# Sociocultural Forces

Speaking about cultural differences among Europeans . . . it is no good focusing on similarities and common interests and hoping things will work out. We have to recognize the differences and work with them."

—Dr. Allan Hjorth, Copenhagen Business School, trainer in cross-cultural behavior

## Six Quick Rules of Thumb for Doing Business across Cultures

Knowing your customer is just as important anywhere in the world as it is at home, whether you are aiming to sell computers in Abidjan or soft drinks in Kuala Lumpur. Each culture has its logic, and within that logic are real, sensible reasons for the way they do things. The businessperson who can figure out the basic pattern of the culture will be increasingly effective interacting with foreign clients and colleagues. The following six rules of thumb are helpful:

1. *Be prepared.* Whether traveling abroad or selling from home, approach a foreign market having done your homework. A mentor is most desirable, complemented by lots of reading on social and business etiquette, history and folklore, current affairs (including relations between your two countries), the culture's values, geography, sources of pride (artists, musicians, sports), religion, political structure, and practical matters such as currency and hours of business. Read local newspapers. The Internet can be a helpful source of information, and a good site for international newspaper links is www.refdesk.com/paper.html/.

2. *Slow down.* Americans are clock-watchers. In many countries, Americans are seen to be in a rush—in other words, unfriendly, arrogant, and untrustworthy. In other countries, the Japanese and Germans are considered to be somewhat time-obsessed.

3. *Establish trust.* Often, American-style crisp business relationships will get you nowhere. Product quality, pricing, and clear contracts compete with the personal *relationship and trust* that are developed carefully and sincerely over time. The marketer must be established as *simpatico,* worthy of the business and dependable in the long run.

4. *Understand the importance of language.* Obviously, translations must be done by a professional who speaks both languages fluently, who has a vocabulary sensitive to nuance and connotation, and who has talent with the idioms and imagery of each culture. Having an interpreter is often critical and may be helpful even when one of the parties speaks the other's language.

5. *Respect the culture.* Manners are important. The traveling representative is a guest in the country and must respect the host's rules. As a Saudi Arabian official states in one of the *Going International* films, "Americans in foreign countries have a tendency to treat the natives as foreigners, and they forget that actually it is *they* who are the foreigners themselves!"

# 4

## learning objectives

After reading this chapter, you should be able to:

**LO4-1**  **Describe** what culture is.

**LO4-2**  **Explain** the significance of national-level culture differences for international business.

**LO4-3**  **Describe** Hall's concept of high and low context.

**LO4-4**  **Describe** Hofstede's framework.

**LO4-5**  **Outline** Trompenaars' dimensions.

**LO4-6**  **Discuss** the sociocultural aspects of culture as a phenomenon.

6. *Understand components of culture.* Any region is a sort of cultural iceberg with two components: surface culture (fads, styles, food, etc.) and deep culture (attitudes, beliefs, values). Less than 15 percent of a region's culture is visible, and strangers to the culture must look below the surface. Consider the British habit of automatically lining up on the sidewalk when waiting for a bus. This surface cultural trait seems to reflect a deep cultural desire to lead neat and controlled lives. Or think of the Japanese victim's response to the March 2011 earthquake and tsunami. Knowledge about other cultures and how they affect the way people do business may show businesspeople working in a culture different from their own that their solutions are not always the appropriate ones.

Understanding that our way is not the only way or the best way is the first step in learning to use cultural differences to gain a strategic advantage. Mishandling or ignoring cultural differences can cause numerous problems, such as lost sales, the departure of competent employees, and low morale that contributes to low productivity. When cultural differences are blended successfully, however, they can result in innovative business practices superior to those that either culture could produce by itself.

Source: Lisa Hoecklin, "Managing Cultural Differences," www.latinsynergy.org/strategicjointventure.htm#CHILE (December 27, 2000; inactive March 16, 2011); "How to Negotiate European Style," *Journal of European Business,* July–August 1993, p. 46; and "Japanese Punctuality," http://joi.ito.com/achives/2005/04/28/japanese_punctuality.html (August 4, 2006; inactive March 16, 2011).

# What Is Culture?

**LO4-1 Describe** what culture is.

There are many useful definitions of culture. Most anthropologists, whose focus is on culture, view it as the *sum total of the beliefs, rules, techniques, institutions, and artifacts that characterize human populations.*[1] In other words, culture consists of the "individual worldviews, social rules, and interpersonal dynamics characterizing a group of people set in a particular time and place."[2] Most anthropologists also agree that:

1. Culture is *learned;* we are not born with a culture.
2. The various aspects of culture are *interrelated.*
3. Culture is *shared, patterned, and mutually constructed through social interaction.*
4. Culture *defines the boundaries* of different groups.[3]

> *"Culture is a little like dropping an Alka-Seltzer into a glass—you don't see it, but somehow it does something."*
>
> *—Hans Magnus Enzensberger*

**sociocultural**
Description of the social world through which we observe the effects of culture

Society is composed of people living within their cultural frameworks, so, to understand a specific group (either an organization or a society), how it works, and what its norms and values are, we need to understand its culture. Yet culture cannot be directly observed; we have to learn about it by observing the social world in which it exists. Because of their close linkage, the concepts *social* and *cultural* are often combined into the term **sociocultural,**[4] and we follow this practice. Culture occurs at all levels, within all groups, so it is evident in organizations, social groups, ethnic groups, and regional groups. Here, we are interested in culture at the national level; you will also want to pay attention to understanding the organization's culture and the various local subcultures.

**ethnocentricity**
Assuming one's own culture to be superior to other cultures

When people work in societies and cultures different from their own, they have to communicate across cultural borders, with cultures they may not understand. A failure to communicate across one cultural border is problematic; such problems are magnified with the multiple cultures of a firm's foreign markets. In addition, most societies consider their culture superior to all others (**ethnocentricity**). Given that, every culture's members tend to think that its ways are best, most attempts by outsiders to introduce their home culture approach in a business environment (the "German way" or the "British way") will be met with stubborn resistance.

How do international businesspeople learn to live with, work in, and meet business goals in other cultures? The first step is to realize that the other cultures are different from their own.

Then they need to learn the characteristics of those cultures so that they may adapt to them. The anthropologist E. T. Hall claims this can be accomplished in only two ways: (1) spend a lifetime in a culture or (2) undergo an extensive training program that covers the main characteristics of a culture, including the language. Such a program is much more than a briefing on a country's customs. It is a study of what culture is and what it does, building an understanding of the various ways in which human behavior has been institutionalized in the country.[5]

Hall suggests that to be successful in their relationships with people in other countries, international businesspeople need to be students of culture. They need factual knowledge about the different culture, which is relatively easy to obtain, but they must also become sensitive to the nuances of cultural differences, a type of knowledge more difficult to obtain. Most newcomers to international business do not have the opportunities Hall recommends. They need to hit the ground running, so to speak, and can rarely afford the time necessary for in-depth study of new cultures. They can, however, take the important first step of realizing that there *are* other cultures. In this chapter, we point out some of the important areas of sociocultural difference that concern businesspeople. We hope that you will remember that there are cultural differences for which you must look, and that you will seek out opportunities to build your knowledge of other cultures.

The concept of culture is broad; it includes everything. Ethnologists break their study of culture into focused areas such as aesthetics, attitudes and beliefs, religion, material culture, language, societal organization, education, legal characteristics, and political structures. We will look at several of these specific areas once we review the significance of culture for business and explore several conceptual frameworks international managers find useful as they build their understanding of other cultures.

As we explore culture, we need to be reminded that the national characteristics of culture we discuss are generalizations. They are broadly true, but they follow a normal distribution curve, and there are always exceptions. Furthermore, characteristics or characterizations may change over time. The Scandinavians were considered by a 10th-century writer to be "the filthiest race God ever created," and a noted 18th-century writer was amazed at the lack of German military spirit and how easygoing Germans were compared to the French.[6]

# Culture Affects All Business Functions

Everything we do is influenced by culture, and most of us realize that about other cultures, but not always about our own. To think about how national cultural differences can affect the functional areas of a business with an international presence is a good place to begin our focus on culture.

## MARKETING

In marketing, the wide variation across cultures in attitudes and values requires that many firms use different marketing mixes in different markets. To develop effective marketing campaigns, the marketer has to understand the foreign market the firm is selling into, and the understanding has to be beyond a surface awareness of differences. The closer the marketer can come to understanding how potential purchasers in the target market give meaning to what occurs in their worlds and how they think their worlds should be, the better. Many businesses have made costly mistakes with product introductions into foreign markets, in physical property design, inappropriate copy for advertisements, and pricing. Through these errors, they learn the importance of understanding their markets, even though acquiring knowledge about a new culture is both time consuming and expensive. Major misunderstandings in marketing due to cultural misunderstandings abound. One international marketing consultant tracks and reports on them in a blog and on a website: www.deborahswallow .com/2009/08/20/cross-cultural-marketing-blunders.

## HUMAN RESOURCES

Sociocultural values play key roles in motivation and evaluation of employees. In some cultures, individual effort is rewarded, while in others, group effort is more highly valued. Other values that come into play in human resources (HR) often connect to attitudes toward status. Is social status something we earn, through achievements (what we do), or is it a result of our

## Disneyland: Successes and Failures, One after Another

Why is it that Disneyland Paris had problems with falling attendance and losses while Tokyo's Disneyland and Disney Sea have steadily increasing attendance and are the most profitable Disney parks? Why is it, too, that, while Tokyo Disneyland is so successful, Hong Kong Disneyland is struggling? The experts who predicted that Tokyo Disneyland attendance would peak in the first year and then taper off were wrong; it has increased steadily. The park owes some of its success to its location in a metropolitan area of 35 million people, but a cultural change that may be the result of its close local partnership is believed to be a major reason for its success. Some say that Walt Disney Productions has written a new chapter in Japanese social history by popularizing the idea that family outings can be fun. Families now account for half of the park's visitors. An executive of Disney states, "Leisure was not always a part of the Japanese lifestyle. Fathers used to see family outings as a duty."

In Paris, the early staggering losses at Disneyland stemmed from the high interest costs and high overheads, many of which were caused by cultural errors. Disneyland Paris is a solo project for Disney; there is no local operating-level partner. To cover the project's $4 billion cost, Disney put up just $170 million for 49 percent of the operation, and public shareholders paid $1 billion for the 51 percent they own. The $2.9 billion balance was borrowed at interest rates of up to 11 percent. Disney management expected to reduce the debt by selling the six big hotels it had built, but the $340-per-night price it charged had kept them about half full. Moreover, the guests weren't staying as long or spending as much as Disney had expected.

Disney executives believed, incorrectly, that they could change the French attitude of not wanting to take their children from school during the school year, as Americans do, and of not wanting to take more short breaks during the year, instead of one long vacation during the month of August. If these changes had happened, and the French used their shorter vacations to visit Disneyland Paris, this would have given Euro Disney steady, high attendance all year rather than for just one month.

One reason the European visitors didn't spend as much per visit as Disney had predicted was the extremely high prices. Almost two years passed before Disney lowered them. Another reason the guests didn't spend more, even though in this case they wanted to, was also due to a cultural problem: the breakfast debacle. Apparently, a decision involving millions of dollars in revenue was based not on research but only on what someone told Disney. One executive said, "We were told that Europeans don't take breakfast, so we downsized the restaurants." However, when the park opened, everyone wanted breakfast and wouldn't settle for just croissants and coffee; they wanted bacon and eggs. Disney tried to serve 2,500 breakfasts in hotel restaurants seating 350 people. The Disney solution for the French public, known worldwide as connoisseurs of good eating: prepackaged breakfasts delivered to hotel rooms. Disney also decided initially not to serve alcohol, as is their policy in the United States. They misjudged the local transport scene, as well, expecting Europeans to take golf cart transportation from their hotels to the park, while the Europeans wanted to walk. So ample sidewalks were built.

family's social position (who we are)? For example, Americans, who expect to be promoted based on their accomplishments, often are surprised to learn of the significant role schooling in the "right" institutions and family background play in this process in Great Britain. Differences in attitudes toward authority, another sociocultural variable, may also lead to personnel problems. Is the expected role of the manager to be the *patron,* an authoritarian figure responsible for their employees' welfare? Or is the manager one among equals? Is the control process of an annual review widely seen as a way to credit the employee's work and help the employee grow or as a way to exact higher labor output from the worker? The answers to these questions, which are important to HR practices, frequently lie in deeply embedded cultural values.

### PRODUCTION

Production managers have found that cultural values and attitudes toward change can seriously influence the acceptance of new production methods. Plant layout is also influenced by culture. The assembly line is the product of minds socialized in a linear culture in which the task receives primary focus, not the social relationship. Contrast the linear system with the Uddevalla approach found in some Volvo plants in Sweden in the 1980s, where small, autonomous teams assembled the total car in several hours.[7] In procurement, sociocultural norms and rules structure the way the firm acquires resources. In much of Asia, procurement often exists in a web of social relationships and friendships, whereas in the United States, transparency and price frequently drive the process.

After 1995, Disneyland Paris worked to correct the cultural and financial errors that kept attendance down and losses up. The park cut admission prices by 22 percent and hotel rates by one-third. In addition to the original expensive, sit-down restaurants that Disney mistakenly believed all Europeans would demand, cheaper fast food is now available in self-service restaurants. Instead of marketing the park to Europe as if it were a single country, Disneyland Paris has offices in all the main European capitals, and each office tailors tour packages to fit its own market. Today, Disneyland Paris is one of France's top tourist attractions and a major attraction for Europe, as well.

Tokyo Disneyland was next on Disney's development list. Disney had learned from its Parisian mistakes. In Japan, Disney partnered with a local company, so they had ready access to local knowledge. Disneyland Tokyo has been successful beyond forecast. Then came Hong Kong Disney, a 48–52 joint-venture partnership with the Hong Kong government. Yet, to the surprise of Disney, Hong Kong has been struggling since its opening in 2005. Just as in Paris, Hong Kong Disney stumbled early, with low attendance and confusion among guests as to what to expect. Disney responded with a new marketing campaign and dozens of changes inside the park, including more seats because Chinese guests take an average of 10 minutes longer to eat than Americans. Management has also taken steps to see that Mandarin speakers don't accidentally get in the lines to hear English-speaking guides.

The issues in Hong Kong, though, seem to be more related to the product concept rather than to execution issues. People in Hong Kong don't get the Disney magic. They don't have the Disney fairytale stories lodged deeply in their collective unconscious, the way Westerners do (and as the Japanese acquired after WWII). Local visitors in Hong Kong are only 41 percent of all visitors, while in Tokyo they are 96.8 percent. So, Disney will add non-Disney characters and themes. Another issue is that Hong Kong taxpayers, whose government owns the majority share in Disney, want more transparency about Disneyland results: the Hong Kong government has not been transparent in its release of Disney's results, and the local community wants more details about financial results. So, citizens are angry about their government's investment, an emotion that further challenges the growth of Disney's magic. Perhaps, when they understand their investment more fully, they'll visit and help Hong Kong Disney build its magic.

Meanwhile, Disney is moving ahead with plans for China, in Shanghai, which will be many times larger than the Hong Kong theme park. Here, there are also local partners with a majority stake. The planned opening is 2014. We'll be able to see if Disney applies what it has learned in Paris, Tokyo, and Hong Kong, as China comes online.

**Questions:**

1. Why did Disney go solo and avoid joint ventures or other collaborations in its foreign market entries?

2. Do you think Disney, a peculiarly American fantasy concept, can appeal to Asians who don't have much knowledge of American culture?

Sources: "Euro Disney's Fortunes Turn as Number of Visitors Rises," *Financial Times*, November 14, 1997, p. 13; "The Kingdom inside a Republic," *The Economist*, April 13, 1996, pp. 66–67; "Tokyo Disney Shifts Japanese Ideas on Leisure," *The Columbian*, May 1, 1994, p. F7; "Mickey n'est pas fini," *Forbes*, February 14, 1994, p. 42; "Euro Disney's Wish Comes True," *The Economist*, March 19, 1994, p. 83; Merissa Marr and Geoffrey A. Fowler, "Chinese Lessons for Disney," *The Wall Street Journal*, June 12, 2006, pp. A1, A5; "Disneyland Resort Paris," Wikipedia, http://en.wikipedia.org/wiki/Disneyland_Resort_Paris (accessed March 20, 2011); "Mojo Eludes Disney in Hong Kong," *Japan Times*, February 4, 2010, http://search.japantimes.co.jp/cgi-bin/nn20100204f1.html (accessed March 20, 2011).

## ACCOUNTING AND FINANCE

A culture's accounting controls directly relate to the culture's assumptions about the basic nature of people. Are the controls tight throughout the organization, perhaps suggesting low levels of trust at cultural levels, or loose, suggesting that the culture assumes people will act honestly, even when they are not closely monitored? Are the controls administered by formal institutions, gaining compliance through rules and sanctions, or by informal institutions, gaining compliance through social norms (described in Chapter 3)? Treasurers realize the strength of sociocultural forces when, armed with excellent balance sheets, they approach local banks, only to find that the banks in some cultures attach far more importance to who they are than to how strong their companies are or how strong they appear to be on paper. Also, in some cultures financial statements are notoriously unreliable, because the local culture allows creative accounting to keep the tax man away.

## PREFERRED LEADERSHIP STYLES

Leadership traits vary by culture, as well. Is the usual relationship between leader and followers hierarchical or more lateral? Is the leadership model paternalistic? Heroic? Does the ideal leader come up through the ranks, or is the ideal leader someone placed in the leadership position due to family or status? The function of leadership also may be understood differently, depending on culture. Does leadership integrate a group of people or does it provide direction for a collection of individuals?

# Frameworks to Understand Cultures

We have seen that sociocultural forces are important to international business. Increasingly, one useful way managers quickly build a general sense of what to expect in a culture is to use an analytical framework. These frameworks help managers build ways to understand behavior patterns across cultural borders. As we review these frameworks, remember that their use is comparative: our own culture functions as an implicit reference point.

The studies of national-level differences in values on which the frameworks are based include work by Kluckhohn and Strodtbeck,[8] Hall,[9] House,[10] Hofstede,[11] Trompenaars,[12] and Schwartz.[13] Here, we briefly look at three of these frameworks, those developed by Hall, Hofstede, and Trompenaars. This material is an introduction to a rich area of research in several disciplines, including international business, marketing, psychology, anthropology, and sociology. Vas Taras has a "Catalogue of Instruments for Measuring Culture" that lists 143 separate instruments. (www.vtaras.com/Culture_Survey_Catalogue). Hall's theoretical framework is simple and yet powerful; Hofstede's dimensions are empirically derived and have received significant attention from both managers (because they apply easily) and scholars (because they raise significant methodological issues); Trompenaars' work integrates concepts that are derived from the social sciences. If you find yourself interested in further study in this area, Schwartz's work merits your attention. His focus is on values, and his analysis clusters them into openness to change, self-transcendence, self-enhancement, and conservation. House's Globe Study, an ambitious and interesting project that examines leadership patterns around the globe, uses value and practice dimensions to measure culture and may also be useful.

## HALL'S HIGH AND LOW CONTEXT

**LO4-3 Describe** Hall's concept of high and low context.

Hall offers a classification of cultures based upon communication styles and, specifically, on the role that **context** plays in the communication patterns. The context of the communication act is the relevant environment beyond the explicit communication. For example, part of context may be the speaker's and participants' body language, place in the room, and who speaks before and after the speaker. In a high-context culture, the participants have social ties that are long-standing and close, so people know what the communication will be from long experience with the other and from communication signals. In a low-context culture, the relationships are of shorter duration and so more of the communication has to be explicit. In our families, we probably find a higher context, even though we may be members of low-context cultures.

**context**
The relevant environment

Hall suggests that in high context (HC), the communication tends to be implicit and indirect. Context plays an exceedingly strong role, actually carrying much of the meaning. In these cultures, such as Japan, China, Latin America, and the Middle East, communication is more subtle and inferred. (See Figure 4.1.)

In contrast, Hall notes that people in low-context cultures have explicit communication patterns. They do not rely so greatly on the context of the communication. The explicit communicator is direct and unambiguous: what you say is what you mean. In North America, communication tends to be low context (LC), direct, and to-the-point. In LC cultures, to "tell it like it is" is understood to be a positive trait. Figure 4.2 shows examples of HC and LC cultures, along with examples of the concept applied to occupations.

Now we look at the social dimensions of Hall's framework. In LC cultures, people tend to have many connections that endure for short time periods. Because the stored mutual history is minimal, explicit communication ensures that the intended meaning is communicated. In HC culture societies, people have close connections over a long period of time, so much of the meaning is already known because it resides in the context. Figure 4.1 shows these communication relationships and further describes behaviors connected with these two communication patterns.
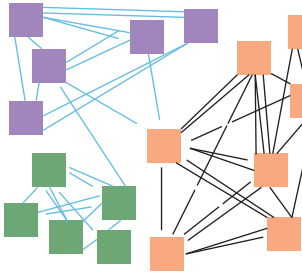
**monochronic**
Having to do with linear time, sequential activities

Hall's work also suggests that LC cultures tend to be **monochronic,** with time characterized as linear, tangible, and divisible into blocks, consistent with the economic approach to time.[14] Monochronic time emphasizes planning and the establishment of schedules, with
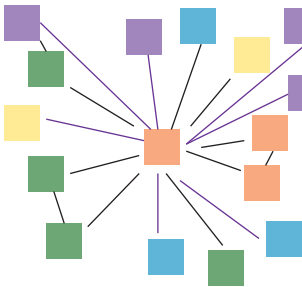
FIGURE 4.1     High and Low Context Attributes

**High Context**



- Less verbally explicit communication, less written/formal information
- More internalized understandings of what is communicated
- Multiple cross-cutting ties and intersections with others
- Long term relationships
- Strong boundaries—insider/outsider
- Knowledge is situational, relational
- Decisions and activities focus around personal face-to-face relationships, often around a central authority person

**Low Context**



- Rule oriented, people play by external rules
- More knowledge is codified, public, external, and accessible.
- Sequencing, separation—of time, of space, of activities, of relationships
- More interpersonal connections of shorter duration
- Knowledge is more often transferable
- Task-centered. Decisions and activities focus around what needs to be done, division of responsibilities.

Source: Modified from www.culture-at-work.com/highiow.html (accessed june 5, 2010).

significant energy put into the maintenance of established schedules. In contrast, HC cultures tend to be **polychronic.** That is, two or more activities are carried out within the same clock block; switching among activities can be both desirable and productive. We think of this as multi-tasking.[15]
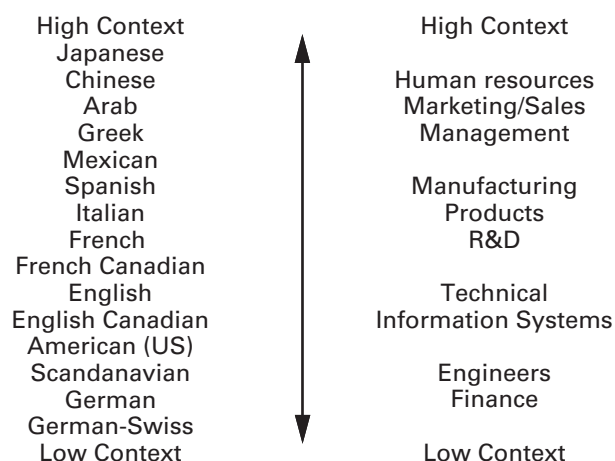
**polychronic**
Having to do with simultaneous activities, multi-tasking

## HOFSTEDE'S FIVE DIMENSIONS

LO4-4 **Review**
Hofstede's framework.

Hofstede, a Dutch business researcher and consultant trained in anthropology, developed his framework from surveys he administered to global IBM employees in the late 1960s, and later augmented them. His framework is concerned primarily with work values.[16] He developed four dimensions with which to classify the survey data that underlie and differentiate cultures: individualism-collectivism, power distance, uncertainty avoidance, and masculinity-femininity. In collaboration with researchers in Asia, he later added a fifth dimension, long-term orientation, having recognized that his earlier work represented a Western

FIGURE 4.2

Examples of High- and Low-Context Cultures and Occupations

| High Context | High Context |
|---|---|
| Japanese | |
| Chinese | Human resources |
| Arab | Marketing/Sales |
| Greek | Management |
| Mexican | |
| Spanish | Manufacturing |
| Italian | Products |
| French | R&D |
| French Canadian | |
| English | Technical |
| English Canadian | Information Systems |
| American (US) | |
| Scandanavian | Engineers |
| German | Finance |
| German-Swiss | |
| Low Context | Low Context |

perspective. This fifth dimension is sometimes referred to as **Confucian dynamism.** His initial database had not included Asian cultures because IBM had little exposure in Asia when Hofstede did the studies. These five dimensions provide managers with a way to understand how national-level cultural differences affect organizations and management methods. They also assist in showing that management skills are culturally specific; that is, "a management technique or philosophy that is appropriate in one national culture is not necessarily appropriate in another."[17] Now to the dimensions.

### Individualism-Collectivism[18]

*The individualism-collectivism dimension* measures the degree to which people in the culture are integrated into groups. People in highly *collectivistic* cultures belong to strong, cohesive in-groups that look after them in exchange for loyalty. The force of this dimension can be illustrated with the Japanese saying: "the nail that sticks up gets hammered down." In contrast, people in highly *individualistic* cultures are more loosely connected and look after themselves and their immediate family. The United States is highly individualistic; the culture rewards independence; the education system rewards outstanding individuals. This dimension plays out strongly in employee motivation and decision making. Countries with predominantly individualist cultures are the United States, Canada, the United Kingdom, Australia, the Netherlands, New Zealand, Sweden, France, and Germany. Cultures that are collectivist include Guatemala, Ecuador, Panama, Indonesia, Pakistan, Taiwan, China, Japan, and West and East African countries.

### Power Distance

*Power distance* is the extent to which members of a society expect and accept power to be distributed unequally. Power distance is similar to inequality, but defined from below, not from above. The dimension suggests that a society's level of inequality is endorsed by followers as well as by leaders. In large power distance societies, seniority, age, rank, and title are important. People will want directions, and formality is emphasized. In a small power distance environment, a consultative style of leadership predominates, informality tends to be the norm, and there is equal distance among people. For example, from season ticket holders of box seats at major sporting events to fast-food workers, just about everyone in the United States self-identifies as middle class. Examples of large power distance cultures are Malaysia, Guatemala, Panama, Philippines, Arab countries, India, West African countries, and Singapore. Examples of small power distance countries include Austria, Israel, Denmark, New Zealand, the Republic of Ireland, Sweden, Norway, Canada, the United States, and Germany.

### Uncertainty Avoidance

*Uncertainty avoidance* describes a society's comfort with uncertainty. Hofstede points out that this dimension "ultimately refers to man's search for Truth" because it describes the extent a culture programs its members to feel either uncomfortable or comfortable in unstructured situations. Cultures that avoid uncertainty try to minimize the possibility of such situations by "strict laws and rules, safety and security measures." Strong uncertainty avoidance cultures resist change, including career change and organizational change, expect clear procedures, and preserve the status quo. Weak uncertainty avoidance cultures see conflict as having positive aspects, expect innovation, encourage risk taking, and reward career change. Examples of strong uncertainty avoidance cultures are Greece, Portugal, Guatemala, Uruguay, Japan, France, Spain, and South Korea. Examples of weak uncertainty avoidance cultures include Singapore, Jamaica, Denmark, Sweden, Hong Kong, the United States, Canada, Norway, and Australia.

### Masculinity-Femininity

The *masculinity-femininity* dimension describes the distribution of roles between the genders. Hofstede's data indicate that "women's roles across cultures differ less than do men's, and that men's values among countries vary considerably, from very assertive and competitive and maximally different from women's values on the one side, to modest and caring and similar to women's values on the other." The assertive pole is masculine, and the caring one feminine. "The women in feminine countries have the same modest, caring values as the men; in the masculine countries

they are somewhat assertive and competitive, but not as much as the men, so that these countries show a gap between men's values and women's values." Note that this dimension is about *the gap between* men and women's roles in the culture. In a feminine culture, there is relatively less variation between male and female roles, which suggests that leadership and decision-making roles would be equally open to men and women. In a feminine culture, quality of work life is important, people work in order to live, and environmental issues matter from a business perspective. In a masculine culture, male roles are more likely to be task focused and female roles relationship focused, achievements are emphasized, economic growth is central, people live in order to work, and business performance is the primary goal. Examples of masculine cultures include Japan, Austria, Venezuela, Italy, Mexico, and the Philippines. Examples of feminine cultures include Sweden, Norway, the Netherlands, Denmark, Costa Rica, and Finland. A word of caution: to think that feminine cultures are not concerned with production and business success is an error. Just think of the globally successful Scandinavian firms in order to correct your misapprehension: IKEA, Nokia, Lego, Volvo, Ericsson, H&M, Bang & Olufson, and Carlsberg begin the list.

### Long-Term Orientation/Confucian Dynamism[19]

This is the added dimension, as a result of a study among students in 23 countries around the world, using a questionnaire designed by Chinese scholars. Hofstede describes it as dealing with Virtue regardless of Truth, that is, the level to which people in the culture will persevere to overcome obstacles they cannot overcome with will or strength. In long-term-oriented societies, people value actions and attitudes that affect the future: persistence/perseverance, thrift, saving face at the group level, and shame. In short-term-oriented societies, values connected to the present and past are stronger: respect for tradition, fulfilling social obligations, high consumption patterns, and protecting face at the individual level. Because this dimension is often misinterpreted, a brief chart is shown in Table 4.1. Table 4.2 presents the scores for Hofstede's five dimensions for about one-third of the countries in his sample.

Figure 4.3 plots the scores for selected nations on the power distance and uncertainty avoidance dimensions. The Latin American countries in the second quadrant had high power

---

**TABLE 4.1** Characteristics of Long-Term and Short-Term Orientation

| Long-Term Orientation Characteristics | Short-Term Orientation Characteristics |
|---|---|
| Social order | Personal survival/security |
| Hierarchical relationships | Personal respect/dignity |
| Collective face-saving | Individual face-saving |
| Long-term planning | Short- to medium-term planning |
| Thrift-centered | Spending-centered |
| Long-term outcomes | Short- to medium-term outcomes |
| **Examples** | **Examples** |
| China | Pakistan |
| Hong Kong | Nigeria |
| Taiwan | Philippines |
| Japan | Canada |
| South Korea | Zimbabwe |
| India | United Kingdom |
| Brazil | United States |
| Singapore | Germany |

Source: Modified from Ting-Toomey, Table 3.5.

TABLE 4.2

**TABLE 4.2**    Selected Scores for Hofstede's Cultural Dimensions

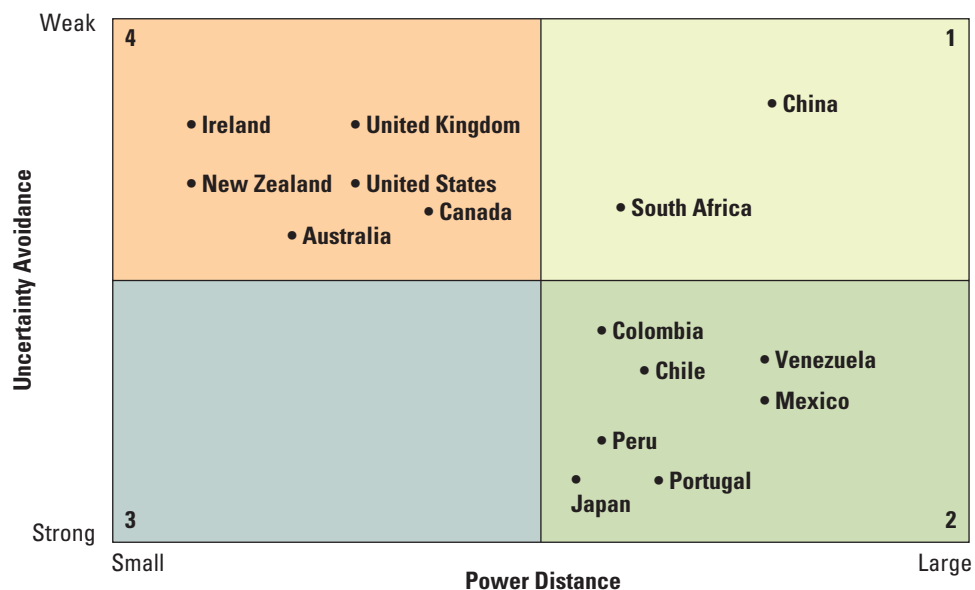| Country | Power Distance | Uncertainty Avoidance | Individualism | Masculinity | Long-Term Orientation* |
|---|---|---|---|---|---|
| Mexico | 81 | 82 | 30 | 69 | |
| Venezuela | 81 | 76 | 12 | 73 | |
| Colombia | 64 | 80 | 13 | 64 | |
| Peru | 90 | 87 | 16 | 42 | |
| Chile | 63 | 86 | 23 | 28 | |
| Portugal | 63 | 104 | 27 | 31 | |
| China | 80 | 30 | 20 | 66 | 118 |
| Japan | 52 | 92 | 46 | 95 | 80 |
| United States | 50 | 46 | 91 | 62 | 29 |
| Australia | 49 | 51 | 90 | 61 | 31 |
| South Africa (SAF) | 49 | 49 | 65 | 63 | |
| New Zealand | 45 | 49 | 79 | 58 | 30 |
| Canada | 39 | 48 | 80 | 52 | 23 |
| United Kingdom | 35 | 35 | 89 | 66 | 25 |
| Ireland | 28 | 35 | 70 | 68 | |

*Data for long-term orientation have not been collected for many countries yet, so these are blank.

Source: Geert Hofstede, "Cultural Dimensions in Management and Planning," *Asia Pacific Journal of Management,* January 1984, p. 83.

distance and strong uncertainty avoidance. These scores suggest that lines of communication in organizations in these countries will be vertical, employees will prefer directive management styles, and risk taking will be avoided. By clearly defining roles and procedures, the organizations are very predictable. The Anglo nations in the fourth quadrant had small power distance and weak uncertainty avoidance. Organizations in these countries are characterized by less formal controls and fewer layers of management, along with more participative leadership styles. Relationships tend to be informal. Note, too, that Japan and China have quite different scores.

**FIGURE 4.3**

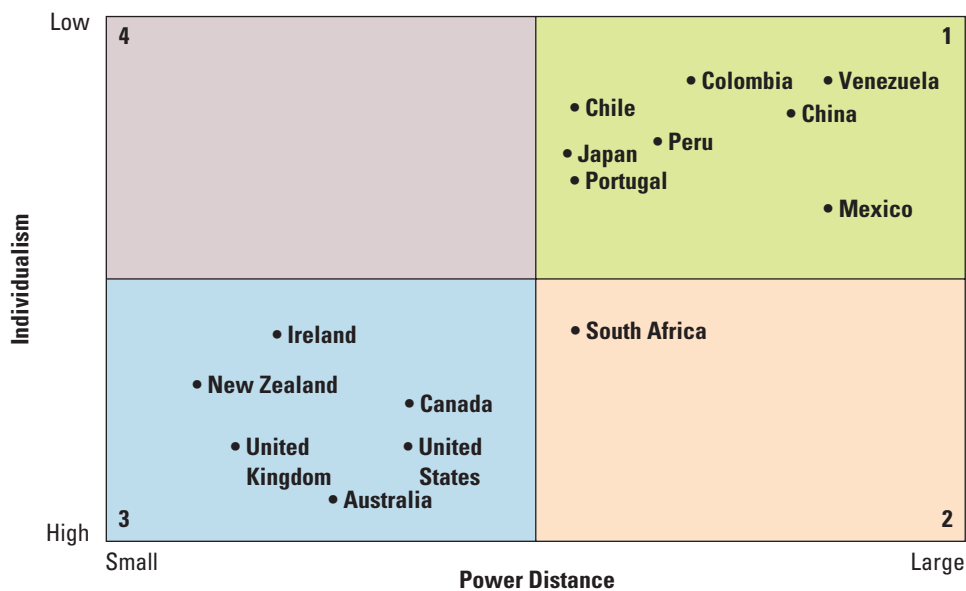Plot of Selected Nations on Power Distance and Uncertainty Avoidance

**FIGURE 4.4**

Plot of Selected
Nations on
Individualism and
Power Distance

The scores for individualism and power distance are plotted in Figure 4.4. The Latin and Asian countries (first quadrant) scored relatively high on power distance and weak on individualism. Employees tend to expect their organizations to look after them and defend their interests. They expect close supervision and managers who act paternally. On the other hand, people in the Anglo countries (third quadrant) have small power distance and high individualism, suggesting that they would prefer to do things for themselves and would not expect organizations to look after them.

## TROMPENAARS' SEVEN DIMENSIONS

Fons Trompenaars, trained as an economist, is also Dutch. His seven-dimension framework for understanding culture is derived from the social sciences, and his initial data are from 47 countries, later greatly expanded in collaboration with Hampden-Turner. The first five dimensions address the culture's patterns for relationships among people, and the final two have to do with time and nature.[20] Trompenaars' dimensions are interesting because, unlike Hofstede's dimensions, which describe values, many of Trompenaars' dimensions describe the behavior that is the result of the underlying cultural value. For example, the specific-diffuse dimension describes the behavior to which values about privacy lead. In a specific culture, the idea that privacy is close and the entry barriers high leads to social patterns that are specific.

Universalism vs. Particularism (rules vs. relationships)    This dimension addresses whether rules or relationships regulate behaviors. A culture's values that are **universalist** apply to all people. The rules are for everyone in all situations. **Particularist** values consider the context. Universalist cultures tend to be rules-based, while particularist cultures tend to be relationship-based. The United States tends to be moderately rules-based (in ethics, for example, we think that everyone should follow the guidelines or rules), whereas in other cultures, the judgment is situational—it all depends.

Individualism vs. Communitarianism    This dimension has to do with whether people plan their actions with reference to individual benefits or group benefits. You will note its similarity to Hofstede's individual-collectivism dimension.

Neutral vs. Affective (unemotional vs. emotional)    This dimension describes the culture's rules for display of emotions. People in neutral cultures tend to withhold emotional expression, while people in affective cultures are much more expressive.

LO4-5 **Outline** Trompenaars' dimensions.

**universalism**
Condition in which concepts apply to all

**particularism**
Condition in which context determines what concepts apply

**communitarianism**
Belief that the group is the beneficiary of actions

**neutral vs. affective**
Withholding emotion vs. expressing emotion

## Specific vs. Diffuse

The **specific vs. diffuse** dimension distinguishes among cultures based on the social patterns for public and private life. In *specific* cultures, there is a small private life that is kept private, with a large public life that is easy to enter, with many relationships that may be brief. In a *diffuse* culture, there is a large private life and a smaller public life that is more difficult to enter. For example, introductions may play a role in doing business. In a diffuse culture, the distinction between work life and private life is less clear than in a specific culture.

## Achievement vs. Ascription

This dimension focuses on the basis of social status and reward, with status being related to either who a person is or what a person does. *Ascription* cultures consider who a person is by family lineage or age, or other attributes. *Achievement* cultures are meritocracies that reward what you do. In the United States, for example, achievement is the primary determinant of social status. This dimension may be especially helpful with staffing and interpersonal dynamics.

## Attitudes toward Time

Trompenaars' time dimension has two aspects. The first is where the primary focus exists—on the past, the present, or the future. Past-focused cultures use history as a lens to view the present. Present-focused cultures focus on what is happening now. Future-oriented cultures plan, anticipate, and see a better world evolving. The second aspect to the time dimension is whether actions are sequential (linear) or synchronous (polychronic).

## Attitudes toward the Environment

The relationship with nature is the basis of this dimension. Is the culture in harmony with nature, or does our understanding of the natural order of things (i.e., culture) suggest that we control nature? North American Anglo cultures tend to assume that they are meant to dominate nature. This can-do attitude does not allow natural obstacles such as oceans and mountains get in the way of progress. Other cultures may be more inclined to seek harmony with nature rather than to dominate it. The impact of this dimension influences areas such as infrastructure development and also ways people think about obstacles in the external world. Do they adjust or reconfigure?

Figure 4.5 illustrates an application of Trompenaars' dimensions to China, Mexico, and the United States.

### SUGGESTIONS FOR USING THE FRAMEWORKS

As we conclude this review of culture frameworks, a caveat about how to use them is in order: both Hofstede's and Trompenaars' data represent a normal distribution within a national culture of the specific dimension. The score of each dimension represents its mean for each country, the central tendency. Thus, you will find people in the culture at all points on the distribution curve. The dimensions suggest that people from a specific culture tend to think and behave in a certain way. Do remember that such generalizations are at best sophisticated stereotypes of the complex culture we are trying to understand.[21] They are best used to establish likelihood and to predict; they can be misleading because they ignore complexity and subtlety. This is an important caution.

Remember, too, that these data have been analyzed on a national level and do not recognize the existence of subcultures. Cultural frameworks are useful tools, especially when we recognize their limitations. The frameworks help us to set expectations so that we can begin to build an understanding, but we are not wedded to these expectations. As humans, we are infinitely variable. As Shakespeare has Hamlet observe, "What a piece of work is a man! how noble in reason! how infinite in faculties! in form and moving how express and admirable!"[22]

# Sociocultural Aspects of Culture

Now that we have discussed what culture is, its importance to international business managers, and the frameworks available to help build our understanding of specific cultures, we focus on some of the sociocultural aspects of cultural variation—that is, how a society's

FIGURE 4.5

Examples of
Country Rankings
on Trompenaars'
Dimensions

**China**

**Dimension**

Universal ----------------------------------------- X ---- Particularist
Individualist ----------------------------------- X ------- Collectivist
Neutral------------------------------------X ----------- Affective
Specific--------------------------------------------X--- Diffuse
Achievement-------------------------------------- X -- Ascription

**Mexico**

**Dimension**

Universal ------------------------------X---------------- Particularist
Individualist ------------X------------------------------ Collectivist
Neutral------------------------------------------- X - Affective
Specific-------------------------------X------------------ Diffuse
Achievement------ X ----------------------------------- Ascription

**United States**

**Dimension**

Universal -- X ------------------------------------------- Particularist
Individualist - X ------------------------------------- Collectivist
Neutral-------------------------------- X --------------- Affective
Specific------------ X ---------------------------------- Diffuse
Achievement-X ---------------------------------------- Ascription

culture manifests or shows itself. Culture manifests in everything, and we look briefly at some of the major areas, aesthetics, religion, material culture, language, and social organization. We close with brief observations about an area in which there is often confusion, and where many cross-culturally confusing signals are sent: gift giving.

## AESTHETICS

**Aesthetics** describe a culture's sense of beauty and taste and is expressed in many areas, most directly in art, drama, music, folklore, and dance.

**aesthetics**
A culture's sense of beauty and good taste

Art   Art including color and form, is of particular interest to international businesspeople because of its symbolic meanings. Colors carry different meanings in different cultures. For example, the color of mourning is black in the United States and Mexico, black and white in the Far East, red in South Africa, and purple in Brazil and Thailand. Green is a propitious color in the Islamic world, and any ad or package featuring green is looked at favorably there.

Aesthetics apply to our ideas about our bodies and their physical beauty, as well. The view of an ideal weight differs markedly across cultures. Often, in richer countries, the better-off are thinner, while in poorer countries, the poorer are thinner. In Japan, sumo athletes are obese, and in some areas of Nigeria, girls enter "fattening rooms" to bulk up. Tattoos are another aspect of body aesthetic value differences across cultures. In some cultures, they are seen as beauty-enhancing, while in others, a desecration. The oldest preserved human, the Iceman found between Austria and Italy, is tattooed. In an interesting reversal, at one time in

Japan, criminals were tattooed by authorities as a way to identify them, a negative meaning. Today, the Yakuza tattoo themselves to establish their in-group identity.

**Music and Folklore**  Musical tastes vary across cultures, and, although commercials with music are generally popular worldwide, the marketer must know what kind of music each market prefers. Thus, a commercial that used a ballad in the United States might be better received if accompanied by the tune of a bolero in Mexico or a samba in Brazil.

A culture's folklore can disclose much about a society's way of life. The incorrect use of folklore can sometimes cost the firm a share of the market. For example, associating a product with the cowboy would not obtain the same results in Chile or Argentina as in the United States, because in those countries, the cowboy is a far less romantic figure—it is just a job. On the other hand, Smirnoff's use of an image of late revolutionary leader Ernesto "Che" Guevara in an advertisement for spicy vodka sparked controversy in Cuba, where Guevara is a national hero.[23] In many areas, especially where nationalistic feeling is strong, local firms have been able to compete successfully with foreign affiliates by making use of indigenous folklore in the form of slogans and proverbs. An example of this is the use of Colonel Sanders' statues outside KFC stores in Japan. This marketing draws on the Japanese respect for elders and the perceived Japanese-ness of the Colonel. Loy Weston, who established KFC in Japan, claims that luck was in play here, but that luck was based on tremendous cultural sensitivity.

## RELIGION

Religion, an important component of culture, is responsible for many of the attitudes and beliefs affecting human behavior. A knowledge of the basic tenets of the religions of your markets will be useful as you build your understanding of those cultures. Each religion has various forms and traditions within it and expresses its beliefs through particular

kinds of worship and prayer, rituals, dietary rules, and modes of dress.[24] Knowledge of the local religion will also help you to communicate your respect for the culture. The following paragraphs describe briefly the main beliefs or principles that define five major religions.

Christianity has many denominations, but all of them share a belief that there is one God who is revealed through human history. Christians believe that Jesus was God's Son who came to earth as a man and lived in Israel, then called Palestine; he was killed about 30 C.E. by authorities of the Roman Empire, but came back to life and ascended to heaven. Christians claim that all who profess their belief in the Resurrection of Jesus will be received into heaven after death.

**Islam** began in the 7th century C.E. and, like Christianity and Judaism, originated in the Middle East. From an Arabic word meaning, "submitting," Islam also professes belief in one God, Allah. Muslims (those who practice Islam) focus on living their lives according to God's will, which is revealed through the "Qur'an" (the Scripture) and a long line of messengers. Mohammed is revered as the last and most important prophet of the religion and is said to have received the words of the Qur'an directly from God in a series of visions.

**Buddhism** was founded between the 6th and 4th centuries B.C.E. in northeastern India. Based on the teachings of Siddhartha Gautama, a royal prince who became known as the Buddha (Enlightened One), it encompasses several schools of thought, established over the centuries by different teachers. In general, Buddhists believe that earthly life is a continuous cycle of birth and death (reincarnation) that is the cause of human suffering. When we finally escape this cycle to achieve a state of being called "nirvana": we become, like the Buddha, enlightened.

**Hinduism** is the oldest of the major world religions and began in India around 2500 B.C.E. Hindus believe in one Supreme Reality, called Brahman, which takes many forms and names. Hindus seek to be in harmony with Brahman by living an ethically good life through self-discipline, the sharing of wealth, and following the teachings of the

| TABLE 4.3 | Followers of Five Major World Religions |

| Religion | Number of followers (in millions) | Cultural Tradition |
|---|---|---|
| Christianity | 2,200 | Abrahamic religions |
| Islam | 1,650 | Abrahamic religions |
| Buddhism | 1,500 | Indian religions |
| Hinduism | 1,000 | Indian religions |
| Judaism | 18 | Abrahamic religions |

Sources: World Christian Database Gordon–Conwell Theological Seminary Centre for the Study of Global Christianity, http://world christiandatabase.org; Pew Forum, http://pewforum.org/Mapping-the-Global-Muslim-Population.aspx; *CIA World Factbook,* 2011, www.cia.org; "Philosophy of Religion". *Encyclopædia Britannica.* 2010, www.britannica.com/EBchecked/topic/497132/philosophy-of-religion (all accessed March 19, 2011).

Scriptures (Vedas). Like Buddhists, they believe in reincarnation (the cycle of rebirth) and seek to escape it to achieve union with God.

**Judaism** began about 1900 B.C.E. in Israel, then known as Canaan, and shares the belief that God acts in human history, especially in times of struggle and oppression. The "Tanak," Judaism's Scripture, tells the story of how the Jews were repeatedly conquered and enslaved by foreign powers, but were freed by God's power acting through figures such as Abraham, Moses, and David. Jews believe that God made a "covenant" or promise to protect them as long as they continue to believe in and worship the one God.[25]

Table 4.3 shows the world's five major religions, while Figure 4.6 maps the major religions.

## MATERIAL CULTURE

**material culture or artifacts**
All human-made objects; concerned with *how* people make things (technology) and *who* makes *what* and *why* (economics)

**Material culture or artifacts** are all the human-made objects of a culture; people who study material culture are concerned with *how* people make things (technology) and *who* makes *what* and *why* (economics). Every culture has certain parts of its material culture of which it is especially proud. Some awareness of these objects and the meaning they have for people in the culture can communicate interest in the culture.

## LANGUAGE

Probably the most apparent cultural distinction that the newcomer to international business perceives is in language. Differences in the spoken language are readily discernible, and after a short period in the new culture, variations in the unspoken language become apparent, as well. Language is an important key to a culture, and without it, people find themselves locked out of all but a culture's perimeter. As illustrated in Chapter 5, spoken languages demarcate cultures just as physical barriers do. In fact, nothing equals the spoken language for distinguishing one culture from another.
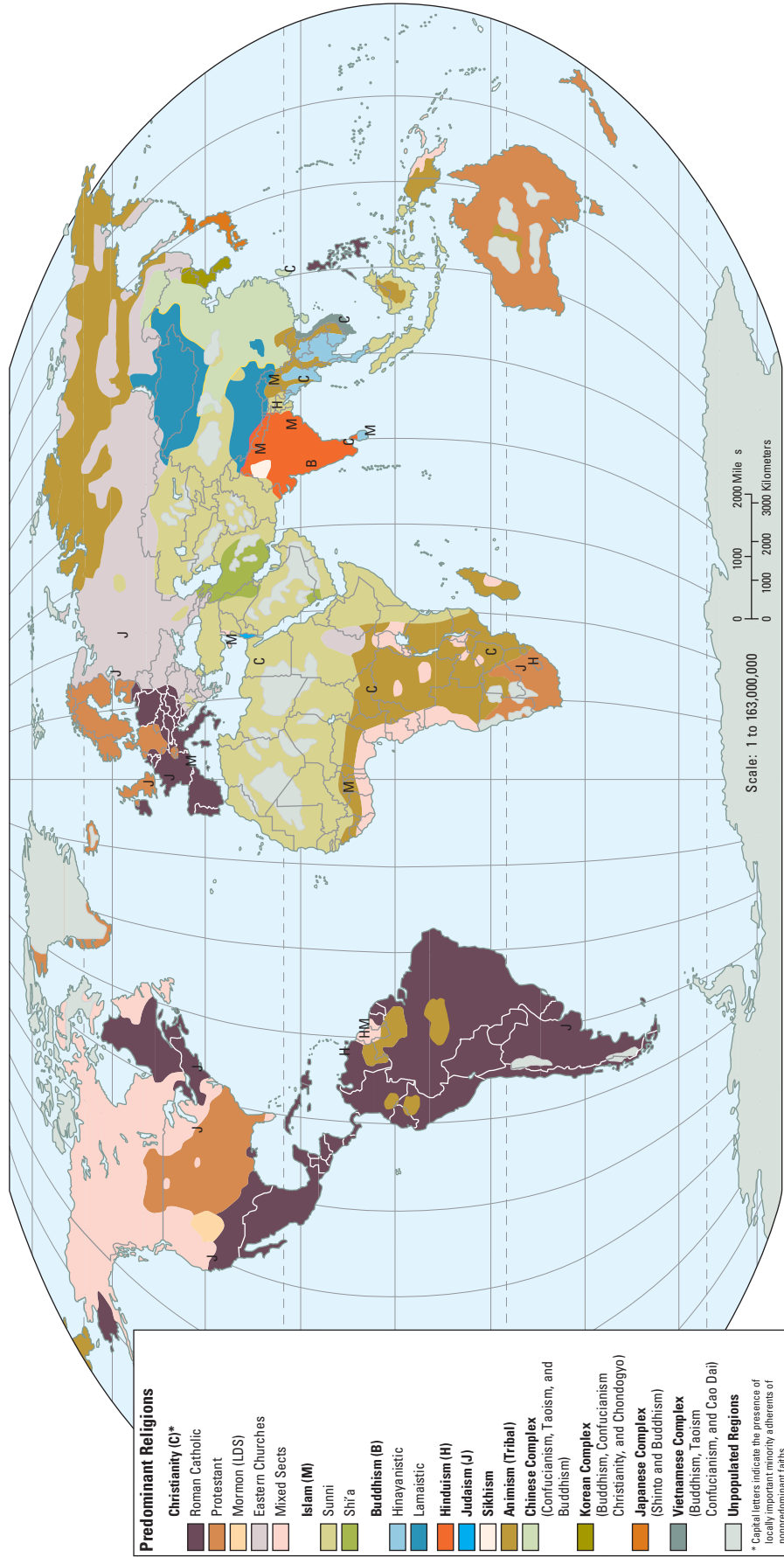
Even though many global businesspeople speak English, when they buy, they often want to do business in their own language. The foreign seller who speaks the local language has a competitive edge. Figure 4.7 shows a map of the major languages of the world.

Nonverbal communication, or the unspoken language, can often tell businesspeople something that the spoken language does not—if they can understand it. High-context cultures tend to use unspoken language more intensively than do low-context cultures and thus, people in HC cultures often have developed advanced "reading ability" of unspoken language. Because context plays such an important role in their home culture, they are aware of this medium. Eye contact, posture, and subtle facial expressions are all cues on which HC cultures rely.

Gestures are a common form of cross-cultural communication, yet they vary from one region to another. For instance, Americans and most Europeans understand the thumbs-up
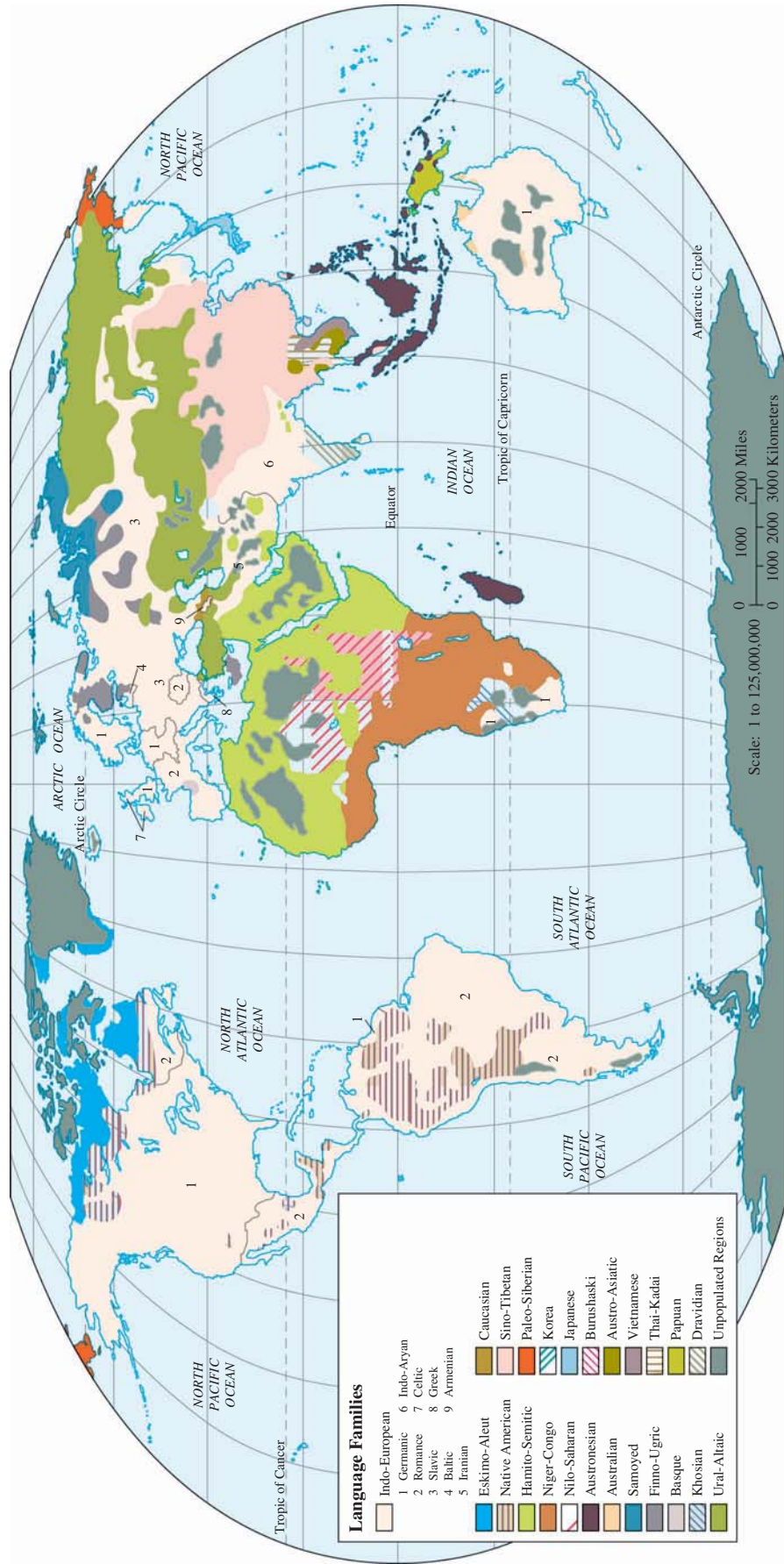
**FIGURE 4.6** Maps of the World's Religions

**Predominant Religions**

**Christianity (C)***
Roman Catholic
Protestant
Mormon (LDS)
Eastern Churches
Mixed Sects

**Islam (M)**
Sunni
Shi'a

**Buddhism (B)**
Hinayanistic
Lamaistic

**Hinduism (H)**
**Judaism (J)**
**Sikhism**
**Animism (Tribal)**

**Chinese Complex**
(Confucianism, Taoism, and Buddhism)

**Korean Complex**
(Buddhism, Confucianism Christianity, and Chondogyo)

**Japanese Complex**
(Shinto and Buddhism)

**Vietnamese Complex**
(Buddhism, Taoism Confucianism, and Cao Dai)

**Unpopulated Regions**

* Capital letters indicate the presence of locally important minority adherents of nonpredominant faiths.

Scale: 1 to 163,000,000

0   1000   2000
0   1000   2000   3000 Kilometers
0   1000   2000 Mile s

**FIGURE 4.7**    Major Languages of the World



**Language Families**

Indo-European

| 1 Germanic | 6 Indo-Aryan |
| 2 Romance | 7 Celtic |
| 3 Slavic | 8 Greek |
| 4 Baltic | 9 Armenian |
| 5 Iranian | |

Eskimo-Aleut
Native American
Hamito-Semitic
Niger-Congo
Nilo-Saharan
Austronesian
Australian
Samoyed
Finno-Ugric
Basque
Khoisan
Ural-Altaic

Caucasian
Sino-Tibetan
Paleo-Siberian
Korea
Japanese
Burushaski
Austro-Asiatic
Vietnamese
Thai-Kadai
Papuan
Dravidian
Unpopulated Regions

Scale: 1 to 125,000,000

| 0 | 1000 | 2000 Miles |
| 0 | 1000 2000 | 3000 Kilometers |

gesture to mean "all right," but in southern Italy and Greece, it transmits a vulgar message. Similarly, making a circle as the "OK" sign, with the thumb and the forefinger, is friendly in the United States, but it means, "you're worth nothing" in France and Belgium and is vulgar in Greece and Turkey.

The unspoken language also includes spatial relationships, including aspects of workspaces. In the United States, an office door that is closed suggests a request for privacy; the normal position of the door is open. Germans regularly keep their doors closed. Hall suggests that the closed door does not mean that the person behind it wants no visitors, but only that he or she considers open doors to be sloppy and disorderly.[26] Office size and location can mean different things in different cultures. In the United States, the higher the status of the executive, the larger and more secluded the office, but in the Arab world, the company president may be in a small, crowded office. In Japan, the senior person is likely to be closest to the center of the room, and the least valuable places on an office floor are by the windows. The French also locate important department heads in the center of activities, with their assistants located outward on radii from this center.

Conversational distances, the space between people in a conversation, tend to vary across cultural borders, as well. For example, they tend to be much smaller in the Middle East than in Anglo cultures. Seeing two people with differing expectations for conversational distance, such as an American and a Saudi, move across a floor as one tries to close the space and the other expand it is not uncommon at social gatherings, if you watch for it. Conversational distances vary by gender as well, and comfortable distance may also vary by the degree of familiarity of the parties involved.

## SPECIAL FOCUS: GIFT GIVING

Gift giving is an important aspect of every international manager's life, and a confusing aspect for many. In all cultures, some sort of entertainment outside of office hours and the exchange of gifts are part of the process of getting better acquainted. In high-context cultures and cultures with large power distance, the etiquette for gift giving is markedly different than in low-context cultures and cultures with small power distance.

Marcel Mauss, an anthropologist who looked at gifts in early societies, theorized that gift giving operated within the society as a way to acknowledge interrelationships and obligations. Mauss argued that in "archaic" societies, individual, family, and communal interests combined to make a social system that needed to acknowledge interrelationships and obligations.[27] He suggests that gift giving creates reciprocal relationships involving three obligations: the obligation to give, to receive, and to reciprocate. A gift has a magiclike quality, he points out, because it carries with it more than the item itself; it carries some of the giver—and that quality results in an obligation of the receiver to reciprocate. Thus, the ritual of gift giving in international business is important because it creates a social bond to be a giver, a receiver, and one obligated to the other. This series of roles and reciprocal obligations creates solidarity.

The first point about gifts from a practical viewpoint is to figure out how the ritual plays out. What constitutes an acceptable gift in the culture, and what is the role of gift giving? In Japan, for example, one never gives an unwrapped gift or visits a Japanese home empty-handed. A gift is presented with the comment that it is only a trifle, which implies that the humble social position of the giver does not permit giving a gift in keeping with the high status of the recipient. The recipient, in turn, will not open the gift in front of the giver, in order to spare him or her any embarrassment. The intention of gift giving in Japan is to convey thoughtfulness and consideration for the receiver, who, over time, builds up trust and confidence in the giver.

Every country will have an etiquette and set of implicit rules around the giving of gifts: their timing, their value, how they are presented. Know what these are.[28] Many organizations have policies related to gift giving designed to separate this cultural pattern from bribery or extortion, so managers will want to keep their organization's guidelines in mind.

### When in Rome, Should You "Do as the Romans Do" . . . and Feel Comfortable about It?

Overseas travel, whether for work or vacation, may place us in the position of needing to decide whether to follow local practices. With some local practices, there is no choice. When in Britain, you drive on the left side of the road. Some local practices, though, may not seem to make sense, while others may seem liberating. The Japanese protect delicate tatami mats by removing their shoes. Do you conform? If you are a non-Muslim woman, do you wear a headscarf and long cloak when in a conservative Islamic country such as Saudi Arabia?

At a more complex level, other customs may conflict with our home culture's moral or perhaps legal standards. If you are from a country where cannabis is illegal or reserved for medicinal use, do you visit the Grasshopper, a cannabis coffee shop, when you are in Amsterdam? If you are American and you observe the drinking age of 21, do you drink in environments where there is no drinking age?

At the business level, do you follow the corporate tax law as you would in your home country, or do you underreport and then negotiate, along with the locals, in Italy? Do you pay fixers or agents, invisible hands, in cultures where this is a process widely followed? Agreed, such practices will contradict most company ethical codes, but what if your competitors follow such practices? If you are American, do you follow the Foreign Corrupt Practices Act in cultures where your competition greases palms? Do you outsource your legal or moral issue to an agent? The issue here is, to what extent should we follow local practices and conform to local customs? What do you think?

**Questions:**

1. Are all actions that conform to local customs morally defensible?
2. Recommend an approach to resolving ethical issues in the international arena.

## SOCIETAL ORGANIZATION

Every society structures its social relationships, and these patterned arrangements of relationships define an important aspect of culture. There are two main classes of social institutions, based on the conditions of their formation: *kinship* and *free association.*

The family is the basic unit of institutions based on kinship. Unlike the American family, which is generally composed of parents and their children, families in many nations are extended to include all relatives by blood and by marriage. Many of these cultures will be high context. For the foreign firm, this extended family is a source of employees and business connections. The trust that people place in their relatives may motivate them to buy from a supplier owned by their cousin's cousin, even though the price is higher. Local personnel managers may fill the best jobs with family members, regardless of qualifications. Although the extended family is large, each member's feeling of responsibility to it is strong. This practice goes against the common Western idea that nepotism is to be avoided, except in family businesses.

Associations not based on kinship may be formed by age, gender, or common interest.[29] These groups are important for international managers to understand, because they influence behavior at a fundamental level and their rules and organization are likely to differ across cultural borders. Consumer organizations, for example, have forced firms to change their products, promotion, and prices. A new kind of association has emerged with Facebook and other social networks, with their own unwritten cultural rules. In the spring of 2011, we are seeing that they have a significant influence on international political organizations in the Middle East. We can expect to see much more e-influence on firms.

In Chapter 4, we have looked at what culture is and its significance for international business, reviewed three of the most useful cultural dimension frameworks, and addressed some of the more significant sociocultural aspects of societies, including aesthetics, religion, material culture, and language. Moving forward to other external forces that managers must address and over which they have limited control, please remember that all of these forces are influenced by culture. You might think of culture as a collection of rules, many of them unwritten, that social groups use to solve their problems and differentiate themselves from one another. Understanding culture at a significant level provides international managers with a rich way to build understanding, and possibly value, across cultural borders.

## Mallory Wedeking: Attitude Is Everything!



Mallory Wedeking has studied and worked in Uganda and Rwanda. When asked to give advice to students studying international business and wondering if it is for them, she has some very interesting observations. Here are her comments:

My concentration in school is entrepreneurship and my career goals are to pursue a career in business in the context of International Development. I became interested in International Business when I first traveled after I graduated high school. Interacting with different cultures and different lifestyles inspired in me creativity and a desire to learn. I craved the excitement and added texture to doing business in an international context.

The most influential time abroad I have experienced would be the four months I studied in Uganda and Rwanda, two countries located in East Africa. While I was there, in addition to studying, I was also able to do an internship through the non-profit Food for the Hungry. My duties in the internship involved working with a rural village in Eastern Africa to help foster economic development and financial responsibility within the community.

I chose this location because I desired to expand my knowledge and cultural awareness beyond that of the Western, developed world. Obviously, I knew I was going to experience a much broader cultural gap than I had in Europe and was nervous about the transition. I briefly familiarized myself with the culture (which would definitely be necessary in more formal cross-cultural interactions), but most of the cultural awareness, including "Dos" and "Don'ts," I learned along the way. I learned early on that mistakes were unavoidable and that the attitude in which you deal with them is what matters.

Learning another culture is truly a humbling experience. Along those lines, if I had to give anyone advice in working abroad, I would have to say that attitude is everything. Cultural

miscommunications will happen no matter how much you prepare ahead of time. I do not think I would have been able to learn in the capacity that I did if I wasn't able to get back up on my feet (literally, in some cases) and keep moving forward. Also, I would recommend understanding the phases of culture shock and being able to properly identify where you are in order to deal with your current feelings and emotions. There is a tendency at certain points of culture shock to retreat from the culture and surround yourself with only things familiar and comfortable. I experienced this feeling two months into my stay abroad, often retreating with my fellow American students and watching movies like Ferris Bueller's Day Off or Star Wars. I had to force myself to continue interacting with the Ugandan people, against all my other desires.

Surprisingly, I found that returning to the United States was a much more difficult cultural adjustment than arriving in East Africa. One reason was because I had not expected that my home for twenty years of my life could feel overwhelming and unfamiliar. It took about six months to completely feel comfortable here again. I learned that the process cannot be rushed, and it is important to give yourself time to really absorb everything you learned while abroad. You shouldn't expect or want yourself to be the same exact person you were before you left.

My greatest enjoyment while I was working abroad was finding different ways to connect with people. I realized that though we were worlds apart culturally, not to mention mileage, there were so many ways we could relate to each other, especially through song and dance. Emphasizing the things you have in common, rather than the differences (which easily outnumber the commonalities), is so important in learning to relate with one another. After all, we are all human, and that's a huge thing in common!

I would highly recommend working internationally. The daily surprises keep things interesting and teach you invaluable qualities and skills. Even traveling for pleasure purposes or studying abroad teaches you skills such as being adaptable, thinking and making decisions quickly, learning on the go and developing advanced communication skills, all of which are extremely desirable to employers.

### Resources for Your Global Career

Test your Cultural IQ and knowledge of business etiquette by taking the international cultural quizzes on these links:

- http://www.getcustoms.com/2004GTC/quiz.html
- http://www.mannersinternational.com/etiquette_tips_business.asp
- *The Economist:* Country Briefings and "Doing Business In . . . " Series: http://audiovideo.economist.com/?fr_chl=a841d118e68f7ad627812b42ce2cb5a134fc691e&rf=bm

Here are your etiquette and protocol guides for doing business in major cities and countries in the world—you can never learn enough!

- http://www.economist.com/blogs/gulliver/etiquette/
- http://www.executiveplanet.com/index.php?title=Main_Page

# Summary

**LO4-1 Describe what culture is.**

Anthropologists, who study culture, describe it as the *sum total of the beliefs, rules, techniques, institutions, and artifacts that characterize human populations.* In other words, culture consists of the "individual worldviews, social rules, and interpersonal dynamics characterizing a group of people set in a particular time and place." Most anthropologists also agree that:

1. Culture is *learned;* we are not born with a culture.
2. The various aspects of culture are *interrelated.*
3. Culture is *shared, patterned, and mutually constructed through social interaction.*
4. Culture *defines the boundaries* of different groups.

**LO4-2 Explain the significance of national-level culture differences for international business.**

Everything we do is influenced by culture, and most of us realize that about other cultures, but not always about our own. National cultural differences affect the functional areas of international business. For example, assumptions about the need for controls in accounting systems rest of cultural values having to do with trust. Leadership is greatly influenced by culture. What is leadership thought to be? Is it patriarchal and hierarchical? It the leader one among equals? HR practices are greatly influenced by cultural values as well. What is the role of social class in employee relationships? Is employee evaluation a development aid or an adversarial process? Every business action is influenced by national-level cultural values. Organizational and local-level values also play a role.

**LO4-3 Describe Hall's concept of high and low context.**

In a high-context culture, the participants have social ties that are long-standing and close, so people know what the communication will be from long experience with the other and from communication signals. In a low-context culture, the relationships are of shorter duration, and so more of the communication has to be explicit. In our families, we probably find a higher context, even though we may be members of low-context cultures. In high context (HC), the communication tends to be implicit and indirect. Context plays an exceedingly strong role, actually carrying much of the meaning. In these cultures, such as Japan, China, Latin America, and the Middle East, communication is more subtle and inferred. In contrast, Hall notes that people in low-context cultures have explicit communication patterns. They do not rely so greatly on the context of the communication. The explicit communicator is direct and unambiguous: what you say is what you mean.

**LO4-4 Describe Hofstede's framework.**

Hofstede's framework is concerned primarily with work values. It originally had four dimensions that were used to classify the survey data that underlie and differentiate cultures: individualism-collectivism, power distance, uncertainty avoidance, and masculinity-femininity. In collaboration with researchers in Asia, he later added a fifth dimension, long-term orientation. This fifth dimension is sometimes referred to as Confucian dynamism.

**LO4-5 Outline Trompenaars' dimensions.**

Trompenaars' seven-dimension framework for understanding culture is derived from the social sciences, and his initial data are from 47 countries, later greatly expanded in collaboration with Hampden-Turner. The first five dimensions address the culture's patterns for relationships among people, and the final two have to do with time and nature. Trompenaars' dimensions are interesting because, unlike Hofstede's dimensions, which describe values, many of Trompenaars' dimensions describe the behavior that is the result of the underlying cultural value. His dimensions are universalism vs. particularism (rules vs. relationships), individualism vs. communitarianism, neutral vs. affective (unemotional vs. emotional), specific vs. diffuse, achievement vs. ascription, attitudes toward time, and attitudes toward the environment.

**LO4-6 Discuss the sociocultural aspects of culture as a phenomenon.**

Culture is not directly observable. The sociocultural aspects of cultural are how a society's culture manifests or shows itself. Culture manifests in everything. The major areas include aesthetics, religion, material culture, language, and social organization.

**sociocultural** (p. 94)

**ethnocentricity** (p. 94)

**context** (p. 98)

**monochronic** (p. 98)

**polychronic** (p. 99)

**Confucian dynamism** (p. 100)

**universalism** (p. 103)

**particularism** (p. 103)

**communitarianism** (p. 103)

**neutral vs. affective** (p. 103)

**specific vs. diffuse** (p. 104)

**achievement vs. ascription** (p. 104)

**aesthetics** (p. 105)

**material culture or artifacts** (p. 108)

# Questions

1. Drawing on Hall's high and low context, describe some of the communication issues that might well arise when an Arab company officer who has spent his career in the Middle East is sent on temporary assignment to Germany for a year to integrate a process developed in one of the Middle East production facilities.

2. If you are a Mexican who has just accepted a short-term assignment in Ireland, what are some of the expectations you may have about Irish behavior, drawing on Hofstede's cultural dimensions?

3. Thinking about the definitions and descriptions of culture offered in this chapter, would you expect the objective discipline of accounting to be influenced by culture?

4. If you had the choice of sending either an American or a Mexican, both equally qualified and at about the same level and in the same functional areas, to Japan for a three-year assignment, why might sending the Mexican offer less risk?

5. How could Trompenaars' universalism-particularism dimension be helpful in sorting out confusion in the international division over ethical behavior?

6. Give a short description of an example of Trompenaars' achievement-ascription dimension.

7. If you were advising a French colleague on her first work assignment to your home culture, and she asked you what aspects of the material culture she should pay attention to, what advice would you give her?

8. What is the significance of the extended family for international managers?

9. Some societies view change differently than do Americans. What impact does this have on the way Americans operate in those areas?

10. Discuss the role of gift giving in high-context societies.

# Research Task

globalEDGE    globalEDGE.msu.edu

Use the globalEDGE site (http://globalEDGE.msu.edu/) to complete the following exercises:

1. Assume you own an exporting company that specializes in consumer products. You have been selling your products in several different countries but have yet to enter the Asian market. You have chosen Singapore as the first Asian country to enter. Because you have not previously sold your products in any Asian market, you think it would be a good idea to form a strategic alliance with a local firm. You strongly believe that first impression is important. Therefore, you have decided to collect some information regarding the business

culture and local habits of Singapore from the *Kwintessential* website. Prepare a short report on the most shocking characteristics that may influence business interactions in this country.

2. The cultural distance of countries in which your firm operates is one of the many explanations of significant differences that your U.S.-based employees face when traveling to different affiliates worldwide. Typically, an index of cultural distance can be determined by summing the differences of country-level scores such as those introduced by Hofstede's cultural dimensions. At the present time, your firm has operations in Turkey,

Poland, Costa Rica, South Africa, and Indonesia. Using the *Hofstede Cultural Dimensions Resource Center* based on studies involving cultural dimensions to assess all five countries, determine which affiliates are located in a culture that is least and most similar to the United States. As there are four main components of each overall cultural distance score, which component(s) can be considered most influential for each country?

## Minicase: Who Gets the Assignment?

Your international company headquartered in New Jersey is sending an expatriate to China for a three-year assignment to staff up and run a new branch of its industrial products business. The main Chinese customers are using the products in their Middle Eastern and North African petroleum operations. You are chair of the selection committee, have extensive overseas experience, and presently serve as VP, Human Resources. There were 12 internal people interested in the position, and your committee has narrowed this to three final candidates who want this assignment. Here are the candidates:

Tom is a mid-level finance manager with stellar performance reviews. He has no foreign experience and would like to develop his career in this direction. He is single, has an MBA, and has been out of school for 20 years. His background is in finance at the undergrad level, which he studied at Ohio State, only 50 miles from his hometown. He is involved in the local Council on Foreign Relations and is an accomplished athlete.

Firdaus is a deputy VP of HR at corporate. Her family emigrated from Yemen to Chicago when she was in grade school, and she speaks reads and writes Arabic, both classical and the Yemen dialect. She is married, with two children. Her husband George is a professor of history and does not speak Arabic. She has a Ph.D. in engineering, joined the company on the operations side, and has made the mid-career transition to HR successfully. She finished her PhD at the University of London before she began with the company and is now early mid-career. Her performance reviews are stellar. She encountered an incident at the company's headquarters several years ago when there was a discussion about her wearing a headscarf, but this was resolved without her changing her practice. She is well known and well liked throughout HQ. Her husband is ready to take a leave of absence for three years to accompany her.

Gunther is VP of the German-based EU company. His functional background is accounting, and he is credited with the success of the company in the EU. He built the business from a small operation in Frankfurt to the EU sector leader in only seven years. He speaks German and English and is known for being well-organized and "button-upped." His work is timely, accurate, and detailed. Gunther's boss, the president of the international side, was a bit surprised that Gunter expressed interest in this position, because it is perceived as junior to the position he has now, although it would have an equivalent title on paper. Gunter has an undergraduate degree in anthropology and took graduate-level accounting courses earlier in his career.

The company would like someone who could get the operation up and running, stay for three years, and then transfer the position to a local hire they would develop for the responsibility. Drawing on the culture dimensions that we have reviewed, along with your business knowledge, whom would you recommend for the position?

*This page intentionally left blank*

# Political and Trade Forces



In nearly every economic crisis, the root cause is political, not economic.

*—Former Prime Minister Lee Kuan Yew of Singapore*

## Branding and Rebranding a Country

In February 2008, a new nation was born—Kosovo, a former province of Serbia. As one means of putting this new nation "on the map," the advertising agency Ogilvy developed a 10-foot-high, 79-foot-long, 3-foot-deep metal sculpture spelling the word "newborn." On the day the country was established, citizens signed the sculpture. It is now part of the landscape in the new capital, Pristina.

At about the same time, in a different part of the world, Israel also was engaged in a "rebranding" effort. Just over 60 years since the nation's founding, Israel is trying to attract more visitors by rebranding as a "lifestyles-oriented destination." Israel's public relations problem is serious. Except for Iran, it has the lowest public perception of any country in the world. The gap between an advanced level of economic and social development and a low image creates a burden that hinders its attraction as a destination for tourism or economic activity. So Israel, in addition to launching a campaign called "Women of the Israeli Defense Forces" which ran in *Maxim,* a men's magazine, has country websites on MySpace and Facebook and a blog, Israeli.org. These efforts are intended to shift perceptions of Israel from lenses of war, occupation, and religion to "a human lens." In Kosovo, the task is to develop any perception of the country at all. Further, the country will need to dissociate itself from the violence that has plagued that part of the world for a number of years. However, on a positive note, the $5.9 million "Kosovo—The Young Europeans" branding campaign that was developed by the advertising agency BBR Saatchi & Saatchi won the top award in the nation branding category at the 2010 M&M Awards ceremony in London. According to the organizers of the competition, "the judges were particularly impressed by the 'genuinely intriguing' nature of the campaign, by the very cost effective activation, and by the results."

Source: Ron Friedman, "Re-branding Israel? If only I Could," *Jerusalem Post,* February 11, 2010, www.jpost.com/Israel/Article.aspx?id=168506 (accessed June 23, 2011); "Kosovo 'Nation Branding' Campaign Wins M&M Award," http://nation-branding.info/2010/10/09/kosovo-nation-branding-campaign-wins-mm-award/ (June 23, 2011); and David Kaufman, "Best Face Forward: How Israel, Approaching Sixty, Is Rebranding Itself to Attract More Visitors," *AdWeek,* March 17, 2008, pp. 20–21, http://nyi-www.brandweek.com/aw/content_display/esearch/e3i47dc2082d6980ced5f03bf7b4b0e4072?pn=3 (June 23, 2011).

# 6

## learning objectives

After reading this chapter, you should be able to:

**LO6-1** **Discuss** nationalization and privatization of business.

**LO6-2** **Explain** what terrorism is and the range of activities that terrorists can engage in, as well as countermeasures that companies and their employees might take.

**LO6-3** **Evaluate** the importance to business of government stability and policy continuity.

**LO6-4** **Explain** country risk assessment by international business.

**LO6-5** **Discuss** types of trade restrictions and the arguments for imposing them.

In many ways, the political climate of a country in which a business operates is as important as the country's topography, its natural resources, and its climate. Hospitable, stable governments can encourage business investment and growth despite geographic or weather obstacles and a scarcity of natural resources. The opposite is equally true. Some areas of the world that are relatively blessed with natural resources and manageable topography and weather have been little developed because of government instability. Occasionally, a country's government is hostile to investment in its territory by foreign companies, even though they might provide capital, technology, and training for development of the country's resources and people.

Many of the political forces with which business must cope have ideological sources, but there are a large number of other sources. These sources include nationalism, government-owned business, terrorism, and unstable governments, among other factors. The international company itself can also be a political force. Some firms have budgets or sales larger than the gross national income (GNI) of some of the countries with which they negotiate. Although budgets and GNIs do not translate directly into power, it should be clear that companies with bigger budgets and countries with bigger GNIs possess more assets and facilities with which to negotiate.

This chapter provides an indication of the types of risks political forces pose to private business. As we shall see, some of the risks can stem from more than one political force. We also look at some of the ways international trade is heavily influenced by political forces.

# Government Ownership of Business

One might assume that government ownership of the factors of production is found only in communist countries, but that assumption is not correct. From country to country, there are wide differences in the industries that are government-owned and in the extent of government ownership.

## WHY FIRMS ARE NATIONALIZED

Governments put their hands on firms for a number of reasons. Some of these reasons are (1) to extract more money from the firms, if the government suspects that the firms are concealing profits; (2) profitability—the government believes it can run the firms more efficiently and make more money; (3) ideology; (4) job preservation—to save jobs by putting dying industries on life-support systems; (5) because the government has pumped money into a firm or an industry, and control usually follows money; and (6) happenstance, as with the nationalization after World War II of German-owned firms in Europe.

## UNFAIR COMPETITION?

Where government-owned companies compete with privately owned companies, the private companies sometimes complain that the government companies have unfair advantages. Some of the complaints are that: (1) government-owned companies can cut prices unfairly because they do not have to make profits, (2) they get cheaper financing, (3) they get government contracts, (4) they get export assistance, and (5) they can hold down wages with government assistance.
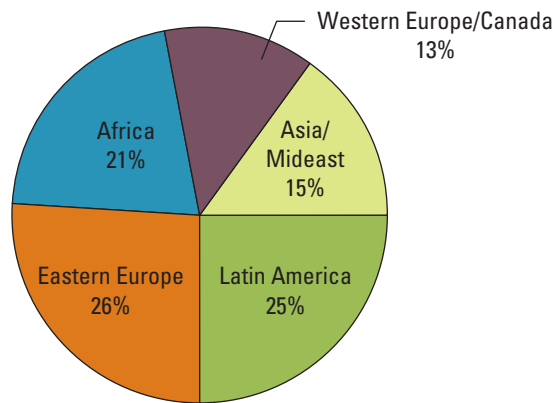
Another advantage state-owned companies may enjoy over privately owned business comes in the form of direct subsidies: payments by the government to those companies. The EU Commission has been trying to discourage such subsidy payments. For years it has required annual financial reports from state-controlled companies as part of a crackdown on the subsidies that can distort competition.

**privatization**
The transfer of public sector assets to the private sector, the transfer of management of state activities through contracts and leases, and the contracting out of activities previously conducted by the state

# Privatization

Britain's former prime minister, Margaret Thatcher, was a leader of the **privatization** movement. During her years in office, Thatcher decreased state-owned companies from a 10 percent share of Britain's GNP to 3.9 percent. She sold more than 30 companies, raising some $65 billion. Similarly, from 1975 to 1989, Chile's Pinochet sold government stakes in

FIGURE 6.1

Privatizations
by Region



Source: "Privatization Worldwide Summary," prepared for the Trans-national Corporations and Management Division of the United Nations. Used here by permission of the author, Michael S. Minor.

more than 160 corporations and 16 banks and more than 3,600 agro-industrial plants, mines and real estate, not including the return of property expropriated during the previous government of Salvador Allende.

## PRIVATIZATION ANYWHERE

Privatization does not always involve ownership transfer from government to private entities. Activities previously conducted by the state may be contracted out: Mozambique has contracted a British firm to run its customs administration, and Thailand has private companies operating some of the passenger trains of its state-owned railroad. Germany's *Deutsche Post* was privatized and is often counted as a privatization success story. In general, the solvency and stability of the banking sector were found to be improved by the privatization of industrial and commercial companies. Privatized companies have improved their profitability more rapidly, which has led to notable improvements in the banks' loan portfolios.[1]

Figure 6.1 shows privatization by geographic region. The percentages in the figure total 100 without reference to the United States; neither the U.S. government nor the individual state governments are participating substantially in the privatization trend.

## Government Protection

A historical function of government, whatever its ideology, has been the protection of the economic activities—farming, mining, manufacturing, and so forth—within its geographic area of control. These activities must be protected from attacks and destruction or robbery by bandits, revolutionaries, foreign invaders, or terrorists. In 1990, the Iraqi armed forces invaded Kuwait, quickly overwhelming the defenders of that smaller country.

The aftermath of this war demonstrates the influence of politics on business. In gratitude for American fighting in Desert Storm, Kuwait and other Gulf Cooperation Council countries—Saudi Arabia, Qatar, Bahrain, the United Arab Emirates, and Oman—bought some $36 billion of American arms. But in a 1997 competition to sell Kuwait 72 self-propelled howitzers, a Chinese company beat out an American company's widely considered superior versions. In private conversations, Kuwaiti officials said their reasons for buying Chinese had nothing to do with range, price, or accuracy and everything to do with politics. It seems China suggested it would withhold its support at the United Nations for extending trade sanctions against Iraq unless Kuwait gave the estimated $300 million order to the Chinese company. "Sometimes you get to a state when you feel you're being blackmailed," a senior Kuwaiti official said. "We lean toward the U.S. equipment, but we have to find a way to please the Chinese and not upset them in the Security Council."[2]

## Terrorism in Second Life



Terrorism has been around for decades in the real world. However, terrorism attacks are no longer exclusive to the real world. Recently, several attacks occurred in the virtual world environment called "Second Life." A group of dissatisfied older residents of the virtual world started to protest against the "authoritarian leadership" of the Second Life founding company Linden Labs. The group named themselves the Second Life Liberation Army (SLLA).

SLLA members were frustrated because of the rapid increase of newcomers and by the entrance of real-world companies into Second Life. As they claim, nobody asked them anything about the change that occurred and were made solely by Linden Labs. They're arguing that by being residents of this world, they should have more voice in decision making. They also made an official statement of demands:

> The establishment of basic "rights" for Second Life players. Having consulted widely we now believe the best vehicle for this is for Linden Labs to offer public shares in the company. We propose that each player is able to

---

**LO6-2 Explain**
what terrorism is and the range of activities that terrorists can engage in, as well as countermeasures that companies and their employees might take.

**terrorism**
Unlawful acts of violence committed for a wide variety of reasons, including for ransom, to overthrow a government, to gain release of imprisoned colleagues, to exact revenge for real or imagined wrongs, and to punish nonbelievers of the terrorists' religion

## TERRORISM

**Terrorism** involves unlawful acts of violence committed for a wide variety of reasons, including for ransom, to overthrow a government, to gain release of imprisoned colleagues, to exact revenge for real or imagined wrongs, and to punish nonbelievers of the terrorists' religion. Since at least the 1970s, various groups have hijacked airplanes, shot and kidnapped individuals, and bombed people and objects. Al Qaeda is by no means the only terrorist organization in the world. Among the better-known groups involved in terrorism are the Irish Republican Army (IRA), Hamas, Hezballah, Abu Nidal and other Islamic fundamentalist groups, the Basque separatist movement (ETA), the Japanese Red Army, the German Red Army Faction, and various terrorist organizations in Latin America.

A number of organizations rank countries and territories for their level of terrorism risk. For example, the 2010 Terrorism Risk Index from the global risk advisory company Maplecroft listed the 10 highest risk nations (in order) as Somalia, Pakistan, Iraq, Afghanistan, Palestinian Occupied Territory, Columbia, Thailand, Philippines, Yemen, and Russia.[3]

### Kidnapping for Ransom
Kidnapping is another weapon used by terrorists. The victims are held for ransom, frequently very large amounts, which provides an important source of funds for the terrorists. Estimates are that there are 8,000 to 10,000 ransom and kidnapping situations per year and that kidnappers take home up to $500 million. One firm engaged in corporate risk consulting notes that large ransoms can be physically daunting—$1 million in mixed $20 and $100 bills weighs about 66 pounds! Mexican kidnappings have increased by more than 300 percent since 2005, and pirates from Somalia are hijacking dozens of ships per year in the Indian Ocean, holding an estimated 700 hostages at a time.[4]

### Paying Ransom Becomes Counterproductive
The hostage business is booming. A remarkable deal concluded in the Philippines explains why.

buy one share for a set-price. This would serve both the development of the world and provide the beginnings of representations for avatars [residents of the virtual world] in Second Life.

The SLLA organized several terrorist attacks on various companies operating in SL. The attacks, which began in late 2006 included bombs planted outside the Reebok store; a bomb that hit the ABC headquarters; a helicopter that flew into the Nissan building; and forced entry into the American Apparel store, attacking several customers. Although there are no real victims in these cases, the goal is to create confusion that will cause unpleasant experiences for other residents and companies.

How did companies react? Some companies took the attacks seriously. In Nissan's case they responded similarly as they would in a real-world attack situation. Nissan online officials cleaned up the crime scene, removed the bodies, and put them in virtual coffins. Although they treated the attack seriously, they still did not close their business.

On the other hand, the American Apparel store closed its business and moved out. ABC took precautions in order to protect its sites, especially its most popular site called Sandbox. On that site, visitors are allowed to build objects, and ABC officials found that several objects were inappropriate for ABC. To prevent that, it started to monitor the site and visit it on a regular basis.

Companies that expand their business into Second Life are harmed by those attacks. Fearing broader impacts, the U.S. Congress held a hearing about a potential link between virtual worlds like Second Life and terrorism, including the potential to launder funds for terrorist organizations. More chillingly, some security experts believe that in the wake of the closure of training camps in Pakistan and elsewhere, the virtual world is being used as a training ground for future missions in "First Life"—the real world.

Source: Sharon Weinberger, "Congress Freaks Out over Second Life Terrorism," *Wired*, April 4, 2008, www.wired.com/dangerroom/2008/04/second-life/ (June 23, 2011); Preeti Aroon and Dean Takahashi, "Terrorists in Second Life," *Foreign Policy,* March–April 2008, p. 93; Iain Thomson, "Cyber-Terrorists Storm Second Life," *What PC?* February 22, 2007; Natali O'Brien, "Virtual Terrorists," July 31, 2007, www.theaustralian.com.au/news/features/virtual-terrorists/story-e6frg6z6-1111114072291 (accessed June 23, 2011); and Wayne Porter, "Exclusive Interview with Second Life Liberation Army and Reflections on Snow," December, 4, 2006, www.revenews.com/wayneporter/exclusive-interview-with-second-life-liberation-army-leader-slla/ (June 23, 2011).

Libya's Colonel Muammar Qaddafi, trying to shake off that country's pariah status, bought the release of several Western hostages held by a band of Islamist bandits in the Philippines. The price was about $1 million each. The kidnappers evidently learned two lessons: holding a few hostages keeps the army away, and grabbing more keeps the money rolling in. Within weeks after receiving the ransom money, the Philippine kidnappers bought new weapons and a new speedboat with which to capture more people to sell.[5] As an illustration of the global reach of terrorism, the Philippine group, which calls itself Abu Sayyaf, is thought to have links with al Qaeda.

### Countermeasures by Industry

Insurance to cover ransom payments, antiterrorist schools, and companies to handle negotiations with kidnappers have come into being. The insurance, which is called KRE (kidnap, ransom, and extortion) and generates $500 million in premiums each year, can pay for the ransom, the fees of specialist negotiators, the salary of the hostage, and counseling for the victim and the family. Fees for the security of CEOs have ranged up to $1.7 million per year for Larry Ellison, former chairman of Oracle Corp., down to $239 for a home-alarm monitoring service for the chair of Valero Energy Corp.[6]

As kidnapping and extortion directed against businesses and governments have become common fund-raising and political techniques for terrorists, insurance against such acts has grown into a multimillion-dollar business. The world's largest kidnapping and extortion underwriting firm is located in London. The firm, Cassidy and Davis, says that it covers some 9,000 companies. Cassidy and Davis runs antiterrorism training courses for executives, with subjects ranging from defensive driving techniques—escape tactics and battering through blockades—to crisis management. Country-by-country risk analyses are instantly available on international computer hookups.

Antiterrorist surveillance detection and evasive driving training are also available. International Training Inc. (ITI) teaches some 5,000 students each year how to frustrate would-be assassins and kidnappers. The students are company executives and high-wealth individuals. To enhance your chances of success with your driver's training, you can harden your automobile. For example, Carat Security Group offers multilayered ballistic

glass, protected car floors, run-flat tires and protected fuel tanks for the automobiles of potential victims. It cites the recent violence in Mexico as a boon to the armored car industry.

**Chemical and Biological Terrorism**   In 1995, the Aum Shin Rikyo cult launched a nerve gas attack in the Tokyo subway that killed 12 people and injured 5,500, many of whom suffered severe nerve damage. A malfunction in the bomb delivery system is believed to have prevented thousands of additional casualties. Sarin was the nerve gas used in the Tokyo subway attack. Chemical information about sarin is available on the Internet, making threats possible from self-taught terrorists anywhere.

# Government Stability

LO6-3 **Evaluate** the importance to business of government stability and policy continuity.

**stability**
Characteristic of a government that maintains itself in power and whose fiscal, monetary, and political policies are predictable and not subject to sudden, radical changes

**instability**
Characteristic of a government that cannot maintain itself in power or that makes sudden, unpredictable, or radical policy changes

Government **stability** can be defined in two ways. One can speak of either a government's ability to maintain itself in power, or the stability or permanence of a government's policies. It is safe to generalize that business prospers most when there is a stable government with permanent—or gradually changing—policies. **Instability** on the other hand is when a government cannot maintain itself in power or makes sudden, unpredictable, or radical policy changes. It is hard for business to flourish when government is unstable.

**Stability and Instability**   **Example of Zimbabwe** Zimbabwe was a relatively rich African country that was a net exporter of food. After a successful liberation movement against white-minority rule, the Zimbabweans elected resistance leader Robert Mugabe as prime minister in 1980. In the 1990s he decided to seize land and equipment from big farms and redistribute them to small landholders. People close to Mugabe were able to get the best of the land, but they have failed to work it and produce food.

There is now a severe food shortage, and the country depends on foreign aid. But the aid-donating countries have grown impatient with corruption and are cutting back their aid. It is also generally conceded that Mugabe stole the presidential election in 2008. The resulting instability caused a loss of confidence by potential foreign investors, so money, expertise, and technology are no longer coming in. Poverty and starvation are the lot of many Zimbabweans.

# International Companies

International business is not merely a passive victim of political forces. It can be a powerful force in the world political arena. About half of the world's 100 biggest economic units are firms, not nations.

International companies (ICs) repeatedly make decisions about where to invest, where to conduct research and development, and where to manufacture products. The country or area in which an investment is made or where a laboratory, research facility, or manufacturing plant is located can benefit as jobs are created, new or improved technology becomes available, or products are produced that can be exported or substituted for imports.

Of course, the IC will seek the country and area in which it can operate most beneficially and profitably. It will negotiate with the national and local areas in which it is considering an investment or plant location in efforts to maximize benefits such as tax breaks, infrastructure improvements, and worker training programs.

The financial size of many ICs provides them with a strong negotiating position. And an IC's power need not rest solely on size. It can come from the possession of capital, technology, and management skills, plus the capability to deploy those resources around the world. An IC may have the processing, productive, distributive, and marketing abilities necessary for the successful utilization of raw materials or for the manufacture, distribution, and marketing of certain products. Those abilities are frequently not available in developing countries. Recognition of the desirability of IC investments is growing.[7] For example, China has operations in a wide variety of African states, such as oil exploration in Chad, the Congo, and Guinea, and building projects in Ivory Coast, Nigeria, and Angola.

| TABLE 6.1 | Country Risk Rankings | | |
|---|---|---|---|
| **Economist.com Country Operational Risk, February 2009** | | **Euromoney Country Risk Rankings, March 2011** | |
| **1 equals highest level of operational risk** | | **Higher numbers represent higher levels of country risk; ranks of 100 reviewed nations** | |
| 1 | Sudan | 100 | Mozambique |
| 2 | Kyrgyz Republic | 99 | Algeria |
| 2 | Kenya | 98 | Belarus |
| 2 | Nigeria | 97 | Seychelles |
| 5 | Chad | 96 | Paraguay |
| 6 | Ecuador | 95 | Nigeria |
| 7 | Eritrea | 94 | Mongolia |
| 8 | Tajikistan | 93 | Venezuela |
| 9 | Venezuela | 92 | Albania |
| 10 | Uzbekistan | 91 | Lebanon |
| 11 | Turkmenistan | 90 | Argentina |
| 12 | Zimbabwe | 89 | Ukraine |
| 13 | Myanmar | 88 | Egypt |
| 14 | Iraq | 87 | Macedonia |
| 14 | Guinea | 86 | Serbia |

Source: Adapted from "Risky Business: Doing Business Is Getting Riskier in Many Countries around the World," *The Economist*, March 16, 2009, www.economist.com/node/13251992?story_id5E1_TPNVTJJN&CFID5172695079&CFTOKEN576845053 (June 23, 2011); and "Country Risk March 2011: Country Rankings and Acknowledgements," *Euromoney*, www.euromoney.com/Article/2773235/Country-risk-March-2011-Country-rankings-and-acknowledgements.html (June 23, 2011).

# Country Risk Assessment

The political events of recent years have caused firms to concentrate much more on country risk assessment. **Country risk assessment (CRA)** is an evaluation, conducted by a bank or business, that assesses a country's economic situation and policies and its politics to determine how much risk exists of losing an investment. Because of recent turmoil, firms that had already done CRA updated and strengthened the function, and many other companies began to engage in the practice.

## TYPES OF COUNTRY RISKS

Country risks are increasingly political in nature. Among them are wars, revolutions, and coups. Less dramatic, but nevertheless important for businesses, are government changes caused by election of a new government that may be hostile to private business and particularly to foreign-owned business.

The risks may be economic or financial. Countries may have persistent balance-of-payments deficits or high inflation rates. Repayment of loans may be questionable. Labor conditions may cause investors to pause. Labor productivity may be low, or labor unions may be militant. Laws may be changed in regard to such subjects as taxes, currency convertibility, tariffs, quotas, and labor permits. The chances for a fair trial in local courts must be assessed. And terrorism may be present. If it is, can the company protect its personnel and property?

**country risk assessment (CRA)** An evaluation, conducted by a bank or business, that assesses a country's economic situation and policies and its politics to determine how much risk exists of losing an investment or not being paid

## INFORMATION CONTENT FOR CRA

The types of information a firm will need to judge country risks vary according to the nature of its business and the length of time required for the investment, loan, or other involvement to yield a satisfactory return.

**Nature of Business**  Consider the needs of a hotel company compared with those of mining companies. Sometimes variations exist between firms in the same industry or on a project-to-project basis also. The home country of the company may be a factor: does the host country bear a friendly attitude toward the home country or not?

**Length of Time Required**  Export financing usually involves the shortest period of risk exposure. Typically, payments are made within 180 days—usually less—and exporters can get insurance or bank protection.

Bank loans can be short, medium, or long term. However, when the business includes host-country assembly, mixing, manufacture, or extraction of oil or minerals, long-term commitments are necessary. With long-term investment or loan commitments, risk analysis entails inherent problems that cannot be resolved. Most such investment opportunities require 5, 10, or more years to pay off. But the utility of risk analyses of social, political, and economic factors decreases rapidly over longer time spans.

## WHO DOES COUNTRY RISK ASSESSING?

General or specific analyses; macro or micro analyses; and political, social, and economic analyses have been conducted for years. The Conference Board located bits and pieces of CRA being performed in various company departments—for example, the international division and the public affairs, finance, legal, economics, planning, and product-producing departments. Sometimes the people in one department were unaware that others in the company were similarly involved.

Outside consulting and publishing firms are another source of country risk analysis. As CRA has mushroomed in perceived importance, a number of such firms have been formed or have expanded. Some of the better-known outside consulting and publishing firms for CRA include:

- Business Environment Risk Intelligence (BERI) S.A.
- Business Monitor International.
- Coface.
- Control Risk Solutions.
- Economist Intelligence Unit (EIU).
- Euromoney.
- Eurasia Group.
- STRATFOR.
- *Harvard Business Review*'s Global Risk Navigator.
- The PRS Group.
- Standard and Poor's Rating Group.
- Moody's Investor Services.

Instead of or in addition to using outside consultants, a number of firms have hired such experts as international business or political science professors or retired State Department, CIA, or military people.

# Trade Restrictions

**LO6-5 Discuss** types of trade restrictions and the arguments for imposing them.

Perhaps no foreign event (except fashion shows) is the subject of more writing by journalists than trade. For example, we are currently witnessing trade restrictions on rice, even as world food prices may increase as much as 40 percent. Infant industry arguments are being made in China; genetically modified and related food restrictions have appeared in Europe. Although we have strong theory in support of free trade's benefits, the WTO is experiencing difficulty getting the trade negotiations completed successfully due to political barriers, and this is likely to be exacerbated in coming years with more inflationary pressure, climate-related problems, and resource limitations.

The government officials who make decisions about import restrictions are particularly sensitive to the interest groups that will be hurt by the international competition. These groups consist of a small, easily identified body of people or organizations—as contrasted to the large, widespread number of consumers who typically benefit from free trade. In political debates over a proposed import restriction, the protectionist group will usually be united in exerting pressure on government officials, whereas pro-trade consumers rarely mount an organized effort.

## ARGUMENTS FOR TRADE RESTRICTIONS

A number of arguments have traditionally been presented in support of efforts to restrict trade. We address several of the most common such arguments here, as well as associated rebuttal arguments.

### National Defense

The national defense argument for trade restrictions suggests that certain industries need protection from imports because they are vital to security and must be kept operating even though they are not competitive with foreign suppliers. For example, the U.S. shoe industry requested that Congress impose restrictions because growing reliance on imported footwear was "jeopardizing the national security of the United States." Speaking to the Armed Services Committee of the U.S. Congress, the president of the Footwear Industry of America stated: "In the event of war or other national emergency, it is unlikely that the domestic footwear industry could provide sufficient footwear for the military and civilian population. . . . Improper footwear can lead to needless casualties and turn sure victory into possible defeat." A Defense Department spokesman said he knew of no plan to investigate the prospects of a wartime shoe crisis. Furthermore, federal law already requires the armed forces to buy U.S.-made footwear exclusively.[8]

Critics of the defense argument claim it would be far more efficient for the government to subsidize a number of firms to maintain sufficient capacity for wartime use only. Moreover, a subsidy would clearly indicate to taxpayers the cost of maintaining these companies in the name of national security—something that some interests may not want known. Currently, most American ocean shipping companies receive government subsidies without which they could not remain in business because of the competition from foreign firms with lower operating costs. In this way, we have a merchant marine ready in case of hostility, and we know what this state of readiness costs us.

Similar arguments have been offered in support of bans on the export of advanced technologies. Such bans, proponents argue, prevent valuable technologies from being used to strengthen competitors, especially militarily. However, these bans can reduce export revenues for the country's manufacturers by closing off potential markets. The bans can also impede efforts to sustain international market share and fund continued innovation, enabling competitors from other nations to improve their competitiveness.

### Sanctions to Punish Offending Nations

A related argument for imposing trade restrictions is to inflict economic damage on other nations in order to punish them or otherwise encourage them to modify behavior. A common approach is to pass legislation that prohibits trade with the "offending" nation.

But sanctions not only seldom achieve their goal of forcing change in the targeted country; they also tend to produce collateral economic damage in the nations applying them.[9] Economic sanctions during the 1990s may have cost the United States some $15 billion to $23 billion annually in exports, in addition to losses resulting from restrictions on foreign direct investment, capital flows, tourism, and other sources of income or output.[10] During the time, that the United States was imposing sanctions on Iraq that prohibited American firms from doing business there, companies from France, Russia, and other nations were generating billions of dollars from business contracts from which American firms were excluded.

### Protect Infant (or Dying) Industry

Advocates for the protection of an infant industry may claim that in the long run the industry will have a comparative advantage but

that firms need protection from imports until the required investment capital is obtained, the labor force is trained, production techniques are mastered, and economies of scale are achieved. Without the protection, advocates argue, a firm will not be able to survive because lower-cost imports from more mature foreign competitors will underprice it in its local market.

Efforts to protect emerging industries are not limited to developing nations, of course. For example, former Representative Ken Salazar of Colorado argued for the maintenance of a protective 54-cents-a-gallon import duty on foreign-produced ethanol, including imports from low-cost producer Brazil, in order to give "our infant industries a greater chance to grow." The cost of subsidizing the American ethanol industry is estimated at $1 billion to $5 billion annually.[11]

A related argument concerns the protection of a "dying" industry, one threatened by an onslaught of imports that endangers the survival of domestic companies and the jobs they provide. Under this argument, it takes time to make the necessary adjustments to move labor and capital out of the industry and into other sectors. Protecting the industry from imports can therefore facilitate a smoother transition. This logic has been used in justifying protection for textiles and footwear in the United States and Europe. Other aid, such as subsidies for relocating to different geographic areas and for providing assistance to displaced workers, may also be part of the proposed solution.

### Protect Domestic Jobs from Cheap Foreign Labor

Protectionists who use this argument usually compare lower foreign hourly wage rates to those paid in their home country. They conclude that foreign exporters can flood the home country's market with low-priced goods, and thus simultaneously eliminate jobs of home-country workers. The first fallacy of this argument is that wage costs are neither all of the production costs nor all of the labor costs, so a comparison merely based on relative hourly wages would be misleading.

Second, the productivity per worker may be much greater in richer countries because of more capital per worker, superior management, and advanced technology. As a result, the labor cost component of the goods being produced could be lower even though wages are higher.

### Scientific Tariff or Fair Competition

Supporters of this argument say they believe in fair competition. They simply want an import duty that will bring the cost of the imported goods up to the cost of the domestically produced article. This will eliminate any "unfair" advantage that a foreign competitor might have because of superior technology, lower raw material costs, lower taxes, or lower labor costs. It is not their intent to ban exports; they wish only to equalize the process for "fair" competition. If this were law, no doubt the rate of duty would be set to protect the least efficient producer, thereby enabling the more efficient domestic manufacturers to earn large profits. The efficient foreign producers would be penalized, and, of course, their comparative advantage would be nullified. The impact on consumers might also be viewed as unfair, since the import duty would result in an increase in the prices that they pay.

### Retaliation

Representatives of an industry whose exports have had import restrictions placed on them by another country may ask their government to retaliate with similar restrictions. An example of how retaliation begins is the ban by the European Union (EU) on imports of hormone-treated beef from the United States. Because the use of hormones in animal production is considered a health hazard in the EU, the European Union closed its market to American beef (12 percent of total U.S. meat exports) in 1988. American beef producers complained that no scientific evidence supported the claim, and the United States promptly retaliated by putting import duties on about $100 million worth of EU products, including boneless beef and pork, fruit juices, wine coolers, tomatoes, French cheese, and instant coffee. The EU then threatened to ban U.S. shipments of honey, canned soybeans, walnuts, and dried fruit worth $140 million. In reply, the United

States announced that it would follow the EU ban with a ban on all European meat. If that had happened, about $500 million in U.S.–EU trade would have been affected.

Generally, disputes like these go to the World Trade Organization (WTO). After having its beef banned by the EU for eight years, the United States launched a formal dispute settlement procedure with the WTO in May 1996, challenging the ban. When the WTO Appellate Body announced that the EU ban had been imposed without reason, the EU declared that it would implement the Appellate Body ruling, but it did not comply by the date set by the WTO. The WTO authorized the United States to retaliate, resulting in imposition of a 100 percent import duty on a list of EU products with an annual trade value of $116.8 million. In 2003, the EU announced a new directive that it asserted was in compliance with the WTO's ruling, although it still banned most American and Canadian beef. The United States claimed the new EU guidelines still violated WTO requirements and maintained sanctions. In 2009, the two sides agreed that the Americans would lift sanctions gradually, corresponding with a phased increase in allowed importation into the EU of hormone-free beef from the United States. In 2011, a year ahead of schedule, the United States ended retaliatory sanctions on EU goods. The EU still has until 2012 to honor its part of the deal, or else face a renewal of sanctions.[12]

**Dumping**    Retaliation also occurs for **dumping.** The WTO defines dumping as selling a product abroad for less than (1) the average cost of production in the exporting nation, (2) the market price in the exporting nation, or (3) the price to third countries. A manufacturer may dump products to sell excess production without disrupting prices in its domestic market, as a response to cyclical or seasonal factors (e.g., during an economic downturn or at the end of a fashion season), or as a way to raise market share. A manufacturer may also lower its export price to force the importing nation's domestic producers out of business, expecting to raise prices once that objective is accomplished. This latter behavior is called *predatory dumping.*
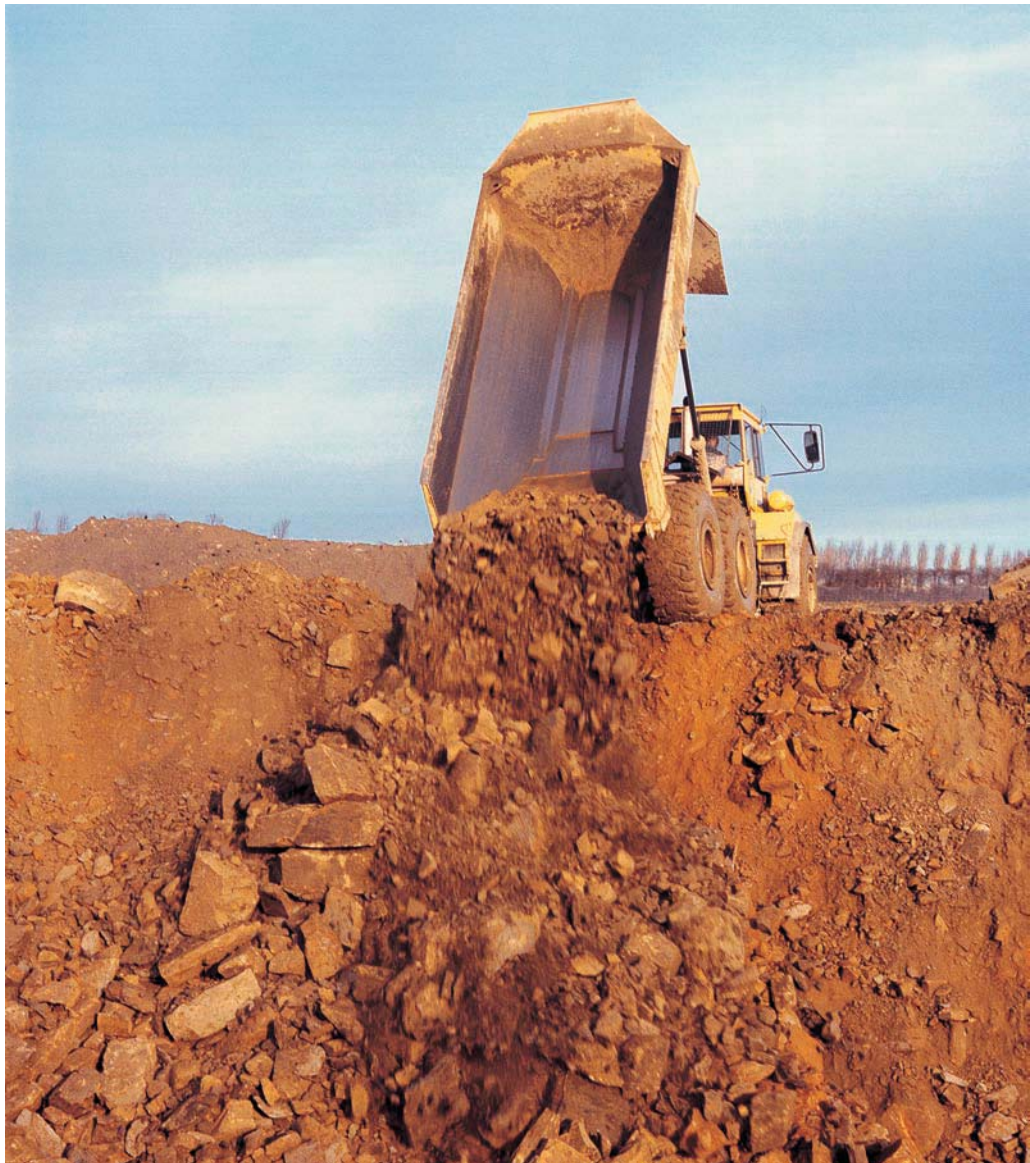
The United States became the first country to prohibit dumping of foreign goods into its own market in 1916 (there is no U.S. law prohibiting American firms from dumping their goods abroad, though). Dumping is now within the domain of the WTO, which is the recipient of many related complaints through appeals by countries opposing the imposition of antidumping protections against their companies. Most governments retaliate when dumping is perceived to be harming local industry

**dumping**
Selling a product abroad for less than the cost of production, the price in the home market, or the price to third countries

**New Types of Dumping**    There are at least five new kinds of dumping for which fair-trade lobbies consider sanctions to be justified in order to level the playing field for international trade. In reality, these special-interest groups calling for level playing fields are seeking to raise the production costs of their overseas competitors to protect local high-cost producers. The classes of dumping include:

1. *Social dumping*—unfair competition caused by firms, usually from developing nations with lower labor costs and poorer working conditions, which undermines social support systems, including worker benefits.
2. *Environmental dumping*—unfair competition caused by a country's lax environmental standards. It has been argued that globalization provides incentives to national governments to set weak environmental policies, particularly for industries whose plants can be relocated internationally.
3. *Financial services dumping*—unfair competition caused by a nation's low requirements for bank capital-asset ratios.
4. *Cultural dumping*—unfair competition caused by cultural barriers aiding local firms.
5. *Tax dumping*—unfair competition caused by differences in corporate tax rates or related special breaks. Slovakia was accused of tax dumping because its low corporate tax rate and generous incentive policies were perceived to give it an advantage over other European nations in attracting investment from multinationals.[13]
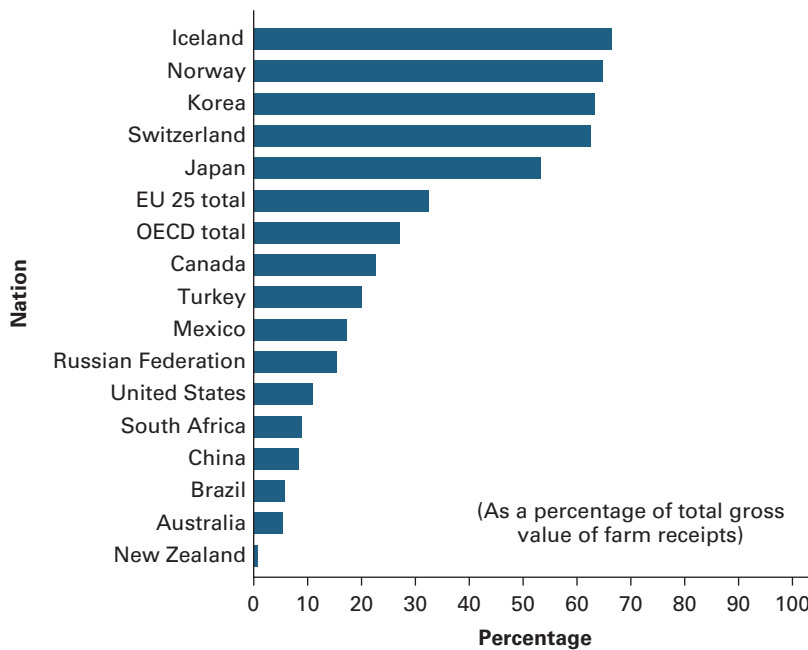
**subsidies**
Financial contributions, provided directly or indirectly by a government, which confer a benefit, including grants, preferential tax treatment, and government assumption of normal business expenses

**countervailing duties**
Additional import taxes levied on imports that have benefited from export subsidies

Subsidies    Another cause of retaliation may be **subsidies** that a government makes to a domestic firm either to encourage exports or to help protect it from imports. Some examples are cash payments, government participation in ownership, low-cost loans to foreign buyers and exporters, and preferential tax treatment. For example, as shown in Figure 6.2, the OECD nations provide billions of dollars per year in subsidies to their farmers. Perhaps the greatest damage caused by this assistance is its effect on the millions of farmers in the poorest nations. High customs duties restrict access to wealthy countries' markets, while subsidized overproduction in developed countries artificially depresses prices in world markets, harming the income of farmers in poorer nations. Most of the agricultural subsidies in developed countries go to a small percentage of recipients, usually large enterprises. The nearby Global Debate box provides a more detailed example of subsidies for sugar producers in the United States.

Competitors in importing nations frequently ask their governments to impose **countervailing duties** to offset the effects of a subsidy. In the United States, when the Department of Commerce receives a petition from an American firm claiming that imports from a particular country are subsidized, it first determines whether a subsidy actually was given. If so, Commerce imposes countervailing duties equal to the subsidy's amount.

FIGURE 6.2

(As a percentage of total gross value of farm receipts)

Source: Adapted from OECD, *Agricultural Policies in OECD Countries: Monitoring and Evaluation 2007* (Paris: OECD, 2007), www.oecd.org/document/0/0,3343,en_2649_33727_39508672_1_1_1_1,00.html (June 23,2011).

# GLOBAL DEBATE

## Sugar Subsidies: Sweet for Producers, Not for Consumers

Although they lack comparative advantage in sugar production, the United States, Japan, and the EU, among others, have maintained strong protection for their domestic sugar industries. A World Bank report called sugar the "most policy-distorted of all commodities." Protectionism by developed countries harms foreign sugar producers, many of which are poor farmers in developing countries, by reducing demand and prices for their product. Oxfam estimated, for example, that EU sugar supports had caused Malawi to experience losses that exceeded its total budget for primary health care. Before being forced by the WTO into making changes in November 2005, the EU maintained domestic sugar prices that were triple world market prices.

In the United States, sugar tariffs have been in place since 1789. Imports are allocated through tariff-rate quotas among 40 nations and limited to about 15 percent of the U.S. market, except in years when there is a shortfall in the U.S. domestic supply, as in 2005 after Hurricane Katrina. High price supports result in overproduction of sugar domestically, yet at the same time the price of raw sugar in the United States has averaged more than double the world price during the past decade, costing American consumers and businesses an estimated $4 billion annually. The benefits are highly concentrated among a small number of companies. A mere 1 percent of sugar growers enjoys 42 percent of the benefits from protectionist U.S. sugar policies.



Nicaraguan Jackson Riveras carries a load of freshly cut sugarcane on a plantation near Turrucares of Alajuela, Costa Rica. Like many Nicaraguan immigrants, Ramirez came to Costa Rica to work the harvest season in order to earn higher wages and send money back to his family.

*(continued)*

Excess sugar production also contributes to environmental problems. In Florida, for example, pollution and disruption of water flows from sugar production have been cited as a major contributor to environmental degradation of the Everglades. Similar pollution concerns have been voiced in South Texas, where the annual "burn" sends burnt chaff into the sky.

Mechanization has eliminated the labor intensity of producing sugar from sugar beets or sugarcane in the United States. Sugar is produced in 18 states and supports 146,000 American jobs, although only about 60,000 people now work directly in the production or refining of sugar. Movement to free trade in sugar would result in an estimated loss of fewer than 2,500 workers in the sugar industry, meaning that the cost for each protected job is more than $1.5 million. In addition, protection of the U.S. sugar industry has cost thousands of jobs in other sectors, such as food and beverage manufacturing. For example, sugar accounts for 32.7 percent of the total cost of producing breakfast cereals, and high sugar prices led to the loss of an estimated 112,000 jobs at sugar-consuming companies between 1997 and 2009. High sugar prices were also a major factor in companies' decisions to relocate operations to non-U.S. sites, especially Canada and Mexico, contributing to an increase in imports of sugar-containing products. As one Commerce Department executive said, "We are seeing U.S. jobs move to countries that don't have the competitive disadvantage of high sugar prices that we face in the United States."

Efforts to reform protection of the sugar industry have made limited progress, at least partly due to the strength of the sugar lobby. Sugar accounts for less than 1 percent of U.S. agricultural sales but an estimated 17 percent of all agricultural political contributions since 1990. "It's a very effective lobby," commented Claude Barfield of the American Enterprise Institute. "They've traditionally given a lot of money to both parties." Sugar lobbying resulted in the complete exclusion of sugar from the U.S.–Australia free trade agreement, the first bilateral trade treaty in which the United States required that a product be entirely excluded—and a dangerous precedent.

However, change may yet occur. In 2008, the United States and Mexico finally ended their decade-long battle over access to the U.S. sugar market under NAFTA, with all barriers to trade in sugar being removed between the two countries. In 2011, legislation was introduced into the U.S. Congress to completely eliminate sugar subsidies, although the likelihood of its passage was questioned by many.

Source: Bill Straub, "Lugar Again Sets Sights on Sugar Subsidies," *Evansville Courier & Press*, www.courierpress.com/news/2011/apr/03/no-headline---04a0xsugar/ (June 23, 2011); Investors.com, "Close the Candy Store," April 12, 2011, www.investors.com/NewsAndAnalysis/Article/568924/201104121859/Close-The-Candy-Store.aspx (June 23, 2011); Mary Barley, "Big Sugar and the Everglades," *The Gainesville Sun*, April 8, 2011, www.gainesville.com/article/20110408/NEWS/110409559/-1/news?p=all&tc=pgall&tc=ar (June 23, 2011); Michael Schroeder, "Sugar Growers Hold Up Push for Free Trade," *The Wall Street Journal*, February 3, 2004, p. A13; and Oxfam International, "Dumping on the World: How EU Sugar Policies Hurt Poor Countries," March 2004.

**Other Arguments**   The arguments we have examined are probably the ones most frequently given in support of trade restrictions. Others include the use of protection from imports to (1) permit diversification of the domestic economy or (2) improve the balance of trade. You should have gathered from this discussion that protection from imports generally serves the narrow interests of a special-interest group at the expense of many. Although the application of trade restrictions can sometimes buy time for the protected industry to modernize and become more competitive in the world market, a real danger exists that a nation's trading partners will retaliate with restrictions of their own, causing injury to industries that have received no protection. Let's examine these restrictions, beginning with tariff barriers.

## TARIFF BARRIERS

**tariffs**
Taxes on imported goods for the purpose of raising their price to reduce competition for local producers or stimulate local production

**Tariffs,** or import duties, are taxes levied on imported goods primarily for the purpose of raising their selling price in the importing nation's market to reduce competition for domestic producers. A few smaller nations also use them to raise revenue on both imports and exports. Exports of commodities such as coffee and copper are commonly taxed in developing nations. However, imposition of tariffs can result in retaliation that is harmful rather than helpful for a country and its well-being.

For example, in the late 1920s, declining economic fortunes caused American farmers to lobby Congress for tariff protection on agricultural products. Over time, more domestic producers joined with agricultural interests, seeking their own protection from foreign competitors. The resulting legislative proposal increased tariffs for more than 20,000 items across a range of industries. The broad support for the legislation caused the Democratic and Progressive parties to join the Republicans on October 28, 1929, in supporting the Smoot-Hawley Tariff Act to establish some of the highest levels of tariffs ever imposed.

That day the stock market crashed, falling 12 percent. In the following months, 34 foreign governments filed protests against Smoot-Hawley. Nevertheless, on June 17, 1930, President Herbert Hoover signed the bill. The result was a trade war that engulfed most of the world's economies. World trade plummeted from $5.7 billion in 1929 to $1.9 billion in 1932, unemployment skyrocketed, and the world entered a decade-long economic depression.

**Ad Valorem, Specific, and Compound Duties**   Import duties are (1) ad valorem, (2) specific, or (3) a combination of the two called compound. An **ad valorem duty** is stated as a percentage of the invoice value of the product. For example, the U.S. tariff schedule states that flavoring extracts and fruit flavors not containing alcohol are subject to a 6 percent ad valorem duty. Therefore, when a shipment of flavoring extract invoiced at $10,000 arrives in the United States, the importer is required to pay $600 to U.S. Customs before taking possession of the goods. A **specific duty** is a fixed sum of money charged for a specified physical unit of the product. A company importing dynamite in cartridges or sticks suitable for blasting would have to pay $0.37 per pound irrespective of the invoice value. When the flavoring extracts and fruit flavors just mentioned contain more than 50 percent alcohol by weight, they are subject to a specific duty of $0.12 per pound plus a 3 percent ad valorem. Thus, on a $10,000 shipment weighing 5,000 pounds, the importer would have to pay a **compound duty** of $900 [($.12 $\times$ 5,000  pounds) + (0.03 $\times$ $10,000) = $600 + $300]. Note that in an inflationary period, a specific duty soon loses its importance unless changed frequently, whereas the amount collected from an ad valorem duty increases as the invoice price rises. Sometimes, however, an exporter may charge prices so much lower than domestic prices that the ad valorem duty fails to close the gap. Some governments set *official prices* or use *variable levies* to correct this deficiency.

**Official Prices**   Official prices are included in the customs tariff of some nations. The official price guarantees that a certain minimum import duty will be paid irrespective of the actual invoice price. It thwarts a fairly common arrangement that numerous importers living in high-duty nations have with their foreign suppliers, whereby a false low invoice price is issued to reduce the amount of duty to be paid. The importer sends the difference between the false invoice price and the true price separately.

**Variable Levy**   One form of **variable levy,** which guarantees that the market price of the import will be the same as that of domestically produced goods, has been used by the EU for imported grains. Calculated daily, the duty level is set at the difference between world market prices and the support price for domestic producers.

**Lower Duty for More Local Input**   Import duties are set by many nations in such a way that they encourage local input. For example, the finished product ready for sale to the consumer may have a 70 percent duty. However, if the product is imported in bulk so that it must be packaged in the importing nation, the duty level may be 30 percent. To encourage some local production, the government may charge only a 10 percent duty on the semifinished inputs. These situations can provide opportunities for foreign manufacturers of low-technology products, such as toiletries, to get behind a high-tariff wall with very modest investments.

When tariffs are assessed at very low rates, they are sometimes referred to as *nuisance tariffs*. That is because importers are still required to go through the frequently lengthy process of paying these tariffs, even though their low levels may no longer serve their original intention, such as protecting domestic producers.

## NONTARIFF BARRIERS

**Nontariff barriers (NTBs)** are all forms of discrimination against imports other than the import duties we have been examining. As nations reduced import duties, nontariff barriers assumed greater relative importance, and their use has been increasing. For example,

---

**ad valorem duty**
An import duty levied as a percentage of the invoice value of imported goods

**specific duty**
A fixed sum levied on a physical unit of an imported good

**compound duty**
A combination of specific and ad valorem duties

**variable levy**
An import duty set at the difference between world market prices and local government-supported prices

**nontariff barriers (NTBs)**
All forms of discrimination against imports other than import duties

government-required testing and certification requirements have increased exponentially since the mid-1990s. NTBs can take many forms, including the quantitative and nonquantitative ones discussed next, and the additional costs they impose on producers and exporters help to discourage trade.

Quantitative    One type of quantitative barrier is **quotas,** which set numerical limits for specific kinds of goods that a country will permit to be imported during a specified period. If the quota is *absolute,* once the specified amount has been imported, further importation for the rest of the period (usually a year) is prohibited. Quotas are generally *global;* that is, a total amount is fixed without regard to source. They may also be *allocated,* in which case the government of the importing nation assigns quantities to specific countries. The United States allocates quotas for specific tonnages of sugar to 40 nations. Some goods are subject to *tariff-rate quotas,* which permit a stipulated amount to enter duty-free or at a low rate, but when that amount is reached, a much higher duty is charged for subsequent importations.

Some producers have used transshipping to evade allocated quotas. In such cases, the finished goods are first shipped to a country with an unfilled quota, where the goods are labeled as products of that country, and then shipped to the quota-imposing nation. Prior to the ending of the Multi-Fiber Agreement in 2004 that limited textile imports from other nations, this deceptive labeling scheme was estimated to have brought $2 billion in illegal clothing imports from China into the United States annually. Gitano, for example, pled guilty to charges of fraud for importing Chinese blouses labeled "Made in the Maldives Islands."

For many years there has been an agreement among nations against imposing quotas unilaterally on goods (except agricultural products). Therefore, governments have negotiated **voluntary export restraints (VERs)** with other countries (e.g., the Japanese government established a VER to restrict the number of automobiles that its manufacturers could export to the United States annually, and the Canadian government agreed to a VER to limit the amount of Canadian lumber to be exported to the United States).

Orderly Marketing Arrangements    **Orderly marketing arrangements** are VERs consisting of formal agreements between the governments of exporting and importing countries to restrict international competition and preserve some of the national market for local producers. Usually, they stipulate the size of the export or import quotas that each nation will have for a particular good.

Nonquantitative Nontariff Barriers    Many international trade specialists claim that the most significant nontariff barriers are the nonquantitative type. Governments have tended to establish nontariff barriers to obtain the protection formerly afforded by import duties. A study of nonquantitative barriers revealed more than 800 distinct forms, which may be classified under three major headings: (1) direct government participation in trade, (2) customs and other administrative procedures, and (3) standards.

1. *Direct government participation in trade.* The most common form of direct government participation is the subsidy. Besides protecting industries through subsidies, as was mentioned earlier, nearly all governments subsidize agriculture. Agricultural support programs are often promoted as being targeted toward protecting smaller farms and traditional rural economies. However, in most OECD nations, the largest 25 percent of farms receive between 60 and 80 percent of the total level of agricultural support.[14]

*Government procurement policies* are also trade barriers because they usually favor domestic producers and restrict purchases of imported goods by government agencies. Policies may also require that products purchased by government agencies have a stipulated minimum *local content.* Since the WTO Government Procurement Agreement went into effect, most nations have opened their government business to foreign bidders

to comply with its requirements. However, as noted by the EU, the American government still has policies in place that may substantially interfere with international trade. For example, similar to practices in Canada and elsewhere in the world, the Buy America Act has a range of measures that either prohibit public sector organizations from purchasing from foreign suppliers of goods or services or hinder such purchases through mechanisms such as requirements for local content or the provision of advantageous pricing terms for American suppliers. The Department of Defense, which is the U.S. government's largest public procurement agency, excludes foreign suppliers from many contracts.[15]

2.  *Customs and other administrative procedures.* These barriers cover a large variety of government policies and procedures that either discriminate against imports or favor exports. For example, in China, a product being imported may be subject to different rates of duty, depending on the port of entry and an arbitrary determination of the customs value. Because of this flexibility, customs charges often depend on negotiations between Chinese customs officials and managers. It is alleged that corruption is often involved.[16]

    Governments have also found ways to discriminate against the exportation of services. When serving international markets, airlines face a number of situations in which the national airline receives preferential treatment, such as in the provision of airport services, airport counter locations, and number of landing slots. Other examples of discrimination are the Canadian government's giving tax deductions to local businesses that advertise on Canadian TV, but not doing so when they use American stations across the border, and Australia's requiring that television commercials be shot in Australia.

3.  *Standards.* Both governmental and private standards to protect the health and safety of a nation's citizens certainly are desirable, but for years exporting firms have been plagued by many standards that are complex and discriminatory. For example, the European Parliament passed biotech food labeling requirements that impose mandatory traceability of genetically modified (GM) organisms and stringent labeling of foods that contain GM ingredients. The requirements include labels stating "This product is produced from GM organisms" and strict limits on mixing GM and non-GM ingredients in food exported to the EU. The United States is one of the world's leading producers and exporters of GM crops, with 75 percent of soybeans, 71 percent of cotton, and 34 percent of corn being GM. In the United States and Canada, 55–63 percent of customers see GM food as "bad," while this rises to 81 percent and 89 percent disapproving in Germany and France, respectively.[17]

    Exporting companies need to be informed about the changing status of tariff and non-tariff barriers in the countries where they are doing business or would like to do business. Those that have stayed away from markets with extremely high import duties or nontariff barriers, such as product standards or customs procedures designed to keep out foreign products, may find these barriers no longer exist.

## COSTS OF BARRIERS TO TRADE

Trade restraints in the United States and other countries cost consumers tens of billions of dollars per year, while benefiting a relatively small number of companies in the protected sectors of the economy. The sugar industry provides an interesting example of this situation, as discussed in the earlier Global Debate, "Sugar Subsidies: Sweet for Producers, Not for Consumers."

Sugar is not an isolated example of the costs associated with trade barriers. A recent study of just 20 product groups in protected industries showed that the average consumer cost per job saved was $231,289 per year. This means that consumers paid more than seven times the average annual compensation of manufacturing workers to preserve jobs through import constraints. Many of these sectors have been shielded from imports for 45 years or more. Studies done in other countries show similar results.[18]

## Fernando Villanueva: "There Is So Much Beauty in the World."



Fernando Villanueva has advice for others wanting to join him in international business. He is from Palo Alto, California, completed a bachelor's degree in International Business at the California Polytechnic State University San Luis Obispo, and financed most of his own college education. He has been dancing Mexican Folklore since the age of 15, and he is pasionate about traveling and meeting new people. Here's his advice about pursuing a career in international business:

My interest in obtaining a degree in International Business first arose after I traveled to France in 1998. I was 16 at the time. I had the opportunity to participate in a program called The Experiment in International Living. This program allowed me to experience the French culture by living with a French family and taking language courses with people from all over the world. Ever since then, I knew international business was the right place for me.

A year after graduating from Cal Poly, I was able to work and live in the Czech Republic thanks to an AIESEC traineeship with the Univerzita Pardubice. Some of my responsibilities were conducting research work for business-related articles, coordinating and conducting presentations for professors in the European Union, coordinating events for students in the Erasmus program, and editing and reviewing articles being considered for publication. While working for the Univezita Pardubice, I was credited as one of the official translators/editors in two published books. I was also able to travel for work or leisure to Austria, Belgium, Czech Republic, Denmark, Egypt, England, Finland, France, Germany, Greece, Hungary, Italy, Luxembourg, Netherlands, Poland, Scotland, Slovakia, Spain, Sweden, Turkey, and Wales.

When traveling to new destinations, I always try to research the country and city I will be visiting. This allows me to have some basic knowledge of where I am going. My experience with locals has been that they appreciate my efforts to familiarize myself with their city beforehand. Knowing some basic words or phrases has always been helpful and equally appreciated. Another thing I try to do when in a new country is eat the traditional local dishes. I try to avoid spending a lot of time with other foreigners, interacting instead with the locals. I have found that this helps me adapt to the culture and people much more quickly.

The reason I chose to be an AIESEC trainee was to obtain experience working internationally, thus making me a valuable asset for any company I choose to work for in the future. Having successfully completed my traineeship will show future employers that I am able to adapt to new environments and successfully function in complex situations. Thanks to my experience with AIESEC, I have learned how to communicate and work with people from all over the world.

Two of my biggest challenges while working abroad, and with people from various parts of the world, were adjusting to the different modes by which business was conducted and to bureaucracy. Ever since my first international experience, I have had to remind myself that business is not always conducted in the same mode in each country and that I must be able to adjust to new forms of business practices. Working with other government entities can be challenging; I have accepted this fact and I try to not let this discourage me from working with them. I have discovered that achieving good cooperation with other government entities and learning to work with them can be beneficial for both me and the company I work for.

I have really enjoyed working abroad because it has allowed me to travel to various countries and it has also allowed me to acquire the ability to successfully function in nearly any business environment, both internationally and domestically. While in these countries, I have met many interesting and amazing people, and I have maintained a good relationship with many of the people I have met throughout this experience. I have learned a lot from the people I have met, both professionally and personally. Thanks to my international experience, I have learned that culturally we are all different, yet we also share a lot in common. I have found this to be true no matter where I have traveled.

When you are visiting a country that you do not reside in, always remember that you are a guest of that country—no matter what your purpose for visiting may be. A recommendation I have for anyone who is, or will be, working internationally is to not assume that the way things are done back home is always the way things are done everywhere else. Telling a person that he or she is doing a task wrong just because they are doing that task in a different way than it is done back home normally does not go well. Also, people do not like to hear what you believe is wrong about their country and what makes yours better. If you focus most of your energy on pointing out what is wrong, or what you hate, about the country you are visiting you will lose the opportunity to see what is great about it. There is so much beauty in the world; allowing yourself to have the opportunity to see a small part of it is truly amazing.

## Resources for Your Global Career

**Your Understanding of the Impact of Political Risk and Geopolitics on International Business**

Every international business transaction is affected by two governments, that of the home country and that of the host country. You must abide by the laws, rules, and regulations of each country. You must also understand the political orientation of each country and geographic region in which you do business because the government and its political structure will determine your ability to do business in that country. Geopolitics goes well beyond government and politics. It includes, but is not limited to, such issues as:

- Country and regional economics.
- Terrorism and its support or condemnation.
- Military alliances.
- Human rights.
- Religion and the degree of separation between "church and state."
- Public policy.
- Natural resources.
- Governmental stability.
- Attitudes toward dumping and counterfeiting products.
- Arms control.
- Chemical and biological warfare.
- Nuclear proliferation and threat.

Political risk assessment is a major component of doing a potential market entry analysis to determine the feasibility and risks of entering into a specific foreign market. Keeping current with the ever-changing global political scene and doing political risk assessment in market entry planning are two critical tools of the successful international business professional.

**Your Primer on World Terrorism:** To understand the incidence and scope of world terrorism, suspected or identified, look at the Global Incident Map, a real-time global display of terrorism and other suspicious events updated as they are reported: www.globalincidentmap.com/user.php.

**Resources for Geopolitical Issues and Careers:** To build your base of understanding of current geopolitical events and to help you locate internship and career opportunities in this area, the following resources may be useful:

- STRATFOR gives reports and analyses of geopolitical events as they relate to global economics and trade, energy, military, politics, terrorism and security: www.stratfor.com
- SIPRI (Stockholm International Peace Research Institute) provides in-depth information on Political Risk issues: www.sipri.org
- EURO Intelligence provides daily reports on macroeconomic, financial, and political issues focusing on Europe: www.eurointelligence.com/
- FP (Foreign Policy) PASSPORT, foreign policy blog: http://blog.foreignpolicy.com/node
- Foreign Policy Association: www.fpa.org/
- *World Politics Review*—a foreign policy and national security daily: www.worldpoliticsreview.com/
- Techniques for Assessing and Managing Risk in International Markets: http://findarticles.com/p/articles/mi_qa3615/is_200712/ai_n21279424?tag=rbxcra.2.a.1
- *Oxford Analytica* analyzes the implications of international developments and their impact on corporations, governments, financial, and international institutions: www.oxan.com

For internships or career opportunities in geopolitical-related organizations, see websites such as the following:

- U.S. Department of State: www.state.gov/p/io/empl/
- Foreign Policy Association: www.fpa.org
- Devex—International Development: www.devex.com/jobs

---

# Summary

**LO6-1 Discuss nationalization and privatization of business.**

From time to time governments take firms or organizations out of private and into government hands. Some of the reasons for this are (1) to extract more money from the firms, (2) profitability, (3) ideology, (4) job preservation, (5) because the government has pumped money into a firm or an industry, and (6) happenstance. Where government-owned companies compete with privately owned companies, the private companies sometimes complain that the government companies have unfair advantages. Governments sometimes sell government assets to private parties or contract with private firms to perform functions usually performed by governments. That is called privatization.

**LO6-2 Explain what terrorism is and the range of activities that terrorists can engage in, as well as countermeasures that companies and their employees might take.**

Terrorism involves unlawful acts of violence committed for a wide variety of reasons, including for ransom, to overthrow a government, to gain release of imprisoned colleagues, to exact revenge for real or imagined wrongs, and to punish nonbelievers of the terrorists' religion.

Terrorism introduces instability into a country, making it difficult for businesses to know what the political environment will be in the future, and some terrorist groups have developed a global reach. In some cases, terrorism is also

personally hazardous to firm employees and to their families. Some countermeasures that can be taken include insurance for covering kidnapping, ransom, and extortion; antiterrorist surveillance and evasive driving training; and using specialists for handling negotiations with kidnappers.

**LO6-3 Evaluate the importance to business of government stability and policy continuity.**

Businesses can operate under almost any set of rules as long as those rules don't change often, so that businesses can make plans. When policy (tax rates is an example) changes frequently, businesses have difficulty complying with the rules, as well as difficulty setting prices, employment policies, etc.

**LO6-4 Explain country risk assessment by international business.**

Country risk assessment is a form of assessment that includes political risks, but also others, such as difficulties in remitting profits, local content requirements, possible terrorist action, and the like. Businesses may choose to have CRA done inside the firm, the firm may hire outsiders, or even both.

**LO6-5 Discuss types of trade restrictions and the arguments for imposing them.**

In response to demands for protection, governments impose import duties (tariff barriers); nontariff barriers, such as quotas, voluntary export restraints, and orderly marketing arrangements; and nonquantitative nontariff barriers, such as direct government participation in trade, customs, and other administrative procedures and standards for health, safety, and product quality. Special-interest groups demand protection for defense industries so that their country will have these industries' output in wartime and will not depend on imports, which might not be available. New industries in developing nations frequently request barriers to imports of competing products from developed countries. The argument is that the infant industry must have time to gain experience before having to confront world competition. Protectionists argue for protection from cheap imports by claiming that other countries with lower hourly labor rates than those in the protectionist's nation can flood the protectionist's nation with low-priced goods and take away domestic jobs. Others want "fair" competition, that is, an import duty to raise the cost of the imported good to the price of the imported article to eliminate any "unfair" advantage that the foreign competitor may have. This, of course, nullifies the comparative advantage. Companies will also demand that their government retaliate against dumping and subsidies offered by their competitors in other countries.

## Key Words

| | | |
|---|---|---|
| **privatization** (p. 158) | **countervailing duties** (p. 168) | **quotas** (p. 172) |
| **terrorism** (p. 160) | **tariffs** (p. 170) | **voluntary export restraints (VERs)** (p. 172) |
| **stability** (p. 162) | **ad valorem duty** (p. 171) | |
| **instability** (p. 162) | **specific duty** (p. 171) | **orderly marketing arrangements** (p. 172) |
| **country risk assessment (CRA)** (p. 163) | **compound duty** (p. 171) | |
| **dumping** (p. 167) | **variable levy** (p. 171) | |
| **subsidies** (p. 168) | **nontariff barriers (NTBs)** (p. 171) | |

## Questions

1. Why might governments nationalize firms, and why might a government-owned firm have an unfair advantage over privately owned companies?

2. What options does a company have for helping to prevent terrorism or to better manage terrorist actions if they occur?

3. Why might business fear sudden changes in government policies?

4. How can ICs use their strengths to influence government policies?

5. Is country risk assessment an exact science? Explain.

6. It seems that free, unrestricted international trade, in which each nation produces and exports products for which it has a comparative advantage, will enable everyone to have a higher level of living. Why, then, does every country have import duty restrictions?

7. "We certainly need defense industries, and we must protect them from import competition by placing restrictions on competitive imports." True or false? Is there an alternative to trade restrictions that might make more economic sense?

8. It seems entirely reasonable for a government to undertake efforts to protect a new or recently established—often called an "infant"—industry. Why, then, might international trade professionals argue against governmental efforts to protect a new or recently established industry?

9. According to the WTO, what is dumping? Why would a government be opposed to having their citizens or businesses be able to obtain products at lower costs?

10. "Workers are paid $20 an hour in the United States but only $4 in Taiwan. Of course, we can't compete. We need to protect our jobs from cheap foreign labor." What are some possible problems with this statement?

11. There are two general classifications of import duties: tariff and nontariff barriers.

    a. Describe the various types of tariff barriers.

    b. What are some of the nontariff barriers?

---

**globalEDGE** globalEDGE.msu.edu

## Research Task

Use the globalEDGE site (http://globalEDGE.msu.edu/) to complete the following exercises:

1. Your company is considering opening a new factory in Latin America. As such, the strategic management division is in the process of evaluating the specific locations for such an operation. The pool of candidate countries has been narrowed to Colombia, Panama, and Paraguay. By using Country Insights, a resource provided by globalEDGE, prepare a short report comparing the risks of conducting business in these

countries. Based on this information, in which country would you open the new factory?

2. You work for a national chain of clothing stores that is considering importing textiles from India into the United States. You want to determine whether the goods are subject to import quotas. Using information provided by the *U.S. Customs and Border Protection,* prepare a report highlighting the elements that determine whether a shipment is subject to this type of trade restriction.

---

## Minicase: Is Your Chocolate the Result of Unfair Exploitation of Child Labor?

When you last savored a bar of rich chocolate, a cup of hot cocoa, or a piece of chocolate cake or scoop of chocolate ice cream, did you know that you may have unwittingly been consuming a product made with child slaves?

Chocolate is one of the most-traded agricultural products in the world. The top 10 chocolate-consuming nations are all developed countries in Europe or the United States, yet about 70 percent of the world's cocoa is produced in West Africa. In practice, beans from different nations are usually mixed together during their exportation and transport to processing plants in the importing nations. So Hershey bars, Snickers, M&Ms, KitKats, Nestlé chocolates, fudge, hot chocolate—essentially all of these delicacies that are regularly enjoyed by hundreds of millions of consumers—will include cocoa from West Africa, especially the Côte d'Ivoire (Ivory Coast). With about 46 percent of the world's total cocoa production, Côte d'Ivoire produces nearly twice the level of the second-largest cocoa producer, Ghana.

Results of a survey on child labor in West Africa, released in 2002, found that 284,000 children were working in hazardous conditions on West African cocoa farms, with the majority (200,000) working in Côte d'Ivoire. Nearly two-thirds of the child laborers were under the age of 14. Working

conditions were described as slave-like, with 29 percent of the surveyed child workers in the Côte d'Ivoire indicating that "they were not free to leave their place of employment should they so wish." Many of these children had been brought into the cocoa-growing areas from distant regions of the Côte d'Ivoire or from poverty-stricken countries such as Burkina Faso, Mali, and Togo, often after being kidnapped. Some of the child laborers had been sold by their parents in the expectation that the child's earnings would be sent home. Although paid less than 60 percent of the rate of adult workers, children frequently worked for more than 12 hours per day, 6 days a week, and were regularly beaten. More than half of the children applied pesticides without protective gear. Only 34 percent of the children working on cocoa farms went to school, which was about half the level for children who were not working on cocoa farms. The rate of school enrollment was even lower for girls.

These child laborers seemed to be trapped in a vicious cycle: they were forced into work due to kidnapping or economic circumstances faced by themselves and/or their families; they earned subsistence wages; and because most had not been to school and had minimal skills, their prospects for seeking other employment options were limited.

Efforts to raise awareness of the exploitation of child labor in the cocoa industry faced great challenges, and even today, a majority of consumers seem unaware of the circumstances behind the production of their favorite chocolate treats. Yet the atrocious nature of the child labor situation in the cocoa industry compelled the media, public interest groups, and others to continue their efforts. Hard-hitting news stories began to appear on television and radio and in magazines and newspapers across North America and Europe.

Fearing the implications of boycotts, trade sanctions, or certification and labeling requirements in key markets such as the United States and Europe, representatives from the chocolate industry attempted to develop a strategy for dealing with the problem. The Chocolate Manufacturers Association hired former senators George Mitchell and Bob Dole to lobby against legislation establishing certification and labeling requirements. Once that defeat was secured, the industry agreed to self-regulate and attempted to change the child labor practices. A protocol for the industry was developed that established a timetable for eliminating child labor and forced labor in the production of cocoa. A self-imposed deadline was set for establishing a viable monitoring and certification system: July 1, 2005.

Some important cocoa-producing nations have worked with the International Labor Organization and the International Programme on the Elimination of Child Labour (IPEC) to establish national programs to eliminate child labor in their countries. However, as of 2010, there was evidence suggesting that child labor continued to be a widespread problem in Côte d'Ivoire and Ghana. Industry representatives have complained that progress toward eliminating child labor in cocoa production has been hindered by traditional culture in the agriculturally based producing nations, compounded by civil war and other complications.

In the absence of prompt and effective action by the chocolate and cocoa industry, a number of companies have begun producing fair-trade-certified chocolate. Through observing a strict set of guidelines associated with fair-trade certification, these companies guarantee that a consumer of one of their chocolate products is "not an unwitting participant in this very inhumane situation." Fairtrade Labeling Organizations International, a consortium of fair-trade organizations from Canada, the United States, Japan, Australia, New Zealand, and 15 European nations, establishes certification standards.

Fair-trade practices essentially involve international subsidies to farmers in developing countries, ensuring that farmers who are certified as engaging in fair-trade practices will receive a price for their produce that will at least cover their costs of production. By providing a price floor, fair-trade practices protect Third World farmers from the ruinous fluctuations in commodity prices that result from free trade practices. At the same time, fair-trade certification requires that farmers engage in appropriate social, labor, and environmental practices, such as paying livable wages and not using child or slave labor. In addition to the cocoa program, fair-trade certification programs have been implemented for a range of other products, such as coffee, bananas, nuts, spices, tea, and crafts.

Although still a nascent movement, sales of fair-trade certified products are growing and are projected to reach $9 billion in 2012. Will there be a similar result for chocolate? Already, more than 50 companies make fair-trade chocolate products in the United States, including ClifBar, Cloud Nine, Newman's Own Organics, Scharffen Berger, and Sweet Earth Chocolates.

**Questions**

1. Should labor practices in another country be a relevant consideration in international trade? Why or why not?

2. With regard to trade in products such as cocoa, what options are available to governments, businesses, and consumers for dealing with practices such as child labor or slave labor in other countries? What are the implications associated with each of these options?

3. How would international trade theorists view the fair-trade movement?

Source: "Cocoa Production in Cote d'Ivoire," http://en.wikipedia.org/wiki/Cocoa_production_in_C%C3%B4te_d%27Ivoire (June 23, 2011); Jose D. Perezgonzalez, "Child Labor in Cocoa Production—2010," *Journal of Knowledge Advancement and Integration,* 2011, pp. 1–4, www.lulu.com/product/ebook/child-labour-in-cacao-production/15575910 (accessed June 23, 2011); "Fairtrade Certification," http://en.wikipedia.org/wiki/Fairtrade_certification (June 23, 2011); "Slave-Free Chocolate," http://vision.ucsd.edu/~kbranson/stopchocolateslavery/main.html (June 23, 2011); and "Fair-Trade Q&A," www.globalexchange.org/campaigns/fairtrade/fairtradeqa.html (accessed June 23, 2011).

*This page intentionally left blank*

# Intellectual Property and Other Legal Forces



The role which the Court [International Court of Justice] plays, through the power of justice and international law . . . is widely recognized and evidenced by the number of cases on the Court's docket. . . . It is not uncommon that these cases deal with issues concerning international peace and security. In performing its dispute resolution function, the Court, which embodies the principle of equality of all before the law, acts as a guardian of international law, and assures the maintenance of a coherent international legal order.

*—Judge Shi Jiuyong, former president of the International Court of Justice, to the General Assembly of the United Nations*

## Counterfeit Pharmaceuticals: A Health and Intellectual Property Challenge Worldwide

You are feeling under the weather while traveling abroad, so you visit a doctor, fill your prescription at a local pharmacy, and swallow a pill with your bottled water. Soon you will be feeling better. Or will you? Are the pharmaceuticals you just ingested genuine or fake?

A special kind of challenge confronting both developed and developing nations is the counterfeiting of pharmaceuticals. Counterfeiting is the use of a well-known manufacturer's brand name on illicit copies of the firm's merchandise. Besides the production of exact copies of branded pharmaceuticals, other kinds of pharmaceutical counterfeiting include: (1) making products that contain the correct active ingredients but in the wrong proportions, (2) making products that do not contain any active ingredients, and (3) making products that contain toxic ingredients or other impurities.

With an estimated $75 billion of worldwide sales in 2010, 90 percent higher than 2005 and increasing at nearly double the rate of legitimate pharmaceutical sales, counterfeit drugs represent an industry that is growing rapidly in size—and in its risk to public health—worldwide.[a] The globalization of manufacturing supply chains has meant more steps, and more geographic spread, between the production and consumption of drugs. About half of all drugs sold through "questionable" Internet pharmacies are estimated to be counterfeit, according to the World Health Organization (WHO). The proportion of counterfeit drugs ranges from under 1 percent in some developed countries to 10 to 50 percent in developing nations.[b] "Counterfeiters can make more money than hard-drug traffickers, and they have less of a chance to go to prison," according to Interpol policewoman Aline Plançon.[c] The profit margin from selling counterfeit Viagra, for example, is roughly 10 times that from selling heroin, and the legal consequences are lower. While traffickers of hard drugs may face prison or death, those trafficking in counterfeit pharmaceuticals usually face charges under trademark, fraud, or similar laws.

## Counterfeit Products Can Be Dangerous

Besides causing legitimate manufacturers to lose sales, fake drugs sometimes bring tragedy to users when, as is common, they fail to perform as well as the original.

1. In Mexico, officials confiscated 15,000 counterfeit burn remedies because many contained sawdust or dirt and caused raging infections, while hundreds of infants and others

## learning objectives

After reading this chapter, you should be able to:

**LO7-1** **Discuss** the complexity of the legal forces that confront international business.

**LO7-2** **Explain** the possibilities for international dispute settlement.

**LO7-3** **Recognize** the need and methods to protect intellectual property.

**LO7-4** **Explain** the risk of product liability legal actions.

**LO7-5** **Discuss** some of the U.S. laws that affect international business operations.

were killed in recent years in Bangladesh, Panama, Nigeria, Haiti, and India after using cough syrup containing diethylene glycol, a toxic chemical used for making antifreeze.

2. The World Health Organization estimates that 25 percent of antimalarial medicines used in developing nations are counterfeit or substandard—more than 50 percent in parts of Africa and Asia—which contributes to malarial outbreaks and associated illness and death. Among the chemicals discovered in malaria pills are the antibiotic erythromycin, an ingredient for the street drug ecstasy, and an active incredient from the erectile dysfunction drug, Viagra.

3. In 2008, the European Union tracked and seized more than 34 million illegal pills during a two-month investigation, and the U.S. Food and Drug Administration has repeatedly warned consumers about "potentially significant risks" associated with counterfeit Lipitor, Viagra, and other popular prescription drugs that are sold by pharmacies in Mexican border towns or through online sources to U.S. consumers.[d]

The problem of counterfeiting is not limited to the pharmaceutical industry, of course. Troubling levels of counterfeit goods have been reported across a broad array of products, ranging from music, books, and clothing to aircraft parts, semiconductors, computer software, agricultural pesticides and fertilizers, and pet food. Indeed, the Federal Bureau of Investigation considers counterfeiting and other forms of theft of intellectual property to be "the crime of the 21st Century."[e]

## Combating Imitations

A range of public and private sector organizations have organized efforts to fight the rapidly spreading global outbreak of counterfeit drugs.

This includes the Pharmaceutical Security Institute (which tracks pharmaceutical counterfeiting), the European Alliance for Access to Safe Medicines (which is working to exclude counterfeit and substandard medicines from supply chains), and the WHO-sponsored International Medical Products Anti-Counterfeiting Taskforce (IMPACT). Progress is being made in raising awareness of the nature and extent of the problem, developing appropriate legislation and enforcement efforts to locate and punish offenders, and identifying innovative ways of ensuring the safety of pharmaceutical supply chains from raw material to consumer. Despite these efforts, protecting the health of consumers and the intellectual property rights of pharmaceutical makers and other companies remains an ongoing challenge worldwide.

[a]Estimate by the U.S.-based Center for Medicines in the Public Interest, NanoGuardian, "NanoGuardian Extends NanoEncryption Technology to Pre-Filled Syringes and Vial Caps," www.nanoguardian.net/pressDisplay.php?pressNum=35 (accessed June 25, 2011).

[b]U.S. Food and Drug Administration, "Counterfeit Drugs Questions and Answers," December 2, 2010, www.fda.gov/Drugs/DrugSafety/ucm169898.htm (accessed June 25, 2011); and Sarah Everts, "Fake Pharmaceuticals," *Chemical & Engineering News* 88, no. 1 (January 4, 2010), pp. 27–29, http://pubs.acs.org/cen/science/88/8801sci1.html (accessed June 25, 2011).

[c]Ibid.

[d]World Health Organization, "WHO Calls for an Immediate Halt to Provision of Single-Drug Artemisinin Malaria Pills," www.who.int/mediacentre/news/releases/2006/pr02/en/ (accessed June 25, 2011); World Health Organization, "Counterfeit Medicines," www.who.int/medicines/services/counterfeit/impact/ImpactF_S/en/ (accessed June 25, 2011); and "Counterfeit Lipitor, Viagra, and Evista Sold in Mexican Border Towns," www.medicinenet.com/script/main/art.asp?articlekey=47114 (accessed June 25, 2011).

[e]Jon W. Dudas, "Statement of Jon W. Dudas, Acting Undersecretary of Commerce for Intellectual Property and Acting Director of the United States Patent and Trademark Office Before the Committee on Judiciary, United States Senate, March 23, 2004," www.ogc.doc.gov/ogc/legreg/testimon/108s/dudas0323.htm (accessed June 25, 2011).

Although seldom as severe as those associated with deadly counterfeit pharmaceuticals, myriad issues related to intellectual property and other legal forces confront international companies wherever they operate. Participants in international business should understand the enormous breadth and depth of laws and legal issues in various jurisdictions worldwide. Anyone studying legal forces affecting international business soon realizes that the variety of these forces complicates the task of understanding the laws.

While on the one hand, businesses must be aware of laws in order to comply, on the other hand, businesses also expect that laws will assist them when necessary. An issue of great

concern to businesses that operate internationally is the stability of a host government and its legal system. When a business enters a country, the firm needs to know whether the country's host government will be able to protect the foreign business with an adequate legal system. The legal system must be able to enforce contracts and protect the basic rights of employees. In examining international legal forces, one must keep in mind that a stable government and an adequate court system are necessary to ensure a welcome environment for foreign businesses.

This chapter examines international law and international dispute settlement, including those dealing with intellectual property and other key company assets. It also looks at specific national laws that influence international business.

# International Legal Forces

## RULE OF LAW

International businesspeople need to determine whether a country is governed by the rule of law, instead of rule by a political dictatorship or rule by a powerful elite. If a country's legal system is based on the rule of law, this encourages foreign investment because foreign businesses know that their interests will be protected. Following the rule of law also makes ensuring protection of human rights of local people easier.

For example, Hong Kong has an advantage over Shanghai in attracting foreign investors because Hong Kong has a tradition of law adopted from British colonial days, while Shanghai courts tend to favor Chinese litigants. This disparity in legal systems between the two cities is seen to give Hong Kong an advantage as a location for foreign firms.[1]

## WHAT IS INTERNATIONAL LAW?

Each sovereign nation is responsible for creating and enforcing laws within its jurisdiction. Once laws cross international borders, the matter of enforcement is complicated by the necessity of agreement between nations. The same concepts that apply to domestic laws do not always apply to international law.

What is called *international law* can be divided into public international law and private international law. **Public international law** includes legal relations between governments, including laws concerning diplomatic relations between nations and all matters involving the rights and obligations of sovereign nations. In contrast, **private international law** includes laws governing the transactions of individuals and companies crossing international borders. For example, private international law would cover matters involved in a contract between businesses in two different countries.

**public international law**
Legal relations between governments

**private international law**
Laws governing transactions of individuals and companies that cross international borders

## SOURCES OF INTERNATIONAL LAW

International law comes from several sources, the most important of which are bilateral and multilateral **treaties** between nations. Treaties are agreements between countries and may also be called *conventions, covenants, compacts, or protocols.* International organizations such as the United Nations have provided a forum for creation of many treaties. The UN has sponsored many conferences that have led to multinational agreements on a range of matters, including postal delivery and use of driver's licenses in other countries. Also, the International Court of Justice, an organ of the UN, creates international law when it decides disputes brought before it by member-nations.

Another source of international law is customary international law, which consists of international rules derived from customs and usage over centuries. An example of customary international law is the prohibition against genocide (there is also a specific international statute against genocide), or the immunity from prosecution of visiting foreign heads of state.

**treaties**
Agreements between countries, which may be bilateral (between two countries) or multilateral (involving more than two countries); also called *conventions, covenants, compacts,* or *protocols*

## EXTRATERRITORIALITY

Many countries, including the United States and members of the European Union, often attempt to enforce their laws outside their borders. This is referred to as **extraterritorial application of laws.** This attempt to enforce laws abroad is done not by force but through traditional legal means. For example, the U.S. government imposes taxes on U.S. citizens and U.S. permanent residents regardless of either the source of income or the residence of the taxpayer. If a U.S.

**extraterritorial application of laws**
A country's attempt to apply its laws to foreigners or non-residents and to acts and activities that take place outside its borders

citizen is living in Madrid and receives all of her income from Spanish sources; the United States will still expect the taxpayer to comply with U.S. tax laws. Likewise, when U.S. companies operate in other countries with U.S.-based personnel, the U.S. companies must comply with U.S. laws, including employment laws. Of course, these companies must also comply with the laws of the host country. Extraterritorial application of laws has been extended in many other areas including antitrust, employment, and environmental laws. Also, the Alien Tort Statute allows non-U.S. nationals to file lawsuits in U.S. courts for alleged violations of international law. In 2010, Coca-Cola was sued (in New York) for alleged violence against workers in Guatemala.

# International Dispute Settlement

## LITIGATION

**litigation**
A legal proceeding to determine and enforce a particular legal right.

**Litigation,** which is a legal proceeding conducted in order to determine and enforce particular legal rights, can be extremely complicated and expensive. In addition to involving the trial itself, most lawsuits in the United States entail lengthy pretrial activities, including a process called *discovery*. Discovery is the means of finding facts relevant to the litigation that are known to the other side, including obtaining documents in the other side's possession. Some discovery methods can seem quite intrusive because courts grant parties great latitude in obtaining information in the possession of the opposing side. Discovery is one reason many people outside the United States dislike litigation in the United States.

Litigation involving disputes that cross international lines can arise in both state and federal courts. Special rules exist for obtaining discovery in other countries, and they vary from country to country. Some countries freely allow U.S. litigators to obtain discovery. Others have restrictions. For example, if discovery is to occur in Switzerland even in a case involving only U.S. parties, permission must be obtained from Swiss authorities. Failure to obtain permission may result in penalties, including possible criminal sanctions.

One of the major problems usually involved in cross-border litigation is the question of which jurisdiction's law should apply and where the litigation should occur. Each country (and each state in the United States) has elaborate laws for determining which law should apply and where litigation should occur. As with any other disputed matter, the final decision on these issues rests with the court. Occasionally, courts in two countries (or two states) will attempt to resolve the same dispute. Again, this is resolved by reference to the particular choice of law provisions and can be quite complicated. For this reason, it is prudent to include in contracts a choice-of-law clause and a choice-of-forum clause in the event of a dispute. A *choice-of-law clause* in a contract specifies which law will govern in the event of a dispute. For example, if there is a U.S. seller and an Australian buyer, the parties may agree that Australian law would govern any dispute. A *choice-of-forum clause* in a contract specifies where the dispute will be settled. For example, the parties in the preceding example may agree to have the dispute decided in California state courts in Los Angeles County, California.

## PERFORMANCE OF CONTRACTS

Whenever businesses enter into agreements with other businesses, the possibility exists that there may be problems getting the other side to perform its obligations. No worldwide court has the power to enforce its decrees. The worldwide courts that do exist, such as the UN's International Court of Justice, rely on the voluntary compliance of the parties before it. Each nation in the world is a sovereign nation and has its own rules for recognizing decrees and judgments from other nations.

When contracting parties are residents of a single country, the laws of that country govern contract performance and any disputes that arise between the parties. That country's courts have jurisdiction over the parties, and the courts' judgments are enforced in accordance with the country's procedures. When residents of two or more countries contract, those relatively easy solutions to dispute resolution are not available. Enforcing contracts that cross international lines is often quite complicated.

### United Nations Solutions
When contract disputes arise between parties from two or more countries, which country's law is applicable? Many countries, including the United States, have ratified the UN Convention on the International Sale of Goods (CISG) to solve such problems.

The CISG established uniform legal rules to govern the formation of international sales contracts and the rights and obligations of the buyer and seller. The CISG applies automatically to all contracts for the sale of goods between traders from different countries that have ratified the CISG. This automatic application will take place unless the parties to the contract expressly exclude—opt out of—the CISG.

Private Solutions—Arbitration    As mentioned before, many people outside the United States dislike the U.S. court system. Likewise, many U.S. businesspeople dislike or at least fear litigation in other countries. For these reasons, international businesspeople often agree that any disputes will be resolved by arbitration, rather than by going to court in any country. **Arbitration** is a dispute resolution mechanism that is an alternative to litigation. Arbitration is usually quicker, less expensive, and more private than litigation, and it is usually binding on all parties. At least 30 organizations now administer international arbitrations, the best known of which may be the International Court of Arbitration of the International Chamber of Commerce in Paris. In addition, London and New York are centers of arbitration. Some organizations specialize in the type of arbitration cases they will consider. For example, the World Intellectual Property Organization (WIPO) Arbitration and Mediation Center handles technological, entertainment, and intellectual property disputes. In 2009 the Center settled a dispute between Research in Motion Ltd. and a private party over domain names using variations of the word BLACKBERRY.[2] The International Centre for the Settlement of Investment Disputes specializes, logically, in investment disputes.

In summary, people and businesses may prefer arbitration for several reasons. They may be suspicious of foreign courts. Arbitration is generally faster than law courts, where cases are usually backlogged. Arbitration procedures are usually more informal than court procedures. Arbitration may be confidential, avoiding the perhaps unwelcome publicity accompanying an open court case. And generally it may be less expensive.

Other organizations are working toward a worldwide business law. For example, the 11 **Incoterms** of the International Chamber of Commerce and its Uniform Rules and Practice on Documentary Credits receive almost universal acceptance, and new definitions of some Incoterms went into effect in 2011. These terms are explained in Chapter 14. (See Table 7.1 for examples of commonly used Incoterms for water transport.) The UN Commission on International Trade Law and the International Institute for the Unification of Private Law are doing much useful work. The Hague-Vishy Rules on Bills of Lading sponsored by the International Law Association have been adopted by a number of countries.[3]

**arbitration**
A process, agreed to by parties to a dispute in lieu of going to court, by which a neutral person or body makes a binding decision

**Incoterms**
Universal trade terminology developed by the International Chamber of Commerce

## DESPITE LEGAL UNCERTAINTIES, INTERNATIONAL BUSINESS GROWS

Despite legal uncertainties of doing business in other countries, international business activities will increase in the future. For this reason, international businesspeople must be aware of the legal environment in which they find themselves. Legal systems vary significantly from country to country, and it is important to understand the differences. The assumptions one makes on the basis of the U.S. legal system may not apply in other countries.

| **TABLE 7.1** | Examples of Incoterms |
| --- | --- |

1. *FAS (free alongside ship—port of call).* The seller pays all the transportation and delivery expense up to the ship's side and clears the goods for export.
2. *CIF (cost, insurance, freight—foreign port).* The price includes the cost of the goods, insurance, and all transportation and miscellaneous charges to the named port of final destination.
3. *CFR (cost and freight—foreign port).* CFR is similar to CIF except that the buyer purchases the insurance, either because it can be obtained at a lower cost or because the buyer's government, to save foreign exchange, insists on use of a local insurance company.

# Intellectual Property

A *patent* is a government grant giving the inventor of a product or process the exclusive right to manufacture, exploit, use, and sell that invention or process. *Trademarks* and *trade names* are designs and names, often officially registered, by which merchants or manufacturers designate and differentiate their products. *Copyrights* are exclusive legal rights of authors, composers, creators of software, playwrights, artists, and publishers to publish and dispose of their works. *Trade secrets* are any information that a business wishes to hold confidential. All are referred to as **intellectual property.**

Trade secrets can be of great value, but each country deals with and protects them in its own fashion. The duration of protection differs, as do the products that may or may not be protected. Some countries permit the production process to be protected but not the product. International companies must study and comply with the laws of each country where they may want to manufacture, create, or sell products.

## PATENTS

In the field of **patents,** the International Convention for the Protection of Industrial Property, sometimes referred to as the Paris Union, provides some degree of standardization. This convention is adhered to by 173 countries.

A major step toward the harmonization of patent treatment is the European Patent Organization (EPO). Through EPO, an applicant for a patent need file only one application in English, French, or German to be granted patent protection in all 27 EU member-states. Before the EPO, an applicant had to file in each country in the language of that country. Often multiple companies are involved. For example, the U.S. Supreme Court ruled in 2008 on a U.S. patent for computer chipsets, which South Korea's LG Electronics Inc. licensed to Intel Corp. When a Taiwan manufacturer used the chips, LG sued.

As indicated in the introductory vignette for this chapter, the prescription drug industry relies heavily on patents and other intellectual property. Multinational pharmaceutical companies say they need years of patent protection to recoup expensive investments in research and development of new drug treatments. Pfizer Inc. has a blockbuster drug in Lipitor, an anti-cholesterol drug: Pfizer's revenue from Lipitor is about $13 billion per year. Pfizer's patent ran out in June 2011—so Pfizer negotiated an agreement with Indian generic-drug maker Ranbaxy Laboratories Ltd. to keep Ranbaxy's generic version off the U.S. market until November 2011. This extension for Pfizer is important, given that revenues average more than $1 billion per month.[4]

The World Intellectual Property Organization (WIPO) is a UN agency that administers 24 international intellectual property treaties. WIPO advises developing countries on such matters as running patent offices and drafting intellectual property legislation. Interest in intellectual property matters has been growing in developing countries. There is also another agreement called TRIPS (trade-related aspects of intellectual property) that operates under the aegis of the World Trade Organization, as mentioned in Chapter 3. In addition, in late 2010 the United States, European Union, Mexico, Japan, Morocco, New Zealand, Singapore, Switzerland, Australia, South Korea, and Canada reached an "agreement in principle" for ACTA, the Anti-Counterfeiting Trade Agreement.[5] Passage of the agreement may make it easier for border inspectors to search laptops for pirated contents, for example. Opponents allege that the ACTA would negatively affect the flow of information on the Internet.

At the UN, smaller nations have been mounting attacks on the exclusivity and length of patent protection. They want to shorten the protection periods from the current 15 to 20 years down to 5 years or even 30 months. But multinational companies are resisting the changes. They point out that the only



Many companies such as Coca-Cola market their products throughout the world and understand the importance of protecting trademarks worldwide

| TABLE 7.2 | The International Framework for IP Protection |
| --- | --- |

| Organization | Parent |
| --- | --- |
| World Intellectual Property Organization (WIPO) | UN |
| Trade Related Aspects of Intellectual Property (TRIPS) | WTO |
| Anti-Counterfeiting Trade Agreement (ACTA) (Proposed) | Free-standing |

incentives they have to spend the huge amounts required to develop new technology are periods of patent protection long enough to recoup their costs and make profits.

An added dimension is the growth of so-called patent trolls, who can be likened to modern-day highway robbers cashing in on loopholes in IP protection. These are lawyers and investors who buy patents that were mistakenly granted, mostly to failed companies. In one case, a patent troll claimed that a patent bought for about $50,000 was infringed by Intel's microprocessors and threatened to sue Intel for $7 billion in damages. This is a fascinating subworld populated not just by trolls but also patent pirates, patent thickets, and the like.

## TRADEMARKS

**Trademarks** can be a shape, a color or design (such as the Levi's small red tag on the left side of the rear pockets of its jeans), a catchy phrase, an abbreviation, or even a sound. Although blacksmiths who made swords in the Roman Empire may have been the first to use trademarks, Löwenbräu and Stella Artois claim use since the 14th century. Trademark protection varies from country to country, as does its duration, which may be from 10 to 20 years (with possible renewals). Such protection is covered by the Madrid Agreement of 1891 for most of the world, although there is also the General American Convention for Trademark and Commercial Protection for the Western Hemisphere. In addition, protection may be provided on a bilateral basis in friendship, commerce, and navigation treaties.

An important step in harmonizing the rules on trademarks was taken in 1988 when regulations for a European Union trademark law were drafted. A single European Trademark Office known as the Office of Harmonization in the Internal Market (OHIM) is responsible for the recognition and protection of proprietary marks in all EU countries, including trademarks belonging to companies based in non-EU member-countries.

## TRADE NAMES

**Trade names** (name of a business) are protected in all countries that adhere to the International Convention for the Protection of Industrial Property, which was mentioned earlier in connection with patents. Goods bearing illegal trademarks or trade names or false statements about their origin are subject to seizure upon importation into these countries.

## COPYRIGHTS

**Copyrights** are protected under the Berne Convention of 1886, which is adhered to by 164 countries, the WIPO Copyright Treaty, and the TRIPS Agreement, to which all WTO members agree to abide.

## TRADE SECRETS

**Trade secrets** are any information that is not generally known to the public and that a business wishes to hold confidential. Trade secrets may include formulas, processes, patterns, designs, or other information or sets of information that could give a company an economic advantage over its competitors. The value of a trade secret is maintained by not allowing it to be publicly known, and companies must exercise reasonable efforts to ensure that trade secrets are not disclosed. While protection of trade secrets is not subject to expiration after a set period of time, as with patents, there is no guarantee of the protection of trade secrets if another party independently discovers the information.

**trademark**
A shape, a color, design, catchy phrase, abbreviation, or sound used by merchants or manufacturers to designate and differentiate their products

**trade name**
A name used by merchants or manufacturers to designate and differentiate their products

**copyright**
Exclusive legal rights of authors, composers, creators of software, playwrights, artists, and publishers to publish and dispose of their works

**trade secret**
Any information that a business wishes to hold confidential

### Virtually Ripped Off? Intellectual Property Issues in Second Life's Virtual World



Second Life virtual world.

The Second Life virtual world, once considered a haven for geeks, has reached mainsteam success with more than 20 million users worldwide. It is a self-sufficient universe with everything the real (read "first") world has, including intellectual property rights. Introduced in the previous chapter as a potential new staging area for terror, here we consider it as a potential rat's nest for IP issues.

As the virtual world becomes more and more like the real world, the need for realism increases. Brand owners are finding that their trademarked products appear online without their authorization. Virtual lawyer, Benjamin Duranske, found 15 shops advertising Ferrari cars; 40 stores selling virtual Rolex and Chanel watches; and another 50 that carried sunglasses branded as Gucci, Prada, Rayban, and Oakley.

Creaters of virtual goods for sale in virtual worlds are also expressing concern with violation of their intellectual property rights. Linden Lab, which owns Second Life, was sued by an entrepreneur who created virtual erotic "SexGen" beds and other goods that he sold to residents in Second Life. The entrepreneur sued, claiming that Linden Lab permitted Second Life residents to counterfeit his creations and sell them for Linden dollars (known as L$). His lawsuit claimed, "The manner in which this has occurred is akin to the knockoff handbags and purses sold near Canal Street in New York City." Another entrepreneur, who sells virtual clothing in Second Life, joined the lawsuit, alleging that by allowing other marketers to copy and sell fake versions of her designs, Linden Labs was infringing on her copyright. These two litigants are seeking class-action status

## Standardizing Laws around the World

Many attempts have been made to standardize laws among various countries. To international business, the advantage of standardization is that business flows much better when there is a uniform set of rules. Worldwide harmonization is progressing slowly, though, in most areas. For now, businesspeople must confront the reality of differing standards.

In the tax area, there are tax conventions, or treaties, among nations. Each country tries to make each such treaty as similar as possible to the others, and so patterns and common provisions may be found among them.

In antitrust, the EU member-nations operate under Articles 81 and 82 of the Treaty of Rome, which are similar to the antitrust laws in the United States. In an unusual bilateral move, Germany and the United States signed an executive agreement on antitrust cooperation. This was the first attempt by national governments to cooperate on antitrust matters concerning firms operating in both countries. There have been proposals to create worldwide agreements on antitrust.

Some agreement exists in the field of international commercial arbitration, including enforcement of arbitration awards. If the disputed contract involves investment from one country into another, it can be submitted for arbitration by the International Center for Settlement of Investment Disputes at the World Bank. Chapter 3 covered a number of other UN-related organizations and other worldwide associations. Each of them has some harmonizing or standardizing effect on laws in the member-countries.

The UN Convention on the International Sale of Goods (CISG) provides some uniformity in international sales agreements for those parties who elect to use it. It has been signed by 74 states. There have been attempts to make accounting and bankruptcy standards

in U.S. District Court in California. They claim, "Linden Lab has created in Second Life a system in which it directly engages in piracy, actively allows its users to engage in piracy by providing the tools for it, and by which it profits from its own piracy and the piracy of its users."

So, who cares? First, these virtual knockoffs are bought and sold, in Second Life, and although L$ are used, L$ can be exchanged for real currency. Admittedly the sums are still small, with the equivalent of only about $29 million in L$ in circulation during the first quarter of 2011.[a] Courts are still trying to determine how to handle the issues raised by lawsuits involving virtual worlds like Second Life. Regarding the lawsuit mentioned above, Eric Goldman of Santa Clara University's High Tech Law Institute said, "It's not an easy case. This particular area of law is unsettled."

A greater risk is that companies producing trademarked goods and services in the real world may lose their ability to exploit the virtual site for their own marketing purposes in the future. Further, they may meet with opposition when they try to renew their trademarks from rivals who say they have abandoned their rights by failing to police third-party use. Finally, there is simply the issue of loss of control. In a similar situation, the British telecom company BT was unhappy to find that the central character in a PlayStation 2 game, "The Getaway," pretends to be a BT engineer before carrying out a killing spree.

It's worth noting that Second Life is just the tip of the virtual world iceberg: there are many other virtual worlds such as China-based HiPiHi, Germany-based Twinity and Smeet, New Zealand–based SmallWorlds, U.S.-based IMVU and Kaneva, and Canada-based Utherverse. Reflecting this concern, there is a Second Life Patent and Trademark Office (SLPTO) runs by SL inhabitants. Linden Labs, creator of Second Life, has started a "Brand Center" office to protect its own "Second Life" name and logo.

**Questions:**

1. What should be the relationship beween rights—and their enforcement—associated with intellectual property in a virtual world game context and those in a "real"world?

2. With the proliferation of virtual worlds in cyberspace, how can a company effectively monitor the variety of different sites in order to effectively protect its intellectual property rights?

[a]George Trefgarne, "Brussels Clears Way for $220bn Merger," *The Telegraph*, www.telegraph.co.uk/finance/4468341/Brussels-clears-way-for-220bn-merger.html (June 25, 2011); and Stephen Castle, "EU Fine Sends Message to Microsoft and Others," www.nytimes.com/2008/02/27/technology/27iht-msft.4.10498942.html (accessed June 25, 2011).

Source: "The Brand Reality of the Virtual World," *Managing Intellectual Property*, December 1, 2007, www.managingip.com/Article/1788109/The-brand-reality-of-the-virtual-world.html (accessed June 25, 2011); "Second Life," http://en.wikipedia.org/wiki/Second_Life (accessed June 25, 2011); Wendy David, "Second Life Sued for Allowing Sale of Imposter Virtual Goods," www.mediapost.com/publications/?fa=Articles.showArticle&art_aid=113576 (accessed June 25, 2011); and http://virtuallyblind.com/2008/03/26/sl-brand-center/ (accessed June 25, 2011).

uniform worldwide. A Model Law on Cross-Border Insolvencies from UNCITRAL (UN Commission on International Trade Law) served as the basis for Chapter 15 of the U.S. Bankruptcy Code, for example.

Two standardizing organizations are the International Organization for Standardization (ISO) and the International Electrotechnical Commission (IEC). The IEC promotes standardization of measurement, materials, and equipment in almost every sphere of electrotechnology. The ISO recommends standards in other fields of technology. Most government and private purchasing around the world demands products that meet IEC or ISO specifications.

# Some Specific National Legal Forces

## COMPETITION LAWS

**Competition laws** (known in the United States as **antitrust laws**) are intended to prevent inappropriately large concentrations of economic power, such as monopolies. Actions brought to enforce competition laws or antitrust laws usually involve government actions brought against business, but also may involve business actions against other businesses.

### U.S. Laws and Attitudes Are Different—But the Differences Are Narrowing
U.S. antitrust laws are strict, and they are vigorously enforced. They are laws to prevent price fixing, market sharing, and business monopolies. The U.S. Department of Justice is charged with enforcing U.S. antitrust laws. Other countries and the European Union are becoming more active in the antitrust field, and more than 80 countries

**competition laws**
The EU equivalent of antitrust laws

**antitrust laws**
Laws to prevent inappropriately large concentrations of power and the potential abuse of such power through price fixing, market sharing, and business monopolies

now have antitrust laws. The EU Commission is responsible for enforcing EU competition policy. In addition to enforcing competition policy against businesses, the EU Commission also has the power to force EU member-governments to dismantle state monopolies that block progress toward an open, communitywide market.[6]

A number of important differences in antitrust laws, regulations, and practices exist between the United States, other nations, and the EU. One difference is the *per se* concept of the U.S. law. Under the U.S. laws, certain activities, such as price fixing, are said to be illegal *"per se."* This means that they are illegal even though no injury or damage results from them. The EU Treaty of Rome articles dealing with restrictive trade practices do not contain the per se illegality concept of U.S. antitrust law. For example, a cartel that allows consumers a fair share of the benefits is legally acceptable in the EU. Also, the treaty is not violated by market dominance—only by misuse of that dominance to damage competitors or consumers.

The U.S. focus on antitrust legislation is concerned with the impact of the business deal on the consumer, while the EU is more concerned about the industry's competitive structure and thus pays attention to rivals' objections. In Japan, antitrust legislation was introduced by the United States during its occupation of Japan after World War II. This legislation, the Japanese Anti-Monopoly Law, was modeled on U.S. antitrust law and did not harmonize well with the existing cooperative *zaibatsu* (conglomerates) the Japanese government had established. In fact, the Japanese approach to a rational development of the economy regarded antitrust measures as an impediment. However, with increasing foreign presence, Japanese companies have incorporated antitrust thinking into their strategies. Because the Japanese culture so values cooperation, this is a challenge, especially when it comes to cartels.[7]

## Japan's "Toothless Tiger"

Japan's Fair Trade Commission (FTC), whose responsibility is to enforce antitrust laws, has been nicknamed the "toothless tiger." It is viewed as one of the weakest bodies in Japanese government, easily bullied by other powerful ministries, such as finance and international trade and industry (MITI), which have vested interests in ensuring that Japan's traditional, collaborative ways of doing business prevail. Most of the FTC's targets are small, foreign, or weak; when it has investigated powerful industries such as domestic cars, car parts, and construction, it has punished them at worst with "recommendations." The recommendations are usually accepted by the targeted company. If not, hearings follow, and then directives. However, Japanese courts lack power to hold defendents in contempt for failure to comply with the FTC's cease and desist orders.

A major difference between American and Japanese trust busting is that around 90 percent of U.S. complaints are initiated by private parties, while in Japan a private antitrust action can be brought only if the FTC has investigated the case first. Because of Japan's limited discovery laws, the only way the FTC can obtain information on a firm is to raid it. As a result, the FTC won't make a move unless it is sure the laws are being broken. It is almost impossible to be sure of that without information. Given all this, it is easy to understand why the FTC is considered to be a toothless tiger, limited "to merely gumming violators hard."[8]

## Worldwide Application of U.S. Antitrust Laws

The U.S. government often attempts to enforce its antitrust laws extraterritorially. For example, a grand jury in Washington, D.C., indicted three foreign-owned ocean shipping groups on charges of fixing prices without getting approval from the U.S. Federal Maritime Commission. The other governments, European and Japanese, protested bitterly, arguing (1) that shipping is international by definition, so the United States has no right to act unilaterally, and (2) that the alleged offenses were both legal and ethical practices outside the United States. The U.S. Supreme Court has repeatedly permitted overseas application of U.S. antitrust laws, although recent court decisions appear to have curtailed the potential of foreign plaintiffs to use U.S. courts in order to seek relief.[9]

### EU Extraterritorial Application of Its Competition Policy

Like the U.S. Department of Justice, the EU Commission has increasingly sought enforcement of its competition policy abroad when there is an effect on commerce within the EU. For example, the EU Commission had to give its approval before merger talks between America Online and Time Warner could proceed. Before its approval was given to the merger, AOL–Time Warner had to agree to sever all ties with the German media group Bertelsmann. The EU has also viewed Microsoft as anticompetitive and in 2008 fined the firm €899 million ($1.3 billion).[10]

### Criminal Cases

U.S. antitrust laws contain both civil and criminal penalties.* A decision by the U.S. federal court of appeals held that criminal antitrust laws apply to foreign companies even if the conspiracy took place outside the United States. While earlier decisions had permitted U.S. antitrust laws to be used against foreign companies in civil cases, this decision, which was against Nippon Paper Industries, set the precedent that antitrust laws could be used also to get criminal convictions.

### Proposal for Global Antitrust Approval

It is often difficult for international businesses to comply with the variety of antitrust laws worldwide. A good example is Microsoft. In the 1990s, the U.S. government and several U.S. states brought antitrust actions against Microsoft. The actions continued well into the early 21st century. The EU also brought several actions against Microsoft, one of which we mentioned earlier. In 2008, China began examining whether Microsoft has a monopoly position. The Microsoft case is a good example of how one company with international operations can get bogged down with antitrust laws in multiple jurisdictions. In light of the numerous countries that impose antitrust rules worldwide, many argue that greater worldwide cooperation in antitrust enforcement is needed. Some think that the WTO is the proper avenue for such worldwide cooperation. Others believe an international antitrust authority would be appropriate. Reaching such an agreement would be difficult because of the differing interests involved.[11] The U.S. government has proposed a world organization for the clearance of antitrust issues. If approved, the organization would probably take the form of a clearinghouse for merger filings. Calls for such an entity are increasing because of the multinational nature of most large mergers.

### Tariffs, Quotas, and Other Trade Obstacles

Trade obstacles are legal forces as well as political and financial forces. For that reason, we mention them again here. Every country has laws on these subjects. The stated purpose of a tariff is to raise revenue for the government, but it may serve the additional objective of keeping certain goods out of a country. Quotas limit the amount or source of imports.

There are many other forms of protection or obstacles to trade in national laws. Some are health or packaging requirements. Others deal with language, such as the mandatory use of French on labels and in advertising, manuals, warranties, and so forth, for goods sold in France, including websites located on servers physically in France. When Vietnam catfish imports into the United States flooded the market, lawyers for the U.S. catfish industry successfully argued that the Vietnamese product was not catfish but a different family of fish. After this failed to stop the imports, they reversed themselves and alleged that these catfish were being "dumped" on the U.S. market.[12] Table 7.3 provides a sampling of trade barriers.

In many countries, U.S. and EU exports may encounter weak patent or trademark protection, high tariffs, quarantine periods, and a variety of other obstacles.

The United States has many options in dealing with trade obstacles abroad. It can impose retaliatory barriers on products from countries imposing barriers against U.S. goods. It sometimes uses tariffs and quotas. It also uses a form of quota called by some "voluntary"

*Civil liability calls for payment of money damages. Criminal liability may result in fines or imprisonment.

TABLE 7.3

## Worldwide Examples of Tariffs and Other Trade Barriers

| Product | Destination | Barrier |
|---|---|---|
| U.S. rice | Japan | Government managed rice imports allocate U.S. rice almost exclusively to nonconsumer use (e.g., industrial food processing or re-export as food aid) and without identifying source as U.S. rice |
| European wines and spirits | India | Federal and state additional duties of 150 percent or more |
| Diammonium phosphate fertilizer | China | Value-added tax exemption for all phosphate fertilizers except diammonium phosphate, giving benefit to domestic fertilzer producers |
| Internet gambling from EU providers | United States | Discriminatory legislation |
| Commercial aircraft | EU | EU government subsidies to Airbus, reducing its risks versus those faced by Boeing of the United States and other aircraft manufacturers |
| Motion pictures | Canada | Prohibition on non-Canadian films shown on Canadian Broadcasting Corporation networks between 7 p.m. and 11 p.m. unless released at least 2 years previously and not in the top 100 grossing films for at least 10 years |
| U.S. poultry and pork | Russia | Import restrictions (quotas) |

Source: Office of U.S. Trade Representative, *2010 National Trade Estimate Report on Foreign Trade Barriers,* www.ustr.gov/about-us/press-office/reports-and-publications/2010 (accessed June 25, 2011); and European Commission, "Report to the Trade Barriers Regulation Committee," http://trade.ec.europa.eu/doclib/docs/2009/june/tradoc_143405 .pdf (accessed June 25, 2011).

# GLOBAL DEBATE

## A Threat to National Sovereignty? America's Dolphin-Safe Tuna Labeling versus the WTO



In May 2011, a World Trade Organization panel ruled that long-standing American "Dolphin Safe" labeling requirements for tuna violated international trade rules. As the first case examining the compatibility of voluntary product labeling with the WTO agreement, results of this finding against the United States could establish an important precedent—for governments, public interest organizations, consumers, and other stakeholders—of other informational labeling efforts worldwide.

First a bit of background on the case. In 1959, fishermen in the Pacific Ocean region stretching from southern California to South America began using purse seine fishing methods to harvest tuna. *Purse seining* deploys a wall of netting a mile or more in length that encircles entire schools of fish, the bottom is pulled closed like a drawstring purse, and everything inside the net is pulled into a boat to be processed. Dolphins in this part of the Pacific tend to swim in schools above large schools of tuna, so fishing fleets seek out dolphins and encircle them with nets in order to capture the tuna that swim below. While successful in netting tuna, consequences for dolphins can be catastrophic. Millions of dolphins were trapped in nets and drowned between 1959 and 1972, and dolphin populations plummeted. Congress passed the Marine Mammal Protection Act (MMPA) in 1972, which prohibited the use by American tuna fisherman of fishing methods that would cause dolphin deaths. In 1988, the MMPA was amended to ban tuna imports from nations whose fishing fleets caught

*(continued)*

tuna using purse seine nets. In 1990, the Dolphin Protection Consumer Information Act (DPCIA) was passed by Congress, and the "dolphin safe" label was created. Tuna caught with purse seine nets were prohibited from using this label in the United States. These actions dramatically reduced dolphin deaths, from 500,000 per year in the 1960s to 15,550 in 1992 and further declines since then, reducing the threat to endangered dolphin populations. The cost of implementing dolphin-safe labeling legislation, conducting negotiations with foreign governments, and preventing the sale of tuna caught with dolphin-unsafe methods was estimated by the Congressional Budget Office at $6 million per year.

The WTO ruling represents a victory for Mexico's three largest tuna producers: Grupo Herdez, Grupo Maritimo Industrial, and Pescados Industrializados, which collaborated with the Mexican ministries of Agriculture and Economy in the long-running battle to sell tuna in the United States. Beginning in 1980 under the WTO predecessor, the General Agreement on Tariffs and Trade (GATT), Mexico has repeatedly challenged American "dolphin safe" standards in what was dubbed "GATT-zilla versus Flipper." The most recent case was filed by Mexico in 2008. Although 315,000 tons of tuna were imported into the United States in 2010, Mexico asserted that "dolphin safe" standards resulted in unreasonably greater challenges to sell their tuna in the United States and violated trade rules.

"Dolphin safe" labeling is a voluntary measure, and tuna harvested with "dolphin unsafe" methods can legally be sold in the United States (but not with the "dolphin safe" label), which appears to comply with WTO guidelines. However, the WTO ruled that "dolphin safe" was a technical regulation rather than a standard. The WTO asserted that anything impeding nonlabeled tuna's "marketing opportunities in the United States" represents a barrier to trade and that "dolphin safe" labeling violates Article 2.2 of the WTO agreement, which prohibits technical regulations that are "more trade-restrictive than necessary to fulfill a legitimate objective." Therefore, the United States must discontinue the "dolphin safe" labeling program or face WTO sanctions. There is limited opportunity for the United States to appeal the ruling, and because the United States agreed to the WTO treaty, Article VI of the U.S. Constitution holds that the WTO agreement "shall be the Supreme Law of the Land; and the Judges in every State shall be bound thereby."

This WTO ruling on "dolphin safe" labeling has been viewed by some as evidence that trade agreements such as the WTO can erode national policies enacted on the basis of public interest and welfare. Several observers have expressed concern that the WTO has established a dangerous precedent that could be extended to a range of other public policy issues, such as environmental protection (e.g., habitat protection, clean air and water) or food chain safety (e.g., limitation on use of potentially damaging fertilizers or pesticides, existence of genetically modified organisms in food products).

**Questions:**

1. Do you think that the WTO should be able to prohibit voluntary labeling efforts that provide information of potential value to consumers in a particular nation? Why or why not?

2. Should the WTO be able to overrule nations when national laws are based on sound science? How could the WTO ensure that the science behind local laws and regulations is sound and not a cover for protectionism?

3. Some people have argued that member nations give up national sovereignty rights by joining the WTO and allowing that organization to make decisions that are not in the best interest of a particular nation, especially since many WTO meetings are not open to the public. Do you agree with this interpretation and, if so, what could be done to address the situation?

Source: World Trade Organization, "Difference between a Technical Regulation and a Standard," *Technical Information on Technical Barriers to Trade*, www.wto.org/english/tratop_e/tbt_e/tbt_info_e.htm (June 26, 2011); Food and Agriculture Organization of the United Nations, "Tuna Purse Seining," www.fao.org/fishery/fishtech/40/en (June 26, 2011); Sam Williford, "WTO Eliminates 'Dolphin Safe' Labeling," *Economy in Crisis*, May 23, 2011, www.economyincrisis.org/content/wto-eliminates-%E2%80%9Cdolphin-safe%E2%80%9D-labeling, June 26, 2011); "U.S. Constitution—Article 6," www.usconstitution.net/xconst_A6.html (June 26, 2011); Public Citizen, "U.S. Dolphin-Safe Tuna Labeling Rule Deemed a WTO Violation," May 20, 2011, http://citizen.typepad.com/eyesontrade/2011/05/us-dolphin-safe-tuna-labeling-rule-deemed-a-wto-violation.html (June 26, 2011); American Albacore Fishing Association, "WTO Court Rules Against US Dolphin Safe Label Requirement," May 24, 2011, www.americanalbacore.com/wto-court-rules-against-us-dolphin-safe-label-requirement (June 26, 2011); and Loraine Mitchell, "Dolphin-Safe Tuna Labeling," *Economics of Food Labeling*, pp. 22-25, http://agritrade.cta.int/en/layout/set/print/content/view/full/4738 (June 26, 2011).

restraint agreements (VRAs) and by others "voluntary" export restraints (VERs). *Voluntary* is in quote marks because these barriers are imposed by the U.S. government on the exporting countries. The inevitable result is higher costs to American consumers, because exporters send only the higher-priced top of their lines and importers charge more for scarcer products. The United States is not the only country that imposes VRAs and VERs on its trading partners—far from it. Japan, Canada, the EU countries, and many others require that countries exporting to them "voluntarily" limit the number or value of goods exported.

## TORTS

**torts**
Injuries inflicted on other people, either intentionally or negligently

**product liability**
Standard that holds a company and its officers and directors liable and possibly subject to fines or imprisonment when their product causes death, injury, or damage

**strict liability**
Standard that holds the designer/manufacturer liable for damages caused by a product without the need for a plaintiff to prove negligence in the product's design or manufacture

Torts are injuries inflicted on other people, either intentionally or negligently. Tort cases in the United States may result in awards of very large sums of money. Other countries have tort laws that restrict the amount of money that can be obtained in tort actions.

### Product Liability
One important area of torts, especially in the international arena, is **product liability.** Product liability laws hold a company and its officers and directors liable and possibly subject to fines or imprisonment when its product causes death, injury, or damage. Such liability for faulty or dangerous products was a growth area for the U.S. legal profession beginning in the 1960s. Liability insurance premiums soared, and there were concerns that smaller, weaker manufacturing companies could not survive. In the 1980s that boom spread to Europe and elsewhere. As foreign firms buy or build U.S. plants, they are being hit by the same liability and insurance problems have long been faced by U.S. companies.[13]

Manufacturers of products are often held to a standard of **strict liability,** which holds the designer/manufacturer liable for damages caused by a product without the need for a plaintiff to prove negligence in the product's design or manufacture. There are several reasons to believe that the impact of strict liability on product designers and manufacturers in Europe and Japan will not be as heavy or severe as it is in the United States. The EU allows companies to use "state-of-the-art" or "developmental risks" defenses, which allow the designer/manufacturer to show that at the time of design or manufacture, the most modern, latest-known technology was used. They also are permitted to cap damages. By comparison, damages awarded by American juries have been in the hundreds of millions of dollars.

Other differences in legal procedures in the United States compared with those in Europe and Japan will limit or prevent product liability awards by European and Japanese courts. As mentioned, in the United States, but not elsewhere, lawyers take many cases on a contingency-fee basis, whereby the lawyer charges the plaintiff no fee to begin representation and action in a product liability case. The lawyer is paid only when the defendant settles or loses in a trial, but then the fee is relatively large, running between one-third and one-half of the settlement or award. In addition, outside the United States, when the defendant wins a lawsuit, the plaintiff is often called upon to pay all the defendant's legal fees and other costs caused by the plaintiff's action.

In the United States, product liability cases are heard by juries that can award plaintiffs actual damages plus punitive damages. As the name indicates, punitive damages have the purpose of punishing the defendant, and if the plaintiff has been seriously injured or the jury's sympathy can be otherwise aroused, it may award millions of dollars to "teach the defendant a lesson." Outside the United States, judges, not juries, hear product liability cases. Judges are less prone to emotional reactions than juries are, and even if the judge is sympathetic toward a plaintiff, punitive damages are not awarded by non-U.S. courts.

### Punitive Damage Effects
Multimillion-dollar punitive damage awards by U.S. courts have caused foreign firms to keep their products out of the United States. For instance, Axminster Electronics, a British firm whose devices help prevent crib death by monitoring a baby's breathing, does not sell in the United States because it cannot secure product liability insurance. Within the United States, every drug company knows that if a person uses a drug and subsequently gets ill, there is a chance that a jury somewhere in the United States may impose liability on the manufacturer and order it to pay damages.

### Buyer Beware in Japan
The Japanese law on product liability requires that the plaintiff prove design or manufacturing negligence, which is difficult with complex, high-tech devices. The plaintiffs' difficulties are exacerbated by the unique Japanese legal

procedures to provide discovery, the process by which plaintiffs can seek defendants' documents relevant to their cases. Discovery is available to plaintiffs in U.S. courts but is limited in Japan.[14]

## MISCELLANEOUS LAWS

Individuals working abroad must be alert to avoid falling afoul of local laws and police, army, or government officials. Some examples make the point.

- A Plessey employee, a British subject, was given a life sentence in Libya for "jeopardizing the revolution by giving information to a foreign company." Saudi Arabia may strictly enforce sanctions against importing or drinking alcohol and wearing revealing clothing. Foreigners in Japan who walk out of their homes without their alien registration cards *(gaikakujin toroku)* can be arrested, as happened to one man while he was carrying out the garbage. An Australian writer was sentenced in Thailand to three years in jail for writing a novel (seven copies sold) that insulted the crown prince. Brunei has caned nearly 500 foreigners since 2004 for settling illegally in the sultanate.

- A New York law firm, International Legal Defense Counsel (ILDC), has made a reputation by dealing with countries where American embassies and consulates are of little legal help. One of its cases involved a Virginia photographer named Conan Owen, who agreed to transport a package of cocaine from Colombia to Spain, where he was arrested and slapped with a stiff prison sentence. The U.S. Attorney General personally interceded with no success, and Owen languished in prison for nearly two years. Then, ILDC obtained his freedom through the use of a bilateral prisoner transfer treaty that permits American inmates in foreign jails to do their time in a facility back home. Once in the United States, Owen was quickly freed.

# U.S. Laws That Affect the International Business of U.S. Firms

Although every law relating to business arguably has some effect on international activities, some laws warrant special notice. We will look briefly at several U.S. laws. Although many U.S. laws affect activities of international firms, there has not been a successful effort to coordinate them. Some are even at cross-purposes, and some diminish the ability of U.S. businesses to compete with foreign companies.

## FOREIGN CORRUPT PRACTICES ACT

During the 1970s, revelations of **questionable or dubious payments** by American companies to foreign officials rocked governments in the Netherlands and Japan. Congress considered corporate bribery "bad business" and "unnecessary." As a result, the **Foreign Corrupt Practices Act (FCPA)** became law. Key provisions of the act involve bribery of foreign officials and requirements for transparency of accounting transactions.

There are a number of uncertainties about terms used in the FCPA. An interesting case in point involves "grease." According to the FCPA's drafters, the act does not outlaw *grease,* which refers to facilitating payments made solely to expedite nondiscretionary official actions. Such actions as customs clearance and telephone calls have been cited. However, there is no clear distinction between supposedly legal grease payments and illegal bribes. To confuse matters further, U.S. Justice Department officials have suggested that they may prosecute some grease payments anyway under earlier antibribery laws written to get at corruption in the United States. The act is very broad in what constitutes a foreign official, and the government's relevant criterion for a bribe is not the amount but rather the intent of the payment.

**questionable or dubious payments**
Bribes paid to government officials by companies seeking to purchase contracts from those governments

**Foreign Corrupt Practices Act (FCPA)**
U.S. law against making payments to foreign government officials for special treatment

Other doubts raised by the FCPA concern the accounting standards it requires for compliance. That matter is connected to questions about how far management must go to learn whether any employees, subsidiaries, or agents may have violated the act; even if management were unaware of an illegal payment, it could be in violation if it "had reason to know" that some portion of a payment abroad might be used as a bribe.*

The FCPA makes it unlawful to bribe foreign government officials to obtain or retain business. Facilitating payments for routine government actions such as visa issuance, import approvals, and the processing of government papers are permissible under the FCPA. In January 2010, nearly two dozen U.S. corporate executives were indicted in an undercover "sting" operation for bribing an African minister of defense. After a record-setting level of enforcements in 2010, there are indications that increased efforts at enforcement of the FCPA will produce a growing level of prosecutions and fines in subsequent years.[15]

Critics believed that the FCPA would harm American companies' competitiveness abroad because it would demand of American companies a higher standard of behavior than was common in the competitive environment. Congress decided that the potential economic damage to exports would be minimal and that the only companies that would be hurt would be those whose only means of competing was through the payment of bribes. The United States actively lobbied the international community to introduce similar legislation, which it did in 1997, with the OECD Convention on Bribery. In response, the FCPA was amended in 1998 to incorporate antibribery conventions developed by the OECD.

You may wonder if U.S. laws on bribery place U.S. businesses at a disadvantage in international competition. What seems to have happened on the bribery front is interesting. The FCPA, along with the OECD convention and the UN initiative, have brought a discussion of bribery and transparency out into the open. Such discussions were further stimulated by the Asian financial crisis of 1997, one of whose causes was widely attributed to lack of transparency in financial dealings. Having an international reputation for transparency and being perceived as "aboveboard" have become increasingly important for global companies. There appears to be a strong move for company values that support integrity in the belief that integrity is better for business than are corrupt activities.

**Other Antibribery or Anticorruption Statutes**   There are other laws regulating corruption and bribery. Among the most noteworthy is the UN Convention against Corruption (UNCAC), signed by more than 151 countries as well as the EU as of 2011.[16] The UNCAC goes beyond bribery to address a broader range of corruption, such as general abuse of power and trading in official influence, as well a the recovery of assets from officials accused or convicted of engaging in corruption.

In 2011, the United Kingdom Bribery Act came into force, which includes penalties for corporate failure to prevent bribery. The person engaging in a bribe does not need to be British and the act of bribery does not need to have occurred in the United Kingdom. A corporation can be charged under this law as long as it engages in "a business or part of a business" in the United Kingdom, suggesting that this law may be applied extraterritorially. As new legislation, this act is accompanied by a substantial amount of uncertainty regarding what would qualify as adequate procedures to prevent bribery and how broadly the association with potential bribe-payers is interpreted (e.g., are joint venturers liable for the actions of their partners?).[17]

**Measuring Likelihood of Bribery Abroad: The Bribe Payers Index**   The organization Transparency International publishes a bribe payers index (see Table 7.4). This index assesses the likelihood that firms from industrialized nations will engage in bribery abroad. Its data for 2008 (the latest survey) are based on a survey of 2,742 respondents from 26 countries.

*Other words with similar connotations are *dash, squeeze, mordida, piston, cumshaw,* and *baksheesh.*

## TABLE 7.4 — Bribe Payers Index

| Country | Rank for Year of Study | | | |
| --- | --- | --- | --- | --- |
| | 1999 | 2002 | 2006 | 2008 |
| Canada | 2 | 5 | 5 | 1 |
| Belgium | 8 | 6 | 9 | 1 |
| Switzerland | 5 | 2 | 1 | 3 |
| Netherlands | 6 | 6 | 8 | 3 |
| United Kingdom | 7 | 8 | 6 | 5 |
| Germany | 9 | 9 | 7 | 5 |
| Japan | 14 | 13 | 11 | 5 |
| Australia | 2 | 1 | 3 | 8 |
| Singapore | 11 | 9 | 12 | 9 |
| France | 13 | 12 | 15 | 9 |
| United States | 9 | 13 | 9 | 9 |
| Spain | 12 | 11 | 13 | 12 |
| Hong Kong | n.a. | 15 | 18 | 13 |
| South Korea | 18 | 18 | 21 | 14 |
| Taiwan | 17 | 19 | 26 | 14 |
| South Africa | n.a. | n.a. | 24 | 14 |
| Italy | 16 | 17 | 20 | 17 |
| Brazil | n.a. | n.a. | 23 | 17 |
| India | n.a. | n.a. | 30 | 19 |
| Mexico | n.a. | n.a. | 17 | 20 |
| China | 19 | 20 | 29 | 21 |
| Russia | n.a. | 21 | 28 | 22 |

\* n.a. = data not reported.

Source: Transparency International, *Bribe Payers Index 2008,* www.transparency.org/policy_research/surveys_ indices/bpi (June 24, 2011); Transparency International, *Bribe Payers Index 2006,* www.transparency.org/policy_ research/surveys_indices/bpi/bpi_2006 (June 24, 2011); Transparency International, *Bribe Payers Index 2002,* www.transparency.org/policy_research/surveys_indices/bpi/bpi_2002 (June 24, 2011); Transparency International, *Bribe Payers Index 1999,* www.transparency.org/policy_research/surveys_indices/bpi/bpi_1999 (June 24, 2011); and Transparency International, "TI Report: Emerging Economic Giants Show High Levels of Corporate Bribery Oversees," December 9, 2008, www.transparency.org/news_room/latest_news/press_releases/2008/bpi_2008_en (accessed June 24, 2011).

## ACCOUNTING LAW

Investor confidence in the integrity of financial reporting and corporate governance has been shaken by financial scandals worldwide. This crisis of confidence has substantially damaged the economic prospects of numerous companies, employees, retirees, customers, suppliers, and other stakeholders.

U.S. accounting practice is guided by the Securities and Exchange Commission (SEC) and the Financial Accounting Standards Board (FASB) and follows standards known as generally accepted accounting principles (GAAP), while most other countries, including those in the EU, follow standards issued by the International Accounting Standards Board (IASB) known as the International Financial Reporting Standards (IFRS). These standards differ in many aspects, but a number of projects looking toward convergence are expected to be completed in 2015. This area is further explored in Chapter 18.

### Rory Burdick: Career Launch in International



Rory Burdick graduated from California Polytechnic State University with a business major and economics minor, both with an international concentration. Then he traveled, just for the adventure of it all. The following are comments he has made about this journey.

After completing my courses at Cal Poly, I joined a group of friends who were traveling to South Africa from East Asia. I went on to travel through London, Amsterdam, Berlin, and Prague. After emptying my bank accounts, I returned to San Francisco to work in various technology startups.

I joined a successful startup whose customer base eventually grew to a size that required 24/7 customer support, and the decision was made to implement "follow-the-sun" coverage across the United States, Europe, India, and China. This decision led to my first international work experience—managing the training of these offshore support groups. During this project, I learned how to overcome cultural, communication, and time zone issues. A college friend moved to Paris, which was a good excuse for a road trip originating in Amsterdam, then traveling through Paris, Marseille, Barcelona, back to Paris through the Pyrenees, and finally returning to Amsterdam.

Shortly after that road trip, I was approached with an opportunity to interview for a position at Google. Once a part of Google, I joined a small global team and traveled on assignment to Atlanta, New York, and Frankfurt. A director visiting my group in Mountain View mentioned he was looking for someone to take a position in Brazil. Knowing very little about the country or the opportunity, I expressed interest and arranged an interview with the hiring manager, which led to a six-month assignment in São Paulo that included a short assignment in Buenos Aires. Since

returning to the United States, I have spent time with my family in British Columbia and Nuevo Vallarta, and I am writing this profile from Sardinia, Italy.

I'd like to tell you my personal travels have been well-thought-out cultural excursions, but in reality I've chosen my destinations for surfing (South Africa, Mexico), snowboarding (Canada, Santiago), festivals (Europe, Jamaica), and the opportunity to travel with good friends in countries with favorable exchange rates! After joining Google, I worked hard to establish myself with local management as an ambitious self-starter who could be trusted with difficult projects where individual contributors would have minimal support from management. Once established as a strong individual contributor and leader, I was asked to travel to locations that were short-handed or needed project-specific burst labor. My travels enabled me to interface with employees from different locations around the world, which helped me make a name for myself. This strategy allowed me to make a case for taking the position in Brazil for a related group in a position I had never before performed.

Roughly four months passed between initially expressing my interest and being offered the position in Brazil, but I only had three weeks to prepare for departure! After the initial interview, I was given the names of several people who had worked or were currently working in South America. Some were Americans like me, and others were Brazilians who had grown up in or around São Paulo. I conducted a series of informational interviews with these staff members to hear what they had to say about their experiences. I asked about the culture of Brazil, personal safety, cost of living, and what the city of São Paulo had to offer. All of them had insightful comments, but nothing would fully prepare me for my assignment.

I can honestly say my time in Brazil was both the most challenging and most rewarding experience of my life. São Paulo has one of the most ethnically diverse populations in the world, and because of this I blended in with everyone else. I inherited a project that was behind schedule and suffered from various vendor and contractor issues, as well as internal customer issues. I had to quickly find solutions despite my language shortcomings, while maintaining a positive relationship with our Brazilian business partners. I managed this by closely watching the cultural norms of those around me and maintaining a positive attitude with a quiet confidence. By demonstrating my desire to perform well and my interest in establishing positive relationships, my Brazilian counterparts were extremely interested in working with me to find mutually beneficial solutions to the hurdles we faced.

There were many amazing aspects of my trip, but three stand out from the rest. Portuguese is a beautiful language with elements of Italian, Spanish, and French. Being thrown into full submersion without any previous experience was quite humbling, but it has provided me with a language foundation that allows me to communicate with most Latin populations. In addition to their beautiful language, it is hard not to fall in love with the Brazilian people and their culture. Warm and outgoing, they were eager to engage me in conversations ranging from my family back home to political issues we face as new American

cultures. Most importantly for me, I was able to singlehandedly bring a project back onto schedule while building relationships in an international context.

Relocating to a foreign country for an employment opportunity is an exciting and overwhelming experience that is difficult for anyone to prepare for fully. While I would definitely recommend talking to people or reading about the culture and history of the country you will be visiting, even more important is language and a positive attitude. My experience has been that people are curious about and outgoing toward visitors who show interest in learning about them. The more able you are to communicate with people, the more they will tell you about their culture, their country and themselves. The knowledge I have gained from my studies pales in comparison to what I have learned from interacting with people on a personal level.

## Resources for Your Global Career

**International Law and Culture Cue**

When traveling and conducting business globally, always keep in mind that the laws of many countries are steeped in the country's religious heritage. This means that breaking a law in these countries may also be seen as an act of huge disrespect for one's religious beliefs. World religions such as Muslim, Hindu, and Buddhism, also termed "code religions," clearly define accepted behavior and serve as a basis for the laws in countries where these religions are dominant. Become sensitive to and respectful of the religious influences in the countries with which you trade. It is wise to show respect and interest when others may tell you about their religious beliefs, but be astute to keep your religious preferences and beliefs to yourself. Never put yourself in a position where your religious beliefs may be interpreted as superior to those of the country you are in. You just might also be breaking a local law.

***Your Worldwide Resources for Foreign and International Law:***

- EISIL (Electronic Information System for International Law): www.eisil.org/
- American Bar Association Section on International Law: www.abanet.org/intlaw/home.html
- Careers in International Law: www.luc.edu/law/career/pdfs/International.pdf
- Career Resources in International Law, www.nyls.edu/centers/harlan_scholar_centers/center_for_international_law/career_resources
- International Law Review Association: http://studentorgs.law.smu.edu/ILRA
- Finding Foreign Law Online when Going Global: www2.lib.uchicago.edu/~llou/global.html
- Foreign and International Law Resources: www.washlaw.edu/forint/alpha/a.html
- Worldwide Legal Directories: www.hg.org/internat.html
- International Law Blog: http://blogs.law.harvard.edu/internationallaw/
- Worldwide Legal Resources and Legislation Affecting Marketing: www.theglobalmarketer.com/law/index.jsp
- Worldwide Legal Directories and Resource for International Law Articles: www.hg.org/guides.html
- International Intellectual Property Law Resources: www.asil.org/ip1.cfm and www.lib.uchicago.edu/e/law/intlip.html

## Summary

**LO7-1 Discuss the complexity of the legal forces that confront international business.**

International business is affected by many thousands of laws and regulations issued by states, nations, and international organizations. Some are at cross-purposes, and some diminish the ability of firms to compete with foreign companies.

**LO7-2 Explain the possibilities for international dispute settlement.**

International dispute settlement possibilities include litigation and arbitration. Litigation across borders often raises the issue of which jurisdiction's law should apply and where the litigation should occur. Arbitration is often less expensive, faster, and more informal than litigation. Both litigation and arbitration face difficulties in enforcement.

**LO7-3 Recognize the need and methods to protect your intellectual property.**

Patents, trademarks, trade names, copyrights, and trade secrets are referred to as intellectual properties. Pirating of those properties is common and is costly for their owners. The UN's World Intellectual Property Organization (WIPO) was created to administer international property treaties, as was TRIPS, a WTO agency with a similar purpose.

**LO7-4 Explain the risk of product liability legal actions.**

Product liability refers to the civil or criminal liability of the designer or manufacturer of a product for injury or damages it causes. In several ways, product liability is treated differently in the U.S. legal system than it is in other countries. For example, only in the United States does one find lawyers' contingency fees, jury trials of these cases, and punitive damages. Although the principle of strict liability has been adopted in Europe, defendants are permitted to use state-of-the-art defenses and countries can put a cap on damages. Product liability is virtually unknown in Japan.

**LO7-5 Discuss some of the U.S. laws that affect international business operations.**

Many U.S. laws affect international business operations, both of U.S. and of foreign companies. The United States applies

federal employment laws to any U.S. company operating anywhere. This extraterritoriality means that U.S. companies operating in foreign countries are required to follow U.S. employment law as it applies to U.S. nationals. The Foreign Corrupt Practices Act also applies to U.S. businesses in their foreign operations and to foreign businesses that conduct operations in the United States.

## Key Words

public international law (p 183)

private international law (p 183)

treaties (p 183)

extraterritorial application of laws (p 183)

litigation (p 184)

arbitration (p 185)

Incoterms (p 185)

intellectual property (p 186)

patent (p 186)

trademark (p 187)

trade name (p 187)

copyright (p 187)

trade secret (p 187)

competition laws (p 189)

antitrust laws (p 189)

torts (p 194)

product liability (p 194)

strict liability (p 194)

questionable or dubious payments (p 195)

Foreign Corrupt Practices Act (FCPA) (p 195)

## Questions

1. What is the significance of determining whether a country follows the rule of law?

2. How does international law differ from national law? What are the sources of international law?

3. What objections do other countries have to extraterritorial application by the United States of its laws?

4. Why do many people from outside the United States dislike engaging in litigation in the United States?

5. What are advantages of submitting contract disputes to arbitration instead of to litigation in courts?

6. What are the primary types of intellectual property, and why do companies concern themselves with intellectual property issues?

7. What are competition laws, and how do the laws and the approaches differ between the United States and other parts of the world?

8. Are tariffs the only type of obstacle to international trade? If not, name some others.

9. Can product liability be criminal? If so, in what sorts of situations would product liability become criminal behavior?

10. What is the Foreign Corrupt Practices Act? What arguments or evidence can you identify in support or opposition to laws such as the FCPA?

## Research Task

globalEDGE.msu.edu   globalEDGE

Use the globalEDGE site (http://globalEDGE.msu.edu/) to complete the following exercises:

1. Your company is considering expanding to Singapore. Because of this, top management is hoping to better understand the intellectual property (IP) laws of this country. Using the *Intellectual Property Office of Singapore* (IPOS) website, prepare a short report on trademark protection in Singapore. In your report, include a discussion addressing the following: (a) the benefits of trademark registration, (b) registrable and unregistrable marks, and (c) the steps in the application process.

2. Transparency International's *Corruption Perceptions Index* (CPI) is a comparative assessment of a country's integrity performance. Provide a description of this index and its ranking. Using the most recent data, identify the five countries with the lowest and the five with the highest CPI scores according to this index. Do you see any trends between CPI scores and the level of economic and social development of a country?

# Minicase: Determining Country of Jurisdiction for International Business Disputes

A California-based company is expanding very well and has just made its first large export sale. All of its sales and procurement contracts up to now have contained a clause providing that if any disputes arise under the contract, they will be settled under California law and that any litigation will be in California courts.

The new foreign customer, who is Italian, objects to these all-California solutions. She says she is buying and paying for a large volume of the products, so before finalizing the sales contract she says that the California company should compromise and allow Italian law and courts to govern and handle any disputes.

**Questions:**

1. You are the CEO of the California company, and you very much want this large export order. You are pleased with the service your law firm has given, but you know it has no international experience. What are the various forms of dispute resolution available to your California company? What are the advantages and disadvantages of each for your company?

2. In deciding whether to only use California law for settling litigation or to allow the foreign customer's home nation of Italy as the venue for litigation, would your analysis be any different if the customer was from China? From Russia? From the United Kingdom? Why or why not?

# Global Leadership Issues and Practices

Globalization and its demands have shifted the skill set necessary to lead in the twenty-first century. Headhunters are desperately trying to find executives with the right mix of skills, but they are rare and becoming difficult to find.

*—Mendenhall, Osland, Bird, Oddou & Maznevski, Global Leadership: Research, Practice, and Development*

# The Challenge of Finding Global Leaders with the "Right Stuff"

Globalization is not only creating many new business opportunities, it is also creating opportunities for a new breed of leaders that have the "right stuff" for operating in an increasingly globalized world.

Rapid economic growth in the emerging markets, particularly the so-called BRIC nations (Brazil, Russia, India, and China), is creating large new markets for consumer and industrial goods. The revolution in communications and computer technology, including the Internet, social media, smartphones, and other developments, is enabling diverse and geographically dispersed groups of employees to collaborate in their work and to learn from and with each other. Developments in shipping and logistics are heightening pressure on companies to reconfigure their value chains in order to maintain competitiveness. Expanded geographic scope of operations is exposing companies to different regulatory environments, a more diverse set of suppliers and competitors, and exposure to a variety of unfamiliar risks.

International companies require a new type of leader in order to compete successfully in this complex and dynamic global environment. These global leaders need to not only be proficient in terms of their business acumen, but to also evidence an array of additional skills. They must be able to envision the nature and direction of change that is occurring within and across markets of the world and the implications of these changes for the company's strategy. They must show cultural understanding and adaptability, rather than being constrained by experiences only within their home country and culture. They must be able to understand, work with, and inspire individuals from a range of nations and cultures to create new technologies, businesses, and organizations. These skills and more are necessary in order for executives to lead their companies to success in the 21st century.
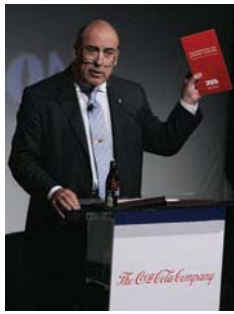
Where are such global leaders found? They can come from anywhere in the world. Indeed, we can see a Brazilian-born son of a French mother and a Lebanese father (Carlos Ghosn) as the leader of both Japan-based (Nissan) and Paris-based (Renault) automakers who are in a strategic alliance to compete in North America and the rest of the world. We can see a Turkish-American son (Muhtar Kent) who attended high school in Turkey and university in the United Kingdom, serving as the leader of U.S.-based Coca-Cola. Or we can see a woman born and educated in India (Indra Nooyi) move up to her role as CEO of a leading global consumer products company (PepsiCo). With the right preparation, global leaders with the "right stuff" can come from anywhere on the planet.

# 11

## learning objectives

After reading this chapter, you should be able to:

**LO11-1**  **Discuss** the importance of creating a company "global mindset."

**LO11-2**  **Describe** what distinguishes the practice of global leadership from its domestic counterpart.

**LO11-3**  **Identify** the competencies required for effective global leadership.

**LO11-4**  **Discuss** approaches for selecting and developing effective global leaders.

**LO11-5**  **Explain** what skills a manager needs in order to effectively lead global teams.

**LO11-6**  **Identify** some of the challenges of leading global change.

Can you be a global leader? If so, what will you need to do to prepare yourself for such a role? As we discuss in this chapter, the nature of the leadership challenge varies by company and context, so there is no universal approach to selecting and developing global leaders. However, obtaining a strong grasp of the business fundamentals that underlie international business is an important first step. Building from that foundation with a well-considered approach for developing cultural, linguistic, and other experiences and skills may also help you to develop the "right stuff" for understanding and managing the complex international challenges that global leaders confront, now and in the future.

This chapter focuses on key issues associated with leaders and leadership for international businesses in our increasingly complex and dynamic global world. Despite the opportunities that international business brings, most companies do not have the quantity and quality of leaders necessary to fully and successfully exploit these opportunities. As noted in the opening vignette, changes in the international environment are creating opportunities for leaders with a new set of skills and experiences, what we will refer to as *global leaders*. In this chapter, we will begin by discussing the concept of a global mindset and its importance for global companies. Then we will examine what global leadership is, how global leadership differs from leadership in domestic contexts, and why global leadership is important. We will identify some of the competencies that are required in order to be an effective global leader, as well as issues associated with selecting and developing candidates for global leadership positions. We will also discuss issues associated with leading global teams and managing global change initiatives.

## The Global MindSet

Research indicates that many CEOs feel that developing a company **global mindset** is a "prerequisite for global industry dominance."[1] Global mindset is defined as "one that combines an openness to and awareness of diversity across cultures and markets with a propensity and ability to synthesize across this diversity." It has been argued that global mindset has two key components: (1) intellectual intelligence, which includes business acumen, and (2) global emotional intelligence, which includes self-awareness, cross-cultural understanding, cultural adjustment, and cross-cultural effectiveness.[2] These two components provide the foundation for the global behavior skills that comprise a person's global leadership style.

Percy Barnevik, who served as the leader for the merger of Swedish Asea with Swiss Brown Boveri to create the global engineering and manufacturing giant ABB, aptly observed, "Global managers have exceptionally open minds. They respect how different countries do things, and they have the imagination to appreciate why they do them that way. But they are also incisive; they push the limits of the culture. Global managers don't passively accept it when someone says, 'You can't do that in Italy or Spain because of the unions,' or 'You can't do that in Japan because of the Ministry of Finance.' They sort through the debris of cultural excuses and find opportunities to innovate."[3] Development of a company global mindset and of a cadre of managers with such a perspective is one of the key challenges that confront global leaders and helps to highlight what is different and important about the topic of global leadership.

## What Is Global Leadership, and Why Is It Important?

Leadership is a complex and multidisciplinary concept. Even a cursory review of the academic or managerial literatures quickly reveals the existence of many different definitions of leadership.[4] Rather than review and debate this point, in this chapter we will use as our working definition the notion that **leadership** refers to the behaviors and processes involved with organizing a group of people in order to achieve a common purpose or goal.

Most experts agree that leadership is not the same thing as management, although there is overlap between the two concepts.[5] Warren Bennis differentiated between the two concepts, including the following distinctions:

- The leader innovates; the manager administrates.
- The leader develops; the manager maintains.
- The leader challenges the status quo; the manager accepts it.
- The leader has a long-range perspective; the manager has a short-term perspective.
- The leader asks "what?" and "why?"; the manager asks "how?" and "when?"
- The leader originates; the manager imitates.
- The leader inspires; the manager controls.[6]

**leadership**
The behaviors and processes involved with organizing a group of people in order to achieve a common purpose or goal

While the preceding distinctions highlight some of the differences between management and leadership, what is different about global leadership?

## HOW GLOBAL LEADERSHIP DIFFERS FROM DOMESTIC LEADERSHIP

Most, or perhaps all, of the leadership competencies associated with leadership in domestic settings are also relevant to leadership within global contexts. However, global leaders confront different contexts than do leaders who operate domestically. Globalization introduces additional challenges for companies, including the development of managers who have the ability to understand and operate in the worldwide business environment and to provide a global perspective on leadership of their organizations.[7]

Scholars have identified four overlapping dimensions of complexity that are relevant to globalization and the challenge confronting global leaders: (1) *multiplicity* (the geometric growth in the volume and nature of issues that must be dealt with by global leaders), (2) *interdependence* (although dispersed geographically, the different units of the company are systematically linked to each other rather than being isolated and are increasingly dependent on external organizations), (3) *ambiguity* (the challenge of dealing with information that lacks clarity and incorporates both quantitative and qualitative dimensions, hindering the understanding of cause-and-effect relationships), and (4) *dynamism* (the international system itself is constantly changing).[8]

Globalization increases the complexity of both the external environment (including the geographic as well as cultural reach of the company) and the internal environment in which the firm's operates (e.g., a broader range of backgrounds and motivations of employees). As a result, globalization places increasing emphasis on recruiting and developing human resources with the capability for operating successfully in such a challenging environment.[9] For example, using leadership data from 17,000 managers in 62 countries, Project GLOBE found that different nations evidenced both similar and dissimilar perspectives regarding the traits of leaders.[10] The leadership traits that were found to be universally *acceptable* included decisive, informed, honest, dynamic, administratively skilled, coordinator, just, team builder, effective bargainer, dependable, win–win problem solver, plans ahead, intelligent, and excellence oriented. Leadership traits that were viewed universally as being *unacceptable* included ruthless, egocentric, asocial, nonexplicit, irritable, noncooperative, loner, and dictatorial. However, the acceptability of a number of leadership traits was found to be contingent on the cultural context in which the leader was operating, including enthusiastic, self-sacrificial, risk-taking, sincere, ambitious, sensitive, self-effacing, compassionate, unique, and willful. These findings help to highlight the context-specific aspect of global leadership and the traits of global leaders.

As mentioned before, most of the competencies associated with domestic leadership success are also required for leading within global contexts. However, the degree of difference in the level of demands on skills and their application is so great—and the nature of the possible outcomes that can be produced within a global context can be so

profoundly greater—that global leadership can ultimately be regarded as being different in kind from domestic leadership.[11] As one team of researchers noted, global leadership:

> *differs from domestic leadership in degree in terms of issues related to connectedness, boundary spanning, complexity, ethical challenges, dealing with tensions and paradoxes, pattern recognition, and building learning environments, teams, and community and leading large-scale change efforts–across diverse cultures.*[12]

# What Competencies Are Required for Effective Global Leadership?

In order for an individual to perform successfully as a global leader, what competencies should he or she embody? In answering this question, it might first be of value to highlight the range of roles that a global leader may need to take. Henry Mintzberg and other researchers have identified a range of such roles, including:

- *Monitoring* (e.g., scanning environments, seeking information, monitoring different units of the company).
- *Spokesperson* (e.g., advocating and representing the company, communicating and disseminating information to and with different levels of stakeholders inside and outside the organization).
- *Liaison* (e.g., networking, coordinating, spanning boundaries within and across organizations).
- *Leader* (e.g., motivating and coaching individuals and teams, building and maintaining corporate culture).
- *Negotiator* (e.g., making deals, managing conflict).
- *Innovator* (e.g., seizing opportunities, generating new ideas, promoting a vision for the company).
- *Decision maker* (e.g., troubleshooting, making decisions).
- *Change agent* (e.g., taking action, developing and implementing change plans for the company).[13]
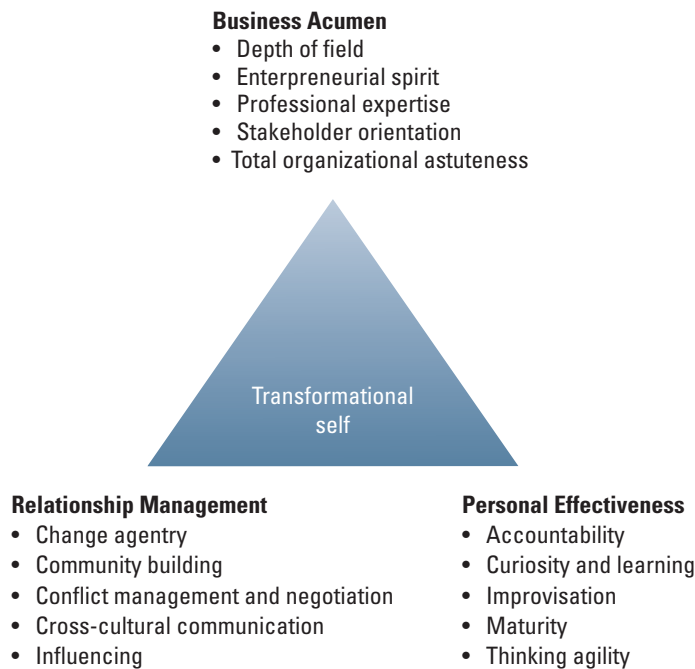
The broad range of duties of global leaders suggests that such individuals require a complex mix of competencies in order to be effective in their duties. Among the many studies that have examined these competencies, a survey conducted by the Corporate Leadership Council identified the following six skills that were considered the most important for global leaders:

- Adaptability across cultures.
- Capability to develop individuals from and across diverse cultures.
- Global strategic thinking.
- Ability to establish business in new markets.
- Capability for building global teams.
- Competency in interacting with local political interests.[14]

Research conducted by the Center for Creative Leadership found that, in order to be effective, global leaders required a similar pattern of traits, capabilities, and role-based skills, as did leaders operating in a strictly domestic setting. However, there was a more significant impact of emotional stability, ability to learn, and decision-making and negotiating roles for global leaders than was the case for domestic leaders.[15] Due to the impact of cultural differences on leadership attributes and performance, researchers from Project GLOBE asserted that a global mindset, cultural adaptability and flexibility, and tolerance for ambiguity were attributes that global leaders needed to have in order to be effective.[16] Terrence Brake created the Global Leadership Triad (see Figure 11.1), which incorporates three interrelated sets of competencies required for effective global leadership: (1) business acumen, (2) relationship management skills, and (3) personal effectiveness skills.[17] Dalton argued that global leaders needed to have four key competencies: (1) a high level of cognitive complexity, in order to collect

FIGURE 11.1

Blake's Global
Leadership Triad

**Business Acumen**
- Depth of field
- Enterpreneurial spirit
- Professional expertise
- Stakeholder orientation
- Total organizational astuteness

Transformational
self

**Relationship Management**
- Change agentry
- Community building
- Conflict management and negotiation
- Cross-cultural communication
- Influencing

**Personal Effectiveness**
- Accountability
- Curiosity and learning
- Improvisation
- Maturity
- Thinking agility

Source: From Terence Brake, *The Global Leader: Critical Factors for Creating the World Class Organization,* 1997, p. 44. Copyright © 1997 The McGraw-Hill Companies. Reprinted with permission.

and comprehend contradictory data from a variety of sources and to subsequently make effective decisions, (2) excellent interpersonal skills in order to enable them to understand how to behave within particular countries and situations, (3) capability for learning from experience, and (4) advanced capacity for moral reasoning in order to comprehend ethical dilemmas.[18]

In contrast to the preceding lists of leadership competencies, the five-level Pyramid Model of Global Leadership, presented in Figure 11.2, attempts to identify a progression of skills required for effective global leadership. At the bottom level is a baseline of global knowledge that is necessary in order for a global leader to perform at even a basic level of competence. Building on this knowledge is a second level of four threshold traits, including humility, integrity, inquisitiveness, and resilience. Level 3 includes attitudes and orientations

FIGURE 11.2

Pyramid Model of
Global Leadership

**Level 5: System skills**
Make ethical decisions
Influence stakeholders
Lead change    Span boundaries
Architecting    Build community
**Level 4: Interpersonal skills**
Mindful communication
Create and build trust
Multicultural teaming
**Level 3: Attitude and orientations**
Global mindset
Congnitive Complexity    Cosmopolitansim
**Level 2: Threshold Traits**
Intergrity    Humanity
Inquisitiveness    Resilience
**Level 1: Global Knowledge**

Source: Adapted from M. E. Mendenhall, J. S. Osland, A. Bird, G. R. Oddou, and M. L. Maznevski, *Global Leadership: Research, Practice, and Development* (New York: Routledge, 2008), Figure 3.3.

## Are Women Appropriate for Global Leadership Positions?

The World Bank has stated that a core development objective is to achieve gender equality and full participation of women in business, particularly in developing nations. Despite this, as noted by Adler,[a] most of the research on leadership has focused on men, with only a minor portion dealing with the potential of women as leaders. Research has continued to show unevenness in terms of the level of participation of women in leadership roles, particularly as reflected in numbers of women leaders in business. Although women occupy more than 51 percent of the managerial and professional positions in U.S. organizations, there are few females in the top tier of corporate leadership.[b] Women CEOs such as Indra Nooyi at PepsiCo or Cynthia Carroll at Anglo American represent a very small minority of the leadership in publicly held corporations. Instead, most of the women who serve as CEOs have either started their own firms or have taken over the leadership of a family business. In a study involving 942 companies from the *Fortune* 1000, it was discovered that almost half of the companies had no women in their top executive ranks. Only 7 percent of the firms had more than two women executives and less than 3 percent had more than three women in top executive positions.[c] Only 14.4 percent of executive officer positions in *Fortune* 500 companies were filled by women in 2010, and only 15.7 percent of the positions on corporate boards.[d] Data such as these suggest that growth in the number of female CEOs in the United States may be constrained in the near future, given the limited quantity of women in the executive pipeline.

Research has shown that women and men differ in terms of their typical leadership styles. For example, women tend to view leadership as an opportunity to empower their subordinates and enhance their potential to excel; men tend to see their leadership position as a chance for exerting control over their subordinates.[e] Adler argues for an increased level of women in global leadership positions, due in part to research suggesting that traits and qualities typically associated with women are consistent with those linked to effective global leadership.[f] For example, she found that global leaders who were women:

- Came from diverse backgrounds, with no predictable pattern associated with their route to leadership positions.

- Were not selected for leadership positions only by women-friendly companies or countries.

- Symbolized hope, change, and unity through their selection as leaders, particularly in light of their position as outsiders who were going against the odds, thereby suggesting the potential for organizational or societal change.

- Were driven to achieve success based on vision, rather than desire for hierarchical status.

- Relied upon broad-based, popular support or support directly from the marketplace, instead of traditional, hierarchy-based structural or party support.

- Pursued paths to power that involved lateral transfers within their organizations, instead of the more traditional path up the hierarchy that was common among men.

- Leveraged the enhanced visibility that they received due to their status as women or as "the first woman." This special status meant that they received more attention from the media than did men, and they were able to use this visibility as a platform to enhance their position and performance.

Consistent with Adler's work, other research has found that women tend to have a leadership style that is more participative, interactional, and relational, with greater levels of emotional intelligence and empathy, than is the case for men.[g] These are attributes that have been suggested as being better suited for leadership performance within a global context. Women have also been found to attribute greater importance to the areas of social responsibility, inclusion and diversity, and global skills—and women were believed to be better prepared in these areas as well—than was the case for men.[h] Women have also been found to use leadership styles that are more participative or democratic and less directive or autocratic than the leadership styles used by men.[i]

### Questions:

1. The research findings presented in this Global Debate suggest that perhaps women might be better suited for the challenges associated with global leadership positions than might be the case for men. Yet how could such a possibility be true, given the small number of women occupying executive leadership positions?

2. What options might be available for increasing the level of participation—and effectiveness—of women in global leadership positions?

[a]N. J. Adler, "Global Leadership: Women Leaders," *Management International Review* 37, no. 1 (1997), pp. 171–96; and N. J. Adler, "Global Leadership: Women Leaders," in M. Mendenhall, T. Kühlmann, and G. Stahl, Eds.) *Developing Global Business Leaders: Policies, Processes and Innovations* (Westport, CT: Quorum Books, 2001), pp. 73–97.

[b]U.S. Department of Labor, Women's Bureau, 2010, "Quick Facts on Women in the Labor Force in 2010," www.dol.gov/wb/factsheets/Qf-laborforce-10.htm (June 13, 2011).

[c]C. Helfat, D. Harris, and P. Wolfson, "The Pipeline to the Top: Women and Men in the Top Executive Ranks of U.S. Corporations," *Academy of Management Perspectives*, 20, no. 4, (2006), pp. 42–64.

*(continued)*

dCatalyst, 2010. "Statistical Overview of Women in the Workplace," March 2011, www.catalyst.org/publication/219/statistical-overview-of-women-in-the-workplace (June 13, 2011).

eJ. Rosener, "Ways Women Lead," *Harvard Business Review* 68, no. 6 (1990), pp. 119–25.

fAdler (2001), pp. 90–96.

gFor example, N. Fondas, "Feminization Unveiled: Management Qualities in Contemporary Writings," *Academy of Management Review* 2, no. 1 (1997), pp. 257–82; and M. A. Brackett, S. E. Rivers, S. Shiffman, N. Lerner, and P. Salovey, "Relating Emotional Abilities to Social Functioning: A Comparison of Self-Report and Performance Measures of Emotional Intelligence," *Journal of Personality and Social Psychology* 91 (2006), pp. 780–95.

hA. Lajtha and A. Carminati-Rabasse, *2008 Women's Research—One Step Ahead of 2011: A New Horizon for Working Women* (2008), https://microsite.accenture.com/mpw/experience/Pages/StepAhead2011.aspx (June 13, 2011).

iA. H. Eagly and B. T. Johnson, "Gender and Leadership Style: A Meta-Analysis. *Psychological Review* 109 (1990), pp. 573–98.

that affect the manner in which global leaders perceive and interpret their world, while the fourth level includes interpersonal skills that enable global leaders to effectively cross cultures. Level 5, at the apex of the pyramid, includes system skills that enable global leaders to effectively influence people and systems inside and outside the company.

The broad array of competencies identified in this section helps to highlight why there is no consensus on the set of competencies that a global leader must possess—simply, the jobs of global leaders tend to be quite diverse. Nevertheless, the preceding discussion identifies many of the attributes that have been identified as facilitating the effectiveness of those individuals who occupy global leadership positions.

# Selecting and Developing Effective Global Leaders

**LO11-4 Discuss** approaches for selecting and developing effective global leaders.

## ASSESSING GLOBAL LEADERSHIP COMPETENCIES

A key challenge confronting companies faced with the challenge of developing global leaders is assessing the competencies of candidates. As discussed earlier in this chapter, there are many different models of the skills and attributes required for effective global leadership, and the variation in components across these models complicates assessment.

To address this challenge of competence assessment, a number of different assessment instruments have been developed. These instruments include the Cross-Cultural Adaptability Inventory (a tool for self-assessment of cross-cultural adaptability),[19] the Intercultural Development Inventory (an instrument for identifying competencies associated with intercultural sensitivity),[20] the Global Competencies Inventory (an instrument to assess personality predispositions linked with effective intercultural behavior and the acquisition of global managerial skills),[21] and the Global Executive Leadership Inventory (a 360-degree feedback approach for identifying leadership competencies and awareness gaps associated with those competencies).[22] Each of these instruments has its own unique strengths and weaknesses, depending on the context in which it will be used.

## MODELS FOR DEVELOPING GLOBAL LEADERS

An important issue facing international companies is developing an understanding of how to develop effective global leaders. Are candidates just "born global," with a special set of skills and attributes that makes them effective in global leadership contexts, or do these capabilities get developed over time as a result of some interplay among personal attributes, experience, and other factors? Most experts in the field tend toward the latter notion, that global leadership effectiveness is the result, at least in part, of a developmental process rather than innate capability.[23] As a result, various models of global leadership development have been proposed. Understanding these models may assist the international company in developing appropriate processes for enhancing the development of their own cadre of global leaders. This section discusses two models: the Global Leadership Expertise Development (GLED) model and the "right stuff" model.
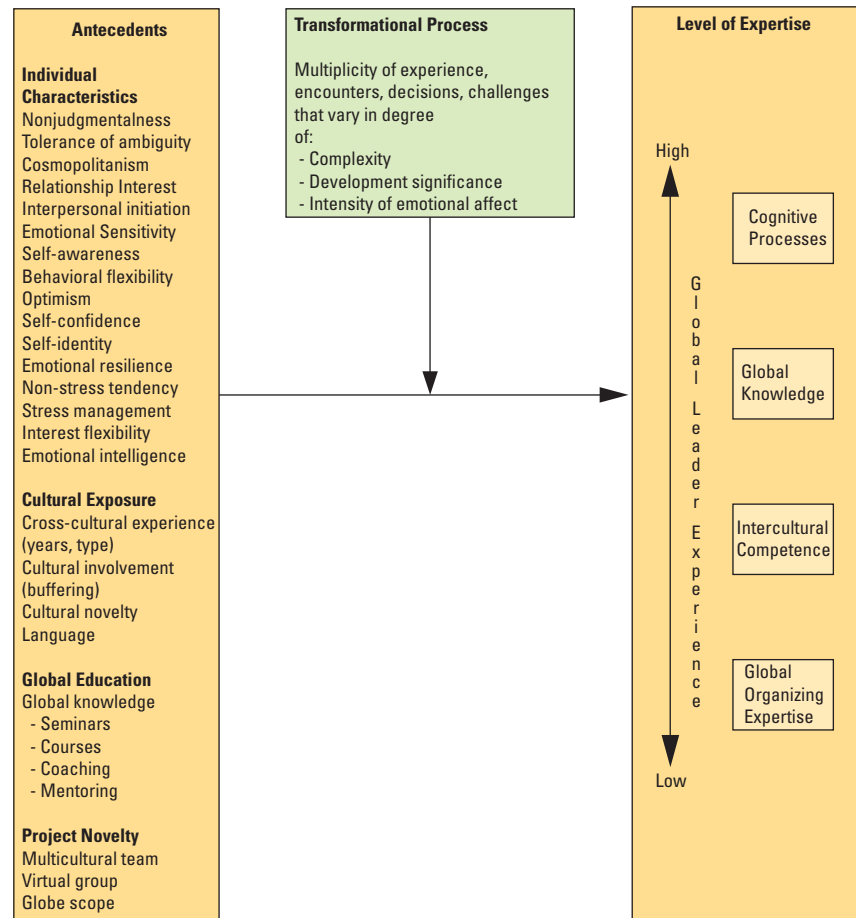
**The GLED Model** A conceptual model designed for developing the expertise of global leaders, the GLED model (Figure 11.3) emphasizes the process by which expertise

**Antecedents**

**Individual Characteristics**
Nonjudgmentalness
Tolerance of ambiguity
Cosmopolitanism
Relationship Interest
Interpersonal initiation
Emotional Sensitivity
Self-awareness
Behavioral flexibility
Optimism
Self-confidence
Self-identity
Emotional resilience
Non-stress tendency
Stress management
Interest flexibility
Emotional intelligence

**Cultural Exposure**
Cross-cultural experience
(years, type)
Cultural involvement
(buffering)
Cultural novelty
Language

**Global Education**
Global knowledge
 - Seminars
 - Courses
 - Coaching
 - Mentoring

**Project Novelty**
Multicultural team
Virtual group
Globe scope

**Transformational Process**

Multiplicity of experience,
encounters, decisions, challenges
that vary in degree
of:
 - Complexity
 - Development significance
 - Intensity of emotional affect

**Level of Expertise**

High

Global Leader Experience

Low

Cognitive Processes

Global Knowledge

Intercultural Competence

Global Organizing Expertise

Source: From J. S. Osland and A. Bird, "Process Models of Global Leadership Development," in M. E. Mendenhall, J. S. Osland, A. Bird, G. R. Oddou, and M. L. Maznevski, *Global Leadership: Research, Practice and Development,* 2008, figure 5.2. Reproduced by permission of Taylor & Francis Books UK.

is developed.[24] This model includes antecedents for the development of global leaders and their expertise, divided among four categories: individual characteristics, cultural exposure, global education, and project novelty. The level of global leadership expertise is hypothesized as being determined collectively by four dependent variables: cognitive processes, global knowledge, intercultural competence, and global organizing expertise. The model asserts that the relationship between outcome measures and antecedents will be mediated by a transformational process. This transformational process is comprised of the set of experiences, interpersonal encounters, decisions, and challenges related to the global leader's expertise, and this process is asserted to be the primary cause of the different levels of global leadership expertise that are observed among leaders with global responsibilities.

**The "Right Stuff" Model**     This model (Figure 11.4) is focused on an outcome of developing global leaders that have the "right stuff" in terms of what they have learned and what they are able to do as leaders. Producing leaders with the right stuff is the result of interaction and partnership between the leader and the organization. The basic talent of the candidates being developed, combined with their developmental experiences and the context in which these experiences occur (and the developmental mechanisms that are employed—the policies and procedures used to ensure that the right people are channeled into the right experiences), will help to produce the right stuff in terms of the global leader's skills and capability. However, this model argues that the company's global business

FIGURE 11.4

The "Right Stuff"
Model

strategy is a major determinant of the relevant lessons that the global leader needs to learn and the skills that will be developed, and therefore what represents the right stuff for a global leader will vary across organizations. In this respect, the strategy and structure of the company determine the number of international jobs in the organization, the types and nationalities of the global leaders, and the skills that the company will require. For example, a company with a strategy that depends on extensive use of alliances with external organizations will require leaders with skills and experience of working with entities beyond the firm's formal boundaries. Correspondingly, an organization's decision to compete in a broad array of less economically developed nations will help determine the number and range of different cultural capabilities that the company's leaders will require.

As the preceding discussion shows, the development of global leaders is a complex process that demands flexibility in order to match the individual, organizational, and external contexts in which the leaders need to learn and to perform. A standardized approach applied to all leadership candidates and across all contexts is unlikely to be successful in developing effective global leaders.

## TOOLS AND TECHNIQUES FOR DEVELOPING GLOBAL LEADERSHIP SKILLS

How can individuals aspiring to positions of global leadership develop the required set of skills and experiences? Development of global leadership skills is a nonlinear process comprised of a set of diverse experiences. Differences in the background and attributes of leadership candidates, as well as the companies and contexts in which they work, suggest that development efforts must be considered on an individualized basis and should consider a variety of different developmental tools and techniques. Global leaders will require strong training in business fundamentals, including international business. A robust comprehension of history, geography, and political science, among other topics, can be invaluable for enhancing understanding and performance within different international settings, as can training in language and culture.

Much of this learning may be achievable through traditional means, such as studying in universities, participating in intensive international business simulations, or attending executive short courses and seminars. However, gaining deeper, nuanced understanding of complex issues such as cross-cultural leadership can seldom be achieved solely through reading books and attending lectures. To develop the skills necessary to deal effectively with the complex, ambiguous, high-level challenges that global leaders face will require these individuals to consider an array of different techniques and experiences, some of which may be undertaken before, during, or shortly after their university studies. Examples include living with host families while studying abroad, in order to enhance language and cultural fluency; international internships, both paid and unpaid; personal and business travel to international locations; working with one's company to identify and participate in short-term or longer-term expatriate assignments within international markets; developing effective networks from contacts at university, work, and other contexts; pursuing opportunities to work within multicultural and virtual teams, including those of an international nature; or pursuing mentoring and coaching opportunities, both on the giving and the receiving end. Consciously considering one's developmental needs and pursuing an appropriate set of activities such as these can be invaluable in developing global leadership capability.

The goal of the leadership development process is to obtain the variety of transformational experiences that are needed in order to truly develop global leadership capability. Of course, not all international and cross-cultural experiences will have the same impact in terms of development of global leadership expertise, and an ongoing sequence of self-reflection and self-assessment will be necessary in order to identify remaining gaps and opportunities for further development. While monitoring career development of prospective global leaders is an important function for a corporation's executives as well as human resource personnel, they cannot force individuals to develop their potential. In that regard, it is important for aspiring leaders to recognize that they have an important role in monitoring and assessing their own development and undertake efforts to ensure that substantive progress is occurring.

## Leading Global Teams

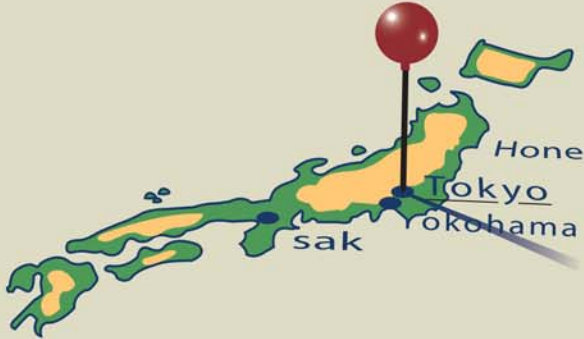LO11-5 **Explain** what skills a manager needs in order to effectively lead global teams.

**global team**
A team characterized by a high level of diversity, geographic dispersion, and virtual rather than face-to-face interaction.

**Global teams** are an increasingly common form for international work. Such teams have members in multiple locations in more than one country. Further, they have several dimensions that add to their complexity. These additional dimensions include members from different national cultures whose locations are in different time zones, different available communication technologies, and different corporate and economic contexts in which their members are being embedded (see Table 11.1). Global teams are characterized by high levels of diversity, geographic dispersion, and virtual rather than face-to-face interaction. In this section, we begin with a discussion of team leading in general, examining the three activities that team leaders usually engage in. Then we explore the added challenges of leading global teams, including their performance management. Note that some scholars use the term *team* to suggest closer psychological bonding than is found in a group; here we are using the terms interchangeably.

| TABLE 11.1 | Differences between Traditional and Global Teams |
|---|---|

| **Traditional Team—Single Context** | **Global Team—Multiple Contexts** |
|---|---|
|  |  |
| **Characteristics** | **Characteristics** |
| 1. One location for work | 1. Multiple locations for work |
| 2. Common national culture in a shared geography | 2. Multiple national cultures in multiple geographies |
| 3. Common economic, political, and social conditions | 3. Multiple dissimilar economic, political, and social conditions |
| 4. Native language speakers, one work language | 4. Native and non-native speakers, several work languages |
| 5. Professional expertise and communication skills | 5. In addition to professional expertise and communication skills, cross-cultural competence and adaptability |
| 6. Task contained within organizational and national boundaries | 6. Task spans organizational and national boundaries |
| 7. Opportunities for frequent face-to-face and informal interactions | 7. Few opportunities for face-to-face and informal interactions, interaction structured and mediated by technology |
| 8. Work within single time zone | 8. Work across multiple time zones |

Source: Adapted from J. Gluesing and C. Gibson, "Designing and Forming Global Teams" in *The Blackwell Handbook of Global Management* (Malden, MA: Blackwell Publishing, 2004), p. 203.

## LEADING TEAMS IS A COMPLEX ACTIVITY

Leading teams in any context involve many activities. Scholars recognize three main activities that are common to most team leadership: establishing teams, coaching team members, and setting team norms.[25] We look at each of these activities and comment on their relevance to global team leadership, and then go on to explore how a global context for team leadership further affects the leadership activities.

The first leadership activity is to establish the team itself. In this process, the leader wants to encourage strong member identification with the team and its norms. Such identification has been shown to lead to better performance. When team members see one another as each member sees him- or herself, and when team members feel that their team is distinctive, even when the team is very diverse, high levels of motivation are likely to exist.[26] The basic task of creating an environment for these team norms to come into play is especially useful in global teams, characterized as they are by high levels of diversity.

The next group leader activity, coaching team members, is critically important in global teams, which usually have high levels of diversity. When faced with diversity, coworkers, if unfamiliar with the work of their group member, tend to expect that person to perform poorly. Chatman and Kennedy point out that such expectations tend to occur regardless of

the person's actual skill level. Such expectations can be self-fulfilling.[27] The team leader can confront this bias by publicizing the strengths of team members. Motivational coaching is also important as the team begins their task, and strategic coaching may be valuable when strategic choices come into play, further along in the team's evolution.

**team norms**
Legitimate, shared standards against which the appropriateness of behavior can be evaluated

Setting team norms is the third key activity for all team leaders. **Team norms** are defined as "legitimate, shared standards against which the appropriateness of behavior can be evaluated."[28] Team norms greatly influence the dynamics of the team, especially in two areas, cooperation and consideration. Cooperation is a critical issue with global teams, especially for those that are not co-located (where team members are not located in the same place). Often in work life, face-to-face interaction takes priority. To respond to requests for collaboration from a nearby coworker is much easier than to put off the coworker so that you can respond to the team member who may be geographically distant, so that synchronous connections are difficult. One way to support cooperation is to increase the level at which team members see one another as members of their in-group. Reward structures also can be set up to encourage group cooperation.

Norms of consideration are also important to teams, and especially so for global teams where the level of diversity is high. By consideration, we mean sensitivity to others. In some of the literature, this area of norms has been described as political correctness, but without the possibly negative associations. We mean something more akin to good manners. For example, when potentially offensive language is self-censored, diverse groups tend to build trust more quickly. The quicker the trust, the sooner the team can move to a constructive focus on the task at hand.

## COMPLEXITY FOR TEAMS IN THE GLOBAL CONTEXT

In addition to these traditional team leader roles, the global team leader is acting within the context of globalization. As described earlier in this chapter, globalization involves a great shift towards increasing complexity. Three specific conditions identified in the international context that contribute to globalization's complexity are increased multiplicity, increased interdependence, and increased ambiguity.[29] We look at these forces a bit more closely in an effort to capture some of the complexity that global team leaders face.

Multiplicity arises from the increased number of players in the game. There are more competitors, more stakeholders, and more customers with globalization. There are many more relationships to manage and many more viewpoints to consider.

Interdependence arises from the very core of globalization and involves economic interdependence, interdependence along the value chain, and interdependence in alliances.

The increased ambiguity results from multiple ways we have to interpret data, of which we have an increasing amount. Yet, the more data we have, the less clear becomes the path for interpreting these data. Cause and effect relationships are not clear, there are multiple plausible interpretations of the same data, and the information itself may not be clear. We are left not knowing how to interpret the data we do have in a way that will guide decisions. This is the complex context in which global teams exist. Table 11.1 summarizes the differences between the simpler, single context team and the global team.

## CULTURE AND GLOBAL TEAM LEADERSHIP

As you can see, global team leaders are challenged in several different ways. In addition to meeting the basic conditions of team performance, that have to do with the team's organization, social processes, and task processes, they face a far more complex context. A major part of this context is culture. Diverse team members bring different cultural expectations to the team environment. Culture controls how the team members even think of the team at deep levels. (Is the team a family? A tribe? A collection of friends? A sports team?) Addressing these differences in connection with the notion of culture can lead to superior performance. Researchers have pointed out, though, that the inclination in diverse teams is to suppress differences and focus on what team members have in common.[30]

As you may remember from Chapter 4, people have differing ways to think about how roles are defined and managed and what acceptable communication and conflict resolution

norms are, depending on their cultural values. In cultures with high power distance, team members will expect, perhaps not fully aware of their expectation, a clear hierarchy and a single leader with decision-making power. These conditions describe the cultural assumptions about leadership in cultures such as Japan and Brazil. In Scandinavian cultures, a more fluid leadership model is expected, where leadership is shared and shifts depending on the task and the leader's ability. In individualistic cultures such as those in the United States or Britain, task roles are clearly defined and responsibility allocated, with individual rewards assumed. Contrast this to more collectivist cultures such as Malaysia and Thailand, where accountability is assumed at the group level and team-level reward assumed. Addressing these differences explicitly builds a foundation for understood and agreed upon roles in the team.

The assumptions about communication and how conflict is handled in the group also need to be directly addressed. Compare some Latin countries, where speaking up at any time is fine, even when someone else is talking, to some Asian countries, in which you respond only to questions and silence is a comfortable way to communicate. How does this cultural predisposition operate in the virtual world? How does the culture deal with disagreement? Is open disagreement appropriate? Or is harmony so valued that disagreement is withheld? It is important for the team to be able to resolve conflict constructively, but, as you can imagine, this may be a difficult process.

Understanding the various cultures of team members is important to the team's functioning. Maznevski suggests a process that can open up the cultural assumptions team members may have, involving three steps: map, bridge, and integrate.[31] *Mapping,* the first step, is to discuss the differences and similarities, that is, to map the relevant characteristics of team members. This is followed by a *bridging* effort. In bridging, team members communicate with each other about the differences and establish how the team members will work with one another. Bridging involves decentering—seeing the other person's point of view—and avoiding blame. Effective bridging also enables *integration,* which is the process of managing the various differences so that team members begin to understand the expectations and assumptions of their team members, as well as their backgrounds and skills.

## VIRTUAL AND GEOGRAPHICALLY DISPERSED TEAMS

Many global teams are geographically dispersed and communicate through technology. Leading a team whose members are on different continents and in different time zones, and that connect through technology, creates unique leadership challenges. Virtual communication, even with video content, lacks the richness of face-to-face communication. Research suggests that initial face-to-face meetings for teams that plan to subsequently work virtually are a good way to build trust among team members. Such trust is critical for the functioning of the team. Most teams meet at their launch and during crises. Maznevski points out that virtual teams with high performance actually schedule regular face-to-face meetings to discuss progress and issues, and to further develop their relationships. Such regular meetings create a kind of regular heartbeat. "[T]eams that have a strong heartbeat can manage all other tasks virtually in between their face-to-face meetings, and . . . this is both less expensive and more effective than getting together 'whenever we need to.'"[32]

## PERFORMANCE MANAGEMENT IN GLOBAL TEAMS

What do we understand about rewarding global team performance in these often culturally diverse, geographically dispersed, and virtual global teams? Researchers suggest that if we could point to one factor to account for many of the failures of global teams, that factor would be ineffective reward and recognition strategies.[33] The critical issues are:

- Are rewards based on individual performance, team performance, or a combination of the two?
- What factors come into play with team-based pay?
- What role can recognition play?

Individual-based rewards are most commonly used, despite the fact that individual contributions to global teams are difficult to discern, especially in a virtual environment. Team-based

rewards are thought to suffer from social loafing. **Social loafing** is the tendency of some people to put forth less effort when they are members of a group. A combination of individual and group rewards is seen by many researchers as a good approach to resolving this issue. There are five areas that will benefit from consideration in establishing a balance of team and individual rewards:

1. What is the nature of the task? How interdependent is it? The greater the task interdependence, the higher the portion of team-based rewards should be.

2. How stable is the team membership? If the team boundaries are fluid or if membership changes are frequent, appropriate team rewards will be difficult to determine.

3. What are the national cultures of the team members? The individualism-collectivism dimension of the cultures needs to be considered. High levels of team rewards are appropriate for teams whose members are from collectivist cultures, and high levels of individual rewards are appropriate for teams whose members are from more individualist cultures. With high levels of cultural diversity, the team should be involved in the development of the reward system.

4. What are the labor laws that affect employee compensation? In many locations, salary levels are set by local or national laws or by labor unions, and their flexibility is constrained.

5. What are the available reward options? In addition to financial rewards, recognition is a valued reward. These rewards are most successful when they incorporate national cultural values of team members.[34]

Remember that performance appraisal for global teams will also be influenced heavily by national level culture and by the other team variables mentioned in our discussion of their rewards and recognition.

Global team leadership is an evolving skill that will be increasingly important going forward. Early research suggests that global teams require the leadership skills that basic teams need, and then the increased awareness and more subtle leadership skills that help the team build on its diversity and its geographic dispersion, all in a context that is increasingly complex.

# Leading Global Change

Leading organizational change is always a difficult process, largely because it deals with changing individual behaviors. Leadership professor Jim Clawson believes that change is the central part of leadership. He writes that leadership has three elements: "(1) seeing what needs to be done; (2) understanding all the underlying forces at play in the situation; and (3) having the courage to initiate actions to make things better."[35] Key players in the change process have to alter their behavior. Their behavior rests on their assumptions, values, beliefs, perceptions, tasks and roles.[36] If the scope of the change that global managers hope to effect is global, then the process becomes exponentially difficult. The difficulty comes from the size of the organization, its geographical dispersion, and, most significantly, the varying expectations and values that surround personal assumptions about change in different national level cultures.

## CHANGE MODELS

Research on global change is in its early stages, and it builds on the more general study of change. Here, we will look first at two models for change and its leadership, and then at the aspects of culture that may influence global change leadership. Each of the models is based on describing the *process* of change and its stages.

Probably the most well-known change model was developed by Kurt Lewin. It is a three-stage process that involves unfreezing, moving, and refreezing. The first stage, *unfreezing,* involves overcoming inertia and preparing people for change, including dealing with defense mechanisms against the proposed change. At this point, there is stress, tension, and recognition of the need for change. The second stage involves *moving* the proposed behaviors into practice, a period often characterized by confusion. *Refreezing* is the final stage, when the new behaviors are either accepted and institutionalized or rejected.

Expanding the level of description found in Lewin's model, John Kotter's approach to change suggests eight steps:

1. Increase urgency, so that people are inspired to move toward real and relevant objectives.
2. Develop the guiding team, so that those involved in leadership are the right people, with high emotional commitment and the right combination and levels of skills.
3. Develop a change vision and strategy.
4. Communicate the vision for buy-in.
5. Empower broad-based action by removing obstacles.
6. Generate short-term wins that are rewarded.
7. Don't let up; foster determination and persistence.
8. Make the change stick through leadership development and succession.[37]

These models might be misconstrued to imply that change is an orderly process and that the steps are nicely sequential. In practice, whether it is incremental or transformative, remember that change is not neat and orderly, largely because it rests on human behavior. Often it involves a lot of learning through trial-and-error approaches.

## CHANGE AND CULTURE

It should not surprise us that aspects of culture are related to the process of change. These aspects of culture include cultural traits related to tolerance of ambiguity, power distance, attitude toward planning, communication styles, flexibility, and other cultural attributes that play out in the change process. Recent research suggests that the influence of national culture is stronger than the influence of organizational culture on change efforts.[38] In her work on the implementation of change, Osland looks closely at this issue, and our discussion is informed by her observations.[39] Cultures that are characterized by high tolerance of ambiguity—that is, cultures that have low uncertainty avoidance—are likely to be more change-friendly. The United States is a prime example of this. Cultures that have high uncertainly avoidance are inclined to avoid change. To lead change in such cultures as Japan, Germany, and France (relative to the United States, Ireland, Denmark, and Jamaica), the process has to be very well outlined and communicated with frequency.

## THE GLOBAL PATH AHEAD

### Chad Henry: Developing Global Leadership Skills and Experience, Beginning with an Internship to Croatia

I was born and raised in Sacramento, California, and went to Cal Poly–San Luis Obispo on a full scholarship to play college football. I initially intended to study architectural engineering, but switched into business administration with a concentration in finance.

After completing my degree and collegiate athletic career, I was searching for direction . I wanted to do something different with my life other than the traditional opportunities that were being offered. I didn't see myself as a traditional "finance" guy and was uncertain if these traditional careers paths would bring personal fulfillment. With the influence of my parents and sports, I had already traveled extensively throughout the United States and thought to myself, "Why not take a step into a new frontier?" At the time, I didn't realize or think about the magnitude of such a decision. As a young man, to me it was an opportunity to work and live abroad.

I ended up applying for and accepting an AIESEC internship to Croatia, a place I knew almost nothing about. I tried to gather as much information as possible about Croatia before leaving. Due to a short time frame, approximately three weeks, I didn't place much thought into my travel. My main preparation focused on understanding exactly where I was going, ensuring that it was safe, and preparing information for my parents so they knew where I was going. The information I gathered was very general.

My internship was only for 12 months. However, I enjoyed the experience and ultimately became fluent with the language, took on a range of different jobs, and lived in Croatia for about 10 years. It was an exciting time in a country undergoing many changes. During this time, I lived in the cities of Split, Varazdin, and Zagreb. I also traveled to a number of countries, including

*(continued)*

Canada, the UK, Netherlands, Denmark, Finland, Germany, Austria, Spain, Italy, France, Belgium, Luxembourg, Switzerland, Poland, Czech Republic, Slovakia, Slovenia, Romania, Bulgaria, Hungary, Croatia, Serbia, Bosnia and Herzegovina, Montenegro, Russia, and the Ukraine, as well as the United States.

Among the jobs that I pursued during my decade abroad, I had positions in export development, strategic development and management consulting (on issues of foreign direct investment, business zone development, organic farming cooperatives, and business process management), investment development (creating a food processing facility), commercial real estate development (for Arena Zagreb, a multifunctional sports hall with 16,000 seats; Arena Centar, a multifunctional shopping and entertainment center; and Ciovo tourist development), and startup development. I also played professional baseball for a Croatian team and coached a team playing American football.

The keys to my successful adjustment while away from the United States included keeping a very open mind and maintaining my determination to succeed. This latter trait helped me deal with challenges as they presented themselves. The biggest challenges I confronted were learning to accept things as they are without making value judgments, remembering that things are more relative rather than absolute. While as individuals we are taught a certain way to do things or approach situations, this doesn't make it right or wrong. When you can learn to accept different viewpoints and see the value in them—even if not necessarily agreeing with them—then it allows you to enjoy and adapt to the culture in which you are immersed.

My greatest rewards from my time abroad included learning to successfully manage people who have intrinsically different values in regard to work; finding a way to work with people, and get the most out of them; and being accepted by peers and friends in another culture. The greatest learning points from my international experience included developing my ability to see and understand things from multiple perspectives and learning to adapt and react to adverse and sometimes hostile situations.

My recommendations regarding what is important to do or not to do to be successful when going abroad include the following:

- It is extremely important to understand the perspective of others while you are abroad. This is developed by cultural differences and values. Without understanding these different perspectives and values, it will be very difficult to resolve differences and disputes. This is also very important in the management of others in regard to both motivation of workers and gaining respect from colleagues.

- Learn the local language.

- Have a general understanding of the history of the country.

- Ask questions.

## Resources for Your Global Career

Building a strong set of business and cultural skills, international experience, and global network of contacts is essential for promoting future success as a global leader. The following sites provide a wealth of different opportunities to assist you in nurturing this set of critical skills and experiences:

- Aperian Global offers a range of useful books, articles, and podcasts dealing with the development of skills for effective performance in cross-cultural and global leadership contexts, and they also have free subscriptions to their newsletter: www.aperianglobal.com/publications_newsletter.asp

- ITAP International, a consulting firm focused on building leadership capability across global and cultural boundaries, offers a variety of articles, recommended readings, YouTube videos, links, and cultural tips: http://itapintl.com/

- The Institute of International Education (IIE) is a nonprofit organization that offers opportunities for study and training for global leadership and development, including the Fulbright Program and Gilman Scholarships that are administered for the U.S. Department of State. Information and resources can be obtained by visiting www.iie.org/What-We-Do.aspx

- The Global Leadership Foundation provides assistance to public sector leaders and governments for improving the quality of governance and political leadership through the direct insights and experience of former national and international leaders: www.g-l-f.org/

- For insight on how to leverage your short-term business travel as a means of enhancing your global leadership potential, see http://onlinelibrary.wiley.com/doi/10.1002/1099-050X(200022/23)39:2/3%3C159::AID-HRM6%3E3.0.CO;2-J/abstract

- Using repatriation policies to enhance the development of global leaders is discussed at www.chrs.rutgers.edu/pub_documents/Article%2059%20Caligiuri%20(2).pdf

- For resources and links to international internships in different regions of the world, for both undergraduate or graduate students, see http://iccweb.ucdavis.edu/international/Internships.htm, http://www.aiesec.org/

- For internship or other job leads for developing international and leadership experience with General Electric, see www.ge.com/careers/students/index.html

- The Center for Creative Leadership provides a broad array of training programs, assessment tools, news, and blogs associated with the development of global leadership capability: www.ccl.org/leadership/index.aspx

People from cultures characterized by high power distance will feel most comfortable with hierarchy and will want top managers to make decisions and issue directives. Likewise, cultures in which respect for the past is strong are likely to resist change. The influence of these varying cultural issues suggests that an ability to communicate across cultural borders and to build trust is essential for global managers as they drive global change in their organizations.

## One Consulting Company's Practical Take on Global Leadership

*"It's the kiss of death to say, 'This is the way we do it back at headquarters.' If they see that you are there to do your job and they are just pawns, you are done and there will be no buy in."*

Aperian Global, a consulting company whose goal is to open the world for its clients (*aperire* in Latin is to open), has researched the issues of how the global context changes what leadership is and what competencies are required for global leadership. Aperian interviewed a 51-member group of corporate leaders, all of whom had 18 months or more on international assignment to a wide variety of locations, where they were judged to be successful leaders. The interviewees came from 24 different countries and had assignments to 31 different countries.

On the first issue, the differences a global context adds to leadership, the responses included an ability to make quick shifts in strategy, business processes and personal styles in order to fit broader ranges of employee motivations and backgrounds. Here is what some of the respondents said:

*The core leadership skills prevail, such as getting results through people . . . but you have to adapt your style to the people, the environment, the way things are done, the things that help you get it done.*

*Global leadership is very different, remarkably different. The business world has some global measures, but how to accomplish those things? We can all agree on growing 10%, but what are the means to get there? The process? The people skills? All these are different to reach the same result.*

Aperian research identified five leadership activities that are important in global leadership, listed here.



Source: http://www.aperianglobal.com/newsletter_archive/publications_newsletter042.asp

- *Seeing differences* is self-awareness in a cultural context. Global leaders need to recognize that their leadership patterns are shaped by their culture, and that other ways to get things done exist.
- *Making connections* is more important in the global environment, because relationships are so important in many cultures, a prerequisite for getting things done. "Results through relationships" is a phrase used to describe this process.
- *Adjusting* is a kind of "frame-shifting" that requires cognitive flexibility to see and respond to differences.
- *Integration and change* describes a complex ability to adjust to some local practices while at the same time, selling other practices into the local environment. It involves a combination of adaptation and questioning the status quo.
- *Localization* is an ability to develop local talent.

In conclusion, global leadership is leadership plus much more, due to the exceedingly complex global environment. You can learn more about Aperian Global's view of global leadership at www.aperianglobal.com.

## Summary

**LO11-1 Discuss the importance of creating a company "global mindset."**

Successful managers in international companies must demonstrate a combination of high knowledge differentiation and high knowledge integration.

**LO11-2 Describe what distinguishes the practice of global leadership from its domestic counterpart.**

Global leadership is leadership behavior that occurs in the more complex global context, where the challenge of leadership is exacerbated based on the dimensions of multiplicity, interdependence, ambiguity, and dynamism. The degree of difference between domestic and global leadership in the level of demands on skills and their applications is so great, and the nature of the possible outcomes that can be produced within a global context can be so profoundly greater, that global leadership can ultimately be regarded as being different in kind from domestic leadership.

**LO11-3 Identify the competencies required for effective global leadership.**

The range of duties of global leaders suggests that such individuals require a complex mix of competencies in order to be effective in their duties. Different researchers have identified different sets of required competencies, including such dimensions as business acumen, adaptability across cultures, capability to develop individuals from and across diverse cultures, global strategic thinking, ability to establish business in new markets, capability for building global teams, competency in interacting with local political

interests, emotional stability, ability to learn, decision-making and negotiating ability, global mindset, cultural adaptability and flexibility, and tolerance for ambiguity. Others have argued for the importance of (1) a high level of cognitive complexity in order to collect and comprehend contradictory data from a variety of sources and to subsequently make effective decisions, (2) excellent interpersonal skills in order to enable them to understand how to behave within particular countries and situations, (3) capability for learning from experience, and (4) advanced capacity for moral reasoning in order to comprehend ethical dilemmas. The Pyramid Model of Global Leadership refers to five levels of competencies, including global knowledge, threshold traits, attitudes and orientations, interpersonal skills, and system skills.

### LO11-4 Discuss approaches for selecting and developing effective global leaders.

Various models of global leadership development have been proposed. Two models discussed in the text include the Global Leadership Expertise Development (GLED) model and the "Right Stuff" model. The GLED model involves antecedents and transformational processes that interact to produce global leadership expertise. The "right stuff" model suggests that the basic talent of the candidates being developed, combined with their developmental experiences and the context in which these experiences occur (and the developmental mechanisms that are employed—the policies and procedures used to ensure that the right people are channeled into the right experiences), will help produce the right stuff in terms of the global leader's skills and capability. However, this model argues that the company's global business strategy is a major determinant of the relevant lessons that the global leader needs to learn and the skills that will be developed, and, therefore, what represents the right stuff for a global leader will vary across organizations.

### LO11-5 Explain what skills a manager needs in order to effectively lead global teams.

Global team leadership is an evolving skill that will be increasingly important going forward. Early research in this new area suggests that global team leadership requires all that basic team leadership needs and then the increased awareness and more subtle leadership skills that help the team build on its diversity and its geographic dispersion—all in a context that is increasingly complex. Among these skills is an understanding of the various cultures of team members. A tool to support this understanding throughout the team is the map-bridge-integrate model. In addition, an ability to create trust in virtual teams is an important skill for leaders of global teams.

### LO11-6 Identify some of the challenges of leading global change.

Leading organizational change is always a difficult process, largely because it deals with changing individual behaviors. Global change involves, in addition to the many challenges of change, an ability to quickly grasp cultural differences in an environment that is often characterized by increased levels of multiplicity, interdependence, ambiguity, and flux.

## Key Words

**global mindset** (p. 280)
**leadership** (p. 281)

**global team** (p. 288)
**team norms** (p. 290)

**social loafing** (p. 292)

## Questions

1. What is a global mindset, and why is it important for international companies?

2. What is the difference between management and leadership?

3. How does global leadership differ from domestic leadership?

4. What are the different types of roles that a global leader may need to take?

5. How does Blake's Global Leadership Triad differ from the Pyramid Model of Global Leadership? How are the two models similar?

6. Compare and contrast the GLED model and the "right stuff" model of leadership development. What is similar between the two models? What is different?

7. What are some of the tools and techniques that an aspiring global leader might be able to use to develop his or her global leadership skills?

8. Describe global teams.

9. Many business managers will say, "Leadership is leadership the world over." What are they missing?

10. How might national level culture affect change?

Use the globalEDGE site (http://globalEDGE.msu.edu/) to complete the following exercises:

1. Your long-term goal is to be in a position of global leadership in a large, multinational corporation. As you take this course, you realize the importance of developing global leadership skills through international and cross-cultural experiences. As a result, you are now considering participating in an international internship program. Using the International Internship Directory provided by globalEDGE, identify internship opportunities in private corporations in Germany. Which three programs do you find most interesting?

2. During your university studies, you have been taking French lessons. Although you are now fluent in the language, you still do not feel comfortable speaking it. Your mentor, a global marketing director at a consumer products company, suggested that you live in France for a period of time to further enhance your French-speaking skills and, at the same time, to develop global leadership capability. Use *Exploring Abroad*—which contains information on working, teaching, studying, and traveling abroad—to prepare a short report on living in France.

# Minicase: Justin Marshall—A Failed Global Leadership Opportunity?

Justin Marshall earned a bachelor's degree in business, with honors, from a prominent state university in the American Midwest. After graduation, he worked for two years in the finance department for a consumer products company and then two additional years in business development, consistently receiving excellent performance reviews from his superiors. He then returned to school to pursue a MBA degree at one of the top-ranked universities, ultimately graduating in the top 5 percent of his class. After being headhunted by several corporations, Justin accepted a lucrative offer to work for a prominent computer software and services company, which we will call Compcorp. Demonstrating stellar performance, Justin quickly worked his way up the corporate hierarchy. By the age of 31, he was promoted to a position as divisional vice president for the United States, where he oversaw the transformation of his division from one with mediocre performance to one of the most profitable divisions in Compcorp's global operations.

Justin's performance as division VP caught the eye of the company's senior executives, and he was offered the opportunity to become VP of one of Compcorp's international operations, a division serving the Asia-Pacific region. Although growing in overall sales, this division had underperformed its major competitors in recent years, and Compcorp's executives told Justin that they wanted to see if he could replicate his earlier success and transform the Asia-Pacific unit's performance.

Justin leaped at this opportunity. He had always dreamed of living and working abroad, and he exuded confidence that he could quickly diagnose the unit's problems and turn things around. Within a month, he had transitioned out of his former position, packed up his family, and moved into an apartment near the Hong Kong headquarters of his division. Applying the skills and experiences he had honed in his earlier positions, Justin began an aggressive evaluation of his new division. He pored over the financial statements and other documentation, met with dozens of key personnel throughout his division, and quickly initiated changes to help ratchet up performance. Rigorous reporting requirements and performance reviews were implemented, and Justin met with each of his country managers and other key personnel to agree on a set of ambitious cost-cutting and revenue growth targets. Individual unit performance was monitored closely and the results of each individual unit were shared across the unit's top managers. As Justin expected, performance showed a strong uptick during his second quarter as division VP. When he traveled back to headquarters for a quarterly review meeting with his superiors and the heads of other divisions, he proudly pointed out his unit's performance improvements and projected even stronger results for upcoming quarters. He basked in the positive feedback and attention he received from his bosses, as well as the substantial performance bonus he had earned. Justin felt that it was only a matter of time until he was promoted again, perhaps into a senior VP position back at headquarters.

During the months after he returned to Hong Kong, results for Justin's third quarter in office evidenced a slight decline, and he was also surprised to receive resignation letters from several key managers from his division. A few of these departing managers took comparable positions with Compcorp's competitors in the region, and rumors of morale problems began to filter back into the Hong Kong offices. Despite Justin's efforts to turn the situation around, the trend of personnel departures and performance declines continued into Justin's fourth quarter in office. A team from the American headquarters visited the region several times, meeting with Justin and a number of his executive team members and other subordinates, trying to discern what the problem was and how it should be resolved.

Justin realized that he needed to do something, and soon, to reverse the performance trend, or his position would be at risk.

Despite his efforts to initiate a number of rapid changes, performance did not improve. Shortly after his unit reported additional subpar performance for Justin's fifth quarter in office, he was invited back to company headquarters for a meeting with the company's president. At that meeting, Justin was informed that he was being reassigned to a VP position in one of Compcorp's less prestigious domestic units and that a replacement executive was being appointed to lead the Asia-Pacific region.

Although termed a lateral transfer, Justin knew that his reassignment was viewed in the company as a demotion and that his once high-flying career path had encountered serious turbulence. Despite his efforts to focus on his new position and reestablish his visibility in the company, and to regain the career trajectory he had once had, Justin felt that his actions were not paying off. Within a year of his transfer, he left the company to pursue opportunities with a different organization.

**Questions:**

1. What might explain Justin's failure to perform well in his new leadership role as the head of the Asia-Pacific division?

2. What might Compcorp have done to enhance prospects for Justin's successful performance? What might Justin himself have done to enhance the likelihood of success in his new assignment and to help avoid derailing an otherwise highly promising career in Compcorp?

*This page intentionally left blank*