as examples of the need for resourcefulness in international marketing research. However, they also raise serious questions about the reliability of data gathered in cross-national research. There is evidence that often insufficient attention is given not only to non-sampling errors and other problems that can exist in improperly conducted multicultural studies, but also to the appropriateness of research measures that have not been tested in multicultural contexts.

### **Research on the Internet: A New Opportunity**

It is literally impossible to keep up with the worldwide growth in Internet usage. We know that at this writing there are more than 20 million users in more than 194 countries. While about 58 percent of the hosts are in the United States, international Internet usage is growing almost twice as fast as American usage. Growth in countries such as Costa Rica has been spurred by the local government's early (1989) decision to reclassify computers as "educational tools," thus eliminating all import tariffs on the hardware. The demographics of users worldwide are: 60%-40% male-female; average age about 32; about 60% college educated; median income of about \$60,000; usage time about 2.5 hours/week; and main activities are e-mail and finding information.<sup>27</sup> The percentage of home pages by language is English—82.3%, German—4.0%, Japanese-1.6%, French—1.5%, Spanish—1.1%, and all others less than 1%. For many companies the Internet provides a new and increasingly important medium for conducting a variety of international marketing research. New product concepts and advertising copy can be tested over the Internet for immediate feedback. Worldwide consumer panels might be created to help test marketing

programs across international samples. Indeed, it has been suggested that there are six different uses for the Internet in international research:

- (1) On-line surveys—these can include incentives for participation, and they have better "branching" capabilities (asking different questions based on previous answers) than more expensive mail and phone surveys.
- (2) On-line focus groups—bulletin boards can be used for this purpose.
- (3) Web visitor tracking—servers automatically track and time visitors' travel through Web sites.
- (4) Advertising measurement—servers track links to other sites and their usefulness can therefore be assessed.
- (5) Customer identification systems—many companies are installing registration procedures that allow them to track visits and purchases over time, creating a "virtual panel."
- (6) E-mail marketing lists—customers can be asked to sign up on e-mailing lists for future direct marketing efforts via the Internet.

It is quite clear that as the Internet continues to grow, even more kinds of research will become feasible, and it will be quite interesting to see the extent to which new translation software has an impact on marketing communications and research over the Internet.<sup>30</sup> Finally, as is the case in so many international marketing contexts, privacy is and will continue to be a matter of personal and legal consideration. A vexing challenge facing international marketers will be the cross-cultural concerns about privacy and the enlistment of cooperative consumer and customer groups. The ability to conduct primary research is one of the exciting aspects about the Internet. However, there are some severe limitations because of the potential bias of a universe composed solely of Internet respondents. Nevertheless, as more of the general population in countries gains

access to the Internet, this tool will be all the more powerful and accurate for conducting primary research. Today the real power of the Internet for international marketing research is the ability to easily access volumes of secondary data. These data have been available in print form for years but now they are much easier to access and, in many cases, more current. Instead of leafing through reference books to find two- or three-year-old data, as is the case with most printed sources, you can often find up-to-date data on the Internet. Such Internet sites as <http://stat-usa.gov> provide almost all data that are published by the U.S. government.

### **Problems in Analyzing and Interpreting Research Information**

Once data have been collected, the final steps in the research process are the analysis and interpretation of findings in light of the stated marketing problem. Both secondary and primary data collected by the market researcher are subject to the many limitations just discussed. In any final analysis, the researcher must take into consideration these factors and, despite their limitations, produce meaningful guides for management decisions. Accepting information at face value in foreign markets is imprudent. The meanings of words, the consumer's attitude toward a product, the interviewer's attitude, or the interview situation can distort research findings. Just as culture and tradition influence the willingness to give information, they also influence the information given. Newspaper circulation figures, readership and listener ship studies, retail outlet figures, and sales volume can all be distorted through local business practice. To cope with such disparities, the foreign market researcher must possess three talents. First, the researcher must possess a high degree of cultural understanding of the market in which research is being conducted. In order to analyze research findings, the social customs, semantics, current attitudes, and business customs of a society or a sub-segment of a society must

be clearly understood. Indeed, at some level it will be absolutely necessary to have a native of the target country involved in the interpretation of the results of any research conducted in a foreign market. Second, a creative talent for adapting research findings is necessary. A researcher in foreign markets often is called on to produce results under the most difficult circumstances and short deadlines. Ingenuity and resourcefulness, willingness to use "catch as catch can" methods to get facts, patience, a sense of humor, and a willingness to be guided by original research findings even when they conflict with popular opinion or prior assumptions are all considered prime assets in foreign marketing research. Third, a skeptical attitude in handling both primary and secondary data is helpful. For example, it might be necessary to check a newspaper press run over a period of time to get accurate circulation figures, or deflate or inflate reported consumer income in some areas by 25 to 50 percent on the basis of observable socioeconomic characteristics. Indeed, where data are suspect, such "triangulation" through the use of multiple research methods will be crucial. These essential traits suggest that a foreign marketing researcher should be a foreign national or should be advised by a foreign national who can accurately appraise the data collected in light of the local environment, thus validating secondary as well as primary data. Moreover, regardless of the sophistication of a research technique or analysis, there is no substitute for decision makers themselves getting into the field for personal observation.

### **Responsibility for Conducting Marketing Research**

Depending on the size and degree of involvement in foreign marketing, a company in need of foreign market research can rely on an outside foreign-based agency or on a domestic company with a branch within the country in question. It can conduct research using its own facilities or employ a combination of its own research force with the assistance of an outside agency.

Many companies have an executive specifically assigned to the research function in foreign operations; he or she selects the research method and works closely with foreign management, staff specialists, and outside research agencies. Other companies maintain separate research departments for foreign operations or assign a full-time research analyst to this activity. For many companies, a separate department is too costly; the diversity of markets would require a large department to provide a skilled analyst for each area or region of international business operations. A trend toward decentralization of the research function is apparent. In terms of efficiency, it appears that local analysts are able to provide information more rapidly and accurately than a staff research department. The obvious advantage to decentralization of the research function is that control rests in hands closer to the market. Field personnel, resident managers, and customers generally have a more intimate knowledge of the subtleties of the market and an appreciation of the diversity that characterizes most foreign markets. One disadvantage of decentralized research management is possible ineffective communications with home-office executives. Another is the potential unwarranted dominance of large-market studies in decisions about global standardization. That is to say, the larger markets, particularly the United States, justify more sophisticated research procedures and larger sample sizes, and results derived via simpler approaches that are appropriate in smaller countries are often unnecessarily discounted. A comprehensive review of the different approaches to multicountry research suggests that the ideal approach is to have local researchers in each country, with close coordination between the client company and the local research companies. This cooperation is important at all stages of the research project from research design to data collection to final analysis. Further, two stages of analysis are necessary. At the individual country level, all issues involved in each country must be identified, and at the multicountry level, the information must be distilled into a format that

addresses the client's objectives. Such recommendations are supported on the grounds that two heads are better than one and that multicultural input is essential to any understanding of multicultural data. With just one interpreter of multicultural data, there is the danger of one's self-reference criterion (SRC) resulting in data being interpreted in terms of one's own cultural biases. Self-reference bias can affect the research design, questionnaire design, and interpretation of the data. If a company wants to use a professional marketing research firm, many are available. Most major advertising agencies and many research firms have established branch offices worldwide. There also has been a healthy growth in foreign-based research and consulting firms. Of the 10 largest (based on revenues) marketing research firms in the world, four are based in the U.S. including the biggest, two are in France, two are in Germany, one is in the U.K., and one is in Japan. In Japan, where it is essential to understand the unique culture, the quality of professional market research firms is among the best. A recent study reports that research methods applied by Japanese firms and American firms are generally quite similar, but with notable differences in the greater emphasis of the Japanese on forecasting, distribution channels, and sales research. A listing of international marketing research firms is printed every July as an advertising supplement in the Marketing News.

### **Estimating Market Demand**

In assessing current product demand and forecasting future demand, reliable historical data are required. As previously noted, the quality and availability of secondary data frequently are inadequate; nevertheless, estimates of market size must be attempted to plan effectively. Despite limitations, there are approaches to demand estimation usable with minimum information. The success of these approaches relies on the ability of the researcher to find meaningful substitutes or approximations for the needed economic and

demographic relationships. Some of the necessary but frequently unavailable statistics for assessing market opportunity and estimating demand for a product are current trends in market demand. When the desired statistics are not available, a close approximation can be made using local production figures plus imports, with adjustments for exports and current inventory levels. These data are more readily available because they are commonly reported by the United Nations and other international agencies. Once approximations for sales trends are established, historical series can be used as the basis for projections of growth. In any straight extrapolation, however, the estimator assumes that the trends of the immediate past will continue into the future. In a rapidly developing economy, extrapolated figures may not reflect rapid growth and must be adjusted accordingly. For this reason, three other methods are recommended: expert opinion, analogy, and income elasticity.

### **Expert Opinion**

For many market estimation problems, particularly in new foreign countries, expert opinion is advisable. In this method, experts are polled for their opinions about market size and growth rates. Such experts may be companies' own sales managers or outside consultants and government officials. The key in using expert opinion to help in forecasting demand is triangulation that is, comparing estimates produced by different sources. One of the tricky parts is how best to combine the different opinions. Developing scenarios is useful in the most ambiguous situations, such as predicting demand for accounting services in emerging markets like China and Russia.

### **Analogy**

Another technique is to estimate by analogy. This assumes that demand for a product develops in much the same way in all countries as comparable economic development occurs in each country. First, a relationship must be established between the item to be estimated and a measurable variable in a country that is to serve as the basis for the analogy. Once a known relationship is established, the estimator then attempts to draw an analogy between the known situation and the country in question. For example, suppose a company wanted to estimate the market growth potential for a beverage in country X, for which it had inadequate sales figures, but the company had excellent beverage data for neighboring country Y. In country Y it is known that per capita consumption increases at a predictable ratio as per capita gross domestic product (GDP) increases. If per capita GDP is known for country X, per capita consumption for the beverage can be estimated using the relationships established in country Y. Caution must be used with analogy because the method assumes that factors other than the variable used (in this example GDP) are similar in both countries, such as the same tastes, taxes, prices, selling methods, availability of products, consumption patterns, and so forth. Despite the apparent drawbacks to analogy, it is useful where data are limited.

### **Income Elasticity**

Measuring the changes in the relationship between personal or family income and demand for a product also can be used in forecasting market demand. In income elasticity ratios, the sensitivity of demand for a product to income changes is measured. The elasticity coefficient is determined by dividing the percentage change in the quantity of a product demanded by the percentage change in income. With a result of less than one, it is said that the income-demand relationship is relatively inelastic; conversely, if the result is greater than one the relationship is elastic. As income increases, the demand for a product

increases at a rate proportionately higher than income increases. For example, if the income coefficient elasticity for recreation is 1.20, it implies that for each 1 percent change in income, the demand for recreation could be expected to increase by 1.2 percent; if the coefficient is 0.8, then for each 1 percent change in income, demand for recreation could be expected to increase only 0.8 percent. The relationship also occurs when income decreases, although the rate of decrease might be greater than when income increases. Income elasticity can be very useful, too, in predicting growth in demand for a particular product or product group. The major problem of this method is that the data necessary to establish elasticities may not be available. However, in many countries income elasticities for products have been determined and it is possible to use the analogy method described (with all the caveats mentioned) to make estimates for those countries. Income elasticity measurements only give an indication of change in demand as income changes and do not provide the researcher with any estimate of total demand for the product. As is the case in all market demand estimation methods described in this section, income elasticity measurements are no substitute for original market research when it is economically feasible and time permits. Indeed, the best approach to forecasting is almost always a combination of such macroeconomic data base approaches and interviews with potential and current customers. As more adequate data sources become available, as would be the situation in most of the economically developed countries, more technically advanced techniques such as multiple regression analysis or input-output analysis can be used.

### **Communicating with Decision Makers**

Most of the discussion in this chapter has regarded getting information from or about consumers, customers, and competitors. It should be clearly recognized, however, that getting the information is only half the job. That information must also be given to decision makers in a timely manner. High-

quality international information systems design will be an increasingly important competitive tool as commerce continues to globalize, and resources must be invested accordingly. Decision makers, often top executives, should be directly involved not only in problem definition and question formulation, but when the occasion warrants it (as in new foreign markets), they should also be involved in the field work of seeing the market and hearing the voice of the customers in the most direct ways. Top managers should have a "feel" for their markets which even the best marketing reports cannot provide. )

## **INTERNATIONAL MARKETING MANAGEMENT**

International Marketing is not the same thing as International Trade. Only a part of the international trade flows represents international marketing. *Marketing in an internationally competitive environment, no matter whether the market is home or foreign is known as international marketing.*

### **Special problems in international marketing**

Special problems in international marketing are as follows

1. Political and legal differences, 2. Cultural differences, 3. Economic differences, 4. Differences in the currency Unit, 5. Differences in languages, 6. Differences in marketing infrastructure, 7. Trade restrictions, 8. High cost of distance, 9. Differences in trade practices.

### **Motives of International marketing**

The motives for international marketing can be classified into Pull factors and push factors. Some of these factors are

1. Profit motive, 2. Growth opportunities, 3. Domestic market Constraints, 4. Competition, 5. Government policies and regulations, 6. Monopoly power 7. Spin – off Benefits and 8. Strategic vision.

## **INTERNATIONAL PLANNING ORGANISATION**

There are different organizational structures for doing international business. The structure is determined by factors such as the extent of commitment of the organisation to the international business and the nature of its international orientation, the size of international business and expansion plans, the number and consistency of product lines, characteristics of the foreign markets etc. The nature of the organisational structure is also influenced by the relative sizes of the domestic and foreign markets or their relative importance. Taggart and McDermott point out that while during the 1960s many US MNCs established an international division to oversee : their growing overseas operations, the international division was largely redundant for European MNCs. This was because the US MNCs still relied upon their large domestic market whereas the European MNCs — specially those from the smaller countries (like the Netherlands, Sweden, and Switzerland) — did not have a large domestic market. International sales often accounted for the bulk of their turnover, rather than a small proportion as was the case in the 1960s for many US MNCs. The European MNCs were, thus, more disposed to internationalisation. The organisational structure would undergo changes during the different stages of the evolution of a domestic firm into a transnational one. The common organisational types are described below:

### **Built-in Export Department**

The built-in export department is the simplest form of export organisation and, I therefore, the easiest to establish. Under this arrangement, as the name indicates, the export organisation is built into the regular domestic system. The function of the special department is usually confined to the actual selling or directing; and all such different functions connected with export transactions as advertising, credit, traffic, shipping and accounting are handled by the appropriate domestic departments. The built-in export department is suitable under certain conditions, such as when the export business is small, the company is new to international marketing, the management philosophy is not oriented towards growth in overseas business, the company resources are limited, etc. The built-in export department may also be regarded as the initial arrangement to do export business. In course of time, as the business expands, it may be developed into a separate export department. The built-in export department suffers from some disadvantages. Under this arrangement, many of the activities connected with international business are carried out by domestic departments. Sometimes, therefore, there may be a tendency to regard export activities as subsidiary to domestic business. Further, the personnel of the domestic departments may not have sufficient knowledge or experience to deal with matters connected with the overseas market. Another danger is that the export manager may not get the required amount of cooperation from the personnel of other departments who are not under his control.

### **Separate Export Department**

Although a relatively large volume of export business may be handled by a built-in form of organisation, this arrangement, when the overseas business substantially increases, becomes unsatisfactory. A separate export department may, therefore, be established to take effective care of all the activities connected with the export business.

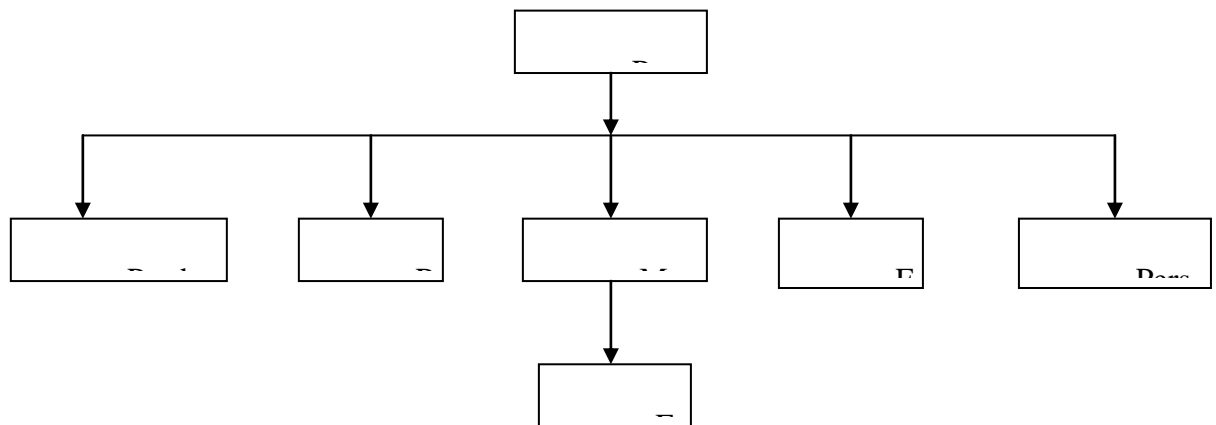


Fig.7.1 Export Department Structure

Further, a company which wants to expand its international business substantially would find a separate export department more useful than the built-in arrangement. Unlike the built-in department, the separate export department is essentially self-sufficient; and it is well equipped to handle all the activities connected with the export business. It is not, therefore, at the mercy of domestic departments. The organisational structure of the export department may vary between companies. The internal organisational structure of a separate export department may be based upon functions, territory, product or a combination of these. Needless to say, any such orientation of the internal organisational structure of the department will depend primarily upon how the marketing task varies. A separate marketing department avoids some of the problems of the built-in department, such as the clash between the international and domestic sides of the firm regarding the time to be spent by domestic marketing personnel on overseas business matters. As a separate department is a full-fledged department, it can do the job more efficiently. It can have personnel trained to perform the international marketing functions. A separate department will also impart an export orientation to the company. Another advantage is that a separate export department may, unlike the built in department, be located at

the most suitable place, which may not be the headquarters of the company. Fig. 7.1 and Fig. 7.2 show two alternate organisational structures. In Fig. 7.1, the export is a division of the marketing department which undertakes both domestic marketing and exports. Fig. 7.2 depicts an organisational structure with a separate, full-fledged, export department.

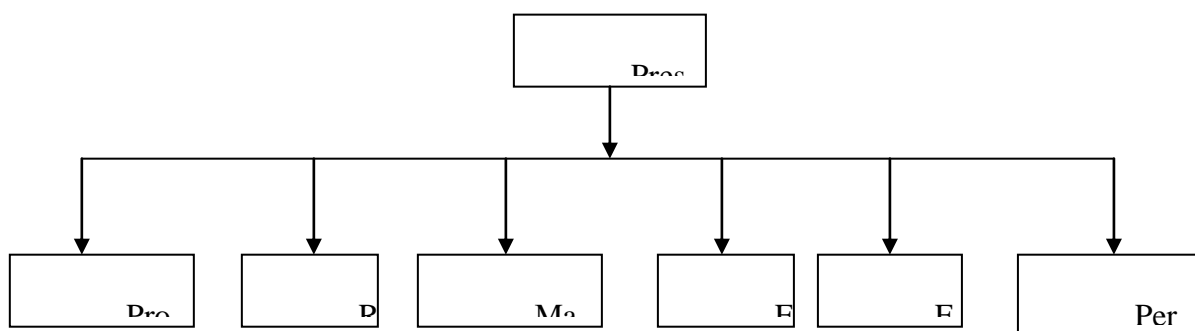


FIG. 7.2 Export Department

### Export Sales Subsidiary

Firms with large export business may establish export subsidiary companies and divorce international marketing activities from domestic operations because of certain advantages associated with it. Although an export sales subsidiary is a separate company, it is wholly owned and controlled by the parent company and is quasi-independent. The subsidiary company purchases products from the parent company and markets them abroad. The subsidiary may even deal in some non-competing products of other companies. An export sales subsidiary enjoys certain advantages. It is more independent than a department, and, therefore, more flexible and adaptable to changing situations. It can more easily develop export marketing facilities and expertise and organise international marketing tasks more effectively. Another

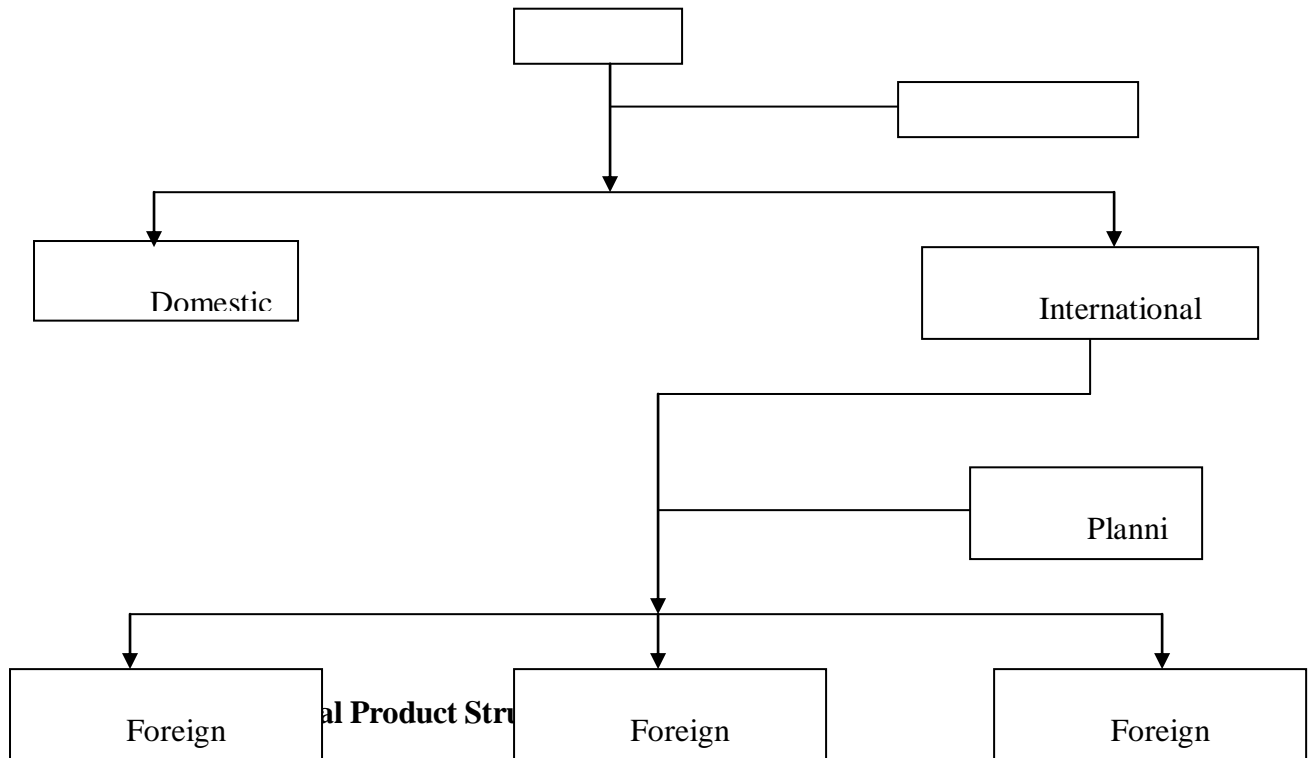
advantage of establishing a separate company and dividing the total business is a lower burden of tax. In terms of internal organisation and the specific activities performed, the sales subsidiary differs very little from a separate export department. Some companies establish subsidiary companies with the main objective of developing export markets and doing export business in a big way. The HMT (International) Ltd., the export marketing subsidiary of the HMT Ltd., has been assigned the tasks of exploring, developing and expanding export markets and enlarging international business.

### **International Division**

An export department or export subsidiary may be suitable for handling large exports but they may not be sufficient for managing the non-exporting international market entry modes. So companies, having foreign subsidiaries whose role is not to sales alone tend to establish an international division to manage the international business. Fig. 7.3 depicts one possible organisation structure with international division. An international division will facilitate concentrated attention on the international business. "However, creating an international division may generate internal problems. Coordinating activities may prove difficult because domestic activities are organised on a product line basis, while international side is organised on an area basis, i.e., non-domestic". The global organisational structures like the global product structure and global geographical structure which seek to integrate domestic and international operations emerged as a solution to this problem.

### **Global Organizational Structures**

The growth of business into global dimensions and the competition on a global basis resulted in the development of different global structures. The basic types of global structures are described below.



The product division structure is popular with large conglomerates with multiple, unrelated, business. Under this structure, different subsidiaries pertaining to different products within the same foreign country report to the head of different product groups at the head quarters. Fig. 7.4 illustrates a product based global organisational structure. The product division structure enhances coordination between different areas for any one product line but it reduces coordination of all product lines within each zone.

### Global Geographic Structure

Under the global geographic divisional structure the market is divided geographically. For example, when the Ranbaxy has restructured its organisation as a part of its global orientation, its export department has been abolished and the world market has been divided into four regions (India along with the Middle East forms one of the four regions). Fig. 8.5 depicts a global geographic divisional structure. In

contrast to the product division structure, the geographic division structure is appropriate for MNCs with narrow product lines. Naturally, this pattern tends to improve coordination of all product lines within each zone but to reduce coordination between areas for any one product line.

### **Global Functional Structure**

Under the functional structure, the head of functional areas, such as production, marketing, finance and personnel, are responsible for the worldwide operations of their own functional areas. In certain industries like energy and mining, a variation of the functional structure known as the process structure, which uses processes as the basis for the structure, is common.

### **Global Customer Structure**

If the global customer groups are so diverse requiring distinctive approaches, the organisational structure may be based on the diversity of the customer groups. This structure would not be appropriate if the product lines are very diverse making customer groups different for each product group.

### **Global Matrix Structure**

All the global organisational patterns depicted above have certain advantages and disadvantages. The mixed, hybrid or matrix structure seeks to combine the advantages and overcome the disadvantages of other alternative structures.

## **MARKET ENTRY STRATEGIES**

One of the most important strategic decisions in international business is the mode of entering the foreign market. On the one extreme, a company may do the complete manufacturing of the product domestically and export it to the foreign market. On the other extreme, a company may do, by itself, the

complete manufacturing of the product to be marketed in the foreign market there itself. There are several alternatives in between these two extremes. The choice of the most suitable alternative is based on the relevant factors related to the company and the foreign market. In some cases, the alternatives available may also be limited. For example, the policy of some governments may not be very positive towards foreign investments. Several governments have a definite preference for joint ventures over complete foreign ownership. In some cases, the government may prefer foreign investment leading to import substitution to perpetual import of a product. Thus, in some cases, government policies may rule out the best alternative if the environment were free.

Important foreign market entry strategies are the following:

- (i) Licensing / franchising
- (ii) Exporting
- (iii) Contract manufacturing
- (iv) Management contract
- (v) Assembly operations
- (vi) Fully owned manufacturing facilities
- (vii) Joint venturing
- (viii) Counter trade
- (ix) Mergers and acquisitions
- (x) Strategic alliance
- (xi) Third country location

### **LICENSING AND FRANCHISING**

Licensing and Franchising, which involve minimal commitment of resources and effort on the part of the international marketer, are easy ways of

entering the foreign markets. Under international licensing, a firm in one country (the licensor) permits a firm in another country (the licensee) to use its intellectual property (such as patents, trade marks, copyrights, technology, technical know-how, marketing skill or some other specific skill). The monetary benefit to the licensor is the royalty or fees which licensee pays. In many countries, such fees or royalties are regulated by the government; it does not exceed five per cent of the sales in many developing countries. A licensing agreement may also be one of cross licensing, wherein there is a mutual exchange of knowledge and /or patents. In cross-licensing, a cash payment may or may not, be involved. Franchising is “a form of licensing in which a parent company (the franchiser) grants another independent entity (the franchisee) the right to do business in a prescribed manner. This right can take the form of selling the franchisor’s products, ‘using its name, production and marketing techniques, or general business approach. One of the common forms of I franchising involves the franchisor supplying an important ingredient (part, material etc.) for the finished product, like the Coca Cola supplying the syrup to the bottlers. Usually franchising involves a combination of many of the elements mentioned above. The major forms of franchising are *manufacturer-retailer systems* (such as automobile dealership), *manufacturer-wholesaler systems* (such as soft drink companies), and *service firm-retailer systems* (such as lodging services and fast food outlets). There are also cases of cross or reverse franchise agreements. For example, the I.T.C. Hotels and ITT Sheraton Corporation had such an agreement under which ITC Hotel’s Welcome Group franchised two of its hotels in Bangkok and Hong Kong ITT Sheraton, holding, in exchange, the franchise for Sheraton in India. Later the partners decided to set up a joint venture — ITC-Sheraton — with Sheraton having a majority stake, to manage all new ITC hotel projects in India. One of the growing trends recently has been trademark licensing. Czinkota and

Ronkainen point out that trademark licensing has become a substantial source of worldwide revenue. The total volume of trademark licensing was expected to reach \$ 75 billion by 1990. The names or logos of designers, literary characters, sports teams, and movie stars appear on clothing, games, foods and beverages, gifts and novelties, toys and home furnishings. A number of foreign companies have entered the Indian market, both industrial and consumer goods, by licensing. The IFB washing machine, for example, was manufactured in India under license from Bosch of Germany. The U.S. multinational General Electric (GE) has licensed its patented technology to a small scale unit in India established for the manufacture of high intensity discharge (HID) fittings. As electrical fittings were reserved for the small scale sector, GE, had, perhaps no alternative to enter the market. After four years of scouting around, Nike International Ltd., the world's largest sports shoe and Apparel Company finally decided in 1995 to enter the Indian market by licensing. Sierra Industrial Enterprises Ltd., the licensee, will invest in setting up the complete quality control, marketing and distribution operations and will pay Nike 5 per cent royalty on ex-factory price of both footwear and apparel for the use of the brand name. International licensing/franchising have grown very substantially. Czinkota and Ronkainen succinctly describe their attractiveness or reasons for popularity: "As an entry strategy, it requires neither capital investment nor knowledge and marketing strength in foreign markets. By earning royalty income, it provides an opportunity to exploit research and development already committed to Licensing reduces risk of exposure to government intervention in that the licensee is typically a local company that can provide leverage against government action. Licensing will help to avoid host country regulations that are more prevalent in equity ventures. Licensing may also serve as a stage in the internationalization of the firm by providing a means by which foreign markets can be tested without

major involvement or capital or management time. Another advantage of licensing is that it may be employed as a preemptive strategy against competitors by combing the foreign markets before the competitors could enter. Thus, as pointed out under the section competition in Chapter 1, the General Electric of U.S.A. by licensing its advanced gas turbine technology to foreign producers who were potential competitors could eliminate possible competition from them. Licensing has been used by many companies also to harvest their obsolete products. This strategy has been employed, in particular, in developing countries. When the market is closed by the host country regulations either to imports or to foreign investment, licensing may provide a viable opportunity to enter such a market. From the point of view of the licensee, licensing provides the great advantage of entering the market with a proven product/technology or marketing intangible without having to run the risk of R & D failures. It also reduces the investment requirements. In the past many U.S. companies with prevalent attitude that “we have enough business right here in the States”, were not seriously looking to expand globally licensing appeared to be a very attractive proposition. For example, between 1960-67, about 200 licensing agreements were concluded between the U.S. and Japanese firms for transfer of T.V. technology to Japan. Firms in several other industries also licensed their technology etc. to foreign firms. But several of them were shocked to learn that they had grossly underestimated the vast potential of the foreign markets. For example, one U.S. firm that licensed an English firm to manufacture and sell its products in the United Kingdom, but agreed to give the English firm an exclusive right to sub-licence the U.S. expertise in other countries, for it then had no marketing commitment to exports. Within a few years, global markets developed for the company’s products, and were stuck with another party getting the benefits. Another U.S. firm, a drug manufacturer, gave an Asian Company a

manufacturing license. The Asian market, which up to then had been nothing at all, boomed, leaving the U.S. firm as almost an outsider.

One of the important risks of licensing is that the licensor would be developing a potential competitor; the licensee would become a competitor after the expiry of the licensing agreement. The licensee may even develop capabilities to introduce better products. The skill of the Japanese in product improvement is well-known. In several electronic products, including T.V., the Japanese have become world leaders or strong competitors in due course. Licensees in the developing countries might gain an edge over the licensor, after the term of the license, because of their low cost of labor which would enable them to compete with the erstwhile licensor in his own home market as well as in the foreign markets. Some companies are, therefore, hesitant to enter into licensing agreements.

### **EXPORTING**

Exporting, the most traditional mode of entering the foreign market is quite a common one even now. As pointed out in Chapter 1, international trade has been growing much faster than the world output resulting in greater world economic integration. Exporting is the appropriate strategy when one or more of the following conditions prevail:

1. The volume of foreign business is not large enough to justify production in the foreign market.
2. Cost of production in the foreign market is high.
3. The foreign market is characterized by production bottlenecks like infrastructural problems, problems with materials supplies etc.
4. There are political or other risks of investment in the foreign country.
5. The company has no permanent interest in the foreign market concerned

or that there is no guarantee of the market available for a long period.

6. Foreign investment is not favored by the foreign country concerned.
7. Licensing or contract manufacturing is not a better alternative.

Exporting is attractive than other modes particularly when underutilized capacity exists. Even when there is no excess capacity, expansion of the existing facility may sometimes be easier and less costly than setting up production facilities abroad. Further, many governments, as in India, provide incentives for establishing facilities for export production. The alternatives to making in foreign countries by the international marketer for marketing the goods in the foreign countries are licensing and contract manufacturing. Although these have certain advantages, there are also certain risks. Hence, if a company does not want to go in for licensing or contract manufacturing, the only avenue open is exporting. Although exporting may turn out to be the best alternative under a given set of conditions or environmental factors, there are several sets of conditions which make exporting less attractive than one or more of other alternatives. Policies of some foreign governments discriminate against imports; in some cases import is even banned. It may be noted that hostility against imports have been encouraging substitution of exports by production in the foreign markets. A number of foreign companies have set up production facilities in the European Community to overcome the import barriers. Japanese transplants in North America have also been caused to a considerable extent by the hostility towards imports. Besides, in a number of cases cost considerations make foreign production or assembly preferable to other entry strategies. Further, as noted in the introductory chapter, exporting marks the first stage in the evolution of international business of many companies. As the international business grows or as the environment changes or to expand the business it may become necessary to change the strategies.

There are, broadly, two ways of exporting, viz., indirect exporting and direct exporting. They are described in the chapter on International Distribution.

### **CONTRACT MANUFACTURING**

Under contract manufacturing, a company doing international marketing contracts with firms in foreign countries to manufacture or assemble the products while retaining the responsibility of marketing the product. This is a common practice in international business. There are a number of multinationals and affiliates of multinationals which employ this strategy in India in respect of some of the products they market, like Park Davis, Hindustan Lever, etc.

Contract manufacturing has the following advantages:

1. The company does not have to commit resource for setting up production facilities.
2. It frees the company from the risks of investing in foreign countries.
3. If idle production capacity is readily available in the foreign country, it enables the marketer to get started immediately.
4. In many cases, the cost of the product obtained by contract manufacturing is lower than if it were manufactured by the international firm. For example, the product cost in the small scale sector is much lower than in the large scale sector for many products because of the lower wages, lower overheads, and tax concessions. Moreover, if excess capacities are available with existing units, it may even be possible to get the product supplied on the marginal cost basis.
5. Contract manufacturing also has the advantage that it is a less risky way to start with. If the business does not pick up sufficiently, dropping it is easy; but if the company had established its own production facilities, the exit would be difficult. It may be interesting to note that the availability of excess capacity with some soap manufactures enabled several foreign companies to experiment With new brands

of toilet soap in the Indian market. For example, Godrej soaps manufactured Dettol for Reckittand Coleman; Clearton for Nicholas Laboratories; Johnson's Baby Soap for Johnson and Johnson; and Ponds Dreamflower, Cold Cream and Sandalwood for Ponds. It may be noted that some of these brands have not succeeded in the market. The cost to the company of the product failure is relatively low when it did not invest in production facilities.

6. Moreover, contract manufacturing may enable the international firm to enlist national support.

Contract manufacturing, however, has the following disadvantages:

1. In some cases, there will be the loss of potential profits from manufacturing.
2. Less control over the manufacturing process.
3. Contract manufacturing also has the risk of developing potential competitors.
4. It would not be suitable in cases of high-tech products and cases which involve technical secrets etc.

### **MANAGEMENT CONTRACTING**

Under the management contract, the firms providing the management know-how may not have any equity stake in the enterprise being managed. In short, "in a management contract the supplier brings together a package of skills that will provide an integrated service to the client without incurring the risk and benefit of ownership. Thus, as Kotler observes, management contracting is a low-risk method of getting into a foreign market and it starts yielding income right from the beginning. The arrangement is especially attractive if the contracting firm is given an option to purchase some shares in the managed company within a stated period. Management contract could, sometimes, bring in additional benefits for the managing company. It may obtain the business of exporting or selling otherwise of the products of the managed company or supplying the inputs required by the

managed company. Management contract enables a firm to commercialize existing know-how that has been built up with significant investments and frequently the impact of fluctuations in business volumes can be reduced by making use of experienced personnel who otherwise would have to be laid off. Management contracts, obviously, have clear benefits for the clients. “They can provide organizational skills not available locally, expertise that is immediately available rather than built up, and management assistance in the form of support services that would be difficult and costly to replicate locally.” Management contracts have disadvantages under certain conditions. As Kotler observes, the arrangement is not sensible if the company can put its scarce management talent to better use, or if there are greater profits to be made by undertaking the whole venture. Management contract may prevent a company from setting up its own operations for a particular period. One possible risk from the point of view of the client is over-dependence and loss of control. The client should enable itself to steadily develop its own capabilities. Some Indian companies—Tata Tea, Harrisons Malayalam and AVT—have contracts to manage a number of plantations in Sri Lanka. Tata Tea also has a joint venture in Sri Lanka, namely, Estate Management Services Pvt. Ltd.

### **TURNKEY CONTRACTS**

Turnkey contracts are common in international business in the supply, erection and commissioning of plants, as in the case of oil refineries, steel mills, cement and fertilizer plants etc.; construction projects and franchising agreements. “A turnkey operation is an agreement by the seller to supply a buyer with a facility fully equipped and ready to be operated by the buyer's personnel, who will be trained by the seller. The term is sometimes used in fast-food franchising when a franchiser agrees to select a store site, build the store, equip it, train the franchisee and employees and sometimes arrange for the financing”.

Many turnkey contracts involve government/public sector as buyer (or seller in some cases). A turnkey contractor may subcontract different phases/parts of the project.

### **FULLY OWNED MANUFACTURING FACILITIES**

Companies with long term and substantial interest in the foreign market normally establish fully owned manufacturing facilities there. As Drucker points out, "it is simply not possible to maintain substantial market standing in an important area unless one has a physical presence as a producer. A number of factors like trade barriers, differences in the production and other costs, government policies etc. encourage the establishment of production facilities in the foreign markets. More information about this is provided in the chapter on *International Investment*. Establishment of manufacturing facilities abroad has several advantages. It provides the firm with complete control over production and quality. It does not have the risk of developing potential competitors as in the case of licensing and contract manufacturing. Wholly owned manufacturing facility has several disadvantages too. In some cases, the cost of production is high in the foreign market. There may also be problems such as restrictions regarding the types of technology, non-availability of skilled labour, production bottlenecks due to infrastructural problems etc. If the market size is small, a separate production unit for the market may be uneconomical. Foreign investment also entails political risks. Fully owned enterprises may not be allowed or favoured in some countries, particularly in low priority areas. Moreover, this method demands sufficient financial and managerial resources on the part of the company.

### **ASSEMBLY OPERATIONS**

As Miracle and Albaum point out, a manufacturer who wants many of the advantage that are associated with overseas manufacturing facilities and yet

does not want to go that far may find it desirable to establish overseas assembly facilities in selected markets. In a sense, the establishment of an assembly operation represents a cross between exporting and overseas manufacturing. Having assembly facilities in foreign markets is very ideal when there are economies of scale in the manufacture of parts and components and when assembly operations are labour intensive and labour is cheap in the foreign country. It may be noted that a number of U.S. manufacturers ship the parts and components to the developing countries, get the product assembled there and bring it back home. The U.S. tariff law also encourages this. Thus, even products meant to be marketed domestically are assembled abroad. Assembling the product meant for the foreign market in the foreign market itself has certain other advantages, besides the cost advantage. The import duty is normally low on parts and components than on the finished product. Assembly operations would satisfy the 'local content' demand, at least to some extent. Because of the employment generation, the foreign government's attitude will be more favorable than towards the import of the finished product. Another advantage is that the investment to be made in the foreign country is very small in comparison with that required for establishing complete manufacturing facilities. The political risk of foreign investment is, thus, not much.

### **JOINT VENTURES**

Joint venture is a very common strategy of entering the foreign market. In the widest sense, any form of association which implies collaboration for more than a transitory period is a joint venture (pure trading operations are not included in this concept). Such a broad definition encompasses many diverse types of joint overseas operations, viz.,

1. Sharing of ownership and management in an enterprise.
2. Licensing/franchising agreements.
3. Contract manufacturing.

#### 4. Management contracts.

Three of the above have already been discussed in the preceding sections. The following paragraphs are confined to the first category referred to above, i.e., joint ownership ventures. What is often meant by the term joint venture is joint ownership venture. The essential feature of a joint ownership venture is that the ownership and management are shared between a foreign firm and a local firm. In some cases there are more than two parties involved. For example, Pepsi's Indian joint venture involved Voltas and Punjab Agro Industries Corporation. A joint ownership venture may be brought about by a foreign investor buying an interest in a local company, a local firm acquiring an interest in an existing foreign firm or by both the foreign and local entrepreneurs jointly forming a new enterprise.

It is also a common practice to split the local interest between a partner and various public participation (including public sector firms or industrial development organisations). Such a strategy may enable the international firm to retain much control despite a minority holding as the power of the remaining shares is spread out. Further, equity holding by the public would help the enterprise get some public support. Partnership with government organisation may help to obtain favourable treatment from the government. In countries where fully foreign owned firms are not allowed or favoured, joint venture is the alternative if the international marketer is interested in establishing an enterprise in the foreign market. Many foreign companies entered the communist, socialist and other developing countries by joint venturing. One important advantage of joint venturing is that it permits a firm with limited resources to enter more foreign markets than might be possible under a policy of forming wholly owned subsidiaries. In some cases, it is also possible to swap know-how (such as patent rights for equity) in forming joint venture as a means of securing ownership in foreign operations. Partnership with local firms has certain specific

advantages. The local partner would be in a better position to deal with the government and the public. Further, there would not be much public hostility when there is a local partner; it would be much less when there is equity holding by the government sector and the public. A right local partner for a joint venture can have a major impact on a firm's competitiveness because such a partner can serve as a cultural bridge between the manufacturer and the market. For example, several successful foreign affiliated companies have demonstrated how the right partnership can strongly enhance a firm's competitive edge and its ability to adapt to and cope with the idiosyncrasies of the Japanese market. As pointed out in the chapter on Globalisation of Indian Business many Indian firms have used the joint venture route to enter foreign markets. The economic liberalisation has caused a spurt in joint ventures in India. In the five years since the liberalisation of 1991, more than four thousand joint ventures were entered into between Indian companies and transnationals. Joint ventures present a mixed picture of success and failure. While some joint ventures are very successful, some face problems from the very beginning and in case of some others problems develop after a period of mutual benefit and success. A McKinsey world wide study of more than 200 alliances (principally joint ventures) has shown that the median life span of them is only seven years and in more than 80 per cent of the cases, it ends in one partner selling out to the other. In fact, joint ventures are not necessarily meant to be permanent. They are meant to serve specific objectives within a period of time and once the objectives are achieved the continuation depends on the reassessment of the situation by the partners. A number of joint ventures fail to achieve the objectives by either or both the partners and this could naturally result in the breakdown of the alliance. A joint venture may go through "several points of crisis, caused by the realisation on the part of either — sometimes both — of the partners that its expectations are not being fulfilled and, perhaps, even being negated". Chances

of such flash points are more with the flattening out of the gains curve on any of the parameters that govern either partner's decision to be involved in the joint venture. For, at this point, the gains of one of the partners become disproportionate to those of the other, leading the former to re-examine the rationality of retaining the relationship." Such flash points, however, need not necessarily result in the termination of the joint venture, they may be managed so that there will be more equitable gains from the joint venture. One of the important reasons for the failure of joint ventures in India is the unequal resource and bargaining powers of the partners. The new business environment that resulted from the liberalisation has increased the cases of failures on account of this factor. Many transnationals wanted to hike their share in the equity of the joint venture. This was the reason for the end of the 28 year old partnership between Royal Dutch Shell and NOCIL. Now that foreign firms are able to set up fully owned subsidiaries, a number of foreign firms have turned to such ventures, discarding or neglecting their existing joint ventures in the country. There are also several cases of the Indian partner's stake, fully or partially, sold to the foreign partner because of financial problems. Similarly, the Indian partner is unable to match with the resourceful foreign firm in bringing in additional funds for expansion, the Indian partner's share of the equity holding falls. A joint venture can succeed only if both the partners have something definite to offer to the advantage of the other, and reap definite advantages, and have mutual trust and respect.

### **THIRD COUNTRY LOCATION**

Third country location is some times used as an entry strategy. When there is no commercial transactions between two nations because of political reasons or when direct transactions between two nations are difficult due to political reasons or the like, a firm in one of these nations which wants to enter the other market will have to operate from a third country base. For example,

Taiwanese entrepreneurs found it easy to enter People's Republic of China through bases in Hong Kong. Third country location may also be helpful to take advantage of the friendly trade relations between the third country and the foreign market concerned. Thus, for example, Rank Xerox found it convenient to enter the USSR through its Indian joint venture Modi Xerox. There are several cases of countries not having direct commercial transactions. For example, it was true of Israel and Arab Countries. In the past, government of India did not permit trade with South Africa and Mauritius. Sometimes commercial reasons encourage third country location. For example, several Japanese companies established production facilities in developing countries to circumvent the non-tariff barriers (like quotas, voluntary export restraints and orderly marketing arrangement) to imports to countries like the United States and also to avail of the preferential treatment accorded by the developed countries to the imports from the developing countries. Further, third country location may be resorted to reduce cost of production and thereby to increase price competitiveness to facilitate market entry or for improving/maintaining the market position. The incentives offered by governments, particularly of the developing countries, for investment and exports encourage such third country location. The export processing zones are particularly attractive in this respect.

### **MERGERS AND ACQUISITIONS**

Mergers and Acquisitions (M & A) have been a very important market entry strategy as well as expansion strategy. A number of Indian companies have also used this entry strategy as noted towards the end of this chapter. Mergers and acquisitions have certain specific advantages. It provides instant access to markets and distribution network. As one of the most difficult areas in international marketing is the distribution, this is often a very important consideration for M & A. The General Electric, (GE), USA, took over Hungary's light bulb maker Tungsram. Instead of starting a 'greenfield'

operation in Hungary by building a new factory and hiring the people needed, why did the multinational giant take over Tungsram, a typical Hungarian enterprise bogged down with so many problems calling for a painful restructuring? The answer is that Tungsram gave GE entry to the East European light bulb market, from which it had been virtually excluded by Philips and Osram. Tungsram's share of the market in the 1980s was a respectable 9 to 10 per cent. Another important objective of M and A is to obtain access to new technology or a patent right. M and A also has the advantage of reducing the competition. Mergers and acquisitions may also give rise to some problems which arise mostly because of the deficiencies of the evaluation of the case for acquisition. Sometimes the cost of acquisition may be unrealistically high. Further, when an enterprise is taken over, all its problems are also acquired with it. The success of the enterprise will naturally depend on the success in solving the problems. It has also been observed that the takeover spree lands several companies in trouble. For example, in the early 1990s a number of Japanese companies began to sell some of the foreign businesses which they had acquired a few years ago. The main reason for this was the financial crunch.

### STRATEGIC ALLIANCE

Strategic alliance has been becoming more and more popular in international business. Also known by such names as entente and coalition, this strategy seeks to enhance the long term competitive advantage of the firm by forming alliance with its competitors, existing or potential in critical areas, instead of competing with each other. "The goals are to leverage ; critical capabilities, increase the flow of innovation and increase flexibility in responding to market and technological changes." Strategic alliance is also sometimes used as a market entry strategy. For example, a firm may enter a foreign market by forming an alliance with a firm in the foreign market for

marketing or distributing the former's products. A U.S. pharmaceutical firm may use the sales promotion and distribution infrastructure of a Japanese pharmaceutical firm to sell its products in Japan. In return, the Japanese firm can use the same strategy for the sale of its products in the U.S. market. Strategic alliance, more than an entry strategy, is a competitive strategy. Strategic alliances which enable companies to increase resource productivity and profitability by avoiding unnecessary fragmentation of resources and duplication of investment and effort are growing in popularity and are very conspicuous in such industries as pharmaceuticals, computer, nuclear, telematics etc. which are characterised by high fixed costs in K and D and manufacturing and/or high and fast changing technology. Examples of cross boarder alliances in the telematics sector which essentially bring together two separate streams of technology — that related to information gathering and processing and that related to information transmission — include IBM's agreements with STET, Italy's state owned telecommunications company and Nippon Telegraph and Telephone (Japan) to develop computer communications services, and a joint research venture with Ericson (Sweden) to explore the linking of data-management technology with digital switching technology.

The automobile industry has been witnessing several alliances for overseas operations. The Isuzu Motors Ltd. and Fuji Heavy Industries Ltd. of Japan have set up a joint plant in the U.S. which can build cars for Fuji and trucks for Isuzu in the same line. Some Japanese automakers have joined forces with foreign big names like General Motors and Chrysler. The European car manufacturers are also teaming up to enhance their competitiveness, often in one-off projects to produce, say, an engine or transmission. Peugeot, Renault and Volvo already share V6 engine. According to an alliance between Tatas and TFR, a leading French leather finisher and European marketer, Tatas will integrate its production with the exact colour, texture and other requirements of

large European buyers, while TFR will provide the existing marketing network, links to key buyers, its name and reputation and knowledge of the latest fashion trends. Tata Tea has entered in to an alliance with Tetley so that the marketing expertise of Tetley is available to market tea abroad. Explaining international production, Dunning observes that within the service sector strategic alliances are less common, but those between hotels, airlines and tour operators and between accountants and management consultants are increasing; while international consortia of investment banking and construction firms have long been a feature of the world commercial scenario.

### **COUNTERTRADE**

Although the major reason for the substantial growth of counter trade is its use as a strategy to increase exports, particularly by the developing countries, countertrade has been successfully used by a number of companies as an entry strategy. For example, Pepsico gained entry to the USSR by employing this strategy. Countertrade is a form of international trade in which certain export and import transactions are directly linked with each other and in which import of goods are paid for by export of goods, instead of money payments. In the modern economies, most transactions involve monetary payments and receipts, either immediate or deferred. As against this, "counter trade refers to a variety of unconventional international trade practices which link exchange of goods — directly or indirectly — in an attempt to dispense with currency transactions.

#### **Forms of Counter trade**

Counter trade takes several forms. The following are the most common among them.

##### **Barter**

Barter refers to direct exchange of goods of equal value, with no money and no third party involved in it. For example, a counter trade deal between the

Minerals and Metals Trading Corporation of India (MMTC) and a Yugoslavian company involved import of 50,000 tonnes of rails of the value of about \$ 38 million by the MMTC and the purchase by the Yugoslavian company of iron ore concentrates and pellets of the same value.

### **Buy Back**

Under the buy back agreement, the supplier of plant, equipment or technology agrees to purchase goods manufactured with that equipment, or technology. Under the buy back \ scheme, the full payment may be made in kind or a part may be made in kind and the balance in cash. Thus, a Rs. 20 crore buy back agreement with the Soviet Union provided for the import of 200 sophisticated looms by the National Textiles Corporation. The buy back ratio j was 75 per cent.

### **Compensation Deal**

Under this arrangement, the seller receives a part of the payment in cash and the rest in products.

### **Counter purchase**

Under the counter purchase agreement the seller receives the full payment in cash but agrees to spend an equivalent amount of money in that country within a specified period. A classic example of this kind of an agreement was Pepsi Cola's trade with the USSR. Pepsi Cola got paid in Rubles for the sale of its concentrates in the USSR but spent this amount for purchase of Russian products like Vodka and wine.

The array of counter trade transactions reported in the trade press is intriguing. Coca Cola has traded its syrup for cheese from a factory it built in the Soviet Union, for oranges from an orchard it planted in Egypt, for tomato paste from a plant it installed in Turkey, for Polish beer, and for soft drink bottles from Hungary. A Swedish band was paid in coal for its concerts in Poland, Boeing exchanged ten 747s for 34 million barrels of Saudi Arabian oil. Argentina awarded a fertilizer factory contract to

Czechoslovakian firms with the stipulation that suppliers buy vegetables and other agricultural goods produced with fertilizer. Many counter trade deals involve more than two parties and the process becomes complex and intricate. If the seller can get in exchange from the buyer the products which he wants or for which he has a ready market, the counter trade deal would be very smooth. However, in several cases the buyer will not be in a position to offer in exchange goods which the seller really needs. In such cases, it may become necessary, for the deal to be struck, for the seller to accept the products the buyer can offer and hunt for buyers for such products, Kolter, for example, cites a very interesting case: Daimler Benz agreed to sell thirty trucks to Romania and accept in exchange 150 Romanian made jeeps, which it sold in Ecuador in exchange for bananas which it brought back to West Germany and sold to a West German super market chain in exchange for Deutsch marks. Through this circuitous transaction, it finally achieved payment in German currency. Such complexities involved in many counter trade deals have given an important role to the international trading houses in such transactions. The insurmountable problem of finding suitable goods in return by the exporters "has redefined the importance in Japan of the trading houses" and "Japan's nine major general trading houses have all now established divisions specifically to research counter trade opportunities." Counter deals were used by the Japanese trading houses as a means to boost their business with hard currency strapped China and the former USSR. These trading houses can take massive and complex counter trade deals "in their strides as they possess expertise in almost every field, practice every conceivable trading pattern, and can mobilize everything from staff to technology to finance. In addition, most are under the umbrellas of Zaibatsu that include powerful banks and/or construction firms. As if this were not enough, the trading houses are prepared to join forces with each other if necessary under the auspices of the awesome Nihon Boekikai, the body they set up themselves for the handling of joint ventures.

### **Growth of Counter trade**

A significant volume of international trade is covered by counter trade. Counter trade, of course, is not a new phenomenon but the nineteen seventies and eighties witnessed a remarkable growth in this type of international trade, encouraged by many governments and actively involved by many trading houses, both private and public, although organizations like GATT (WTO) AND IMF do not favors it. According to one report, the number of countries practicing counter trade increased from 27 in 1973 to more than 90 by mid 1980s. A study by the US Departments of Commerce found that counter trade covered 38 per cent of East-West trade in 1981 compared to 28 percent in 1976. According to the estimates made by the Economist quite some time ago, counter trade accounted for one-fourth of all world trade. However, the GATT in a report had noted that in 1983 counter trade accounted for about 8 per cent of the global trade. A source in the U.S. Department of Commerce expected some time ago that counter trade would be reflected, in one way or the other, in 50 per cent of the world trade by the end of the 20th current century. The political and economic changes in the former USSR and Eastern Europe do not appear to adversely affect the growth of counter trade.

Counter trade has been growing with government patronage. According to Terone report, more than 81 countries across the world had actual pro-counter trade government policies. Counter trade has been made mandatory by a number of countries including Indonesia, South Korea, Malaysia, and Australia in case of government/public sector purchases of above certain specified value. Even though a number of other countries like Bangladesh, Burma, China, Pakistan, Philippines, Singapore, Thailand and Taiwan have no mandatory provisions, all encourage their importers to settle transactions on counter trade basis. Indian public sector agencies like STC and MMTC are active in counter trade. Government of India set up a special cell in the Ministry of Commerce to

monitor international developments in counter trade and to develop appropriate policy to enable Indian canalizing agencies to make best use of opportunities available to boost India's exports through counter trade.

It may be noted that the South Commission has advocated counter trade as a useful mechanism for overcoming difficulties of payments, export credit, and foreign exchange which might otherwise be serious obstacles to the expansion of trade between developing countries. As the commission points out, so far the bulk of counter trade between developing countries has been conducted mostly through intermediaries in the industrial countries. It is the developed countries who have benefited most from this type of trade, and they obviously have no interest in helping the indirect trading partners in the LCDs to establish direct contacts and develop durable trading relationships. Therefore, the developing countries need to organize themselves of counter trade as this can also pave the way for the growth of more conventional trading relations.

### **Reasons for the Growth of Counter trade**

There have been several reasons for the counter trade to become popular. Obviously, the countries or companies concerned have encouraged or involved in counter trade due to certain specific advantages, although some of the benefits may be purely temporary.

(i) Counter trade was very common between the communist countries. It also became popular in respect of trade between the Communist Block and many developing countries because many developing countries were eagerly looking towards this block for increasing their exports, among other things, and this naturally led to the acceptance of the trade practice, preferred by these centrally planned economies.

(ii) Counter trade became popular in the East-West trade mainly due to the foreign exchange problems faced by the East Block. Pepsi Cola is just one

example of a multinational corporation which made considerable international business with the USSR by counter trade.

(iii) When the foreign exchange problem became more severe for the developing countries following the oil price hikes, they began to actively pursue counter trade in a frantic bid to increase their exports by all means.

(iv) Many companies in the advanced countries have resorted to counter trade for various reasons like selling obsolete products, increasing the sale of capital goods, increasing the aggregate business etc. Countertrade has also been resorted to by several companies to mitigate the effects of recession. Such recessionary situations in the capital goods industries in the advanced countries gave the developing countries an opportunity to push their exports by tying the imports of capital goods with exports by counter trade.

The results of a survey of 35 British companies involved in international counter trade by Shipley and Neale accorded with the descriptive literature in so far as the Eastern Bloc 1 countries were the main group of counter trade customers, reflecting their acute currency and international debt problems. Nevertheless, substantial portions of the firms conducted countertrade in the world's less developed regions while there was some limited support for the claims that developed nations counter trade among themselves.

(v) The results of the above survey also suggest that countertrade enables firms to penetrate difficult markets, to increase sales volume and to achieve fuller capacity utilisation. It has also been revealed that countertrade enables firms to dispose of declining products, which is particularly important given the very rapid pace of technological advance. 37 per cent of the companies surveyed reported this benefit.

(vi) Some countries have also made the countertrade a means to increase sales through disguised undercutting of the cartel prices (for example the oil price fixed by the OPEC).

(vii) Having realised the potential of increasing the business by engaging in countertrade, many international trading corporations became active in the countertrade. Their trading with many countries enabled them even to take up such complex transactions as the case of Daimler Benz cited earlier.

It may be noted here that, after the deintegration of the erstwhile Soviet Union, when the Government of India has been finding it difficult to establish two-way trade flows, the Pepsi Foods Private Ltd. made an attractive offer to the Government to enter into counter trade deals with individual enterprises in the Commonwealth of Independent States to import the much needed oil, non-ferrous metals, fertilizers and newsprint.

### **Drawbacks**

Although counter trade has several justifications, particularly in the short run, it suffers from a number of disadvantages and problems, particularly in the long run.

Firstly, counter trade encourages bilateralism at the expense of multilateralism.

Secondly, it adversely affects export market development.

Thirdly, although several developing countries regard counter trade as an easy route to export, they often stand to lose in terms of price. For instance Poland bought Libyan oil at a discount and sold it at a higher price on the Rotterdam spot market.

Fourthly, it very adversely affects competition.

### **ENTRY STRATEGIES OF INDIAN FIRMS**

India's economic integration with the rest of the world was very limited because of the restrictive economic policies followed until 1991. Indian firms confined themselves, by and large, to the home market. Foreign investment by Indian firms was very insignificant. With the new economic policy ushered in 1991, there has, however, been a change. Globalization has in fact become a buzzword with Indian firms now and many are expanding their overseas business by different strategies. Indian industry can move towards globalization by different strategies such as developing exports foreign investments including joint ventures and acquisitions, strategic alliance, licensing and franchising, etc.

### **Exporting**

Exporting is, by far, the most important entry route employed by Indian firms. Because of the inward looking economic policy pursued until 1991, the progress made on the export front was not, in general, something commendable. With the economic liberalization, an environment for globalization of Indian exports, however, is slowly emerging. In a truly globalize environment, the exports will also be very much global: the sourcing of finance, materials and managerial inputs will be global, based on purely business considerations. Several Indian Companies have entered foreign markets targeting their exports at the ethnic population. West Asia, with a large expatriate Indian population, naturally is the first target in many of these cases. The Mumbai based American Dry Fruits (ADF) which began selling a range of packaged foods like chutneys, spices, canned vegetables, ready-to-eat dais etc. under different brand names later moved to other countries with large Indian population.

As foreign firms, generally, have neither the expertise nor interest in the ethnic products, Indian firms do not have to face competition from them, making market entry and growth fairly easy. A firm which makes the ethnic segment of the market its entry point may, in due course, after gaining experience in doing business and establishing a foothold in the foreign market, take up marketing of non-ethnic products and to non-ethnic consumers. Food products are not the only category being targeted at

ethnic population. Raymonds and Birla-VXL, for example, have a number of showrooms in West Asia to sell their range of textile items. Shaw Wallace launched a beer brand called Lai Toofan in U.K. through Shaw Wallace Overseas; the target consumers of this brand sold at the up market Indian restaurants are Indians. India has potential for significantly increasing the exports of many products if appropriate measures are taken. As a matter of fact, in case of number of products several other developing countries which started their exports later than India have gone much ahead of India while India's progress has been slow. With the right policy and procedural reforms and institutional support, with technological up gradation and modernization and enlargement of production facilities, with thrust on quality and value added products, with improvements in infrastructural facilities and with right marketing strategy great strides could be made in the export of a number of products. Broadly there are three strategies to increase the export earnings, viz.,

- (i) Increase the average unit value realization
- (ii) Increase the quantity of exports
- (iii) Export new products

One of the most important considerations in exports should be to achieve maximum unit value realization. Value added exports are a much needed graduation for India to enhance the foreign exchange earnings. A very disquieting fact is that India's agricultural exports still are mostly commodity exports, i.e., they are exported mostly in bulk form and the progress achieved in value added exports is not anything significant. Value added exports assume greater significance particularly in view of the stagnation or fall in the exportable surplus of several commodities—like pepper, cardamom, tea, coffee etc. The major part of India's manufactured exports end up in the low-price segments of the foreign markets. Quality up-gradation and marketing efforts are needed to reach the upper segments and to achieve enhanced value

realization. Technology imports or foreign collaborations are required for this in many cases. In many cases, what come in the way of increasing exports are the supply constraints, this is true of a number of manufactured products as well as agricultural commodities. Given the constraints for area expansion, increase in agricultural production should come mostly from increase in productivity which is very low in India. In respect of many industrial products, the production capacity is very low and highly fragmented so that there are a large number of cases of Indian firms not being able to accept offers from abroad for purchase of large quantities of the products which are far beyond the capacity of these firms to supply. One of the important ways to increase exports is to expand the export basket by adding new products and achieving substantial sales of them abroad. The share of non-traditional items in India's exports has increased very significantly. However, a lot of potential still remains untapped. For identifying new products for exports there are two courses: (i) Explore the export opportunities for products currently produced in India, (ii) Identify products with good demand abroad which can be competitively produced and supplied by India. An important export opportunity for India and other developing countries is provided by the vacation of certain industries or market segments by the developed country firms due to various reasons like environmental consideration, lack of competitiveness, declining industry attractiveness etc. For eg. the developed countries are phasing out production of a wide range of chemicals due to increased expenditure on overheads and high labor costs.

Given the capabilities and limitations of the Indian companies and the international environment, appropriate strategies should be formulated to market different products abroad. Market niching is the right strategy for many Indian companies. Several Indian companies have indeed successfully used this strategy in the foreign markets. In some cases a company can adopt the strategy of *straight extension*, i.e., extending the same product as marketed in the home

country to the foreign markets. It is particularly relevant in respect of other developing countries with similar market characteristics as that of India. A large number of the cases, however, demand quality up gradation, product modification or product development.

### **Foreign Investment**

As pointed out, it is simply not possible to maintain substantial market standing in an important area unless one has a physical presence as a producer. Otherwise, one will soon lose the 'feel' of the market. Besides the advantage of getting a feel of the market, offshore investments are encouraged by such factors as cost advantage, trade barriers etc. The demand for 'local content' is also satisfied by production in the respective countries. In many cases exporting is the beginning stage of international business which in, due course; will be replaced by production in the foreign market. Foreign investment by Indian companies has so far been very limited. The attractiveness of the domestic market, lack of global orientation, government regulations etc. have been responsible for this. By the beginning of 1995, a total of 300 wholly owned subsidiaries (58 in operation and 242 under implementation) were established by Indian companies. The operational ventures were dispersed in 40 countries. With the economic liberalization and growing global orientation, many Indian companies are setting up manufacturing/assembling/trading bases abroad, either wholly or in partnership with foreign firms. These would help these companies to increase their international business. Indian companies have also been making huge investments abroad on acquisitions. The leader in establishing manufacturing bases abroad is the Aditya Birla group. Aditya Birla, whom the Forbes called India's only international businessman, made this strategic move as early as 1970s. The group's drive to set up business overseas is that "we want predominance in the industries that we enter. The objective is to be a low-cost, high-quality and global standard player. A number of large and small Indian

companies are investing abroad as part of their globalization strategy. Several of these overseas investments aim not only at expansion of production base and business abroad but also at consolidation of the domestic business. The Ballarpur Industries of the Thapars are setting up a giant paper mill in Indonesia at an estimated cost of Rs. 1800 crores. A plantation put up on 2,50,000 hectares of land will feed the mill. Any surplus pulp may be exported to India to feed Thapar paper mills here. The significance of it should be viewed against the possible wood and pulp shortage in future in India. The Ceat expects that when the tariff barriers between the SAARC countries come down, part of the South Indian market could be served by its tyre plant in Sri Lanka. Indian companies are also establishing production facilities abroad to get an easy entry into the regional trade blocs. For example, a base in Mexico opens the doors to the NAFTA region for the Aravind Mills. Similarly Cheminor Drugs, one of the Dr. Reddy's Labs Group of companies, has set up a subsidiary in New Jersey.

### **Mergers and Acquisitions**

Mergers and Acquisitions (M & As) are very important market entry as well as growth strategy. M &As have certain advantages. It may be used to acquire new technology, M &As would have the effect of eliminating/reducing competition. One great advantage of M &As in some cases is that it provides instant access to markets and distribution network. As one of the most difficult areas in international marketing is the distribution, this is sometimes the most important objective of M &As. For example, Vijay Mallya's U.B. group acquired a small British company, Wiltshire Brewery. The attraction of Wiltshire for U.B. was that the former offered a readymade chain of 300 pubs throughout Britain which could be used for the marketing of U.B.'s brands of beer like *Kingfisher*, *Kalyani* etc. The U.B. group has gone for such acquisitions in U.S.A. and S. Africa. A number of other Indian companies have also resorted to acquisition of companies abroad to gain a foothold in the foreign market and to increase the

overseas business. Apart from the big players, a host of lesser known companies have bought out cash strapped plants in Europe, USA etc.

### **Joint Ventures**

Joint venturing is a very important foreign market entry and growth strategy in the context of the deficiencies of the Indian firms in resources, technology and marketing. This indeed is a very important strategy employed by Indian firms. It is an important route taken by pharmaceutical firms like Ranbaxy, Core, Lupin, Reddy's etc. In several cases joint ventures, as in the case of foreign subsidiaries, help Indian firms to stabilise and consolidate their domestic business, besides the expansion of the foreign business. Essar Gujarat's joint ventures in countries like Indonesia and Bangladesh to manufacture cold rolled (CR) steel have resulted from a strategy to create an assured market for its hot rolled (HR) coil mother plant at Hazaria (HR coils are inputs for manufacturing CR steel products). The Essel Packaging has taken the joint venture route to expand its business abroad. The joint ventures abroad convert the laminate into tubes to be marketed in foreign markets. The centralisation of the laminates production in India enables the company to reap enormous economies of scale. The high cost of transportation of tubes over laminates makes the conversion of laminates into tubes in the foreign markets more profitable. Further, the establishment of tube production facilities in foreign markets helps to pre-empt competition. The liberalisation of policy towards foreign investment by Indian firms along with the new economic environment seems to have given joint ventures a boost. At the beginning of 1995 although there were 177 joint ventures (with a total equity of Rs.179 crores), in operation, there were 347 (total investment Rs. 1400 crores) under implementation. Not only the number of joint ventures is increasing but also the number of countries and industries in the map of Indian joint ventures is expanding. Further liberalisation, like enhancement of the investment limit of

automatic clearance, is needed for a fast expansion of the Indian investment abroad.

### **Strategic Alliance**

Strategic alliance provides enormous scope for the Indian business to enter/expand the international business. This is particularly important for technology acquisition and overseas marketing. Alliance is indeed an important international marketing strategy employed by several Indian firms.

### **Licensing and Franchising**

Licensing and franchising, which involve minimal commitment of resource and effort on the part of the international marketer, are easy ways of entering the international market. Many Indian firms can use licensing or franchising for the overseas market; particularly the developing countries. For example, Ranbaxy has licensing arrangement in countries like Indonesia and Jordan.

### **Conclusion**

The limitations of national markets, the diversity and unevenness of resource endowments of different nations, complexity of technological developments, differences in the levels of development and demand patterns, differences in production efficiencies and costs, technological revolution in communication and other fields etc. mandate globalisation. The intent of globalisation is efficiency improvement and market optimisation taking advantage of the opportunities of the global environment. Therefore, in many cases, Indian companies have to globalise to survive and grow in the emerging competitive environment. The restrictive economic policies of the past severely affected the competitiveness and growth of the Indian Industry in general. The new economic policy, albeit suffers from certain defects, is a welcome change. If the Indian firms have the facility to obtain the latest technology in the world, to raise

finance from the cheapest source and procure the materials from the best source in the world, they are on equal footing with the foreign firms in many respects. And if the Indian firms can muster some edge over the foreign firms in respect of labour cost, productivity, product quality/features etc. that could be a competitive advantage. In many cases, size is an important factor which influences the competitive power. The economic liberalisation by pruning down the list of industries reserved for the public sector, delicensing and amending the MRTP Act has provided an environment which enables companies to grow fast, both internally and externally. The growth plans of many Indian companies indicate a great leap forward. The turnover of Reliance is projected to more than double from Rs.5300 crores to Rs.12000 crores in a short span of 3 to 4 years. The Modern Group's turnover has more than doubled from Rs.525 crores in 1994-95 in two years time, a fifth of it being exports. The Kirloskar group which had a turnover of about Rs. 1300 crores in 1995 is targeting Rs.7000 crores by the year 2000. The Rs.6000 crores ITC group, is positioning itself to become a prominent Indian MNC by the turn of the century. Out of the turnover of Rs.4280 crores of its flagship company in 1993-94, Rs.822 crores were from exports. The Arvind Mills, whose projected turnover is 1996-97 was about Rs 1100 crores, is planning to more than triple it to \$ 1 billion by the turn of the century. The increase in the size could keep the companies on a strong footing to make further dent into both the domestic and foreign markets. In short, the Indian industry is where they can make jumps compared to the past situation of limping forward. Several Indian companies are already leading players. The Ispat group of the Mittals which has units in countries like the U.S., Canada, Indonesia, Trinidad and Tobago is the largest sponge iron producer in the world. The Aditya Birla group is the world's largest player in viscose fibre and carbon black and also the largest refiner of palm oil. The Essel packaging which is already the world's second largest integrated producer of laminated tubes is aiming to climb up to the number one position.

Arvind Mills, one of the world's largest producers of denim cloth, is making further thrusts. When its ongoing projects are fully implemented, Reliance Industries would be the second largest texturiser in the world to be fully integrated from naphtha to fabrics. India is also a major player in two-wheelers and bicycles. India is the largest producer of several agricultural commodities. The liberalisation in India and in other countries poses a real challenge to the Indian business to prove its mettle.

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## **UNIT-IV**

### **Global Product Management**

A Product is often considered in a narrow sense as something tangible that can be described in terms of physical attributes. Such as sample, dimension, components, form, color and soon. This is a misconception that has been extended to international marketing because many people believe that only tangible product can be exported. But actually in tangible products are a significant part of the American export market. For example, American movies are distributed worldwide and business consulting services. In the financial market, Japanese and European banks have been internationally active in providing financial assistance. In many situations both tangible and intangible products must be combined to create a single, total product. Product describe it as a bundle of utilities or satisfaction.

A product can be defined as a collection of physical, psychological, services and symbolic attributes that collectively yield satisfaction, a benefits, to a buyer or user.

### **Pricing For International Marketing**

Price is an integral part of a product-a product can not exist with out a price. It is difficulty to think or talk about a product with out considering its price. Setting the right price for a product can be the key to success or failure. Even when the international marketer produces the right product, promotes it correctly, and initiates the proper channel of distribution, the effort fails if the product is not properly priced. A product's price must reflect the quality and value the consumer perceives in the product. The company operating in international markets have to identify the best approach for setting price worldwide.

### **Marketing Industrial Products And Services Globally**

Industrial Marketing Consists of all activities involved in the marketing of products and services to organizations i.e., commercial enterprises, profit and not – for profit institutions, government agencies and resellers that use products and services in the production of consumer or individual goods and services, and to facilitate the operation of their enterprises.

The critical issue facing industrial marketing is to remain competitive in what has become an increasingly competitive world. Today all nation complete with one another for markets, capital, technology supplies and raw materials.

### **PRODUCTS: Local. National, International. And Global**

Many companies find that, as a result of expanding existing businesses or acquiring a new business, they have products for sale in a single national market. For example, Kraft Foods at one time found itself in the chewing gum business in France, the ice cream business in Brazil, and the pasta business in Italy. Although each of these unrelated businesses was, in isolation, quite profitable, the scale of each was too small to justify heavy expenditures on R&D, let alone marketing, production, and financial management from international headquarters. An important question regarding any product is whether it has the potential for expansion into other markets. The answer will depend on the company's goals and objectives and on perceptions of opportunity.

Managers run the risk of committing two types of errors regarding product decisions in global marketing. One error is to fall victim to "not invented here" (NIH) syndrome, ignoring product decisions made by subsidiary or affiliate managers. Managers who behave in this way are essentially abandoning any effort to leverage product policy outside the home-country market. The other error has been to impose product decision policy on all affiliate companies on the assumption that what is right for customers in the home market must also be right for customers everywhere.

The four product categories in the local-to-global continuum—local, national, international, and global—are described in the following sections.

### **Local Products**

A local product is available in a portion of a national market. In the United States, the term *regional product* is synonymous with local product. These products may be new products that a company is introducing using a rollout strategy, or a product that is distributed exclusively in that region. Originally, Cape Cod Potato Chips was a local product in the New England market. The company was later purchased by Frito-Lay and distribution was expanded to other regions of the United States.

### **National Products**

National product is one that, in the context of a particular company, is offered in a single national market. Sometimes national products appear when a global company caters to the needs and preferences of particular country markets. For example, Coca-Cola developed a noncarbonated, ginseng-flavored beverage for sale only in Japan and a yellow, carbonated flavored drink called Pasturina to compete with Peru's favorite soft drink, Inca Cola. After years of failing to dislodge Inca Cola, Coke followed the old strategic maxim, "if you can't beat them, buy them," and acquired Inca Cola.

### **International Products**

International products are offered in multinational, regional markets. The classic international product is the Euro product, offered throughout Europe but not in the rest of the world. Renault was for many years a Euro product. When

Renault entered the Brazilian market, it became a multiregional company. Most recently, Renault invested in Nissan and has taken control of the company. The combination of Renault in Europe and Latin America, and Nissan in Asia, the Americas, Europe, the Middle East and Africa, has catapulted Renault from a multiregional to a global position. Renault is an example of how a company can move overnight through investment or acquisition from an international to a global position.

### **Global Products and Global Brands**

Global products are offered in global markets. A truly global product is offered in the Triad, in every world region, and in countries at every stage of development. Some global products were designed to meet the needs of a global market; others were designed to meet the needs of a national market but also, happily, meet the needs of a global market.

Examples: Marlboro, Coke

Sony, Avon, Mercedes, BMW, Volvo

### **Product positioning**

Product positioning is a communications strategy based on the notion of mental “space”. *Positioning* refers to the act of locating a brand in customers’ minds over and against other products in terms of product attributes and benefits that the brand does and does not offer.

Several general strategies have been suggested for positioning products: positioning by attribute or benefit, quality/price, use or application, and use/user. Two additional strategies, high-tech and high-touch, have been suggested for global products.

### **Attribute Or Benefit**

A frequently used positioning strategy exploits a particular product attribute, benefit, or feature. In global marketing, the fact that a product is imported can itself represent a benefit positioning. Economy, reliability, and durability are other frequently used attribute/benefit positions. Volvo automobiles are known for solid construction that offer safety in the event of a crash. In the ongoing credit card wars, VISA's advertising focuses on the benefit of worldwide merchant acceptance.

### **Quality/Price**

This strategy can be thought of in terms of a continuum from high fashion/quality and high price to good value (rather than low quality) at a low price. The American Express Card, for example, has traditionally been positioned as an upscale card whose prestige justifies higher annual fees than VISA or MasterCard. The Discover card is at the other end of the continuum. Discover's value position results from no annual fee and a cash rebate to cardholders each year.

### **USE/USER**

Positioning can also be achieved by describing how a product is used or associating a product with a user or class of users the same way in every market. For example, Benetton uses the same positioning for its clothing when it targets the global youth market. Marlboro's extraordinary success as a global brand is

due in part to the product's association with cowboys—the archetypal symbol of rugged independence, freedom, space, and Americana—and transformation advertising that targets urban smokers.

Can global positioning work for all products? One study suggests that global positioning is most effective for product categories that approach either end of a “high-touch / high-tech” continuum. Both ends of the continuum are characterized by high levels of customer involvement and by a shared language among consumers.

### **High-Tech Positioning**

Personal computers, video and stereo equipment, and automobiles are product categories for which high-tech positioning has proven effective. Such products are frequently purchased on the basis of physical product features, although image may also be important. Buyers typically already possess—or wish to acquire—considerable technical information. High-tech products may be divided into three categories: technical products, special-interest products, and demonstrable products.

Computers, chemicals, tires, and financial services are technical products in the sense that buyers have specialized needs, require a great deal of product information, and share a common language. Computer buyers in Russia and the United States are equally knowledgeable about Pentium microprocessors, hard drives, and random access memory (RAM) requirements. Marketing communications for high-tech products should be informative and emphasize features.

Special-interest products also are characterized by a shared experience and high involvement among users, although they are less technical and more leisure or recreation oriented. Again, the common language and symbols associated with such products can transcend language and cultural barriers. Fuji bicycles, Adidas and Nike sports equipment, Canon cameras, and Sega video game players are examples of successful global special-interest products.

### **High-Touch Positioning**

Marketing of high-touch products requires less emphasis on specialized information and more emphasis on image. Like high-tech products, however, high-touch categories are highly involving for consumers. Buyers of high-touch products also share a common language and set of symbols relating to themes of wealth, materialism, and romance. There are three categories of high-touch products: products that solve a common problem, global village products, and products with a universal theme. At the other end of the price spectrum from high-tech, high-touch products that can solve a problem often provide benefits linked to “life’s little moments.” Ads that show friends talking over a cup of coffee in a cafe or quenching thirst with a soft drink during a day at the beach put the product at the center of everyday life and communicate the benefit offered in a way that is understood worldwide. Upscale fragrances and designer fashions are examples of products whose positioning is strongly cosmopolitan in nature. Fragrances and fashions have traveled as a result of growing worldwide interest in high-quality, highly visible, high-priced products that often enhance social status.

Products may have a global appeal by virtue of their country of origin. The Americanness of Levi's, Marlboro, McDonald's, and Harley-Davidson enhances their appeal to cosmopolitans around the world and offers opportunities for benefit positioning. In consumer electronics, Sony is a name synonymous with vaunted Japanese quality; in automobiles, Mercedes is the embodiment of legendary German engineering.

Some products can be positioned in more than one way, within either the high-tech or high-touch poles of the continuum. A sophisticated camera, for example, could simultaneously be classified as technical and special interest. Other products may be positioned in a bipolar fashion, that is, as both high-tech and high-touch. For example, Bang & Olufsen consumer electronics products, by virtue of their design elegance, are perceived as both high-tech and high-touch.

### **Product Design Considerations**

Product design is a key factor in determining success in global marketing. Should a company adapt product design for various national markets or offer a single design to the global market? In some instances, making a design change may increase sales. However, the benefits of such potential sales increases must be weighed against the cost of changing a product's design and testing it in the market. Global marketers need to consider four factors when making product design decisions: preferences, cost, laws and regulations, and compatibility.

#### **Preferences**

There are marked and important differences in preferences around the world for factors such as color and taste. Sometimes, a product design that is successful in one world region does meet with success in the rest of the world. BMW and Mercedes dominate the luxury car market in Europe and are strong competitors in the rest of the world, with exactly the same design. In effect, these companies have a world design. The other global luxury car manufacturers are Japanese, and they have expressed their flattery and appreciation for the appeal of the BMW and Mercedes look by styling cars that are influenced by the BMW and Mercedes line and design philosophy. If imitation is the most sincere form of flattery, BMW and Mercedes have been honored by their competition.

#### **Cost**

In approaching the issue of product design, company managers must consider cost factors broadly. Of course, the actual cost of producing the product will create a cost floor. Other design-related costs—whether incurred by the manufacturer or the end user—must also be considered. The cost of repair services varies around the world and has an impact on product design. Another example of how labor cost affects product decisions is seen in the contrasting approaches to aircraft design adopted by the British and the Americans. The British approach, which resulted in the Comet, was to place the engine inside the wing. This design meant lower wind resistance and, therefore, greater fuel economy. The American approach to the question of engine location was to hang the engines from the wings at the expense of efficiency and fuel economy to gain a more accessible engine and, therefore, to reduce the amount of time required for engine maintenance and repair. Both approaches to engine location were rational. The British approach took into account the relatively lower cost of

the labor required for engine repair, and the American approach took into account the relatively high cost of labor for engine repair in the United States.

### **LAWS AND REGULATIONS**

Compliance with laws and regulations in different countries has a direct impact on product design decisions, frequently leading to product design adaptations that increase costs. This may be seen especially clearly in Europe. In the food industry, for example, there were 200 legal and regulatory barriers to cross-border trade within the European Union (EU) in 10 food categories. Among these were prohibitions or taxes on products with certain ingredients, and different packaging and labeling laws. Experts predict that the removal of such barriers will reduce the need to adapt product designs and will result in the creation of standardized Euro-products.

### **Compatibility**

The last product design issue that must be addressed by company managers is product compatibility with the environment in which it is used. A simple thing such as failing to translate the user's manual into various languages can hurt sales of American-made home appliances built in America outside the United States. Also, electrical systems range from 50 to 230 volts and from 50 to 60 cycles. This means that the design of any product powered by electricity must be compatible with the power system in the country of use.

Manufacturers of televisions and video equipment find that the world is a very incompatible place for reasons besides those related to electricity.

Three different TV broadcast and video systems are found in the world today: the U.S. NTSC system, the French SECAM system, and the German PAL system. Companies that are targeting global markets design multisystem TVs and VCRs that allow users to simply flip a switch for proper operation with any system. Companies that are not aiming for the global market design products that comply with a single type of technical requirements. Cell phones manufacturers encounter the GSM standard which has been adapted in Europe and in many other countries. However, the United States has three different cell technologies, and Japan has yet another CCU Standard. Measuring systems do not demand compatibility, but the absence of compatibility in measuring systems can create product resistance.

### **Labeling And Instructions**

Product labeling and instructions must comply with national law and regulation. For example, there are very precise labeling requirements for prescription drugs and poisons. In addition, however, labeling can provide valuable consumer information on nutrition, for example. Finally, many products require operating and installation instructions.

In which languages should labeling and instructions be printed? One approach to this issue is to print labels and instructions in languages that are used in all of the major markets for the product. The use of multiple languages on labels and instructions simplifies inventory control: The same packaging can be used for multiple markets. The savings from simplicity must be weighed against the cost of longer instruction booklets and more space on labels for information.

## **Brands in International Markets**

Hand in hand with global products and services are global brands. A **global brand** is defined as the worldwide use of a name, term, sign, symbol (visual and/or auditory), design, or combination thereof intended to identify goods or services of one seller and to differentiate them from those of competitors.

A successful brand is the most valuable resource a company has. The brand name encompasses the years of advertising, good will, quality evaluation, product experience, and other beneficial attributes the market associates with-the product. Brand image is at the very core of business identity and strategy. Customers everywhere respond to images, myths, and metaphors that help them define their personal and national identities within a global context of world culture and product benefits. Global brands play an important role in that process. The value of Kodak, Sony, Coca-Cola, McDonald's, Toyota, and Marlboro is indisputable. One estimate of the value of Coca-Cola, the world's most valuable brand.

## **Global Brands**

Naturally, companies with such strong brands strive to use those brands globally. In fact, it appears that even perceived "globalness" leads to increases in sales. The Internet and other technologies are accelerating the pace of the globalization of brands. Even for products that must be adapted to local market conditions, a global brand can be successfully used with careful consideration.

Ideally a global brand gives a company a uniform worldwide image that enhances efficiency and cost savings when introducing other products associated with the brand name, but not all companies believe a single global approach is the best. Indeed we know that the same brand does not necessarily hold the same meanings in different countries. In addition to companies such as Kodak, Kellogg, Coca-Cola, Caterpillar, and Levi's that use the same brands worldwide, other multinationals such as Nestle, Mars, Procter & Gamble, and Gillette have some brands that are promoted worldwide and other that are country specific. Among companies that have faced the question of whether or not to make all their brands global, not all have followed the same path.

### **National Brands**

A different strategy is followed by the Nestle Company, which has a stable of global and country-specific national brands in its product line. The Nestle name itself is promoted globally, but its global brand expansion strategy is two-pronged. In some markets it acquires well-established national brands when it can and builds on their strengths—there are 7,000 local brands in its family of brands. In other markets where there are no strong brands to be local, people to be regional, and technology to be global, it does, however, own some of the world's largest global brands; Nescafe is but one.

Multinationals must also consider rises in nationalistic pride that occur in some countries and their impact on brands. In India, for example, Unilever considers it critical that its brands, such as Surf detergent and Lux and Lifebuoy soaps, are viewed as Indian brands. Just as is the case with products, the answer to the question of when to go global with a brand is, "It depends—the market dictates." Use global brands where possible and national brands where necessary.

### **Private Brands**

Private brands owned by retailers are growing as challenges to manufacturers' brands, whether global or country specific. In the food-retailing sector in Britain and many European countries, private labels owned by national retailers increasingly confront manufacturers' brands. From blackberry jam and vacuum-cleaner bags to smoked salmon and sun-dried tomatoes, private-label products dominate grocery stores in Britain and in many of the hypermarkets of Europe. Private brands captured nearly 30 percent of the British and Swiss markets and more than 20 percent of the French and German markets. In some European markets, private-label market share doubled in just the past five years.

As it stands now, private labels are formidable competitors. They provide the retailer with high margins; they receive preferential shelf space and strong in-store promotion; and, perhaps most important for consumer appeal, they are quality products at low prices. Contrast that with manufacturers' brands, which traditionally are premium priced and offer the retailer lower margins than they get from private labels.



### **Employ Global Brand-planning Process**

Companies that follow good global brand management practices, use a well-defined planning process. The planning process is similar across markets and products. The similarity can be seen in terms of vocabulary, strategic analysis inputs such as competitor positions and strategies and brand strategy models, and outputs such as brand building programs.

A brand strategy model must make clear which person or group is responsible for the brand and brand strategy. The strategy model must also involve a process template (or outline). The process template must mention the target segment, the brand identity or vision, brand equity goals and measures, and brand-building programs. Effective brand planning programs must

- Involve an analysis of customers, competitors, and the brand.
- Avoid an exclusive focus on product attributes.
- Involve programs that communicate the brand's identity.
- Include brand equity measurement and goals.
- Include a mechanism to the global brand strategies to country brand strategies.

### **Brilliant Brand Building Strategies**

Attaining global brand leadership needs appropriate brand building strategies. The firm has to first consider what type of brand building strategy to adopt. It can follow advertising, sponsorship, increasing retail presence, and promotions for its brand building efforts. The firm has to decide which one best serves its requirements. P&G comes up with exceptional ideas by giving enough freedom to its country teams in developing breakthrough brand building programs.

Another way to stimulate creative ideas is to have more than one advertising agency as the service provider. As mentioned earlier, a single agency can better oversee a campaign.

Brand measurement is necessary to see that brand building is actually going on. The measurement system must be designed in such a way that it measures not only financial performance but also customer awareness, customer loyalty, the brand's personality, and the brand associations that resonate with the public.

### **Brand Piracy**

Creation of brand in itself is not enough. The brand also should be protected from piracy through registrations. Various forms of piracy are: outright piracy, reverse engineering, counterfeiting, and passing off.

### **Counterfeiting**

Counterfeiting means diluting the product quality and selling under the same trademark. This is quite prevalent in clothing industry. For example, counterfeited version of Levi's branded jeans are available in market at Rs 250 when the original product costs more than three times this price.

### **Passing Off**

Some times products are modified, and trademarks are adapted. The pirated product is similar in appearance, phonetic quality or meaning (of its name) to the original product. Immediately after Sony introduced "Walkman" in the market, many other electronic goods manufacturing companies released similar products.

### **Reverse Engineering**

Reverse engineering involves dismantling another firm's product to learn about its special features. This form of piracy is prevalent in the electronic goods industry.

### **Outright Piracy**

When a false product is sold in the same form and same trademark as the original, is referred to as Outright Piracy. Music records and tapes are often sold in this way.

### **Single Brands VS Multiple Brands**

A company can market a single brand or multiple brands the same time. It chooses to market a single brand when the brand needs full attention, and multiple brands when the market is heterogenous and needs to be segmented. (Refer Exhibit 11.3 for P&G's global branding strategy). Each brand is then targeted at a separate segment. A company uses the strategy of multiple brands when it wants to move up or down the segment it is serving. A firm with multiple brands can position some brands in lower price segments and some brands in premium segments.

### **New Products in Global Marketing**

What is a new product? Newness can be assessed in the context of the product itself, the organization, and the market. The product may be an entirely new invention or innovation—for example, the videocassette recorder (VCR) or the compact disc. It may be a line extension (a modification of an existing

product) such as Diet Coke. Newness may also be organizational, as when a company acquires an already existing product with which it has no previous experience. Finally, an existing product that is not new to a company may be new to a particular market.

In today's dynamic, competitive market environment, many Companies realize that continuous development and introduction of new products are keys to survival and growth. Which companies excel at these activities? Gary Reiner, a new-product specialist with the Boston Consulting Group, has compiled the following list: Honda, Compaq, Motorola, Canon, Boeing, Merck, Microsoft, Intel, and Toyota. One common characteristic: They are global companies that pursue opportunities in global markets in which competition is fierce, thus ensuring that new products will be world class. Other characteristics noted by Reiner are as follows:

- 1.They focus on one or only a few businesses.
- 2.Senior management is actively involved in defining and improving the product development process.
- 3.They have the ability to recruit and retain the best and the brightest people in their fields.
- 4.They understand that speed in bringing new products to market reinforces product quality.

### **New Product Development**

There are six distinct steps in new product development. The *first step* is the *generation of new product ideas*. Such ideas can come from any number of sources (e.g., salespersons, employees, competitors, governments, marketing research firms,

customers, etc.). A 3M company chemist, after spilling some liquid on her tennis shoes, found that they had become capable of repelling water and dirt, and that is how Scotch-gard fabric protector was born.

The *second step* involves the *screening of ideas*. Ideas must be acknowledged and reviewed to determine their feasibility. To determine suitability, a new product concept may simply be presented to potential users, or an advertisement based on the product can be drawn and shown to focus groups to elicit candid reactions. As a rule, “corporations usually have predetermined goals that a new product must meet. Kao Corporation, a major Japanese manufacturer of consumer goods, is guided by the following five principles of product development: (1) a new product should be truly useful to society, not only now but also in the future, (2) it should make use of Kao’s own creative technology or skill, (3) it should be superior to the new products of competitors, from the standpoint of both cost and performance, (4) it should be able to stand exhaustive product tests at all stages before it is commercialized, and (5) it should be capable of delivering its own message at every level of distribution.

The *third step* is *business analysis*, which is necessary to estimate product features, cost, demand, and profit. Xerox has small so-called product synthesis teams to test and weed out unsuitable ideas. Several competing teams of designers produce a prototype, and the winning model that meets preset goals then goes to the “product development” team.

The *fourth step* is *product development*, which involves lab and technical tests as well as manufacturing pilot models in small quantities. At this stage the product is likely to be handmade or produced by existing machinery rather than

by any new specialized equipment. Ideally, engineers should receive direct feedback from customers and dealers.

The *fifth step* involves *test marketing* to determine potential marketing problems and the optimal marketing mix.

Finally, assuming that things go well, the company is ready for *full-scale commercialization* by actually going through with full-scale production and marketing.

It should be pointed out that not all of these six steps in new product development will be applicable to all products and countries. Test marketing, for example, may be irrelevant in countries where most major media are more national than local. If the television medium has a nationwide coverage, it is not practical to limit a marketing campaign to one city or province for test marketing purposes.

Unfortunately, it is easier for a new product to fail than to succeed. Naturally, so many things can go wrong (-see Marketing-Strategy 10-1). Therefore, it is just as critical for a company to know when to retreat as when to launch a product. Coca-Cola's Ambasa Whitewater, a lactic-based drink, was removed from the market after eighteen months when sales started to decline.

### **Standardization Vs Differentiation**

**Standardization** Standardized marketing mix involves developing a standard product and marketing it across the national border with the same communication, pricing, and distribution strategy. With the advent and standardization of technology and **more** specifically that of communications, customer needs are globally getting homogenized. This process or homogenization of needs is getting accelerated as trade barriers come down one after another leading to globalization of markets. Worldwide communication has raised customers' expectations and demands for better living standards, work life, and entertainment. This cuts across cultures and religions. Nothing better confirms this than the success of brands like Coke, Pepsi, Levis, Benetton readymade garments, Sony and Panasonic electronic items, and even Hollywood films and soap operas made in the US and different parts of the world that have diverse cultures and religions. These commonalities in customer preferences lead conclusively to the standardization route in corporate strategy.

Standardization helps the firm not only reduce its costs but also to ensure superior quality and consistent brand image across the world market. It helps the firm achieve economies of scale which is not possible in any other approach.<sup>4</sup> Japanese firms have relentlessly pursued this strategy and gained substantial scale economies, often at the expense of their rivals. Global firms compete in different national markets through a standardization strategy and offer appropriate volume—the best combination of price, quality, reliability, and delivery of products.

However, there are pitfalls in this decision. A study shows that the success of a global firm is based on how global decisions are conceptualized, refined, internally communicated, and implemented across the world market. It concludes that firms which lose out in the global marketing warfare are the ones that insufficiently used

marketing research, had a tendency to over standardize, did poor follow-up, and had a narrow global perspective.

### **Differentiation**

Opposed to standardization is the differentiation strategy. This involves responding to differences in customer preferences arising out of cultural, social, and religious barriers that divide nations. This strategy does help in building up sales volumes, but the cost is prohibitive when done at a global level. Imagine Levis, Benetton, Coke, McDonald's, Burger King, and Tacobell having to differentiate their marketing mix to suit different cultural preferences. They will not be able to derive economies of scale and hence their cost of operations in a market will be much higher. This will push up prices for consumers or else they will be out of business. Further, these global firms will never be able to ensure identical brand image across the world market. This goes against the thesis of globalization.

Nonetheless, local preferences and conditions will need to be woven into the marketing mix. The more acceptable route is that of localizing the marketing mix. This involves decentralizing decision making at the local affiliate level. This is useful especially when it comes to areas like marketing communication, distribution, and to a limited extent, in the packaging area. For example, Sunsilk shampoo from Unilever could achieve a higher penetration in the toiletries market in South Asia only when it introduced sachet packs for single use and priced it at an affordable level of Re 1 in India and comparable level in other South Asian countries as well. Maggi noodles, marketed by Nestle, could

achieve a resounding success only when it included cooking instructions in its TV commercials and on the pack and also added taste makers to suit Indian taste buds. However, these and other successful global firms do not leave critical decisions like brand image, brand identity, product focus or positioning to local affiliates.

A study showed that two successful global firms, Nestle and Coca-Cola, standardized their product decisions but adapted their advertising, sales promotion, distribution, and customer service to suit local country preferences and conditions. The authors of this study maintain that local aspirations and strong managements in major country markets must be respected and persuaded to accept standardized products. Even the headquarters needs to listen to local managers and do not rigidly implement their standardized marketing mix in countries showing distinctive customer preferences or needs. The success of global marketing is based on gaining cooperation from affiliates' managers in implementing the strategy. The approach of the headquarters towards affiliates has to focus on both the means and the ends.

### **Environmental Influences on Pricing Decisions**

Global marketers must deal with a number of environmental considerations when making pricing decisions. Among these are currency fluctuations, inflation, government controls and subsidies, competitive behavior, and market demand. Some of these factors work in conjunction with others; for

example, inflation may be accompanied by government controls. Each consideration is discussed in detail next.

### **Currency Fluctuations**

Fluctuating currency values are fact of life in international business. The marketer must decide what to do about this fact. When currency fluctuations result in appreciation in the value of the currency of a country that is an exporter, wise companies do two things: They accept that currency fluctuations may unfavorably impact operating margins, and

<i>When Domestic Currency Is</i>		<i>When Domestic Currency</i>	
	Stress price benefits		Engage in nonprice competition by improving
	Exploit market		Give priority to exports to

	Use full-costing approach but employ marginal-cost pricing		Trim profit margins and use marginal-cost pricing.
			Keep the foreign-earned income in host country slow down
	Minimize expenditures in local or host-country currency.		Maximize expenditures in local or host-country currency.
	Buy advertising, insurance,		Buy needed services abroad
	Bill foreign customers in their own currency.		Bill foreign customers in the domestic currency.

They double their efforts to reduce costs. In the short run, lower margins enable them to hold prices in target markets, and in the longer run, driving down costs enables them to improve operating margins.

For companies that are in a strong, competitive market position, prices increases can be passed on to customers without significant decreases in sales volume. In more competitive market situations, companies in a strong-currency will often absorb any price increase by maintaining international market prices at pre-revaluation levels. In actual practice, a manufacturer and its distributor may work together to maintain market share in international market. If a country's currency weakens relative to a trading partner's currency, a producer in a weak-currency country can cut export prices to hold market share or leave prices alone for healthier profit margins.

- *Purpose:* To protect parties from unforeseen large swings in currencies.
- Exchange rate review is made quarterly to determine possible adjustments for the next period.
- Comparison basis is the three-month daily average and the initial average.

### **Exchange Rate Clauses**

Many sales are contracts to supply goods or services over time. When these contracts are between parties in two countries, the problem of exchange rate fluctuations and exchange risk must be addressed.

An exchange rate clause allows the buyer and seller to agree to supply and purchase at fixed prices in each company's national currency. If the exchange rate fluctuates within a specified range, say plus or minus 5 percent, the fluctuations do not affect the pricing agreement that is spelled out in the exchange rate clause. Small fluctuations in exchange rates are not a problem for most buyers and sellers. Exchange rate clauses are designed to protect both the buyer and the seller from unforeseen large swings in currencies.

### **Pricing In An Inflationary Environment**

Inflation, or a persistent upward change in price levels, is a worldwide phenomenon. Inflation requires periodic price adjustments. These adjustments are necessitated by rising costs that must be covered by increased selling prices. An essential requirement when pricing in an inflationary environment is the maintenance of operating profit margins.

In particular, it is worth noting that the traditional FIFO (first-in, first-out) costing method is hardly appropriate for an inflationary situation. A more appropriate accounting practice under conditions of rising prices is the LIFO (last-in, first-out) method, which takes the most recent raw material acquisition price and uses it as the basis for costing the product sold. In highly inflationary environments, historical approaches are less appropriate costing methods than replacement cost.

### **Government Controls And Subsidies**

If government action limits the freedom of management to adjust prices, the maintenance of margins is definitely compromised. Under certain conditions, government action is a real threat to the profitability of a subsidiary operation.

Government control can also take the form of prior cash deposit requirements imposed on importers. This is a requirement that a company has to tie up funds in the form of a non-interest-bearing deposit for a specified period of

time if it wishes to import products. Such requirements clearly create an incentive for a company to minimize the price of the imported product; lower prices mean smaller deposits. Other government requirements that affect the pricing decision are profit transfer rules that restrict the conditions under which profits can be transferred out of a country. Under such rules, a high transfer price paid for imported goods by an affiliated company can be interpreted as a device for transferring profits out of a country. Government subsidies can also force a company to make strategic use of sourcing to be price competitive in Europe.

#### **COMPETITIVE BEHAVIOR**

Pricing decisions are bounded not only by cost and the nature of demand but also by competitive action. If competitors do not adjust their prices in response to rising costs, management—even if acutely aware of the effect of rising costs on operating margins—will be severely constrained in its ability to adjust prices accordingly. Conversely, if competitors are manufacturing or sourcing in a lower-cost country, it may be necessary to cut prices to stay competitive.

#### **Global Pricing objectives and Strategies**

A number of different pricing strategies are available to global marketers. An overall goal must be to contribute to company sales and profit objectives world wide. Customer oriented strategies such as market skimming, penetration, and market holding can be used.



#### **Other Constraints On International Pricing**

International pricing is also influenced by factors such as the size of the company and the cultural background of parent company executives.

- **Size of the company**

Large multinational companies generally use cost-based systems. Such companies have the advantages of size and reach. As their operations or activities spread across different countries they have more opportunities or advantages in manipulating prices. Operating in markets that are monopolistic or oligopolistic in nature can lend protection to these companies from competitive pressures, which can bring down their profitability levels. The advantages these companies enjoy by operating in these markets allow them to offer their products at low prices in some other markets, and gain market shares. Thus their size turns out to be a huge advantage when competing with companies of smaller size.

### **Cultural background of firms**

Pricing decisions are also influenced by the cultural background of the parent company. For example, firms from the US use cost as the basis in determining the prices. Similarly, firms from Britain, France, and Japan prefer a cost-based approach in deciding the prices. On the other hand, Firms with a Scandinavian or Canadian background use market-based prices<sup>16</sup>. The Germans, Dutch, and Italian firms use a combination of these.

The French firms prefer cost-based prices because this form of transfer pricing permits them to transfer their income to regions where the tax rates are lower. The British firms prefer a cost-based approach to prices because the British banking community expects a specific return on the investment made by them in the firms, and also they pay great attention to real rate of return at the

year-end. The Germans are more concerned about the fixed asset position and stability of the firm in the long run. Their pricing decisions reflect this concern.

### **Company controls and information systems**

Transfer pricing mechanism has to be well understood by people managing control and evaluation functions. Lack of clear understanding might lead to unexpected and undesired distortions. Managers might show exceptional performance on account of the benefits incurred through transfer pricing rather than the real growth they generated for their company. Thus the transfer pricing mechanism should not distort the control system and evaluation criteria. Properly designed information systems can ensure this.

### **Duty and tariff constraints**

High duty and tariff rates provide an incentive to reduce transfer prices. On the other hand, low tax rate motivates the Firm to increase transfer price to show income in the low-tax environment. Thus the level of duty, tariff and tax rate influence the transfer price levels.

### **Government controls**

Government controls often influence the transfer-pricing levels. Governments also force importers to make cash deposits. This type of controls make companies reduce the price of their products. They reduce the price because, lower price means they can get away by making smaller mandatory deposits. Governments also restrict the way firms transfer their profits.

### **Joint ventures**

Companies participating in joint ventures have to reach transfer pricing agreements on different aspects such as:

- Fixing transfer prices when there is a change in exchange rate.

- Changes in transfer prices when manufacturing costs come down due to the learning-curve effect.
- Fixing of royalty rates when the parties of the joint venture build new technology or source it from other sources.
- When the competition impacts volume and overall margins.

Such agreements would avoid conflict between joint venture partners and promote coordination)

Global pricing can also be based on other external criteria such as the escalation in costs when goods are shipped long distances across national boundaries. The issued global pricing can also be fully integrated in the product design process, an approach widely used by Japanese companies. Prices in global markets are not carved in stone; they must be evaluated at regular intervals and adjusted if necessary. Similarly, pricing objectives may vary, depending on a product's life-cycle stage and the country-specific competitive situation.

### **Market Skimming**

The market skimming pricing strategy is a deliberate attempt to reach a market segment that is willing to pay a premium price for a product. In such instances, the product must create high value for buyers. This pricing strategy is often used in the introductory phase of the product life cycle, when both production capacity and competition are limited. By setting a deliberately high

price, demand is limited to early adopters who are willing and able to pay the price. One goal of this pricing strategy is to maximize revenue on limited volume and to match demand to available supply. Another goal of market skimming pricing is to reinforce customers' perceptions of high product value. When this is done, the price is part of the total product positioning strategy.

### **Penetration Pricing**

Penetration pricing uses price as a competitive weapon to gain market position. The majority of companies using this type of pricing in international marketing are located in the Pacific Rim. Scale-efficient plants and low-cost labor allow these companies to blitz the market.

It should be noted that a first-time exporter is unlikely to use penetration pricing. The reason is simple: Penetration pricing often means that the product may be sold at a loss for a certain length of time. Companies that are new to exporting cannot absorb such losses. They are not likely to have the marketing system in place (including transportation, distribution, and sales organizations) that allows global companies such as Sony to make effective use of a penetration strategy. However, a company whose product is not patentable may wish to use penetration pricing to achieve market saturation before the product is copied by competitors.

When Sony developed the portable compact disc player, the cost per unit at initial sales volumes was estimated to exceed \$600. Since this was a "no-go" price in the United States and other target markets, Akio Morita instructed management to price the unit in the \$300 range to achieve penetration. Because Sony was a global marketer, the sales volume it expected to achieve in these markets led to scale economies and lower costs.

### **Market Holding**

The market holding strategy is frequently adopted by companies that want to maintain their share of the market. In single-country marketing, this strategy often involves reacting to price adjustments by competitors. For example, when one airline announces special bargain fares, most competing carriers must match the offer or risk losing passengers. In global marketing, currency fluctuations often trigger price adjustments.

Market holding strategies dictate that source-country currency appreciation will not be automatically passed on in the form of higher prices. If the competitive situation in market countries is price sensitive, manufacturers must absorb the cost of currency appreciation by accepting lower margins in order to maintain competitive prices in country markets.

A strong home currency and rising costs in the home country may also force a company to shift its sourcing to in-country or third-country

manufacturing or licensing agreements, rather than exporting from the home country, to maintain market share.

### **Cost Plus/Price Escalation**

Companies new to exporting frequently use a strategy known as cost-plus pricing to gain a toehold in the global marketplace. There are two cost-plus pricing methods: The older is the historical accounting cost method, which defines cost as the sum of all direct and indirect manufacturing and overhead costs. An approach used in recent years is known as the estimated future cost method.

Cost-plus pricing requires adding up all the costs required to get the product to where it must go, plus shipping and ancillary charges, and a profit percentage. The obvious advantage of using this method is its low threshold: It is relatively easy to arrive at a selling price, assuming that accounting costs are readily available. The disadvantage of using historical accounting costs to arrive at a price is that this approach completely ignores demand and competitive conditions in target markets. Therefore, historical accounting cost-plus prices will frequently be either too high or too low in the light of market and competitive conditions. If historical accounting cost-plus prices are right, it is only by chance. Price escalation is the increase in a product's price as transportation, duty, and distributor margins are added to the factory price.

### **Using Sourcing As a Strategic Pricing Tool**

The global marketer has several options when addressing the problem of price escalation described in the last section. The choices are dictated in part by product and market competition. Marketers of domestically manufactured finished products may be forced to switch to lower-income, lower-wage countries for the sourcing of certain components or even of finished goods to keep costs and prices competitive.

### **Gray market goods**

Gray market goods are trademarked products that are exported from one country to another, where they are sold by unauthorized persons or organizations. Sometimes, gray marketers bring a product produced in one country—French champagne, for example—into a second-country market in competition with authorized importers. The gray marketers sell at prices that undercut those set by the legitimate importers. This practice, known as *parallel importing*, may flourish when a product is in short supply or when producers attempt to set high prices.

In another type of gray marketing, a company manufactures a product in the home-country market as well as in foreign markets. In this case, products manufactured abroad by the company's foreign affiliate for sales abroad are sometimes sold by a foreign distributor to gray marketers. The latter then bring the products into the producing company's home-country market, where they compete with domestically produced goods.

## **Dumping**

Dumping is an important global pricing strategy issue. GATT's 1979 Antidumping Code defined dumping as the sale of an imported product at a price lower than that normally charged in a domestic market or country of origin. In addition, many countries have their own policies and procedures for protecting national companies from dumping. The U.S. Antidumping Act of 1921, which is enforced by the U.S. Treasury, did not define dumping specifically but instead referred to unfair competition. However, Congress has defined dumping as an unfair trade practice that results in "injury, destruction, or prevention of the establishment of American industry." Under this definition, dumping occurs when imports sold in the U.S. market are priced either at levels that represent less than the cost of production plus, an 8 percent profit margin or at levels below those prevailing in the producing country.

Transfer pricing refers to the pricing of goods and services bought and sold by operating units or divisions of a single company. In other words, transfer pricing concerns intracorporate exchanges—transactions between buyers and sellers that have the same corporate parent. For example, Toyota subsidiaries sell to, and buy from, each other. The same is true of other companies operating globally. As companies expand and create decentralized operations, profit centers become an increasingly important component in the overall corporate financial picture.

There are three major alternative approaches to transfer pricing. The approach used will vary with the nature of the firm, products, markets, and the

historical circumstances of each case. The alternatives are (1) cost-based transfer pricing, (2) market-based transfer pricing, and (3) negotiated prices.

### **Cost-Based Transfer Pricing**

Because companies define costs differently, some companies using the cost-based approach may arrive at transfer prices that reflect variable and fixed manufacturing costs only. Alternatively, transfer prices may be based on full costs, including overhead costs from marketing, research and development (R&D), and other functional areas. The way costs are defined may have an impact on tariffs and duties on sales to affiliates and subsidiaries by global companies.

### **Market-Based Transfer Price**

A market-based transfer price is derived from the price required to be competitive in the international market. The constraint on this price is cost. However, as noted previously, there is a considerable degree of variation in how costs are defined. Because costs generally decline with volume, a decision must be made regarding whether to price on the basis of current or planned volume levels. To use market-based transfer prices to enter a new market that is too small to support local manufacturing, third-country sourcing may be required. This enables a company to establish its name or franchise in the market without committing to a major capital investment.

### **Negotiated Transfer Prices**

A third alternative is to allow the organization's affiliates to negotiate transfer prices among themselves. In some instances, the final transfer price may reflect costs and market prices, but this is not a requirement. The gold standard of negotiated transfer prices is known as an arm's-length price: the price that two independent, unrelated entities would negotiate.

### **Global Pricing Alternatives**

Firms operating in international markets follow three pricing approaches, predominantly: ethnocentric, polycentric, and geocentric.

#### **Ethnocentric Approach**

A company following an ethnocentric approach follows the same pricing policy throughout the world. The importer of the product will bear the freight and import duties. This approach is convenient to adopt because there is no need to make any modifications to price based on competitive or market conditions. The firm need not put in efforts to collect information on these market conditions. But by adopting this approach, a firm might fail to make optimum

profits by not fixing the prices of the products based on regional market conditions.

### **Polycentric Approach**

A firm following this approach allows its regional managers to fix the product prices based on the circumstances in which they operate. This approach might prove to be not so good, when the disparity in product prices from one region to another is higher than transportation costs and duties. When this condition prevails, customers will buy the products in markets where they are available at low price and ship them to where the prices are relatively high. This will result in loss of revenue for the firm following this approach.

### **Geocentric Approach**

A firm adopting this approach takes a medium position between fixing a single price worldwide and fixing different prices based on the requirements of subsidiaries. One of the fundamental assumptions underlying this approach is that markets are unique, and specific factors related to them have to be taken into account while making a pricing decision. Also the approach takes into consideration the price coordination necessary at headquarters to deal with international accounts and product arbitrage. This approach is the most practical of all because it takes into consideration both global competition and local rivalry in establishing prices.

## Forms Of International Market Entry

Regardless of the problems and risks involved in international marketing, profit enhancement is a major stimulus for marketing in foreign countries. Increased profit potential rises from the opportunity to utilize unused plant capacity, to offset seasonal fluctuations in sales, to make wider applications of R&D findings, to recover manufacturing investments, to offset declining margins due to saturated markets at home, and to keep pace with competitors who have overseas plants. The impetus for international marketing can also originate from government activities, such as assistance in the financing of export sales, export expansion programs, or trade fairs, as well as through unsolicited orders from abroad.

### The different form of market entry are

**Indirect Exporting.** The most common and least risky form of market entry is indirect exporting. Here the firm sells to intermediaries, who, in turn, sell to foreign markets. While indirect exporting is a good strategy when the firm has little knowledge of exporting to foreign markets, where markets are limited in size, or when the firm does not wish to commit its resources, it places constraints on other marketing strategies as well as on control.

<i>Operational Strategies</i>	<i>Strategic Strategies</i>
<p>Indirect exporting</p> <p>Sells to domestic intermediaries; for example, export trading company or export management company.</p> <p>Direct exporting</p> <p>Sells directly to foreign buyer or foreign intermediaries—local company ships and handles financing and shipping documentation.</p>	<p>Joint ventures</p> <p>Local and foreign firms share ownership, Foreign production</p> <p>Establishes solely owned production facilities in foreign country.</p>

<p>Foreign licensing</p> <p>Exports "know-how" through management contract.</p>	
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**Direct Exporting.** The investment and risk in direct exporting are greater than in indirect exporting. Under direct exporting, the firm has to establish foreign distribution, increase production capacity, and adapt products for foreign markets. Direct exporting places the firm in an overseas market through either a sales branch or subsidiary, or an agent who represents the firm exclusively in the host country.

**Foreign Licensing.** Foreign licensing involves an agreement between a firm in one country (the licensor) and a firm in another country (the licensee) whereby the former permits the latter the use of its manufacturing processes, patents, or trademarks in exchange for a royalty fee.

**Joint Ventures.** When two or more firms or investors share ownership and control over operations and investments, they have entered into a joint venture. Joint ventures provide better knowledge of local markets, a local identity, and a shared risk.

## **International Adaptation Of Conventional Marketing Strategies**

To illustrate how the use of conventional marketing strategies differs as a firm enters international marketing, we turn our attention to international market segmentation, target marketing, and marketing mix strategies.

### **Segmenting the International Market**

In the international arena, market segmentation is usually referred to as “comparative analysis,” that is, segmenting countries on the basis of their similarities and differences. When, a firm selects a number of countries as its target markets, on the basis of these comparative similarities and differences, it is said to be employing "comparative marketing" rather than target marketing.

***Comparative Analysis and Marketing.*** Comparative analysis and marketing sounds simple enough and is no different conceptually from conventional market segmentation and target marketing. However, the term “comparative” emphasizes the international difficulties involved. Given the economic, cultural, and political/ legal differences among nations, determining comparative similarities and differences can be a major undertaking not found in domestic markets.

### **International Product Strategies**

Although products in the international industrial market are more homogeneous than consumer products, there are more product variations internationally than domestically due to the greater number of international economic, cultural, and political/legal variables.

### **International Pricing Strategies**

Although pricing practices appear to be no different internationally than nationally, in some respects there is wide divergence. These differences occur in the areas of transfer pricing, dumping, and governmental influence over price.

**Transfer Pricing.** Transfer prices are the prices placed on products as they are transferred between units belonging to the same company. Transfer prices can be used to mitigate the effects of government regulation.

**Dumping.** Dumping is disposing of goods in a foreign country at less than their full cost. Goods will sometimes be exported at prices that only cover direct costs to dispose of excess inventories. Companies sell their excess inventories overseas to avoid disturbing their own national markets (e.g., reducing prices or causing price wars at home).

### **International Promotional Strategy**

In the international industrial market, the primary element of the promotional mix is personal selling, for only through personal selling can the coordination so essential to the industrial buyer-seller interface be effectively achieved.

Sales promotion in the form of trade fairs is playing an increasingly important role in international marketing because so many prospects can be contacted in one place and because they enable quick comparisons of products. Direct mail is also becoming popular, although mailing lists are usually difficult to obtain. The use of publicity, although growing in popularity, is limited due to language difficulties and media coverage. Advertising is given little attention in the international industrial market, perhaps because of the difficulties in determining media coverage and numerous, widely varying, governmental regulations. Here our discussion concerns personal selling.

### **International Distribution Strategies**

The primary goal of international marketing is achieving wider distribution. E just as in the United States, distribution involves more than physically moving a product. It involves handling, storage, inventorying, sometimes assembling, protective packaging, paperwork, and forecasting.

## WHAT IS INCLUDED IN SERVICES MARKETING

We have seen how HDFC bank in India has emerged as India's best bank in a very short period of time. It has taken less than seven years for the bank to emerge as India's leading bank leaving the State Bank of India, the largest bank in the country, far behind. Service marketing is based on very different paradigms. Since services are highly intangible, its benefits are felt over a period of time and not immediately. The task of the marketer becomes one of creating confidence in the customer's mind that the delivered benefits will, at the least, be the same as that of the promised ones. Two categories of products are included in the range of services marketing. These are:

- (a) Products which are 100 percent intangible and truly fall in the category of services. Typical examples of these are banking, health care, insurance, airlines, hospitality, restaurants, management consultancy, education, and so forth.
- (b) Services in manufactured products are different from the services industry as here the emphasis is more on providing a range of services which the customer is looking for when he buys a manufactured product. Services here help is in augmenting the product and, hence, creates a new set of values for the customer.

Viewed, therefore, from the tangible and intangible perspectives, products can be put on a continuum. At the one end are products which are bought principally for their tangible benefits. Here the customer is not willing to compromise. Typical examples of this category are in industrial products like plant and machinery, equipments, and high value products like aircrafts or a limousines (luxury car). At the other end are products that primarily offer intangible benefits, like medical care. In between the two ends of this continuum are products and services which have both tangible and intangible and components. For example, consumer durables are products that are bought for both tangible and intangible benefits. Hence services in such a category assume a very different meaning.

Similarly, the hospitality sector in the service industry offers both tangible and intangible benefits to the customer. The tangible features are property equipped rooms matching the life style of the target customer, air-conditioning, facilities like television, internet connectivity, facsimile machines, bar refrigerator, and other benefits like health care service, swimming pool, and so on. The intangible dimensions are the services provided by the people in housekeeping, room service, engineering, and / or restaurant services, on the one end of the continuum are services in the manufactured products segment and on the other are the pure services.

Today, the service industry plays a significant role in both the global and domestic economies.

## **SERVICES DEFINED**

Adriyan Payne has defined service as an activity that has an element of intangibility associated with it and which involves the service provider's integration either with the customers or with the property belonging to the customer. The service activity does not involve the transfer or ownership of the output.

According to Philip Kotler, service is "any activity of benefits that one party can offer to another that is essentially intangible and does not result in the ownership of anything. Its production may or may not be tied to a physical product."

Therefore, it can be said that services are those activities which satisfy wants. Some services are offered individually while some services are offered as a supplement to a product purchased or a major service consumed by the customer. Essentially, services are intangible but sometimes they may involve the use of some tangible goods. In such case, the title of goods doesn't change from the service provider to the customer.

### **CHARACTERISTICS OF SERVICES**

The major characteristics of services are intangibility, inseparability, heterogeneity and perishability. They are discussed below:

A product is a physical entity, which can be touched. It can be seen, heard, touched, smelt, tasted and tested even before purchasing it or consuming it. For example, when a consumer decides to buy a bike, he can see

it, touch it and test drive it to understand its performance. Therefore, he has a better idea of the product before deciding whether to buy it or not. But a service is not tangible unless it is experienced or consumed. The quality of a service cannot be established as clearly as it could be done in the case of a product. For example, when a customer decides to employ the services of a bank in obtaining a loan for the first time, he does have an idea about the services offered by the bank, but he can really assess the services only after he avails them. A bike can be defined in terms of its HP and mileage, but a service cannot always be defined in absolute terms.

### **HETEROGENEITY**

Service is offered by a human being, there is a high probability that the same level of service may not be delivered all the time. The service offered by one employee may differ from the service offered by another although they may belong to the same company. Even the service offered by the same employee may be different times of the day. After serving customers continuously for several hours during the day, an employee may not be able to offer the same level of service towards the end of the day. Also, the quality of service offered by employees at one branch of a service organization may differ greatly from the service offered at another branch. But if the variation in service quality becomes extremely obvious, customers may be dissatisfied and switch to a competing firm. Hence, service organization should try to maintain consistency in the services they offer by taking special care in recruitment, selection and training of employees.

## **INSEPARABILITY**

A service is consumed by the customer as soon as it is delivered by the employee. Thus, production and consumption occur simultaneously in case of services as opposed to products which are manufactured, inventoried and then consumed. Services cannot be inventoried and need to be consumed immediately. Since the delivery and consumption of a service are inseparable, there has to be interaction between customers and employees of a service organization. For example, the integration between patients and doctor is essential if the patient has to be treated for an illness. In the case of a hotel, the interaction between a server and the customer is essential for the former to take the order for food and serve it to the customer for consumption.

## **PERISHABILITY**

Unlike products, services cannot be inventoried or stored for future consumption. Suppose, a hotel has 40 rooms. But on a particular day, only 10 rooms are occupied. The hotel has an idle capacity of 30 rooms on that day. This is a lost business opportunity for the hotel owner. The fact that it may be fully booked the next day does not compensate for the idle capacity on that day. It cannot be recovered as it is lost for all time. Thus, the perishability of services is another factor that leads to complexity in management in the service sector. Service organizations need to be extremely cautious in their demand and supply plans.

## **FACTORS INFLUENCING GLOBALIZATION**

Many factors drive globalization. In the Indian scenario, the economic reforms that were introduced in 1991 have paved the way for the free flow of goods and services across the borders. This has benefited the country in many ways, such as creating new business opportunities like in the area of business process outsourcing. Some of the changes that have boosted globalization worldwide include

- Change in social factors
- Changes in technology
- Changes in political and legal conditions
- Competition in the market
- Competitive advantage

### **Changes in Social Factors**

Today, people in one country know more about people in other countries, their culture, lifestyle, food habits, etc. because of their exposure to the media as well as personal experience gained by traveling to those places. We can see that the needs and wants of people across the world are converging, at least in a few services areas. For example, people in the East enjoy western music, while the West relishes the cuisines of India and China. Apart from

visiting new places on a holiday, people also travel across the world for higher education, research, and jobs. Business people from all over the world expect similar facilities and services on flights and in hotels. With limited extent, service providers are finding it easier to offer their services on a global scale. Though this homogenization is superficial, it offers opportunities for local players to go global.

### **Changes in Technology**

Advances in technology have made it possible for even high contact services like healthcare and technical support to be offered to remote customers. For example, if a client based in the US faces a problem with the application installed by a software solution provider from India, the latter can access the client's system and rectify the problem through a server. Similarly, a specialist surgeon can guide another surgeon operating on a patient, virtually from anywhere in the world. This is an advanced form of telemedicine, which enables patients to consult doctors online and be treated. For example, a senior surgeon at London health Science Centre (LHSC) guided surgeons performing a heart surgery at LHSC from a far off location.

### **Changes in Political Condition**

In some countries, political changes have facilitated globalization of services. In China, strict communist principles were followed until the 1970s.

The government owned most of the assets and organization in the country. These were strong restrictions on the inflow of foreign goods and services. However, the political leaders of the '70s recognized the need for a policy change and lifted the restrictions on trade, facilitating a free flow of goods and services. Russia erstwhile USSR), was also a staunch communist country. However, it underwent some major changes during the tenures of Michael Gorbachev and Boris Yeltsin to discover its economic strengths. India too, with introduction of economic reforms in 1991, became a global economy and a force to reckon with. With more and more economies opening their gates to the free flow of goods and services across borders, the world has become a unified global market.

### **Competition in the Market**

Within a country, there may be intense competition among the domestic players, forcing some of them to venture outside in search of better fortunes. When there is no scope for any expansion within the country, a service provider may seek opportunities in other countries in order to utilize its unused potential. It identifies new markets that have a potential demand for its services and exploits the opportunity.

### **Competitive Advantage**

Intense competition in the market forces service providers to develop competencies that give them a competitive advantage over others. In addition, service organizations need to offer superior quality services at attractive prices to customers. To have a competitive cost advantage, companies try to cut down on the cost of operations by choosing places where the cost of production is minimized. They look for places where there is an abundant supply of people with the desired skills and the cost of labour and other services is lower. Therefore, organizations have their headquarters at one place, some operations at another and a few others at yet another place. And this leads to globalization. For example, General Motors has based its advertising and marketing service operations in Great Britain, data processing services in Ireland and legal, banking, and insurance services in the US. Many IT firms like IBM, Microsoft, Dell, and Oracle have set up their operations in India, because of the availability of skilled people and the infrastructure and support offered by the state governments. GE has customer service, technical support and data processing operations in India.

### **Regulations in Home Country**

Sometimes, too many regulations imposed by the government in the home country encourage national players to set up operations in countries where such regulations do not exist. India had a strong licensing system in place after independence. As a result, no Indian company could start any new business, if it was over a certain size. As a result, innovative businessmen like Aditya Birla opened companies in countries like Malaysia and Thailand. Thus, the Birla company became one of the first global companies from India.

### **Lack of Demand in Home Country**

Sometimes, organizations may find that the demand for their services within their own country is either non-existent or too low to gain enough of a margin. For example, IT firms India like Infosys, Satyam, and Mastek concentrated on the global market in their initial stages primarily because Indian companies did not come forward to purchase the advanced IT solutions that they offered.

### **OVERSEAS MARKET ENTRY DECISIONS**

Different organizations enter different markets for different reasons and in different ways. Some of the modes of entry chosen by organizations to venture into foreign markets include exporting, taking up turnkey projects, licensing franchising, getting into joint ventures, and starting a wholly owned subsidiary. Each of these methods has its own advantages and disadvantages. The choice of a company depends on a variety of factors including the nature of the particular product or service and the political, social and competitive scenario in the target market.

### **Exporting**

Most firms begin their global expansion operations with exports. During the 1990s, the volume of exports in the world economy increased significantly due to the demolition of trade barriers in many countries. However, exporting services remained a challenge owing to their inseparability characteristic. Firms planning to export goods/services must identify opportunities in the foreign market, familiarize themselves with the mechanics of exports and learn to deal with the foreign exchange risk.

Firms can avoid the investment required on technology, infrastructure, and manpower in the host country by adopting the channel of exports. For example, an IT firm in India can export the services of its software engineers to overseas customers.

Exporting benefits firms by enabling them to enter foreign markets at minimum cost. It reduces the dependence of an organization on market demand in the home country. It also protects the business from being adversely affected by seasonal fluctuations in the local market.

### **Turnkey projects**

In a turnkey project, the contractors handle every aspect of the project for a foreign client, from the planning and inception stage to completion and hand over. At the completion of the contract, the system or plant is handed over to the foreign client. Turnkey projects are common in the IT, chemical, pharmaceutical, and petroleum refining industries.

The main advantage of turnkey projects is the high financial returns from the built and installed assets. Turnkey projects are useful in cases where the foreign direct investment (FDI) is regulated by the host government. For example, many oil rich countries in the Middle East decided to invest and build their own petroleum refining industry, thus restricting FDIs in their oil and refining sectors. However, since many of these countries did not have the technological knowledge for petroleum refining, they entered into turnkey projects with foreign firms that had the technology. Thus, foreign firms export their process technology to the host country. Turnkey projects are desirable in countries where the political and economic environments do not favor long-term investment.

### **Licensing**

Licensing is an arrangement through which an organization (licensor) grants the rights to intangible property like patents, inventions, formulas, process, designs, copyrights and trade marks to another company (licensee) for a specified period. The licensor in return receives a royalty fee from the licensee for the rights. For example, an organization may transfer its technical expertise to another organization for a specific time, in return for a royalty fee.

### **Franchising**

Franchising is similar to licensing except that it requires a long-term commitment on the part of both the franchiser and the franchisee, the franchiser allows the franchisee to use its intangible property like the brand name and the operating procedures, but insist that the franchisee follows the standards and rules of the business specified by it. The franchiser has an important role to play in a franchise business in terms of marketing and promoting the service as well as training and supporting the franchisee employees. The franchiser receives a royalty payment that is usually a percentage of the franchisee's revenues. With the franchising strategy, a service firm can build a global presence faster and cheaper and lower its financial and operational risks.

### **Joint Ventures**

In contrast to licensing and franchising arrangements, joint ventures allow companies to own a stake and simultaneously play a role in the management of foreign operations. Joint ventures require more direct investment, training, management assistance and technology transfer. For example, in India, many joint ventures exist between global insurance firms and Indian banks. There are joint ventures exist between ICICI Bank and Prudential Insurance; Vysya Bank and ING insurance and the GMR Group; and HDFC and the Chubb Corporation (global non-life insurer)

### **Strategic Alliance**

A strategic alliance is an understanding or arrangement among the players in a market. Firms form strategic alliances to expand to new markets, gain quick access to new technology, extend the product portfolio or avoid competition. In this case, the partnership can last for a fixed tenure, depending on the agreement between the parties involved. Strategic alliances may or may not involve financial commitment. The partners work together on predetermined goals and objectives, and are free to separate once these goals are achieved or when the agreement ends. For example, TCS entered into a strategic alliance with NEC Singapore in 2002, to journey explore new opportunities in the global market.

### **Wholly Owned Subsidiaries**

In a wholly owned subsidiary, the corporate owns 100% equity in the local subsidiary. Wholly owned subsidiaries can be established in a foreign country in two ways. A firm can set up new operations in the foreign country or it can acquire a local firm with an established business and promote its products through that firm.

A wholly owned subsidiary is the preferred mode of entry into foreign countries for firms with strong financial muscle and technological competence. A wholly owned subsidiary allows an organization to have tight control over operations, which is not possible in the case of licensing and

franchising. The firm also does not risk letting go of its competitive advantage. However, a wholly owned subsidiary calls for huge investments and the company has to bear the complete risk while learning from its own experiences.

### **Mergers and Acquisitions**

Mergers and acquisitions (M&As) are also one of the adventure for service organizations to enter foreign markets. M&As became quite popular in the '90s as more and more MNCs expanded their operations across different countries. In a merger, two organizations come together as one, with mutual consent, in a view to synergize their operations and gain more. However, in the absence of effective planning and management, mergers fail to realize the expected benefits. It is important for two merging firms to have some synergies and common features the strengthen the merger. In an acquisition can be hostile, and some, friendly. The acquisition of Daksh e-services by IBM in 2004 has been explained in exhibit.

### **Piggyback**

In this method, an organization takes the help of another organization to market its products/services in a foreign market. The piggyback method is used by organization as a method of entry for various reasons. The organization which carries the product/service into the foreign market through its channel is called the carrier. The organization that uses the

partner's channel is called the rider. When an organization believes that it has a product/service that has immense potential in the new market, but does not want to risk investing large amounts in building the distribution channels, it goes in for the piggybacking method of entry. The partner organization i.e., the carrier) agrees to the arrangement when the product/service offered by the rider complements its own products/services and enhances its growth. Sometimes, the carrier may even offer his brand name to the rider's products/services. This, in turn, may help in quick acceptance of the new products/services. If the rider's services are well received by customers, the carrier's image will also be enhanced and his own business may grow. The carrier may also help the rider by taking the responsibility for promotion and pricing of products/services. The rider can gain access to information on the foreign market and target customer's, without actually entering the market.

### **CHALLENGES IN THE GLOBAL MARKET**

Service organizations that operate globally face various challenges. The special characteristic of services like intangibility, inseparability, heterogeneity and perishability pose specific challenges to global service providers. The intangible nature of services requires service providers to add tangibility to the services they offer, inseparability forces them to train employees to offer impeccable service, heterogeneity requires organizations to ensure consistency in delivering service and perishability requires them to balance demand and capacity effectively. Apart from these challenges, international service organizations face other challenges too like the following:

## **Legal Barriers**

Legal barriers include discriminating laws, subsidies, restrictions on Foreign Service provider's operations, infringement of copyrights and trade marks, etc., specific to each country of operation. For example, in Tanzania, an organization that seeks to establish its banking operations has to face many legal restrictions. It has to satisfy all the terms and conditions laid down by the central bank of Tanzania to earn a license. The proposals for setting up a banking institution should include plans to offer financial services in the rural sectors and training and employment programs for citizens. The approval to any proposal depends on these plans. Further, banks cannot open a new branch or close an existing branch or declare dividends, without prior approval from the central bank.

### **Discriminating laws**

Some countries have a legal system with policies that favour domestic firms and discriminate against foreign firms. For example, the branch offices of a foreign company in India are treated as a foreign company and declare liable for higher income tax of 48%, as against 35.7% for companies set up in India.

### **Subsidies**

Some countries offer subsidies and low interest loans to domestic organizations and protect them against foreign competition. For example, IT firms were given tax holidays by the government a few years ago when the industry was still in the nascent stages in India. The firms were not required to pay taxes for some years from the date of their establishment. Conversely, some countries offer sops to foreign players to encourage foreign investment that can aid development in the country.

### **Restrictions on foreign company's entry**

Some countries do not allow foreign companies to establish wholly owned subsidiaries. Some impose a ceiling on the investment that can be made by foreign companies. In some cases, some of the industries or sectors can be closed to foreign players. For example, foreign companies cannot invest in the agriculture and plantation sector in India. Similarly, a foreign company is not allowed to hold more than a 24% stake in a small-scale industrial unit in India.

### **Infringement of copyrights and trademarks**

Apart from these barriers, Foreign Service organizations also face the problem of violation of copyrights by local firms. Some local firms market their services using the trademark of a well-known Foreign Service organization. This is primarily because of the failure of the local government to strictly enforce copyrights laws. Firms like Microsoft, Oracle, etc., face problems with the sale of pirated copies of their software in many countries.

### **Cultural Barriers**

Though convergence of tastes and preferences can be seen in some developing and developed countries, it is limited. There is still a large cultural gap between the vast population of the eastern part of the world and that of the western countries. People in developing countries from the high-income group or socio-economic class, who get exposed to western culture, are influenced by it. There is still a large section of the society in developing countries, which is unexposed to and uninfluenced by the western culture. Therefore, differences still do exist in cultures, posing challenges to international service organizations. The cultural barriers arise from differences in language, customs and beliefs, values and attitudes, lifestyle, etc.

### **Language**

People in different countries speak different languages and this poses difficulties to service organizations in effectively communicating with

customers. Communication with internal as well as external customers, as we have already studied, is very important for services business to survive and flourish. In the absence of proper translation of messages from one language to another, service organizations can communicate unintended messages and land up in trouble.

### **Customs**

Different countries have different customs and manners. “Customs are established practices, while manners are behaviors that are regarded as appropriate in a particular society.” In some countries, people value time immensely and expect others to do the same. For example, say two parties from two different countries have an appointment at 5.00pm. the first party from country A values time immensely and is there at the appointed venue five minutes before the scheduled the time. The second party of country B however, does not value time and reaches the venue 10 minutes late. This will naturally annoy the first party, and he would cancel the business dealing.

In some countries, it is customary to make or avoid some gestures to show their respect to the other party. The management of a service firm should learn this business etiquette to maintain positive relations with clients and partners.

### **Values and attitudes**

Values and attitudes differ from society to society. For example, most Muslims consider the pig as inauspicious. Hindus revere the cow as a holy animal. Therefore, international service organizations involved in the hospitality industry should take special care not to offer beef or pork so as not to hurt religious sentiments of the people. McDonald's for example, takes special care to avoid beef in its menu in India.

### **Lifestyle**

Lifestyle varies across countries. The way people spend their money, leisure time, etc., differs from one country to another. For example, earlier, people in India emphasized saving. There were not many who spent lavishly. However, things have changed and more and more Indians are willing to spend more on lifestyle and luxury items. The status symbols used by people to reflect their status, also differ from one country to another. For example, in India, most people value assets like jewelry. They try to accumulate as much silver and gold as possible. However, in the west, people prefer to buy luxury products like expensive cars. The way people spend their leisure time is also different. People's perception of beauty and aesthetics also varies across countries. The knowledge of these differences will help services organizations choose the right dress code for employees, the right architecture for buildings and design proper service offerings and marketing programs.

### **Financial Barriers**

Global service organization also faces financial barriers. Organizations planning to expand globally need more funds than those operating locally. Even though the returns are higher, they have to bear higher costs. These costs include the costs due to exchange rates and taxes, investment in a new business in terms of set-up costs, logistics solutions, communication systems, traveling etc.,

### **Changes in currency exchange rates**

Different countries have different currencies. Depending on the economic condition of a country, the value of its currency keeps changing and so does its exchange rate. This poses problems in payments and collections for global service organizations. Any appreciation in the currency of the host country will result in the service provider receiving fewer of home country currency units from clients. Sometimes, they may also face double taxation, in both the exporting and importing country or the host and the home country. This will obviously affect the profitability of the organization. Before making an investment, service organizations should look for countries, which have double tax avoidance treaties with their own countries.

### **Problems with logistics**

Service organizations need to invest in various resources to run their operations successfully in a country. For instance, package carrier companies have to invest heavily in setting up warehouses at appropriate locations. DHL invested about \$200million to expand its facility in the US near Kentucky international airport in Cincinnati in 2002. BPO centers need to make a huge investment on people, equipment and infrastructure.

Fast food outlets like McDonald's have to procure the best quality raw materials and other inputs to serve quality food to customers. McDonald's has to source bread, bun, batter mixes, meat, cheese, sauce, potatoes and other vegetables from the best suppliers, which means a lot of investment.

### **FACTORS INFLUENCING SUCCESS OF A GLOBAL SERVICE FIRM**

Many factors such as innovation, excellence in customer service, efficient operations, etc., contribute to the success of an organization at the global level. A service firm needs to conduct a complete SWOT analysis before taking any major strategic decision. The success and survival of a company depends on its understanding of the differences among its countries of operation in terms of culture, consumer behavior, etc., and its ability to accommodate the differences.

### **Select the right entry mode**

An organization can enter a foreign market through several modes, as discussed earlier. However, it should choose its entry mode carefully so that it does not affect its competitive advantage. If it chooses to enter through a strategic alliance, for example, it should ensure that the partner has a strong hold in the market and can support it in gaining a strong foot hold. Moreover, the partnership should not conflict with the business interest of either party and should benefit both. If the partnership terms favor one party, then the relationship may not last long because the losing partner will be on the constant lookout for exiting from the partnership. Similarly, if an organization decides to enter a foreign market through merger or acquisition, it might face different kinds of difficulties. It might have difficulties in merging the operations of both firms, changing the culture of the workforce, leveraging synergies etc. if an organization wants to establish a wholly owned subsidiary in a foreign country, it should look for the right location to gain benefits like cheap infrastructure, governments support, educated work force, low salaries, political stability, security, favorable laws and regulations, etc.

### **Select the right marketing research methods**

In some countries, people do not want to answer personal questions and dislike being monitored. It would be difficult for organizations to conduct marketing research in such countries. Therefore, service organizations should use indirect measurement techniques, which do not involve approaching

customers directly. Rather, they may have to collect information from service provider's who can provide reliable data and information on consumer behavior.

### **Customize the service offering**

Global service providers should customize their services to suit the tastes and preference of customers in different countries. For example, in some countries, people do not like invasion of privacy. In such situations, service personnel do not take the initiative to try and entertain customers. However, in some countries people may expect the service personnel to keep enquiring about their needs and taking care of them. In such cases, the front-line personnel should be pro-active and approach customers before they feel they are not being attached to. Similarity, during an economics downturn, companies might need to customize their service offering to suit the existing needs of the customers.

### **Train the service personnel**

Service personnel should be educated about the differences in the culture of the customers they serve. For example, the service personnel in a Chinese restaurant need to realize that they have to treat an Indian customer and an American customer differently. The service personnel should be trained to customize their service offering and delivery to suit the customer's preference. In some countries, people are not comfortable talking to a salesperson o the

phone. They expect the salesperson to visit their home/office and explain the service offer to them in person. Service personnel need to feel trained to catch the pulse of the customer immediately and change their approach strategy accordingly.

### **Select the right promotion strategy**

In some countries like Japan, comparative and aggressive advertising is unacceptable. So, in these countries, service firms should emphasize the benefits of their service offering rather than point out the drawbacks of the competitor's service offerings. In countries like the US and India, where such advertising is allowed, at least in some sectors, service organizations should use the opportunity to explain to customers how their service offers out weight those of their competitors. For example, in India, ICICI bank advertises that it does not charge any processing fee from customers who apply for home loans. HDFC claims that it charges a processing fee for home loans, but provides many valuable supplementary services unlike its competitors, who might not charge any processing fee, but include hidden costs for customers.

## UNIT - V

### GLOBAL LOGISTIC MANAGEMENT

The cost and efficiency of the distribution have direct relationship with the logistics. Logistics, therefore, is a factor which affects the competitiveness of a firm.

International logistics is defined as "the designing and managing of a system that contracts the flow of materials into, through, and out of the international corporation. It encompasses the total movement concept by covering the entire range of operations concerned with product movement".

It follows from the above definition that logistics comprises of:

- (i) Management of movement of raw materials, parts and supplies into and through the firm; and
- (ii) Management of movement of finished products to the consumer.

The major objective of the logistics management is to make the physical distribution as effective as required at the lowest cost possible. Attempts to increase the effectiveness of the distribution may sometimes tend to increase the cost and attempts to cut costs may impair distribution effectiveness. The trade off and optimisation, therefore are often a complex problem.

#### Components of Logistics Management

Logistics management comprises of five major interdependent areas.

**Fixed Facilities Location** The major consideration is the location of fixed facilities like production and warehousing in such a way as to maximise the total efficiency of the logistics system. Factors like future potentials of the markets,

future plans of the company, competitive factors, political stability etc. are also import considerations.

### **Transportation:**

The modes of transportation, frequency of shipping etc. are determined on consideration of several factors such as the cost, speed, safety, lead time, transit time, type of product, natural environmental factors etc.

### **Inventory Management:**

The main objective of inventory management is to minimise the cost of the inventory while ensuring smooth supplies. Developments in inventory management by the customers, order processing and in the total logistics system have made inventory management both challenging and efficient.

### **Order Processing:**

The efficiency of order processing by the client as well as the company have important implications for inventory levels and other aspects of the logistics. Rapid order processing shorten the order cycle and allows for lower safety stocks on the part of the client. Exporters from developing countries like India face the challenge of coping up with such situations.

### **Materials Handling and Warehousing:**

Materials handling and warehousing are also an important part of the logistics management. The technologies in use in materials handling and transportation may be different in different countries. Differences in natural factors like climatic and weather conditions may also make warehousing requirements varied.

## **INTERNATIONAL DISTRIBUTION SYSTEM**

### **Channel of Distribution Structures**

In every country and in every market, urban or rural, rich or poor, all consumer and industrial products eventually go through a distribution process.

The distribution process includes the physical handling and distribution of goods, the passage of ownership (title), and most important from the standpoint of marketing strategy the buying and selling negotiations between producers and middlemen and between middlemen and customers.

A host of policy and strategy channel-selection issues confronts the international marketing manager. These issues are not in themselves very different from those encountered in domestic distribution, but the resolution of the issues differs because of different channel alternatives and market patterns.

Each country market has a distribution structure through which goods pass from producer to user. Within this structure are a variety of middlemen whose customary functions, activities, and services reflect existing competition, market characteristics, tradition, and economic development. In short, the behavior of channel members is the result of the interactions between the cultural environment and the marketing process. Channel structure ranges from those with little developed marketing infrastructure found in many emerging markets to the highly complex, multilayered system found in Japan.

### **Import-Oriented Distribution Structure**

Traditional channels in developing countries evolved from economies with a strong dependence on imported manufactured goods. In an import-oriented distribution structure, typically an importer controls a fixed supply of goods and the marketing system develops around the philosophy of selling a limited supply of goods at high prices to a small number of affluent customers. In the resulting seller's market, market penetration and mass distribution are not necessary since demand exceeds supply and, in most cases, the customer seeks the supply. This produces a channel structure with a limited number of middlemen.

Contrast this with the mass consumption-distribution philosophy which prevails in the United States and other industrialized nations. In these markets, one supplier does not dominate supply, supply can be increased or decreased within a given range, and profit maximization occurs at or near production capacity. Generally a buyer's market exists and the producer strives to penetrate the market and push goods out to the consumer, resulting in a highly developed channel structure that includes a variety of intermediaries.

Business attitudes in an import-oriented market system are often the direct opposite of what you would expect. As one observer notes:

Consumers, retailers, and other intermediaries are always seeking goods. This results from the tendency of importers to throttle the flow of goods, and from this sporadic and uneven flow of imports, inventory hoarding as a means of checking the

market can be achieved at relatively low cost, and is obviously justified because of its lucrative and speculative yields.

### **Japanese Distribution Structure**

Distribution in Japan has long been considered the most effective non tariff barrier to the Japanese market. The Japanese distribution structure is different enough from its United States or European counterparts that it should be carefully studied by anyone contemplating entry. The Japanese system has four distinguishing features: (1) a structure dominated by many small middlemen dealing with many small retailers; (2) channel control by manufacturers; (3) a business philosophy shaped by a unique culture; and (4) laws that protect the foundation of the system - the small retailer.

### **High Density of Middlemen.**

There is a density of middlemen, retailers, and wholesalers in the Japanese market unparalleled in any Western industrialized country. The traditional Japanese structure serves consumers who make small, frequent purchases at small, conveniently located stores. An equal density of wholesalers supports the high density of small stores with small inventories. It is not unusual for consumer goods to go through three or four intermediaries before reaching the consumer-producer to primary, secondary, regional, and local wholesaler, and finally to retailer to consumer. The contrast between shorter U.S. channels and the long Japanese channels.

### **Channel Control**

Manufacturers depend on wholesalers for a multitude of services to other members of the distribution network. Financing, physical distribution, warehousing, inventory, promotion, and payment collection are provided to other channel members by wholesalers. The system works because wholesalers and all other middlemen downstream are tied to manufacturers by a set of practices and incentives designed to ensure strong marketing support for their products and to exclude rival competitors from the channel. Wholesalers typically act as agent middlemen and extend the manufacturer's control through the channel to the retail level.

Control is maintained by: (1) inventory financing—sales made on consignment with credits extending for several months; (2) cumulative rebates—rebates given annually for any number of reasons, including quantity purchases, early payments, achieving sales targets, performing services, maintaining specific inventory levels, participating in sales promotions, loyalty to suppliers, maintaining manufacturer's price policies, cooperation, and contribution to overall success; (3) merchandise returns—all unsold merchandise may be returned to the manufacturer; and (4) promotional support—intermediaries receive a host of displays, advertising layouts, management education programs, in-store demonstrations, and other dealer aids which strengthen the relationship among middlemen and the manufacturer.

### **Business Philosophy**

Coupled with the close economic ties and dependency created by trade customs and the long structure of Japanese distribution channels is a unique

business philosophy that emphasizes loyalty, harmony, and friendship. The value system supports long-term dealer/supplier relationships that are difficult to change as long as each party perceives economic advantage. The traditional partner, the insider, generally has the advantage.

A general lack of price competition, the provision of costly services, and other inefficiencies render the cost of Japanese consumer goods among the highest in the world; for example, a bottle of 96 aspirin tablets sells for \$20. Yet the system is slow to change. The Japanese consumer contributes to the continuation of the traditional nature of the distribution system through frequent buying trips, small purchases, favoring personal service over price, and the proclivity for loyalty to brands perceived to be of high quality. Additionally, Japanese law gives the small retailer enormous advantage over the development of larger stores and competition. All these factors support the continued viability of small stores and the system, although changing attitudes among many Japanese consumers are beginning to weaken the hold traditional retailing has on the market

### **Large-Scale Retail Store Law**

Competition from large retail stores has been almost totally controlled by Daitenho the Large-Scale Retail Store Law. Designed to protect small retailers from large intruders into their markets, the law requires that any store larger than 5,382 square feet (500 square meters) must have approval from the prefecture government to be "built, expanded, stay open later in the evening, or change the days of the month they must remain closed." All proposals for new "large" stores are first judged by MITI (Ministry of International Trade and Industry). Then, if local retailers unanimously agree to the plan, it is swiftly approved.

However, without approval at the prefecture level (all small retailers in the area must agree), the plan is returned for clarification and modification that may take several years (10 years is not unheard of) for approval. Designed to protect small retailers against competition from large stores, the law has been imposed against both domestic and foreign companies. It took 10 years for one of Japan's largest supermarket chains to get clearance for a new site. Toys "R" Us fought rules and regulations for over three years before it gained approval for a store.

Besides the Large-Scale Retail Store Law, there are myriad licensing rules. One investigation of the regulations governing the opening of retail stores uncovered 39 different laws, each with a separate license that had to be met to open a full-service store.

Businesspeople in Japan and the United States see the Japanese distribution system as a major nontariff barrier and, by many Japanese, as a major roadblock to improvement of the Japanese standard of living. However, pressure from the United States and the Structural Impediments Initiative (SII) negotiations to pry open new markets for American companies is producing strong cracks in the system. As of this writing, it is reported the Japanese government will repeal the Large-Scale Retail Store Law as early as the end of fiscal 1998.

### **Changes in the Japanese Distribution System**

Agreements between the United States and Japan under the SII have had a profound impact on the Japanese distribution system by leading to deregulation of retailing and by strengthening rules on monopoly business

practices. The retailing law has been relaxed to permit new outlets as large as 1,000 square meters without prior permission. Limits on store hours and business days per year have also been lifted. Officially relaxing laws and regulations on retailing is but one of the important changes signaling the beginning of profound changes in how the Japanese shop.

SII and deregulation will undoubtedly have a part in changing Japanese distribution practices, but those merchants willing to challenge traditional ways and give the consumer quality products at competitive, fair prices will bring about the demise of the way department stores and small shops wedded to the traditional distribution system operate. Specialty discounters are sprouting up everywhere and entrepreneurs are slashing prices by buying direct and avoiding the distribution system altogether. For example, Kojima, a consumer electronics discounter, practices what it calls "global purchasing" and buys merchandise anywhere in the world as long as it can be done as cheaply as possible. Ko-jima's tie-up with General Electric enables it to offer a 410-liter GE refrigerator for \$640, down from the typical price of \$1,925, and the 550-liter model from \$3,462 to \$1,585.



Japanese consumers, described as brand loyal and more interested in services and quality than price, seem to be willing accomplices to the changes taking place, if the price is right. Japanese consumers have traditionally paid the highest prices in the world for the goods they buy. Before Toys "R" Us changed price levels, toys in Japan cost four times as much as toys in any other country. Japanese-made products imported to the United States can be purchased in the U.S. for less than they cost in Japan. Such inequities did not seem to matter to

Japanese consumers when they had no other alternatives. But, more often now, the Japanese consumer has a choice of prices for everything from appliances to beer. Before price competition, a can of Coors beer would cost 240 yen; now it costs 240 yen in a neighborhood liquor store, 178 yen in a supermarket, and 139 yen in a discount store.

### **Trends: From Traditional to Modern Channel Structures**

Today, few countries are so sufficiently isolated that they are unaffected by global economic and political changes. These currents of change are altering all levels of economic fabric, including the distribution structure. Traditional channel structures are giving way to new forms, new alliances, and new processes—some more slowly than others, but all changing. Pressures for change in a country come from within and without. Multinational marketers are seeking ways to profitably tap market segments that are served by costly, traditional distribution systems. Direct marketing, door-to-door selling, hypermarkets, discount houses, shopping malls, catalog selling, e-commerce via the Internet, and other distribution methods are being introduced in an attempt to provide efficient distribution channels.



Some important trends in distribution will eventually lead to greater commonality than disparity among middlemen in different countries. Wal-Mart, for example, is expanding all over the world—from Mexico to Brazil and from Argentina to Asia. Amway and Avon are expanding into Eastern Europe, Mary Kay Cosmetics in China, and L. L. Bean and Lands' End have made successful entry into the Japanese market. In Spain, the Southland Corporation's 7-Eleven Stores are replacing many of the traditional mom-and-pop stores. Hypermarkets

developed in France, and their many spin-offs are expanding all over Europe, Latin America, and Asia. These huge stores, supplied with computerized inventories, may spell a slow death for small shops and midsize retailers in urban areas. The effect of all these intrusions into the traditional distribution systems is change that will make discounting, self-service, supermarkets, and mass merchandising concepts common all over the world and elevate the competitive climate to a level not known before.

### **Distribution Patterns**

International marketers need a general awareness of the patterns of distribution that confront them in world marketplaces. Nearly every international trading firm is forced by the structure of the market to use at least some middlemen in the distribution arrangement. It is all too easy to conclude that, because the structural arrangements of foreign and domestic distribution seem alike, foreign channels are the same as or similar to domestic channels of the same name. This is misleading. Only when the varied intricacies of actual distribution patterns are understood can the complexity of the distribution task be appreciated. The following description should convey a sense of the variety of distribution patterns.

### **General Patterns**

Generalizing about internal distribution channel patterns of various countries is almost as difficult as generalizing about behavior patterns of people. Despite similarities, marketing channels are not the same throughout the world. Marketing methods taken for granted in the United States are rare in many countries.

### **Middlemen Services**

Service attitudes of trades people vary sharply at both the retail and wholesale levels from country to country. In Egypt, for example, the primary purpose of the simple trading system is to handle the physical distribution of available goods. On the other hand, when margins are low and there is a continuing battle for customer preference, both wholesalers and retailers try to offer extra services to make their goods attractive to consumers. When middlemen are disinterested in promoting or selling individual items of merchandise, the manufacturer must provide adequate inducement to the middlemen or undertake much of the promotion and selling effort. Such is the case in China, where wholesalers see their function as storing the goods and waiting for their customers to come to them.

### **Line Breadth.**

Every nation has a distinct pattern relative to the breadth of line carried by wholesalers and retailers. The distribution system of some countries seems to be characterized by middlemen who carry or can get everything; in others, every middleman seems to be a specialist dealing only in extremely narrow lines. Government regulations in some countries limit the breadth of line that can be carried by middlemen and licensing requirements to handle certain merchandise are not uncommon.

### **Costs and Margins**

Cost levels and middleman margins vary widely from country to country, depending on the level of competition, services offered, efficiencies or inefficiencies of scale, and geographic and turnover factors related to market

size, purchasing power, tradition, and other basic determinants. In India, competition in large cities is so intense that costs are low and margins thin; but in rural areas, the lack of capital has permitted the few traders with capital to gain monopolies with consequent high prices and wide margins.

### **Channel Length**

Some correlation may be found between the stage of economic development and the length of marketing channels. In every country channels are likely to be shorter for industrial goods and for high-priced consumer goods than for low-priced products. In general, there is an inverse relationship between channel length and the size of the purchase. Combination wholesaler-retailers or semi wholesalers exist in many countries, adding one or two links to the length of the distribution chain. In China, for example, the traditional distribution system for over-the-counter drugs consists of large local wholesalers divided into three levels. First-level wholesalers supply drugs to major cities such as Beijing and Shanghai. The second-level services medium-sized cities, while the third level distributes to counties and cities with 100,000 people or less. It can

be profitable for a company to sell directly to the two top-level wholesalers and have them sell to the third level which is so small that it would be unprofitable to seek out.

### **Nonexistent Channels**

One of the things companies discover about international channel-of-distribution patterns is that in many countries adequate market coverage through a simple channel of distribution is nearly impossible. In many instances, appropriate channels do not exist; in others, parts of a channel system are available

but other parts are not. In Peru, for example, the informal distribution network accounts for almost a quarter of all retail cash sales. The ubiquitous street markets and ambulatory sellers offer far wider market penetration than formal distribution companies. Further, their prices are generally lower than traditional retailers, partly because of lower overhead costs compared with the higher costs generated by the overextended formal distribution chain of the traditional retailer. Thus, several distinct distribution channels are necessary to reach different segments of a market; channels suitable for distribution in urban areas seldom provide adequate rural coverage.

### **Blocked Channels**

International marketers may be blocked from using the channel of their choice. Blockage can result from competitors' already-established lines in the various channels and trade associations or cartels having closed certain channels. The classic example of blocked channels is Japan, as discussed above, but it is by no means the only example. Associations of middlemen sometimes restrict the number of distribution alternatives available to a producer. Druggists in many countries have inhibited distribution of a wide range of goods through any retail outlets except drugstores. The drugstores, in turn, have been supplied by a relatively small number of wholesalers who have long-established relationships with their suppliers. Thus, through a combination of competition and association, a producer may be kept out of the market completely. In the U.K., simple magnifying reading glasses that can be purchased in a dozen different types of stores in the United States can only be purchased by prescription through registered optical stores, which are controlled by a few large companies.

### **Stocking**

The high cost of credit, danger of loss through inflation, lack of capital, and other concerns cause foreign middlemen in many countries to limit inventories. This often results in out-of-stock conditions and sales lost to competitors. Physical distribution lags intensify their problem so that in many cases the manufacturer must provide local warehousing or extend long credit to encourage middlemen to carry large inventories. Often large inventories are out of the question for small stores with limited floor space. Considerable ingenuity, assistance, and, perhaps pressure are required to induce middlemen in most countries to carry adequate or even minimal inventories.

### **Power and Competition**

Distribution power tends to concentrate in countries where a few large wholesalers distribute to a mass of small middlemen. Large wholesalers generally finance middlemen downstream. The strong allegiance they command from their customers enables them to effectively block existing channels and force an outsider to rely on less effective and more costly distribution.

### **Retail Patterns**

Retailing shows even greater diversity in its structure than does wholesaling. In Italy and Morocco, retailing is composed largely of specialty houses which carry narrow lines, while in Finland, most retailers carry a more general line of merchandise. Retail size is represented at one end by Japan's giant Mitsukoshi Ltd., which reportedly enjoys the patronage of more than 100,000 customers every day. The other extreme is represented in the market of Iberian, Nigeria, where some 3,000 one- or two-person stalls serve not many more customers.

### **Size Patterns**

The extremes in size in retailing are similar to those that predominate in wholesaling. Exhibit 14-3 dramatically illustrates some of the variations in size and number of retailers per person that exist in some countries. The retail structure and the problems it engenders cause real difficulties for the international marketing firm selling consumer goods. Large dominant retailers can be sold direct, but there is no adequate way to directly reach small retailers who, in the aggregate, handle a great volume of sales. In Italy, official figures show there are 865,000 retail stores, or one store for every 66 Italians. Of the 340,000 food stores, fewer than 1,500 can be classified as large. Thus, middlemen are a critical factor in adequate distribution in Italy.

Underdeveloped countries present similar problems. Among the large supermarket chains in South Africa there is considerable concentration. One thousand of the country's 31,000 stores control 60 percent of all grocery sales, leaving the remaining 40 percent of sales to be spread among 30,000 stores. It may be difficult to reach the 40 percent of the market served by those 30,000 stores. Predominantly in Black communities, retailing is on a small scale—cigarettes are often sold singly, and the entire fruit inventory may consist of four apples in a bowl.

Retailing around the world has been in a state of active ferment for several years. The rate of change appears to be directly related to the stage and speed of economic development, and even the least-developed countries are experiencing dramatic changes. Supermarkets of one variety or another are blossoming in developed and underdeveloped countries alike. Discount houses that sell everything from powdered milk and canned chili to Korean TVs and

VCRs are thriving and expanding worldwide. Wal-Mart, already in Mexico, is expanding into Brazil, Argentina, Thailand, Hong Kong, and China.

### **Direct Marketing**

Selling directly to the consumer through the mail, by telephone, or door-to-door is becoming the distribution-marketing approach of choice in markets with insufficient and/or underdeveloped distribution systems. Amway, operating in 42 foreign countries, has successfully expanded into Latin America and Asia with its method of direct marketing. Companies that enlist individuals to sell their products are proving to be especially popular in Eastern Europe and other countries, where many people are looking for ways to become entrepreneurs. In the Czech Republic, for example, Amway Corporation signed up 25,000 Czechs as distributors and sold 40,000 starter kits at \$83 each in its first two weeks of business

Direct sales through catalogs have proved to be a successful way to enter foreign markets. In Japan, it has been an important way to break the trade barrier imposed by the Japanese distribution system. For example, a U.S. mail-order company, Shop America, has teamed up with 7-Eleven in Japan<sup>21</sup> to distribute catalogs in its 4,000 stores. Shop America sells items such as compact disks, Canon cameras, and Rolex watches for 30-50 percent less than Tokyo stores. For example, a Canon Auto boy camera sells for \$260 in Tokyo and \$180 in the Shop America catalog, and a Lady Remington shaver sells for \$86 in Tokyo versus \$46 in the catalog.

### **Resistances to Change**

Efforts to improve the efficiency of the distribution system, new types of middlemen, and other attempts to change traditional ways are typically viewed as threatening and thus resisted. Laws abound that protect the entrenched in their positions. In Italy, a new retail outlet must obtain a license from a municipal board composed of local trades people. In a two-year period, some 200 applications were made and only 10 new licenses granted. Opposition to retail innovation prevails everywhere, yet in the face of all the restrictions and hindrances, self-service, discount merchandising, liberal store hours, and large-scale merchandising continue to grow because they offer the consumer convenience and a broad range of quality product brands at advantageous prices. Ultimately the consumer does prevail.

### **World Wide Web**

The use of the Internet is rapidly becoming an important distribution method for multinational companies and a source of products for businesses and consumers. Computer hardware and software companies, and book and music retailers are the most experienced "e-marketers" in using this method of distribution and marketing. Technically, e-commerce is a form of direct selling; however, because of its newness and the unique issues associated with this form of distribution, it is important to differentiate from other types of direct marketing. E-commerce is used to market business-to-business services, consumer services, and consumer and industrial products via the World Wide Web on the Internet. It involves the direct marketing from a manufacturer, retailer, or some other intermediary to a final user.

Some examples of e-marketers that have an international presence include Dell Computer Corporation, which generates revenues of more than \$3 million per day; in the U.K., 10 percent of its sales are online. Cisco Systems Inc.

generated \$1 billion in sales in 1997. Cisco's Web site appears in 14 languages and has country-specific content for 49 nations. Gateway 2000 has global sites in Japan, France, the Netherlands, Germany and Sweden, Australia, the U.K., and the United States. Sun Microsystems and its after marketing company, Sun Express, have local language information on more than 3,500 aftermarket products. Sun Plaza enables visitors in North America, Europe, and Japan to get information on-line on products and services, and place orders directly and securely in their native languages.

### **Web Malls**

An indication of the impact U.S. e-retailers have had on retail sales in the U.K. is the E-Christmas mall created to counter Christmas gift sales that have been going to the U.S. In an attempt to provide more opportunity for European e-customers to stay at home, a group of 15 of Europe's best-known retailers organized E-Christmas on-line in time for the Christmas selling season. E-Christmas shoppers can choose from one of six languages and 11 currencies. They are presented with prices that include duty when applicable and delivery charges for the 25 countries served by UPS worldwide. Germany also has an e-mail that operates year-around; it is, however, only in German. Both of these shopping malls have U.S. stores included in their lineup.

### **Home-Country Middlemen**

Home-country middlemen, or domestic middlemen, located in the producing firm's country, provide marketing services from a domestic base. By selecting domestic middlemen as intermediaries in the distribution processes,

companies relegate foreign-market distribution to others. Domestic middlemen offer many advantages for companies with small international sales volume, those inexperienced with foreign markets, those not wanting to become immediately involved with the complexities of international marketing, and those wanting to sell abroad with minimum financial and management commitment. A major trade-off for using home-country middlemen is limited control over the entire process. Domestic middlemen are most likely to be used when the marketer is uncertain and/or desires to minimize financial and management investment. A brief discussion of the more frequently used domestic middlemen follows.

### **Global Retailers**

As global retailers like Costco, Sears Roebuck, Toys "R" Us, and Wal-Mart expand their global coverage, they are becoming major domestic middlemen for international markets. Wal-Mart, with 603 stores in nine foreign markets, is an attractive entry point to international markets for U.S. suppliers if they can meet Wal-Mart's stringent shipping requirements. For those that can meet the test, Wal-Mart offers an effective way to enter international markets with a minimum of experience. Pacific Connections, for example, a California manufacturer of handbags with \$70 million in sales in 1997, ventured into overseas markets in Argentina, Brazil, Canada, and Mexico through its ties to Wal-Mart. Wal-Mart executives say that many U.S. vendors lack global expertise and seem ill prepared to supply the retailer in places like China and Brazil.

### **Export Management Companies**

The export management company (EMC) is an important middleman for firms with relatively small international volume or for those unwilling to

involve their own personnel in the international function. EMCs range in size from one person upward to 100 and handle about 10 percent of the manufactured goods exported. An example of an EMC is a Washington, D.C.-based company that has exclusive agreements with 10 U.S. manufacturers of orthopedic equipment and markets these products on a worldwide basis.

The major disadvantage is that EMCs can seldom afford to make the kind of market investment needed to establish deep distribution for products because they must have immediate sales payout to survive. Such a situation does not offer the market advantages gained by a company that can afford to use company personnel. Carefully selected EMCs can do an excellent job, but the manufacturer must remember the EMC is dependent on sales volume for compensation and probably will not push the manufacturer's line if it is spread too thinly, generates too small a volume from a given principal, or cannot operate profitably in the short run. Then the EMC becomes an order taker and not the desired substitute for an international marketing department.

### **Trading Companies**

Trading companies have a long and honorable history as important intermediaries in the development of trade between nations. Trading companies accumulate, transport, and distribute goods from many countries. In concept, the trading company has changed little in hundreds of years.

The British firm, Gray MacKenzie and Company, is typical of companies operating in the Middle East. It has some 70 salespeople and handles consumer products ranging from toiletries to outboard motors and Scotch

whiskey. The key advantage to this type of trading company is that it covers the entire Middle East.

Large, established trading companies generally are located in developed countries; they sell manufactured goods to developing countries and buy raw materials and unprocessed goods. Japanese trading companies (sogo shosha), dating back to the early 1700s, operate both as importers and exporters. Some 300 are engaged in foreign and domestic trade through 2,000 branch offices outside Japan and handle over \$1 trillion in trading volume annually. Japanese trading companies account for 61 percent of all Japanese imports and 39 percent of all exports or about a fifth of Japan's entire GDP.

### **U.S. Export Trading Companies**

The Export Trading Company (ETC) Act allows producers of similar products to form export trading companies. A major goal of the ETC Act was to increase U.S. exports by encouraging more efficient export trade services to producers and suppliers in order to improve the availability of trade finance and to remove antitrust disincentives to export activities. By providing U.S. businesses with an opportunity to obtain antitrust pre clearance for specified export activities, the ETC Act creates a more favorable environment for the formation of joint export ventures. Through such joint ventures, U.S. firms can take advantage of economies of scale, spread risk, and pool their expertise. In addition, through joint selling arrangements, domestic competitors can avoid inter-firm rivalry in foreign markets. Prior to the passage of the ETC Act, competing companies could not engage in joint exporting efforts without possible violation of antitrust provisions. The other important provision of the

ETC Act is to permit bank holding companies to own ETCs. Prior to the ETC Act, banks could not own commercial enterprises.

### **Manufacturer's Export Agent**

The manufacturer's export agent (MEA) is an individual agent middleman or an agent middleman firm providing a selling service for manufacturers. Unlike the EMC, the MEA does not serve as the producer's export department but has a short-term relationship, covers only one or two markets, and operates on a straight commission basis. Another principal difference is that MEAs do business in their own names rather than in the name of the client. Within a limited scope of operation, the MEAs provide services similar to those of the EMC.

### **Home Country Brokers**

The term broker is a catchall for a variety of middlemen performing low-cost agent services. The term is typically applied to import-export brokers who provide the intermediary function of bringing buyers and sellers together and who do not have a continuing relationship with their clients. Most brokers specialize in one or more commodities for which they maintain contact with major producers and purchasers throughout the world.

### **Buying Offices**

A variety of agent middlemen may be classified simply as buyers or buyers for export. Their common denominator is a primary function of seeking and purchasing merchandise on request from principals; as such, they do not provide a selling service. In fact, their chief emphasis is on flexibility and the ability to find merchandise from any source. They do not often become involved

in continuing relationships with domestic suppliers and do not provide a continuing source of representation.

### **Selling Groups**

Several types of arrangements have been developed in which various manufacturers or producers cooperate in a joint attempt to sell their merchandise abroad. This may take the form of complementary exporting or of selling to a business combine such as a Webb-Pomerene export association. Both are considered agency arrangements when the exporting is done on a fee or commission basis.

### **Webb-Pomerene Export Associations (WPEA)**

Webb-Pomerene Export Associations (WPEA) are another major form of group exporting. The Webb-Pomerene Act of 1918 made it possible for American business firms to join forces in export activities without being subject to the Sherman Antitrust Act. WPEAs cannot participate in cartels or other international agreements that would reduce competition in the United States, but can offer four major benefits: (1) reduction of export costs, (2) demand expansion through promotion, (3) trade barrier reductions, and (4) improvement of trade terms through bilateral bargaining. Additionally, WPEAs set prices, standardize products, and arrange for disposal of surplus products. Although they account for less than 5 percent of U.S. exports, WPEAs include some of America's blue-chip companies in agricultural products, chemicals and raw materials, forest products, pulp and paper, textiles, rubber products, motion pictures, and television.

### **Foreign Sales Corporation (FSC)**

A Foreign Sales Corporation (FSC) is a sales corporation set up in a foreign country or U.S. possession that can obtain a corporate tax exemption on a portion of the earnings generated by the sale or lease of export property. Manufacturers and export groups can form FSCs. A FSC can function as a principal, buying and selling for its own account, or as a commissioned agent. It can be related to a manufacturing parent or can be an independent merchant or broker.

### **Norazi Agent**

Norazi agents are unique middlemen specializing in shady or difficult transactions. They deal in contraband materials, such as hazardous waste products or war materials, and in providing strategic goods to countries closed to normal trading channels. The Norazi is also likely to be engaged in black-market currency operations, untaxed liquor, narcotics, industrial espionage, and other illicit traffic. The Norazi exists because tariffs, import taxes, import/export regulations, and excise taxes make illegal movements of goods more profitable than legal movements. Because of high tariffs, the amount of contraband entering Brazil from Paraguay is estimated to be between \$4 and \$12 billion annually. Cigarette smuggling accounts for over one-fourth of all cigarettes sold abroad according to one estimate. In the last few years, money laundering has become a major activity of Norazi agents; some estimate that \$500 billion is laundered worldwide annually.

### **Export Merchants**

Export merchants are essentially domestic merchants operating in foreign markets. As such, they operate much like the domestic wholesaler. Specifically, they purchase goods from a large number of manufacturers, ship

them to foreign countries, and take full responsibility for their marketing. Sometimes they utilize their own organizations, but, more commonly, they sell through middlemen. They may carry competing lines, have full control over prices, and maintain little loyalty to suppliers, although they continue to handle products as long as they are profitable.

### **Export Jobbers**

Export jobbers deal mostly in commodities; they do not take physical possession of goods but assume responsibility for arranging transportation. Because they work on a job-lot basis, they do not provide a particularly attractive distribution alternative for most producers.

Summarizes information pertaining to the major kinds of domestic middlemen operating in foreign markets. No attempt is made to generalize about rates of commission, markup, or pay because so many factors influence compensation. Services offered or demanded, market structure, volume, and product type are some of the key determinants. The data represent the predominant patterns of operations; however, individual middlemen of a given type may vary in their operations.

### **Foreign-Country Middlemen**

The variety of agent and merchant middlemen in most countries is similar to those in the United States. An international marketer seeking greater control over the distribution process may elect to deal directly with middlemen in the foreign market. They gain the advantage of shorter channels and deal with middlemen in constant contact with the market. As with all middlemen, particularly those working at a distance, effectiveness is directly dependent on the selection of middlemen and on the degree of control the manufacturer can and or will exert.

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### **Manufacturer's Representatives**

Manufacturer's representatives are agent middlemen who take responsibility for a producer's goods in a city, regional market area, entire country, or several adjacent countries. When responsible for an entire country, the middleman is often called a sole agent. As in the United States, the well-chosen, well-motivated, well-controlled manufacturer's representative can provide excellent market coverage for the manufacturer in certain circumstances. The manufacturer's representative is widely used in distribution of industrial goods overseas and is an excellent representative for any type of manufactured consumer goods.

### **Distributors**

A foreign distributor is a merchant middleman. This intermediary often has exclusive sales rights in a specific country and works in close cooperation with the manufacturer. The distributor has a relatively high degree of dependence on the supplier companies, and arrangements are likely to be on a long-run, continuous basis. Working through distributors permits the manufacturer a reasonable degree of control over prices, promotional effort, inventories, servicing, and other distribution functions. If a line is profitable for distributors, they can be depended on to handle it in a manner closely approximating the desires of the manufacturer.

### **Foreign-Country Brokers**

Like the export broker discussed in an earlier section, foreign-country brokers are agents who deal largely in commodities and food products. The foreign brokers are typically part of small brokerage firms operating in one country or in a few contiguous countries. Their strength is in having good

continuing relationships with customers and providing speedy market coverage at a low cost.

### **Managing Agents and Compradors**

A managing agent conducts business within a foreign nation under an exclusive contract arrangement with the parent company. The managing agent in some cases invests in the operation and in most instances operates under a contract with the parent company. Compensation is usually on the basis of cost plus a specified percentage of the profits of the managed company. In some countries, managing agents may be called compradors and there are some differences in duties performed.

### **Dealers**

Generally speaking, anyone who has a continuing relationship with a supplier in buying and selling goods is considered a dealer. More specifically, dealers are middlemen selling industrial goods or durable consumer goods direct to customers; they are the last step in the channel of distribution. Dealers have continuing, close working relationships with their suppliers and exclusive selling rights for their producer's products within a given geographic area. Finally, they derive a large portion of their sales volume from the products of a single supplier firm. Usually a dealer is an independent merchant middleman, but sometimes the supplier company has equity in its dealers.

### **Import Jobbers, Wholesalers, and Retailers**

Import jobbers purchase goods directly from the manufacturer and sell to wholesalers and retailers and to industrial customers. Large and small wholesalers and retailers engage in direct importing for their own outlets and for redistribution to smaller middlemen. The combination retailer-wholesaler is

more important in foreign countries than in the United States. It is not uncommon to find large retailers wholesaling goods to local shops and dealers.

### **Government-Affiliated Middlemen**

Marketers must deal with governments in every country of the world. Products, services, and commodities for the government's own use are always procured through government purchasing offices at federal, regional, and local levels. As governments undertake more and more social services, the level of government purchasing activity escalates. In The Netherlands, the state's purchasing office deals with more than 10,000 suppliers in 20 countries. About one-third of the products purchased by that agency are produced outside The Netherlands; 90 percent of foreign purchases are handled through Dutch representatives. The other 10 percent are purchased directly from producing companies.

### **Factors Affecting Choice of Channels**

The international marketer needs a clear understanding of market characteristics and must have established operating policies before beginning the selection of channel middlemen. The following points should be addressed prior to the selection process.

1. Identify specific target markets within and across countries.
2. Specify marketing goals in terms of volume, market share, and profit margin requirements.
3. Specify financial and personnel commitments to the development of international distribution.
4. Identify control, length of channels, terms of sale, and channel ownership.

### **Cost**

There are two kinds of channel cost: (1) the capital or investment cost of developing the channel and (2) the continuing cost of maintaining it. The latter can be in the form of direct expenditure for the maintenance of the company's selling force or in the form of margins, markup, or commissions of various middlemen handling the goods. Marketing costs (a substantial part of which is channel cost) must be considered as the entire difference between the factory price of the goods and the price the customer ultimately pays for the merchandise. The costs of middlemen include transporting and storing the goods, breaking bulk, providing credit, and local advertising, sales representation, and negotiations.

### **Capital Requirement**

The financial ramifications of a distribution policy are often overlooked. Critical elements are capital requirement and cash-flow patterns associated with using a particular type of middleman. Maximum investment is usually required when a company establishes its own internal channels, that is, its own sales force. Use of distributors or dealers may lessen the capital investment, but manufacturers often have to provide initial inventories on consignment, loans, floor plans, or other arrangements. Coca-Cola initially invested in China with majority partners that met most of the capital requirements. However, Coke soon realized that it could not depend on its local majority partners to distribute its product aggressively in the highly competitive, market-share-driven business of carbonated beverages. To assume more control of distribution it had to assume management control and that meant greater capital investment from Coca-Cola.

One of the highest costs of doing business in China is the capital required to maintain effective distribution.

### **Control**

The more involved a company is with the distribution, the more control it exerts. A company's own sales force affords the most control but often at a cost that is not practical. Each type of channel arrangement provides a different level of control and, as channels grow longer, the ability to control price, volume, promotion, and type of outlets diminishes. If a company cannot sell directly to the end user or final retailer, an important selection criterion of middlemen should be the amount of control the marketer can maintain.

### **Coverage**

Another major goal is full-market coverage to (1) gain the optimum volume of sales obtainable in each market, (2) secure a reasonable market share, and (3) attain satisfactory market penetration. Coverage may be assessed on geographic and/or market segments. Adequate market coverage may require changes in distribution systems from country to country or time to time. Coverage is difficult to develop both in highly developed areas and in sparse markets the former because of heavy competition and the latter because of inadequate channels.

### **Character**

The channel-of-distribution system selected must fit the character of the company and the markets in which it is doing business. Some obvious product requirements, often the first considered, relate to perish ability or bulk of the product, complexity of sale, sales service required, and value of the product.

Channel commanders must be aware that channel patterns change; they cannot assume that once a channel has been developed to fit the character of both company and market, no more need be done. Great Britain, for example, has epitomized distribution through specialty-type middlemen, distributors, wholesalers, and retailers; in fact, all middlemen have traditionally worked within narrow product specialty areas. In recent years, however, there has been a trend toward broader lines, conglomerate merchandising, and mass marketing. The firm that neglects the growth of self-service, scrambled merchandising, or discounting may find it has lost large segments of its market because its channels no longer reflect the character of the market.

### **Continuity**

Channels of distribution often pose longevity problems. Most agent middlemen firms tend to be small institutions. When one individual retires or moves out of a line of business, the company may find it has lost its distribution in that area. Wholesalers and especially retailers are not noted for their continuity in business either. Most middlemen have little loyalty to their vendors. They handle brands in good times when the line is making money, but quickly reject such products within a season or a year if they fail to produce during that period. Distributors and dealers are probably the most loyal middlemen, but even with them, manufacturers must attempt to build brand loyalty downstream in a channel lest middlemen shift allegiance to other companies or other inducements.

### **Locating, Selecting, and Motivating Channel Members**

The actual process of building channels for international distribution is seldom easy, and many companies have been stopped in their efforts to develop

international markets by their inability to construct a satisfactory system of channels.

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### **Locating Middlemen**

The search for prospective middlemen should begin with study of the market and determination of criteria for evaluating middlemen servicing that market. The company's broad policy guidelines should be followed, but expect expediency to override policy at times. The checklist of criteria differs according to the type of middlemen being used and the nature of their relationship with the company. Basically, such lists are built around four subject areas: (1) productivity or volume, (2) financial strength, (3) managerial stability and capability, and (4) the nature and reputation of the business. Emphasis is usually placed on either the actual or potential productivity of the middleman.

Setting policies and making checklists are easy; the real task is implementing them. The major problems are locating information to aid in the selection and choice of specific middlemen, and discovering middlemen available to handle one's merchandise. Firms seeking overseas representation should compile a list of middlemen from such sources as: (1) the U.S. Department of Commerce; (2) commercially published directories; (3) foreign consulates; (4) chamber-of-commerce groups located abroad; (5) other manufacturers producing similar but noncompetitive goods; (6) middlemen associations; (7) business publications; (8) management consultants; (9) carriers particularly airlines; and (10) Internet-based services such as Unibex, a global business center.

### **Selecting Middlemen**

Finding prospective middlemen is less a problem than determining which of them can perform satisfactorily. Low volume or low potential volume

hampers most prospects, many are underfinanced, and some simply cannot be trusted. In many cases, when a manufacturer is not well known abroad, the reputation of the middleman becomes the reputation of the manufacturer, so a poor choice at this point can be devastating.

### **Screening**

The screening and selection process itself should follow this sequence: (1) a letter including product information and distributor requirements in the native language to each prospective middleman; (2) a follow-up to the best respondents for more specific information concerning lines handled, territory covered, size of firm, number of salespeople, and other background information; (3) check of credit and references from other clients and customers of the prospective middleman; and (4) if possible, a personal check of the most promising firms. It has become easier to obtain financial information on prospective middlemen via such Internet companies as Unibex (Exhibit 14—8), which provides access to Deloitte & Touches International and Dun & Bradstreet client information resources.

### **The Agreement**

Once a potential middleman has been found and evaluated, there remains the task of detailing the arrangements with that middleman. So far the company has been in a buying position; now it must shift into a selling and negotiating position to convince the middleman to handle the goods and accept a distribution agreement that is workable for the company. Agreements must spell out specific responsibilities of the manufacturer and the middleman, including an annual sales minimum. The sales minimum serves as a basis for evaluation of the distributor, and failure to meet sales minimums may give the exporter the right of termination.

### **Motivating Middlemen**

Once middlemen are selected, a promotional program must be started to maintain high-level interest in the manufacturer's products. A larger proportion of the advertising budget must be devoted to channel communications than in the United States because there are so many small middlemen to be contacted. Consumer advertising is of no value unless the goods are actually available. Furthermore, few companies operating in international business have the strong brand image in foreign environments that they have in their own country. In most countries, retailers and wholesalers are only minimally brand conscious, and yet, to a large degree, they control the success or failure of products in their countries.

### **Terminating Middlemen**

When middlemen do not perform up to standards or when market situations change, requiring a company to restructure its distribution, it may be necessary to terminate relationships with certain middlemen or certain types of middlemen. In the United States, it is usually a simple action regardless of the type of middlemen; they are simply dismissed. However, in other parts of the world, the middleman typically has some legal protection that makes it difficult to terminate relationships. In Colombia, for example, if you terminate an agent, you are required to pay 10 percent of the agent's average annual compensation, multiplied by the number of years the agent served, as a final settlement. In some countries, an agent cannot be dismissed without arbitration to determine whether the relationship should be ended. Some companies make all middlemen contracts for one year to avoid such problems. However, there have been cases

where termination under these contracts has been successfully contested. Competent legal advice is vital when entering distribution contracts with middlemen. But as many experienced international marketers know, the best rule is to avoid the need to terminate distributors by screening all prospective middlemen carefully. A poorly chosen distributor may not only fail to live up to expectations but may also adversely affixture business and prospects in the country.

### **Controlling Middlemen**

The extreme length of channels typically used in international distribution makes control of middlemen particularly difficult. Some companies solve this problem by establishing their own distribution systems; others issue franchises or exclusive distributorships in an effort to maintain control through the first stages of the channels. Until the various world markets are more highly developed, most international marketers cannot expect to exert a high degree of control over their international distribution operations. Although control is difficult, a company that succeeds in controlling distribution channels is likely to be a successful international marketer. Indeed, the desire for control is a major reason companies initiate their own distribution systems in domestic as well as in international business.

## GLOBAL ADVERTISING

Intense competition for world markets and the increasing sophistication of foreign consumers have led to a need for more sophisticated advertising strategies. Increased costs, problems of coordinating advertising programs in multiple countries, and a desire for a common worldwide company or product image have caused Multinational Companies (MNCs) to seek greater control and efficiency without sacrificing local responsiveness. In the quest for more effective and responsive promotion programs, the policies covering centralized or decentralized authority, use of single or multiple foreign or domestic agencies, appropriation and allocation procedures, copy, media, and research are being examined.

### **Pattern Advertising: Plan Globally, Act Locally**

As discussed in the chapter on product development, a product is more than a physical item; it is a bundle of satisfactions the buyer receives. This package of satisfactions or utilities includes the primary function of the product along with many other benefits imputed by the values and customs of the culture. Different cultures often seek the same value or benefits from the primary function of a product; for example, the ability of an automobile to get from point A to point B, a camera to take a picture, or a wristwatch to tell time. But while agreeing on the benefit of the primary function of a product, other features and psychological attributes of the item can have significant differences.

Consider the different market-perceived needs for a camera. In the United States, excellent pictures with easy, foolproof operation are expected by

most of the market; in Germany and Japan, a camera must take excellent pictures but the camera must also be state-of-the-art in design. In Africa, where penetration of cameras is less than 20 percent of the households, the concept of picture-taking must be sold. In all three markets, excellent pictures are expected (i.e., the primary function of a camera is demanded) but the additional utility or satisfaction derived from a camera differs among cultures. There are many products that produce such different expectations beyond the common benefit sought by all. Thus, many companies follow a strategy of pattern advertising, a global advertising strategy with a standardized basic message allowing some degree of modification to meet local situations.<sup>5</sup> As the popular saying goes, "Think Globally, Act Locally." In this way, some economies of standardization can be realized while specific cultural differences are accommodated.

Levi Strauss and Company has changed from all localized ads to pattern advertising where the broad outlines of the campaign are given but the details are not. Quality and Levi's American roots are featured worldwide. In each country market, different approaches will express these two points.

In Japan, the Blue Diamond brand of almonds was an unknown commodity until Blue Diamond launched its campaign of exotic new almond-based products that catered to local tastes. Such things as almond tofu, almond miso soup, and Clarhond—a nutritional snack concocted from a mixture of dried small sardines and slivered almonds—were featured in magazine ads and in promotional cooking demonstrations. Television ads featured educational messages on how to use almonds in cooking, their nutritional value, the versatility of almonds as a snack, and the California mystique and health benefits

of almonds. As a result, Japan is now the Association's largest importer of almonds.

In Korea, the emphasis was on almonds and the West. Commercials featured swaying palms, beach scenes, and a guitar-playing crooner singing "Blue Diamond" to the tune of "Blue Hawaii." And so it goes in the 94 countries where Blue Diamond sells its almonds. Blue Diamond assumes that no two markets will react the same, that each has its own set of differences—be they "cultural, religious, ethnic, dietary, or otherwise"—and that each will require a different marketing approach, a different strategy. The wisdom of adapting its product advertising for each market is difficult to question since two-thirds of all Blue Diamond's sales are outside the United States.

### **Global Advertising and World Brands**

Global brands generally are the result of a company that elects to be guided by a global marketing strategy. Global brands carry the same name, same design, and same creative strategy everywhere in the world; Coca-Cola, Pepsi-Cola, McDonald's, and Revlon are a few of the global brands. Even when cultural differences make it ineffective to have a standardized advertising program or a standardized product, a company may have a World brand. Nescafe, the world brand for Nestle Company's instant coffee, is used throughout the world even though advertising messages and formulation (dark roast and light roast) vary to suit cultural differences. In Japan and the United Kingdom, advertising reflects each country's preference for tea; in France, Germany, and Brazil, cultural preferences for ground coffee call for a different advertising message and formulation. Even in this situation, however, there is some standardization; all advertisements have one common emotional link:

"Whatever good coffee means to you and however you like to serve it, Nescafe has a coffee for you." The debate between advocates of strict standardized advertising and those who support locally modified promotions will doubtless continue.

### **Pan-European Advertising**

The attraction of a single European market will entice many companies to standardize as much of their promotional effort as possible. As media coverage across Europe expands, it will become more common for markets to be exposed to multiple messages and brands of the same product. To avoid the confusion that results when a market is exposed to multiple brand names and advertising messages, as well as for reasons of efficiency, companies will strive for harmony in brand names, advertising, and promotions across Europe.

### **Global Market Segmentation and Promotional Strategy**

Rather than approach a promotional strategy decision as having to be either standardized or adapted, a company should first identify market segments. A market segment consists of consumers with more similarities in their needs, wants, and buying behavior than differences, and thus more responsive to a uniform promotional theme. Market segments can be defined within country boundaries or across countries. Global market segmentation involves identifying homogeneous market segments across groups of countries. Customers in a global market segment may come from different cultural backgrounds with different value systems and live in different parts of the world, but their

commonalities in life-styles and their needs are fulfilled by similar product benefits. Further, while segments in some countries may be too small to be considered, when aggregated across a group of countries, they make a very lucrative total market.

Procter & Gamble has identified mass market segments across the world and designed brand and advertising concepts that apply to all. The company's shampoo positioning strategy, "Pro-V vitamin formula strengthens the hair and makes it shine," was developed for the Taiwan market, and then successfully launched in several Latin American countries with only minor adaptation for hair type and language. L'Oreal's "It's expensive and I'm worth it" brand position also works well worldwide. Unilever's fabric softener's teddy bear brand concept has worked well across borders, even though the "Snuggle" brand name changes in some countries; it's Kuschelweich in Germany, Coc-colino in Italy, and Mimosin in France.

### **Creative Challenges**

The growing intensity of international competition, coupled with the complexity of multinational marketing, demands that the international advertiser function at the highest creative level. Advertisers from around the world have developed their skills and abilities to the point that advertisements from different countries reveal basic similarities and a growing level of sophistication. To complicate matters further, boundaries are placed on creativity by legal, language, cultural, media, production, and cost limitations.

### **Legal Considerations**

Laws that control comparative advertising vary from country to country in Europe. In Germany, it is illegal to use any comparative terminology; you can be sued by a competitor if you do. Belgium and Luxembourg explicitly ban comparative advertising, whereas it is clearly authorized in the U.K., Ireland, Spain, and Portugal. The directive covering comparative advertising will allow implicit comparisons that do not name competitors, but will ban explicit comparisons between named products. The European Commission has issued several directives to harmonize the laws governing advertising. However, member states are given substantial latitude to cover issues under their jurisdiction. Many fear that if the laws are not harmonized, member states may close their borders to advertising that does not respect their national rules.

### **Language Limitations**

Language is one of the major barriers to effective communication through advertising. The problem involves different languages of different countries, different languages or dialects within one country, and the subtler problems of linguistic nuance and vernacular.

### **Cultural Diversity**

The problems associated with communicating to people in diverse cultures present one of the great creative challenges in advertising. Communication is more difficult because cultural factors largely determine the way various phenomena are perceived. If the perceptual framework is different, perception of the message it differs.

Knowledge of cultural diversity must encompass the total advertising project. General Mills had two problems with one product. When it introduced instant cake mixes in the United States and England, it had the problem of

overcoming the homemaker's guilt feelings. When General Mills introduced instant cake mixes in Japan, the problem changed; cakes were not commonly eaten in Japan. There was no guilt feeling but the homemaker was concerned about failing. She wanted the cake mix as complete as possible. In testing TV commercials promoting the notion that making cake is as easy as making rice, General Mills learned it was offending the Japanese homemaker who believes the preparation of rice requires great skill.

### **Media Limitations**

Media are discussed at length later, so here we maintain only that limitations on creative strategy imposed by media may diminish the role of advertising in the promotional program and may force marketers to emphasize other elements of the promotional mix.

A marketer's creativity is certainly challenged when a television commercial is limited to 10 showings a year with no two exposures closer than 10 days, as is the case in Italy. Creative advertisers in some countries have even developed their own media for overcoming media limitations. In some African countries, advertisers run boats up and down the rivers playing popular music and broadcasting commercials into the bush as they travel.

### **Production and Cost Limitations**

Creativity is especially important when a budget is small or where there are severe production limitations, poor-quality printing, and a lack of high-grade paper. For example, the poor quality of high-circulation glossy magazines and other quality publications has caused Colgate-Palmolive to depart from its customary heavy use of print media in the West for other media in Eastern

Europe. Newsprint is of such low quality in China that a color ad used by Kodak in the West is not an option. Kodak's solution has been to print a single-sheet color insert as a newspaper supplement. The necessity for low-cost re-1 production in small markets poses another problem in many countries. For example, hand-painted billboards must be used instead of printed sheets because the limited number of billboards does not warrant the production of printed sheets. In Egypt, static-filled television and poor-quality billboards have led companies such as Coca-Cola and Nestle to place their advertisements on the sails of feluccas, boats that sail along the Nile. Feluccas, with their triangle sails, have been used to transport goods since the time of the pharaohs and serve as an effective alternative to attract attention to company names and logos.

### **Media Planning and Analysis**

#### **Tactical Considerations**

Although nearly every sizable nation essentially has the same kinds of media, there are a number of specific considerations, problems, and differences encountered from one nation to another. In international advertising, an advertiser must consider the availability, cost, and coverage of the media. Local variations and lack of market data require added attention.

Imagine the ingenuity required of advertisers confronted with these situations:

- In Brazil, TV commercials are sandwiched together in a string of 10 to 50 commercials within one station break.
- National coverage in many countries means using as many as 40 to 50 different media.
- Specialized media reach small segments of the market only. In the Netherlands, there are Catholic, Protestant, socialist, neutral, and other

specialized broadcasting systems.

- In Germany, TV scheduling for an entire year must be arranged by August 30 of the preceding year, with no guarantee that commercials intended for summer viewing will not be run in the middle of winter.
- In Vietnam, advertising in newspapers and magazines is limited to 10 percent of space, and to 5 percent of time, or three minutes an hour, on radio and TV.

### **Availability**

One of the contrasts of international advertising is that some countries have too few advertising media and others have too many. In some countries, certain advertising media are forbidden by government edict to accept some advertising materials. Such restrictions are most prevalent in radio and television broadcasting. In many countries there are too few magazines and newspapers to run all the advertising offered to them. Conversely, some nations segment the market with so many newspapers that the advertiser cannot gain effective coverage at a reasonable cost. Gilberto Sozzani, head of an Italian advertising agency, comments about his country: "One fundamental rule. You cannot buy what you want."

In China the only national TV station, CCTV, has one channel that must be aired by the country's 27 provincial/municipal stations. In 1997 CCTV auctioned off the most popular break between the early evening news and weather; a secured yearlong, daily five-second billboard ad in this break went for \$38.5 million. For this price, advertisers are assured of good coverage—over 70 percent of households have TV sets and the government's goal is 90 percent by 2000. One of the other options for advertisers is with the 2,828 TV

stations that provide only local coverage. For a comparison on how much of the advertising dollar is spent on different media in the top 10 global markets.

### **Cost**

Media prices are susceptible to negotiation in most countries. Agency space discounts are often split with the client to bring down the cost of media. The advertiser may find the cost of reaching a prospect through advertising depends on the agent's bargaining ability. The per-contract cost varies widely from country to country. One study showed the cost of reaching one thousand readers in 11 different European countries ranged from \$1.58 in Belgium to \$5.91 in Italy; in women's service magazines, the page cost per thousand circulation ranged from \$2.51 in Denmark to \$10.87 in Germany. Shortages of advertising time on commercial television in some markets have caused substantial price increases. In Britain, prices escalate on a bidding system. They do not have fixed rate cards; instead there is a preempt system in which advertisers willing to pay a higher rate can bump already scheduled spots.

### **Coverage**

Closely akin to the cost dilemma is the problem of coverage. Two points are particularly important: one relates to the difficulty of reaching certain sectors of the population with advertising and the other to the lack of information on coverage. In many world marketplaces, a wide variety of media must be used to reach the majority of the markets. In some countries, large numbers of separate media have divided markets into uneconomical advertising segments. With some exceptions, a majority of the population of less-developed countries cannot be reached readily through the medium of advertising. In India, Video Vans are used to reach India's rural population with 30-minute infomercials extolling the virtues of a product. Consumer goods companies

deploy vans year-round except in the monsoon season. Colgate hires 85 vans at a time and sends them to villages that research has shown to be promising.

### **Lack of Market Data**

Verification of circulation or coverage figures is a difficult task. Even though many countries have organizations similar to the Audit Bureau of Circulation, accurate circulation and audience data are not assured. For example, the president of the Mexican National Advertisers Association charged that newspaper circulation figures are grossly exaggerated. He suggested that as a rule agencies divide these figures in two and take the result with a grain of salt. The situation in China is no better; surveys of habits and market penetration are available only for the cities of Beijing, Shanghai, and Guangzhou. Radio and television audiences are always difficult to measure, but at least in most countries, geographic coverage is known. Research data are becoming more reliable as advertisers and agencies demand better quality data.

### **Specific Media Information**

An attempt to evaluate specific characteristics of each medium is beyond the scope of this discussion. Furthermore, such information would quickly become outdated because of the rapid changes in the international advertising media field. It may be interesting, however, to examine some of the particularly unique international characteristics of various advertising media. In most instances, the major implications of each variation may be discerned from the data presented.

### **Newspapers**

The newspaper industry is suffering in some countries from lack of competition and choking because of it in others. Most U.S. cities have just one or two major daily newspapers, but in many countries, there are so many newspapers an advertiser has trouble achieving even partial market coverage. Uruguay, population three million, has 21 daily newspapers with a combined circulation of 553,000. Turkey has 380 newspapers and an advertiser must consider the political position of each newspaper so the product's reputation is not harmed through affiliations with unpopular positions. Japan has only five national daily newspapers, but the complications of producing a Japanese-language newspaper are such that they each contain just 16 to 20 pages. Connections are necessary to buy advertising space; Asahi, Japan's largest newspaper, has been known to turn down over a million dollars a month in advertising revenue.

### **Magazines**

The use of foreign national consumer magazines by international advertisers has been notably low for many reasons. Few magazines have a large circulation or provide dependable circulation figures. Technical magazines are used rather extensively to promote export goods but, as with newspapers, paper shortages cause placement problems. Media planners are often faced with the largest magazines accepting up to twice as many advertisements as they have space to run them in then they decide what advertisements will go in just before going to press by means of a raffle.

### **Radio and Television**

Possibly because of their inherent entertainment value, radio and television have become major communications media in most nations. Most populous areas have television broadcasting facilities. In some markets, such as

Japan, television has become almost a national obsession and thus finds tremendous audiences for its advertisers. In China, virtually all homes in major cities have a television and most adults view television and listen to radio daily. For number of households covered and rates for TV advertising. Radio has been relegated to a subordinate position in the media race in countries where television facilities are well developed. In many countries, however, radio is a particularly important and vital advertising medium when it is the only one reaching large segments of the population.

Television and radio advertising availability varies between countries. Three patterns are discernible: competitive commercial broadcasting, commercial monopolies, and noncommercial broadcasting. Countries with free competitive commercial radio and television normally encourage competition and have minimal broadcast regulations. Elsewhere, local or national monopolies are granted by the government and individual stations or networks may then accept radio or TV commercials according to rules established by the government. In some countries, commercial monopolies may accept all the advertising they wish; in others, only spot advertising is permissible and programs may not be sponsored. Live commercials are not permitted in some countries; in still others, commercial stations must compete for audiences against the government's noncommercial broadcasting network.

### **Satellite and Cable TV**

Of increasing importance in TV advertising is the growth and development of satellite TV broadcasting. Sky Channel, a United Kingdom-based commercial satellite television station, beams its programs and advertising into most of Europe via cable TV subscribers. The technology that

permits households to receive broadcasts directly from the satellite via a dish the "size of a dinner plate" costing about \$350 is adding greater coverage and the ability to reach all of Europe with a single message. The expansion of TV coverage will challenge the creativity of advertisers and put greater emphasis on global standardized messages. For a comparison of household penetration by satellite, cable, and Internet in the top 10 media markets.

### **Direct Mail**

Direct mail is a viable medium in many countries. It is especially important when other media are not available. As is often the case in international marketing, even such a fundamental medium is subject to some odd and novel quirks. For example, in Chile, direct mail is virtually eliminated as an effective medium because the sender pays only part of the mailing fee; the letter carrier must collect additional postage for every item delivered. Obviously, advertisers cannot afford to alienate customers by forcing them to pay for unsolicited advertisements. Despite some limitations with direct mail, many companies have found it a meaningful way to reach their markets. The Reader's Digest Association has used direct-mail advertising in Mexico to successfully market its magazines.

In Southeast Asian markets, where print media are scarce, direct mail is considered one of the most effective ways to reach those responsible for making industrial goods purchases, even though accurate mailing lists are a problem in Asia as well as in other parts of the world. In fact, some companies build their own databases for direct mail.

### **Other Media**

Restrictions on traditional media or their availability cause advertisers to call on lesser media to solve particular local-country problems. The cinema is an important medium in many countries, as are billboards and other forms of outside advertising. Billboards are especially useful in countries with high illiteracy rates.

In Haiti, sound trucks equipped with powerful loudspeakers provide an effective and widespread advertising medium. Private contractors own the equipment and sell advertising space much as a radio station would. This medium overcomes the problems of illiteracy, lack of radio and television set ownership, and limited print media circulation. In Ukraine, where the postal service is unreliable, businesses have found that the most effective form of direct business-to-business advertising is direct faxing.

In Spain, a new medium includes private cars that are painted with advertisements for products and serve as moving billboards as they travel around. This new system, called Publicoche (derived from the words *publicidad*, meaning advertising, and *coche*, meaning car), has 75 cars in Madrid. Car owners are paid \$230 a month and must submit their profession and "normal" weekly driving patterns. Advertisers pay a basic cost of \$29,000 per car per month, and can select the type and color of car they are interested in and which owners are most suited to the campaign based on their driving patterns.

### **The Internet—A Media Mix Alternative**

Though still evolving, the Internet is emerging as a viable medium for advertising and should be included as one of the media in a company's possible media mix. Its use in business-to-business communications and promotion via catalogs and product descriptions is rapidly gaining in popularity. Since a large

number of businesses have access to the Internet, the Internet can reach a large portion of the business-to-business market.

Another company that is using the Internet as an advertising medium is Levi Strauss & Company. Levi's is using its Web site as an integral part of a global advertising campaign. Customers can surf through North American or European sites, sampling products and brand campaigns. When a new European jeans ad campaign was launched, an accompanying interactive game, and mystery story appeared on the European site. In all there are five different games based on one of five Levi's "brand truths," as established in Levi's mainstream advertising campaign. The company has also launched a specific site for Japan, using kanji, the Japanese language characters.

For consumer products the major limitation of the Internet is coverage. In the United States only a small portion of households have access to a computer, but there are even fewer in other countries. Nevertheless, the small number of Internet households accessible outside the United States generally constitutes a younger, better-educated market segment with higher than average incomes. For many companies, that group is an important market niche. Furthermore, this limitation is only temporary as new technology allows access to the Internet via television and as lower prices for personal computers expand the household base. Net Channel, a new subscription Internet service provider which offers its service via domestic TV sets, will be available initially in the U.K. and the U.S., followed by a rollout across Europe and ultimately into Asia. As an advertising medium it may be the ideal tool for pan-regional areas that cover various languages and cultures. A company's Web site can have as many cultural, linguistic options as it needs. If someone in Thailand lands on the Procter & Gamble site, they can read an ad in Thai for the company's products available in Thailand.

As the Internet grows and countries begin to assert control over what is now virtually a medium without restrictions, limitations will be set. Besides control of undesirable information, issues such as taxes, unfair competition, import duties, and privacy are being addressed all over the world. In Australia, local retailers are calling for changes in laws because of loss of trade to the Internet; under current law Internet purchases do not carry regular import duties. The Internet industry is lobbying for a global understanding on regulation to avoid a crazy quilt of confusing and contradictory rules. As the director of the Asia-Pacific Internet Association commented, "Internationally 1997 has been the year that the Internet has finally been recognized as requiring globally coordinated policy and regulatory understanding and development."

Another limitation that needs to be addressed soon is the competition for Web surfers. The sheer proliferation of the number of Web sites makes it increasingly difficult for a customer to stumble across a particular page. Banners or interceptive sites advertising the site can help but that venue is also becoming crowded. As discussed earlier, serious Internet advertisers or e-marketers will have to be more effective in communicating the existence of their Internet sites via other advertising media. Some companies are coupling their traditional television spots with a Web site; IBM, Swatch Watches, AT&T, and Samsung electronics are among those going for a one-two punch of on-air and online. TV spots are used to raise brand awareness of product regionally, and to promote the company's Web site. Additionally, the company buys ad banners on the Web that will lead enthusiastic consumers to the company's Web that also promotes the product. Some TV networks offer a package deal, a TV spot and ad banners on the network's Web site. For example, the EBN (European Business News) channel offers cross-media

program that includes TV spots and the advertiser's ad banner on the EB Interactive page for \$15,000 a quarter.

### **Sales Promotion**

Sales are marketing activities that stimulate consumer purchases and improve retailer or middlemen effectiveness and cooperation. Cents-off, in-store demonstrations, samples, coupons, gifts, product tie-ins, contests, sweepstakes, sponsorship of special events such as concerts and fairs, and point-of-purchase displays are types of sales promotion devices designed to supplement advertising and personal selling in the promotional mix.

Sales promotions are short-term efforts directed to the consumer and or retailer to achieve such specific objectives as (1) consumer-product trial and or immediate purchase; (2) consumer introduction to the store; (3) gaining retail point-of-purchase displays; (4) encouraging stores to stock the product; and (5) supporting and augmenting advertising and personal sales efforts. An example of sales promotion is the African cigarette manufacturer who, in addition to regular advertising, sponsors musical groups and river explorations and participates in local fairs in attempts to make the public aware of the product. Procter & Gamble's introduction of Ariel detergent in Egypt included the "Ariel Road Show." The puppet show was taken to local markets in villages, where more than half of the Egyptian population still lives. The show drew huge crowds, entertained people, told about Ariel's better performance without the use of additives, and sold the brand through a distribution van at a nominal discount. Besides creating brand awareness for Ariel, the road show helped overcome the reluctance of the rural retailers to handle the premium-priced Ariel.

In markets where the consumer is hard to reach because of media limitations, the percentage of the promotional budget allocated to sales promotions may have to be increased. In some less-developed countries, sales promotions constitute the major portion of the promotional effort in rural and less-accessible parts of the market. In parts of Latin America, a portion of the advertising-sales budget for both Pepsi-Cola and Coca-Cola is spent on carnival trucks, which make frequent trips to outlying villages to promote their products. When a carnival truck makes a stop in a village, it may show a movie or provide some other kind of entertainment; the price of admission is an unopened bottle of the product purchased from the local retailer. The unopened bottle is to be exchanged for a cold bottle plus a coupon for another bottle. This promotional effort tends to stimulate sales and encourages local retailers, who are given prior notice of the carnival truck's arrival, to stock the product. Nearly 100 percent coverage of retailers in the village is achieved with this type of promotion. In other situations, village stores may be given free samples, have the outsides of their stores painted, or receive clock signs in attempts to promote sales.

An especially effective promotional tool when the product concept is new or has a very small market share is product sampling. Nestle Baby Foods faced such a problem in France in its attempt to gain share from Gerber, the leader. The company combined sampling with a novel sales promotion program to gain brand recognition and to build goodwill. Since most Frenchmen take off for a long vacation in the summertime, piling the whole family into the car and staying at well-maintained campgrounds, Nestle provides rest-stop structures along the highway where parents can feed and change their babies. Sparkling clean Le Relais Bebes are located along main travel routes. Sixty-four hostesses at these rest stops welcome 120,000 baby visits and dispense 600,000 samples

of baby food each year. There are free disposable diapers, a changing table, and high chairs for the babies to sit in while dining.

As is true in advertising, the success of a promotion may depend on local adaptation. Major constraints are imposed by local laws, which may not permit premiums or free gifts to be given. Some countries' laws control the amount of discount given at retail, others require permits for all sales promotions, and in at least one country, no competitor is permitted to spend more on a sales promotion than any other company selling the product. Effective sales promotions can enhance the advertising and personal selling efforts and, in some instances, may be effective substitutes when environmental constraints prevent full utilization of advertising.

#### **Global Advertising and the Communications Process**

Promotional activities (advertising, personal selling, sales promotion, and public relations) are basically a communications process. All the attendant problems of developing an effective promotional strategy in domestic marketing plus all the cultural problems just discussed must be overcome for a successful international promotional program. A major consideration for foreign marketers is to determine that all constraints (cultural diversity, media limitations, legal problems, and so forth) are controlled so the right message is communicated to and received by prospective consumers. International communications may fail for a variety of reasons: a message may not get through because of media inadequacy; the message may be received by the intended audience but not be understood because of different cultural interpretations; or the message may reach the intended audience and be understood but have no effect because the marketer did not correctly assess the needs and wants of the target market.

The effectiveness of promotional strategy can be jeopardized by so many factors that a marketer must be certain no controllable influences are overlooked. Those international executives who understand the communications process are better equipped to manage the diversity they face in developing an international promotional program.

In the international communications process, each of the seven identifiable segments can ultimately affect the accuracy of the process. The process consists of (1) an information source—an international marketing executive with a product message to communicate; (2) encoding the message from the source converted into effective symbolism for transmission to a receiver; (3) a message channel the sales force and/or advertising media that conveys the encoded message to the intended receiver; (4) decoding the interpretation by the receiver of the symbolism transmitted from the information source; (5) receiver consumer action by those who receive the message and are the target for the thought transmitted; (6) feedback information about the effectiveness of the message which flows from the receiver (the intended target) back to the information source for evaluation of the effectiveness of the process; and, to complete the process, (7) noise uncontrollable and unpredictable influences such as competitive activities and confusion detracting from the process and affecting any or all of the other six steps.

Unfortunately, the process is not as simple as just sending a message via a medium to a receiver and being certain that the intended message sent is the same one perceived by the receiver. The communications-process steps are encased in Cultural Context A and Cultural Context B to illustrate the influences complicating the process when the message is encoded in one culture and decoded in another. If not properly considered, the different cultural

contexts can increase the probability of misunderstandings. As one researcher notes, "Effective communication demands that there exist a psychological overlap between the sender and the receiver"; otherwise a message falling outside the receiver's perceptual field may transmit an unintended meaning. It is in this area that even the most experienced companies make blunders.

Most promotional misfires or mistakes in international marketing are attributable to one or several of these steps not properly reflecting cultural influences and/or a general lack of knowledge about the target market. A review of some of the points discussed in this chapter serves to illustrate this. The information source is a marketer with a product to sell to a specific target market. The product message to be conveyed should reflect the needs and wants of the target market; however, the marketer's perception of market needs and actual market needs do not always coincide. This is especially true when the marketer relies more on the self-reference criterion (SRC) than on effective research. It can never be assumed that "if it sells well in one country, it will sell in another." For instance, bicycles designed and sold in the United States to consumers fulfilling recreational-exercise needs are not sold as effectively for the same reasons in a market where the primary use of the bicycle is transportation.<sup>53</sup> Cavity-reducing fluoride toothpaste sells well in the United States, where healthy teeth are perceived as important, but it has limited appeal in markets such as Great Britain and the French areas of Canada, where the reason for buying toothpaste is breath control. From the onset of the communications process, if basic needs are incorrectly defined, communications fail because an incorrect or meaningless message is received even though the remaining steps in the process are executed properly.

The encoding step causes problems even with a proper message. At this step such factors as color, values, beliefs, and tastes can cause the international

marketer to symbolize the message incorrectly. For example, the marketer wants the product to convey coolness so the color green is used; however, people in the tropics might decode green as dangerous or associate it with disease. Another example of the encoding process misfiring was a perfume presented against a backdrop of rain which, for Europeans, symbolized a clean, cool, refreshing image, but to Africans was a symbol of fertility. The ad prompted many viewers to ask if the perfume was effective against infertility.

DeBeers, the South African diamond company, found that its stylish ads depicting shadow figures conveying engagement, wedding, and anniversary gifts of diamonds failed among Chinese consumers, some of whom associate shadows with ghosts and death. A totally different ad was developed for the Chinese market. In some Muslim countries the ads had to be altered so that the shadows show silhouettes of women wearing veils, rather than the barefaced women whose shadows are shown in Western markets.

Problems of literacy, media availability, and types of media create problems in the communications process at the encoding step. Message channels must be carefully selected if an encoded message is to reach the consumer. Errors such as using television as a medium when only a small percentage of an intended market is exposed to TV, or using print media for a channel of communications when the majority of the intended users cannot read or do not read the language in the medium, are examples of ineffective media channel selection in the communications process.

Decoding problems are generally created by improper encoding, which caused such errors as Pepsi's "Come Alive" slogan being decoded as "Come out of the grave." Chevrolet's brand name for the Nova model (which means star)

was decoded into Spanish as No Va!, meaning "it doesn't go." In another misstep, a translation that was supposed to be decoded as "hydraulic ram" was instead decoded as "wet sheep." In a Nigerian ad, a platinum blonde sitting next to the driver of a Renault was intended to enhance the image of the automobile but she was perceived as not respectable and so created a feeling of shame. An ad used for Eveready Energizer batteries with the Energizer bunny was seen by Hungarian consumers as touting a bunny toy, not a battery.

Decoding errors may also occur accidentally. Such was the case with Colgate-Palmolive's selection of the brand name Cue for toothpaste. The brand name was not intended to have any symbolism; nevertheless, it was decoded by the French into a pornographic word. In some cases, the intended symbolism has no meaning to the decoder. In an ad transferred from the United States, the irony of a tough-guy actor Tom Selleck standing atop a mountain with a steaming mug of Lipton tea was lost on Eastern Europeans.

Errors at the receiver end of the process generally result from a combination of factors: an improper message resulting from incorrect knowledge of use patterns, poor encoding producing a meaningless message, poor media selection that does not get the message to the receiver, or inaccurate decoding by the receiver so that the message is garbled or incorrect.

Finally, the feedback step of the communications process is important as a check on the effectiveness of the other steps. Companies that do not measure their communications efforts are apt to allow errors of source, encoding, media selection, decoding, or receiver to continue longer than necessary. In fact, a proper feedback system allows a company to correct errors before substantial damage occurs.

In addition to the problems inherent in the steps outlined, the effectiveness of the international communications process can be impaired by noise. Noise comprises all other external influences such as competitive advertising, other sales personnel, and confusion at the receiving end that can detract from the ultimate effectiveness of the communications. Noise is a disruptive force interfering with the process at any step and is frequently beyond the control of the sender or the receiver. The overlapping cultural contexts, noise can emanate from activity in either culture or be caused by the influences of the overlapping of the cultural contexts. The significance is that one or all steps in the process, cultural factors, or the marketer's SRC, can affect the ultimate success of the communication. For example, the message, encoding, media, and the intended receiver can be designed perfectly but the inability of the receiver to decode may render the final message inoperative. In designing an international promotional strategy, the international marketer can effectively use this model as a guide to help ensure all potential constraints and problems are considered so that the final communication received and the action taken correspond with the intent of the source.

### **The Advertising Agency**

Just as manufacturing firms have become international, U.S., Japanese, and European advertising agencies are expanding internationally to provide sophisticated agency assistance worldwide. Local agencies also have expanded as the demand for advertising services by MNCs has developed. Thus, the international marketer has a variety of alternatives available. In most commercially significant countries, an advertiser has the opportunity to employ (1) a local domestic agency, (2) its company-owned agency, or (3) one of the

multinational advertising agencies with local branches. There are strengths and weaknesses with each.

A local domestic agency may provide a company with the best cultural interpretation in situations where local modification is sought, but the level of sophistication can be weak. However, the local agency may have the best feel for the market, especially if the multinational agency has little experience in the market. Eastern Europe has been a problem for the multinational agency that is not completely attuned to the market. In Hungary, a U.S. baby-care company advertisement of bath soap showing a woman holding her baby hardly seemed risqué. But where Westerners saw a young mother, scandalized Hungarians saw an unwed mother. The model was wearing a ring on her left hand; Hungarians wear wedding bands on the right hand. It was obvious to viewers that this woman wearing a ring on her left hand was telling everybody in Hungary she wasn't married. This is a mistake a local agency would not have made.

The best compromise is the multinational agency with local branches because it has the sophistication of a major agency with local representation. Further, the multinational agency with local branches is better able to provide a coordinated worldwide advertising campaign. This has become especially important for firms doing business in Europe. With the interest in global or standardized advertising, many agencies have expanded to provide worldwide representation. Many companies with a global orientation employ one, or perhaps two, agencies to represent them worldwide.

Compensation arrangements for advertising agencies throughout the world are based on the U.S. system of 15 percent commissions. However, agency commission patterns throughout the world are not as consistent as they are in the United States; in some countries, agency commissions vary from

medium to medium. Companies are moving from the commission system to a reward by results system, which details remuneration terms at the outset. If sales rise, the agency should be rewarded accordingly. This method of sharing in the gains or losses of profits generated by the advertising is gaining in popularity and it may become the standard. Services provided by advertising agencies also vary greatly but few foreign agencies offer the full services found in U.S. agencies.

Even a sophisticated business function such as advertising may find it is involved in unique practices. In some parts of the world, advertisers often pay for the promotion with the product advertised rather than with cash. Kickbacks on agency commissions are prevalent in some parts of the world and account in part for the low profitability of international advertising agencies. In Mexico, India, and Greece, the advertiser returns half the media commissions to the agencies. In many of the developing countries, long-term credit is used to attract clients.

The global firm with branches and/or joint ventures with local firms dominate advertising globally. Over the last two decades most of the major ad agencies in the United States, the U.K., and Japan have expanded globally and can easily represent a global company almost anywhere in the world. The top agency in the world in 1995 and 1996 was a Japanese firm, Dentsu, Inc., followed by the U.S. firm McCann-Erickson Worldwide. If you visit the Web site of some of these agencies you will see how extensive their range is. These companies represent the consolidation of advertising agencies that has been going on over the last decade or so.

### **International Control of Advertising**

Consumer criticisms of advertising are not a phenomenon of the U.S. market. Consumer concern with the standards and believability of advertising may have spread around the world more swiftly than have many marketing techniques. A study of a representative sample of European consumers indicated that only half of them believed advertisements gave consumers any useful information, 6 out of 10 believed that advertising meant higher prices (if a product is heavily advertised, it often sells for more than brands that are seldom or never advertised); nearly 8 out of 10 believed advertising often made them buy things they did not really need, and that ads often were deceptive about product quality. In Hong Kong, Colombia, and Brazil advertising fared much better than in Europe. The non-Europeans praised advertising as a way to obtain valuable information about products; most Brazilians consider ads entertaining and enjoyable.

European Community officials are establishing directives to provide controls on advertising as cable and satellite broadcasting expands. Deception in advertising is a thorny issue since most member countries have different interpretations of what constitutes a misleading advertisement. Demands for regulation of advertising aimed at young consumers is a trend appearing in both industrialized and developing countries.

Decency and the blatant use of sex in advertisements also are receiving public attention. One of the problems in controlling decency and sex in ads is the cultural variations around the world. An ad perfectly acceptable to a Westerner may be very offensive to someone from the Mideast, or, for that matter, another Westerner. Standards for appropriate behavior as depicted in advertisements vary from culture to culture. Regardless of these variations, there is growing concern about decency, sex, and ads that demean women and

men. International advertising associations are striving to forestall laws by imposing self-regulation, but it may be too late; some countries are passing laws that will define acceptable standards.

The difficulty that business has with self-regulation and restrictive laws is that sex can be powerful in some types of advertisements. European advertisements for Haagen-Dazs, a premium U.S. ice-cream marketer, and LapPower, a Swedish laptop computer company, received criticism for their ads as being too sexy. Haagen-Dazs' ad shows a couple, in various stages of undress, in an embrace feeding ice cream to one another. Some British editorial writers and radio commentators were outraged. One commented that "the ad was the most blatant and inappropriate use of sex as a sales aid." The ad for LapPower personal computers that the Stockholm Business Council on Ethics condemned featured the co-owner of the company with an "inviting smile and provocative demeanor displayed." (She was bending over a LapPower computer in a low-cut dress.)

The advertising industry is sufficiently concerned with the negative attitudes and skepticism of consumers and governments and with the poor practices of some advertisers that the International Advertising Association and other national and international industry groups have developed a variety of self-regulating codes.<sup>61</sup> Sponsors of these codes feel that unless the advertisers themselves come up with an effective framework for control, governments will intervene. This threat of government intervention has spurred interest groups in Europe to develop codes to ensure that the majority of ads conform to standards set for "honesty, truth, and decency." In those countries where the credibility of advertising is questioned and in those where the consumerism movement exists,

the creativity of the advertiser is challenged. The most egregious control, however, may be in Myanmar (formerly Burma), where each medium has its own censorship board that passes judgement on any advertising even before it is submitted for approval by the Ministry of Information. There is even a censorship board for calendars. Content restrictions are centered on any references to the government or military, other political matters, religious themes, or images deemed degrading to traditional culture.<sup>63</sup> In many countries, there is a feeling that advertising, and especially TV advertising, is too powerful and persuades consumers to buy what they do not need, an issue that has been debated in the United States for many years. South Korea, for example, has threatened to ban advertising of bottled water because the commercials may arouse public mistrust of tap water.

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### **Global Strategies**

Global strategies do not mean huge companies operating in a single world market. They are much more complex. Global competitive strategies are a bit like supernatural creatures: they can be imagined by each individual to suit his or her own reality while evoking a common concern. The best illustrations are the slogans companies use to describe themselves. These range from "Think Local, Act Global" all the way to its opposite "Think Global Act Local, with everything in between,"

### **Defining Global Strategies**

Some 15 years have gone by since the term "global strategy" entered our vocabulary, enough time to bring some clarity to its definition. We now know what it is and what it is not.

Consider first what it is not. Global strategies are not standard product-market strategies that assume the world to be a single, homogeneous, border-free marketplace. The Uruguay Round of trade and investment liberalization notwithstanding, the world is still a collection of different independent economies, each with its own market characteristics. Each, moreover, has its own societal aspirations that occasionally find expression in protectionist policies of one form or another.

Global strategies are also not about global presence or about large companies. A company can very well operate in all countries of the world; but if what it does in one country has no meaning for what it does in another country, it is no different from the domestic companies it competes with in each location.

To qualify as pursuing a global strategy, a company needs to be able to demonstrate two things: that it can contest any market it chooses to compete in,

and that it can bring its entire worldwide resources to bear on any competitive situation it finds itself in, regardless of where that might be.

### **Selective Contestability**

Just as companies possessing a certain set of technologies and business competencies choose particular market segments to concentrate on, a global company can be selective about the countries in which it operates.

Many small, high-technology companies and luxury good manufacturers do just that. They compete where there is adequate demand to justify the investments needed to access the market; they focus their investments to achieve critical mass only in those markets they are interested in.

The important thing is that they can and are prepared to contest any and all markets should circumstances warrant. They constantly scour the world for market openings, they process information on a global basis, and they constitute a "potential" threat even in places they have not yet entered.

Markets where such contestability exists, as a corollary, start to behave almost as if the company had already entered—provided, of course, the threat of entry is a credible one. This explains why telecom markets the world over are so fiercely competitive from the day they are no longer government or private monopolies. The handful of international players in the equipment business not only are waiting in the wings but have products that conform to international standards and resources they can deploy for market access as soon as opportunity arises.

### **Global Resources for Each Main Street**

The corner shop that carries products by IBM, Philips, Coca-Cola, or Du Pont knows from experience that there is something special about these products compared with those supplied by a small local company. In

comparison, products from companies such as Nestle, Unilever, or even Procter & Gamble did not seem so special—in the past at least. Their names, formulations, and the way they were produced and marketed were not too different from domestic ones.

Just being present in several countries, in other words, does not constitute a global strategy. Globalism is an earned notion rather than being entitlement created by the fact of operating in several countries.

A basic characteristic of a global company is its ability to bring its entire worldwide capabilities to bear on any transaction anywhere regardless of the products it makes. This underlies the importance of organizational integration in global strategies. Transporting capabilities across borders on an as-needed basis requires all local units to be connected and permeable, not isolated from one another.

This is also what allows global strategies to be "within-border" strategies while, at the same time, being "cross-border" ones. They are manifest on each Main Street, with local companies sensing they are dealing with a worldwide organization even while the latter employs a local competitive formula.

### **Main Attributes of Global Strategy**

This dual notion of market contestability and bringing global resources to bear on competition wherever a company is present is really what global strategies are about. Industries where such strategies are prevalent assume a character of their own in which strategies that are geared to one country alone cannot be adopted. What companies do in one country has an inevitable consequence for what they do in others.

There is, of course, nothing absolute about global strategies. Being near-cousins of multidomestic strategies, the best way to judge them is in terms of "degrees of globalness." At the risk of oversimplification, the more a company

scores in each of the following five attributes, the more it can be considered a global competitor based on the definition just given. These include possessing a standard product (or core) that is marketed uniformly across the world; sourcing all assets, not just production, on an optimal basis; and achieving market access in line with the break-even volume of the needed infrastructure.

- Standard products and marketing mix. While the advantages of having a standard product and marketing mix are obvious, this attribute involves several trade-offs in practice.

Economies of scale in design, production, and promotion need to be compared to the greater market acceptance that local adaptation often provides.

If a general conclusion can be drawn, it would be the need at least to aim for a standard "core" in the product and limiting marketing adaptations to those absolutely necessary. The more integrated countries become economically, the less latitude there is anyway for things such as price discrimination and channel selection. The same applies to situations where buyers themselves are global and expect similar products and terms on a worldwide basis.

- Sourcing assets, not just products. Sourcing products and components internationally based on comparative advantage and availability has long been a feature of international business. What is new is the possibility to source assets or capabilities related to any part of the company's value chain. Whether it is capital from Switzerland or national credit agencies, software skills from Silicon Valley or Bangalore, or electronic components from Taiwan, global companies now have wider latitude in accessing resources from wherever they are available or cost-competitive.

The implication of this is that global strategies are as much about asset deployment for market access purposes as they are about asset accumulation abroad. The latter include local capital, technical skills, managerial talent, and new product ideas, as well as the host competencies that local partners and

institutions can provide. Also, whereas previously assets accumulated locally were mainly to support a local business, it is increasingly possible—and desirable—to separate those needed for local market access from those intended to support the company's business elsewhere.

It is here that we associate partnerships and alliances with global strategy. They can supplement what a company already possesses by way of assets or complement what is missing, thereby speeding up the creation of the needed infrastructure as well as reducing costs and risks.

- Market access in line with break-even. For a company to be a credible global competitor it does not need to be among the biggest in its industry. But it has to be big enough to generate the volume of sales the required infrastructure demands and to amortize up-front investments in R&D and promotion.

Today, it is the latter investments that count most. In the pharmaceutical industry, for example, it now costs around US\$400 million to come up with a successful new drug. This puts a natural floor on the amount of sales to be generated over the life of the drug. The greater the presence of a company in all of the large markets, and the greater its ability to launch the drug simultaneously in them, the higher the likelihood of profiting from the investment made.

The same argument applies to other investments in intangibles such as brands. If we associate global competitiveness with size, it is chiefly on account of these types of investments. Unlike investments in plants and physical infrastructure, which can result in diminishing returns to scale, intangibles almost always translate into "big is better."

- Contesting assets. Another distinguishing feature of a global company is its ability to neutralize the assets and competencies of its competitors. If a competitor switches its supply from a high-cost to a low-cost factory it too can do so; if a competitor gains access to a critical technology it

can do the same. Similarly, if a competitor is using one market to generate excess cash flow in order to "invest" in another, it is able to neutralize this advantage by going to the relatively more profitable market itself.

Purely domestic companies and even those that are run on a multidomestic basis, lack such arbitrage possibilities. Just as in sourcing, to exploit these requires a global view of the business and the capacity to manage it in an integrated fashion.

- All functions have a global orientation. As much of the foregoing suggests, global competition today is a lot more than simple cross-border competition at the product or service level. It is equally about building and managing a multinational infrastructure. Frequently, the latter means internationalizing all of the competencies and functions of a company: its R&D, procurement, production, logistics, and marketing, as well as human resources and finance.

These functions are all geared to providing customers with superior products and services on a worldwide basis. The more they have a global orientation of their own, the greater their contribution to the overall effort. Hence, even if their focus may be primarily national in scope, supporting a local business with no trade, for example, any contribution they can make to other units of the company helps.

These five attributes, taken together, operationalize a global strategy. The degrees of globalness in a strategy are the extent to which each is fulfilled in practice. The fact of not having a standard global product, for example, diminishes the scope of a global strategy but does not entirely destroy it, provided the company scores high on the other attributes. If anything, stressing one attribute to the exclusion of others can even be counterproductive and unfeasible. A good balance between all of them is needed.

### **Local Adaptation**

Another important point to make about these attributes is that they do not assume a single, open global marketplace. Trade and investment liberalization coupled with improvements in transportation and communications are what have made global strategies possible. Trade protection, labor policies, investment incentives, and a host of regulations continue to force a country-by-country adaptation of strategies.

It is also these realities, along with the sociocultural differences between countries that have caused many companies to stress the "local" dimension in their business. And rightly so, If all companies confront the same set of market conditions, advantage goes to those that adapt their strategies best.

The best way to reconcile these local differences with the attributes required of a global strategy is to see them as constraints to global optimization. Localness, in other words, is another variable to incorporate in decision making. Considering it as the basis for the strategy itself, however, is to deny all of the advantages a global company possesses. This is perhaps the biggest conundrum companies face today.

While adapting strategies to local conditions offers greater opportunities for revenue generation, it has two main impacts: it causes overinvestment in the infrastructure needed to serve markets, and brings about a lack of consistency in whatever strategy is being pursued.

Neither is intrinsically bad. They can even contribute positively to the end result if approached correctly. All that is needed is to factor them in as variables to be considered, without losing sight of the overall objective of competing effectively both within and across borders.

Consider the issue of overinvestment, especially in capital-intensive businesses such as semiconductors. Companies such as Texas Instruments,

NEC, and Mitsubishi Electric have consciously located abroad. This not only permits them to benefit from generous investment incentives provided by local governments that want such facilities, but also means they can mobilize local companies as co-investors to share the capital burden and help with market access.

More contentious is the issue of strategic focus. Should local subsidiaries be allowed to modify products and diversify into businesses that make sense for them only? Or should they be consistent with what the parent company focuses on? The answer to this depends on several things: a company's definition of its business scope and growth vectors; the subsidiary's domain within the overall organization; and the locus of its strategy-making process.

Business scope and growth vectors pertain to a company's attitude to diversification generally. If its products and technologies provide adequate growth opportunities on a worldwide basis, it is probably better off restricting each subsidiary to just those. If, on the other hand, growth is primarily driven through exploring and creating new market opportunities, then local initiatives are usually welcome.

Logitech SA, a world leader in pointing devices for the personal computer industry, for example, permitted and even encouraged its Taiwanese company to develop special software products for the Chinese market because that would be an additional product to fuel its growth, reduce its dependence on the mouse and, incidentally, facilitate access to a new market. A company that comes up with a new cancer treatment, on the other hand, is likely to want to invest all its resources in commercializing that worldwide as quickly as possible.

The more a company's infrastructure and skills become dispersed and the more global responsibilities individual subsidiaries take on, the greater the need to see the initiation of strategies as a global process. What the parent knows and

sees may not be the same as subsidiary management. Giving subsidiaries too narrow a mission based on a centralized notion of between-country competition not only constrains their potential for accumulating local resources but diminishes their potential for competing within their country.

### **Organizational Implications**

How companies ought to structure and manage their international operations has been debated as long as the debate on strategy itself. Because organizations need to reflect a wide range of company-specific characteristics—such as size, diversity, age, culture, technology—in addition to their global posture, it has proven hard to be normative. There are, however, certain key design considerations related to global posture that have dominated thinking and practice in recent years.

The most important consideration has to do with the greater need for organizational integration that global strategies require.

Hence, when companies first tried to adapt their structures in the 1970s and early 1980s, most of them created elaborate matrix organizations giving equal status to products, geography, and functions. While such organizations worked well for some companies, ABB being the leading example, they did not for others. ABB succeeded because of the nature of its business, its superior information system (called Abacus), its investment in developing a number of globally minded managers, and a small but highly effective top management team. What ABB was able to do was to balance finely the need for local autonomy in decision making with the strategic and organizational integration that managing the business on a global basis demanded.

Others that were not able to achieve this balance opted for tilting their matrix in favor of one or the other dimension. Most often, the dominant dimension became product groups or strategic business units, the assumption

being that integrating each product's business system on a worldwide basis was the best way to optimize strategy and achieve coherence among different local units.

Where these "product headquarters" were located mattered less and many companies consciously spread them around as a better way to integrate country organizations, give particular local managers a broader domain to look after, and exploit country-specific assets or competencies. Such dispersal had the attendant benefit of also reducing the role (and size) of corporate headquarters.

This fine-tuning of structures continues today. To the extent one can discern a trend for the 1990s it would be one consisting of three things: reverting to a single locus of direction and control, giving greater emphasis to functional strategies instead of business-by-business ones, and creating simple line organizations based on a more decentralized "network" of local companies.

The move to a single locus is partly on account of the difficulty companies have experienced in managing dispersed product headquarters.

The complex interactions between units they gave rise to, the lack of global reach on the part of some country organizations, and the potential for confusion between corporate roles and business unit functions were apparently not compensated by whatever advantage they offered. But it is equally on account of the recognition of the importance of a coherent set of values, goals, and identity, as well the need to avoid duplication of functions across the world.

Having functions as the primary dimension to coordinate global strategies also reflects the dual nature of the latter, combining asset deployment for market-access reasons and asset accumulation for sourcing purposes. Another virtue of a functional orientation is that it is usually at this level that global alliances and asset accumulation takes place—the R&D function

cooperating with other companies' R&D departments, procurement with suppliers, finance with local finance companies, and so on.

While marketing can and should be managed nationally or regionally, R&D, finance, and manufacturing lend themselves better to global coordination, Texas Instruments Inc., for example, used to manage its business, including manufacturing, on a regional basis. Four years ago, it introduced the notion of the "virtual fab," linking all its 17 manufacturing sites around the world into a single organization.

In addition to standardizing equipment and procedures across plants, this allows the company to transfer expertise across units efficiently, allocate production optimally, and interact with development on a global basis. Whereas previously the company had country-by-country sales forces, it now has market-based teams with global responsibility for a product's success. The latter has proved particularly effective in serving the needs of global customers who expect similar conditions worldwide.

Whether to have a single set of global functions or to have them specialized by business unit depends on how diverse the latter are. The lesson companies have learned, however, is to avoid overly complex matrix structures and to allow local units sufficient autonomy at the business level.

The last point refers to the way individual units in a global company need to be treated. Based on the arguments made earlier, what one is seeing is an upgrading of their role, both as a locus for independent entrepreneurial effort and as contributors to the business worldwide.

To perform this expanded role coherently they need greater empowerment coupled with all of the things that a network organization possesses: a commonly shared knowledge base, common values and goals, a common understanding of priorities and pre-commitments others have made, and a common set of measures to judge performance.

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