

Chapter 1
ASSESSING THE ENVIRONMENT
POLITICAL, ECONOMIC, LEGAL, TECHNOLOGICAL

LECTURE OUTLINE

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The Video Correlation Guide can be downloaded from the Instructor Resource Center. To obtain a user name and password please contact your local Pearson sales representative.

Chapter Learning Objectives

- 1-1. To understand the global business environment and how it affects the strategic and operational decisions which managers must make
- 1-2. To develop an appreciation for the ways in which political, economic, legal, and technological factors and changes impact the opportunities that companies face
- 1-3. To recognize the role of the legal environment in international business
- 1-4. To review the technological environment around the world and how it affects the international manager's decisions and operations

Opening Profile: Assessing Risks in Russia (see slide 1-3)

This opening section briefly describes the top risks involved in assessing risk in Russia to include sanctions-based retaliatory measures and a decline in business activity. The section describes other issues such as the threat of backlash in Russia against Western products, and the continued standoff between Russia and Ukraine; global outcry after Malaysia Airlines Flight 17 shot down. Globalization has compounded the types and levels of business risks. Managers face the challenges of: politics, cultural differences, global competition, terrorism, sustainability, and social obligations (**see slide 1-4**)

I. Chapter Learning Goals (see slide 1-5)

A. What is International Management?

International management (**see slide 1-6**) is the process of developing strategies, designing and operating systems, and working with people around the world to ensure sustained competitive advantage.

1. What is Globalization?

- a. Global competition (**see slide 1-7**) global competition characterized by networks of international linkages that bind countries, institutions, and people in an interdependent global economy. Economic integration results from the lessening of trade barriers and the increased flow of goods and services, capital, labor, and technology around the world.
- b. Some argue that the world is reverting more to *deglobalization*. This retreat, or inversion, is resulting from political crises, cybertheft, protectionism, and increasing trade barriers, which, in turn, have resulted from the global trade slowdown

2. Global Trends (see slide 1-8)

- a. The changing balance of growth toward emerging markets compared with developed ones, along with the growing number of middle-class consumers in those areas.
 - b. The need for increased productivity and consumption in developed countries in order to stimulate their economies.
 - c. The increasing global interconnectivity—technologically and otherwise, as previously discussed, and, in particular, the phenomenon of an “electronically flattened earth” that gives rise to increased opportunity and fast-developing competition.
 - d. The increasing gap between demand and supply of natural resources, in particular to supply developing economies, along with the push for environmental protection.
 - e. The challenge facing governments to develop policies for economic growth and financial stability.
3. 2014-2015 Foreign Direct Investment Confidence Index Top 25 Targets for FDI (**see slide 1-9**)

It is clear that globalization—in the broader sense—has led to the narrowing of differences in regional output growth rates, driven largely by increases led by China, India, Brazil and Russia and South Africa. Global turmoil has curtailed investment, and company executives remained wary of investment in 2015. Emerging economies called MINT (Mexico, Indonesia, Nigeria, Turkey) continue to grow.

According to the 2014-2015 Foreign Direct Investment Confidence Index Top 25 Targets for FDI, the main types of FDI are acquisition of a subsidiary, joint ventures, licensing, and investing in new facilities or expansion. The United States is in the lead since 2013, followed by China, Canada, United Kingdom, and Brazil. India has dropped to seventh from second in two years. Results show confidence in the economic recovery of the United States and Europe. Rapidly developing economies continue to grow.

4. Chapter Learning Goals & Challenges to Globalism (**see slides 1-10 & 1-11**)

The backlash against globalization comes from those who feel that it benefits advanced industrial nations at the expense of many other countries and the people within them who are not sharing in those benefits. Joseph Stiglitz, a Nobel Laureate, for example, argues that such an economic system has been pressed upon many developing countries at the expense of their sovereignty, their well-being, and their environment. Critics point to the growing numbers of people around the world living in poverty.

While the debate about the effects of globalization continues, it is clear that economic globalization will be advanced by corporations looking to maximize their profits with global efficiencies, by politicians and leaders wishing to advance their countries’ economies, and by technological and transportation advances that make their production and supply networks more efficient. However, pressure by parties against those trends, as well as the resurgence in nationalism and protectionism, may

serve to pull back those advances to a more regional scope in some areas, or limit them to bilateral pacts.

5. Effects of Institutions on Global Trade

a. Two major groups of institutions play differing roles in globalization: World Trade Organization and International Labor Organization are examples of supranational institutions which are trying to promote the convergence of how international activities should be conducted. National organizations such as the Food and Drug Administration in the United States sometimes plays a role in making it more difficult for foreign firms to compete in the domestic market.

6. Effects of Globalization on Corporations

a. Global companies are becoming less tied (**see slide 1-12**) to specific locations and their operations and allies are spreading around the world as they source and coordinate resources and activities wherever needed. Companies that desire to remain competitive will have to develop a cadre of experienced international managers.

7. Small and Medium-Sized Enterprises (SMEs)

Small companies also affect and, are affected by globalism. They play a vital role in contributing to their national economies through new job creation and employment, development of new products and services, and international operations such as exporting. There has never been a better time for SMEs to go global; the Internet is as valid a tool for small companies to and customers and suppliers around the world as it is for large companies. By using the Internet, email, and Web-conferencing, small companies can inexpensively contact customers and set up their global businesses.

Discussion Question: Evaluate the statement by Thomas Friedman that the world is flat. What does he mean by this statement?

Teaching Resource: For the latest statistics, have your students visit one of the following Web sites:

World Trade Organization—www.WTO.org

Financial Times—www.ft.com

CEO Express—www.ceoexpress.com

B. The Globalization of Human Capital (**see slide 1-13**)

1. Major changes are occurring in the world labor force, including the following:
 - a. Increased movement across borders for all types of workers
 - b. Increased offshoring of jobs to lower wage countries
 - c. Increased offshoring of white-collar jobs

While firms still offshore manufacturing jobs, some are reshoring jobs to lower shipping costs. For global firms, winning the “war for talent” is one of the most pressing issues, especially as hot labor markets in emerging markets are causing extremely high turnover rates.

C. The Globalization of Information Technology (see slide 1-14)

1. Of all the technological development propelling international business today, the one that is transforming the international manager's agenda probably more than any other is information technology. The explosive growth of information technology is both a cause and an effect of globalism.

Teaching Tip: The Financial Times has a regular monthly special section on information technology. See also Forbes online: <http://www.forbes.com/technology/>

Management in Action: Global Cybertheft of Corporate Secrets (see slide 1-15)

Added to the risks that businesses have encountered in the global environment is cybertheft, which has become common, hard to detect, and difficult to combat. In May 2014, the U.S. Department of Justice (DOJ) charged five Chinese military personnel of cybertheft, stealing trade secrets and identity theft from U.S. Steel, Alcoa, Westinghouse Electrical, Solar World AG, and United Steelworkers. Those companies were targeted because they contested China's trade policies through the World Trade Organization and the Commerce Department. The Chinese government vehemently denied any such activities. Protection of intellectual property is the primary risk in China. China's goal is to achieve technological superiority by importing and adapting technologies

Further allegations were formalized against hackers located in Russia. Although company executives have been aware of such hacking for some time, they are now willing to publicize that information to expose the economic cyber espionage in an attempt to control future damage to their companies. Although then Attorney General Eric Holder acknowledged that those accused would unlikely be brought to trial because there is no extradition treaty with China, he made it clear that there are costs to pay for stealing trade secrets and harming the interests of U.S. companies.

B. Regional Trading Blocs (see slide 1-16)

Much of today's world trade takes place within three regional free-trade blocs (Western Europe, Asia, and the Americas). These trade blocs are continually expanding their borders to include neighboring countries, either directly or with separate agreements.

1. The European Union "EU"

- a. EU (see slide 1-17) comprises a 28-nation, unified, borderless market of approximately 500 million people, as shown in Map 1.2. Countries around the world trade with the EU countries. Although trade continued to grow in 2010 despite the 2008 global financial crisis, the EU GDP growth was only at 1.8 percent that year, and economic problems in some member states continuing into 2015 were adversely affecting the EU as a whole, resulting in global financial repercussions.
- b. "Germany's prosperity is inextricably linked with the success and survival of the single currency, with more than 38 percent of German exports going to its eurozone partners, and almost 58 percent to the 28 members of the European

Union.” Although Germany has about a quarter of the US population, and a quarter of the U.S. GDP (gross domestic product), it exports more than the United States. Germans were concerned that the need to help prop up weaker economies in the eurozone, such as Greece, would dilute their economic strength.

- c. The EU represents the following challenges to global managers
 - 1. How to deal with the possibility of a market closed to outsiders (“fortress Europe”), a market giving preferences to insiders
 - 2. How to deal effectively with multiple sets of national cultures, traditions, and customs within the Eurozone

Teaching Resources: There is an excellent video on the European Monetary Policy, entitled “The history of the European Monetary Policy,” available from Films for the Humanities and Sciences.

The Website www.eurunion.org contains information on all aspects of the European Union as well as links to the country sites of member nations and prospective member nations.

3. Asia (see slide 1-18)

- a. Japan and the Four Tigers of Hong Kong, Singapore, South Korea, and Taiwan,—each of which has abundant natural resources and labor—provide most of the capital and expertise for Asia’s developing countries. ASEAN is negotiating a free trade agreement and moving towards a common market.
- b. The Chinese market offers big opportunities for foreign investment, but you must learn to tolerate ambiguity and find a godfather to look after your political connections.
- c. China has enjoyed success as an export powerhouse, a status built on its strengths of low costs and a constant flow of capital.
- d. India is becoming known as the world’s service supplier, providing highly skilled and educated workers to foreign companies. India is the world’s leader for outsourced back-office services, and increasingly for high-tech services, with outsourcing firms like Infosys becoming global giants themselves. A common comparison says that China grows because of its government and India grows in spite of it. There is an expanding middle class, but many of India’s citizens are still mired in poverty.
- e. South Asia has also developed a trade bloc that includes Bangladesh, Bhutan, India, the Maldives, Nepal, Pakistan, Sri Lanka and Afghanistan.
- f. Although not part of Southeast Asia but, of Oceania, which includes New Zealand and islands in the Pacific Ocean, Australia signed an ASEAN friendship treaty with Southeast Asia.

4. The Americas (see slide 1-19)

- a. The NAFTA free-trade agreement between the United States, Canada, and Mexico has created a trading block—“one America”—with 421 million consumers, making the Northern Hemisphere the largest market in the world. From Mexico’s perspective, the country’s exports have exploded under NAFTA; U.S-Mexico bilateral trade increased from \$88 billion in 1993, the year prior to

the implementation of NAFTA, to \$383 billion (estimated) in 2010, an increase of 335 percent. However, Mexico's dependence on the United States for its exports—NAFTA's greatest success—was shown to be a liability in the global economic downturn as Mexico felt the full brunt of declining consumption in the United States. Brazil: The Federal Republic of Brazil is Latin America's biggest economy and is the fifth largest country in the world in terms of land mass and population, with about 193 million people. According to the U.S. Department of Commerce, Brazil is the 7th largest economy in the world. While most of the developed world has been mired in debt and stunted growth prospects, Brazil's economy is stable and growth prospects are bright. Yet poor infrastructure remains an obstacle (less than 10 percent of roads are paved), and drastic inequality among Brazil's people hampers domestic growth.

- b. The U.S.-Central America Free Trade Agreement (DR-CAFTA) has passed Congress and includes five countries in Central America and the Dominican Republic. The agreement is seen as a stepping stone to the Free Trade Area of the Americas (FTAA) to include 34 countries in the Americas. Cuba is excluded from the proposed agreement.

Teaching Tip: Challenge your students to think about the “threat” associated with “free trade.” Ross Perot once suggested that NAFTA would create a giant sucking sound, drawing jobs away from the United States. A discussion question to raise those issues might be, “If NAFTA was sucking away important U.S. jobs, why was unemployment in the United States at record-low levels after NAFTA came into effect?”

Another question: “If there is a giant sucking sound from Mexico to China as off-shored jobs have gone to China because of its low wages, what should Mexico do to battle unemployment?”

5. Other Regions in the World (see slide 1-20)

- a. Sweeping political, economic, and social changes around the globe represent new challenges to international managers. The move toward privatization has had an enormous influence on the world economy. Economic freedom is a critical factor in the relative wealth of nations.

Teaching Tip: Ask your students, “Can a country be successful if it has economic freedom but not political freedom?”

- b. The Russian Federation—Foreign investment in Russia boded well for the economy until the situation with Ukraine, caused a considerable downturn in confidence. The rate of inflation soared to 11.4 percent over the 2014–2015 period. Forecasts for GDP for 2015 were cut, ranging from zero growth to a contraction of 0.7 percent. Membership in the WTO in 2011 promised trade liberalization.
- c. The changing geopolitical landscape due to the revolutions across the region, which

toppled leaders in Tunisia and Egypt and ousted the regime of Colonel Muammer Gaddafi in Libya, have made investors wary but looking for opportunities. Egypt, where the political landscape has been redrawn in recent months, is beginning to attract interest from Gulf, Western, and Asian international investors. The United Arab Emirates is the most competitive economy in the Arab world, followed by Qatar and Kuwait.

d. **Developing Economies**—characterized by change that has come about more slowly as they struggle with low gross national product (GNP) and low per capita income, as well as burdens of large, relatively unskilled populations and high international debt. Their economic situation and the often-unacceptable level of government intervention discourage the foreign investment they need. Many countries in Central and South America, the Middle East, and Africa desperately hope to attract foreign investment to stimulate economic growth.

e. **The African Union (AU)**

The AU comprises the 53 African countries and was formed from the original Organization of African Unity (OAU) primarily to deal with political issues. According to the International Monetary Fund (IMF), seven of the world's ten fastest growing economies are in Africa. However, there continue to be many major problems in the region. Africa has received little interest from most of the world's investors, although it receives increasing investment from companies in South Africa, the region's biggest economy. Trade between China and Africa has risen to well over \$100 billion today. At a projected growth rate of over 5.4 percent in 2015, prospects for Africa are improving.

f. **South Africa**

The South African economy has been growing since 1998 amid a more stable political environment since the defeat of apartheid. GNP growth has been 2.2 percent from 2008 through 2014. South Africa is a country of 48.7 million people, rich in diverse cultures, people, and natural resources. South Africa is a logical choice for U.S. companies to enter the African continent.

Comparative Management in Focus: China Loses Its Allure (see slide 1-21)

1. **The Allure of doing business in China**
 - a. Until 2010, China grew at 10 percent for 30 years, declining to 7.3 percent in 2014.
 - b. Growth of 7 percent for 2015 was called “a new normal” by Premier Li Keqiang.
 - c. China is a developing country, with differences between urban and rural areas.
 - d. China is the second-largest trading partner with the United States.
 - e. State firms play a significant or dominant role.
2. **Comparative Management in Focus: China Losing Its Allure (see slide 1-22):**
 - a. China's legal and regulatory system is arbitrary.
 - b. China leans toward protecting its local firms.
 - c. Political goals and agendas often take precedence over commercially based decisions.
 - d. Discrepancies of business practices make it difficult for SMEs to get started.
3. **Management Focus: Tips for doing business in China (see slide 1-23)**
 - a. Connections are important.

- b. Negotiations will be different from the U.S. and difficult.
- c. Communication must be clear, honest, and fully prepared for.
- d. Culture matters!

F. Chapter Learning Goals (**see slide 1-24**)

1. The rules of the game for global managers are set by each country and its political and economic agenda, its technological status and level of development, its regulatory environment, its comparative and competitive advantages, and its cultural norms. The astute manager will analyze the new environment, anticipate how it may affect the future of the company, and then develop appropriate strategies and operating styles.

The Global Manager's Role (see 1-25) The Contingency Role of the Global Manager Within the larger context of global trends and competition, the rules of the game for the global manager are set by each country: its political and economic agenda, its technological status and level of development; however the global manager works most intimately within the operating environment, with its regulations, its cultural norms, and focus on social responsibility, ethics, and so on.

II. The Political and Economic Environment (**see slide 1-26**)

A. Proactive globally-oriented firms maintain an up-to-date profile of the political and economic environment of the countries in which they maintain operations.

The top ten risks overall were as follows:

1. Economic slowdown
2. Regulatory/legislative changes
3. Increasing competition
4. Damage to reputation/brand
5. Business interruption
6. Failure to innovate/meet customer needs
7. Failure to attract or retain top talent
8. Commodity price risk
9. Technology failure/system failure
10. Cash flow/liquidity risk

B. Political Risk (**see slide 1-27**)

1. **Political risks** are any governmental actions or politically motivated events that adversely affect the long-run profitability or value of firms doing business. Clearly, as evidenced by the 2011 “Arab Spring” uprisings in Egypt and elsewhere, major political changes can affect the business environment and risk level almost overnight. As far as political risk is concerned, a 2011 survey—based on 211 countries and territories—by Aon Risk Solutions found that the political risk level is rising in more countries than it is declining.
2. **Nationalization** refers to the forced sale of the MNCs assets to local buyers, with some compensation to the firm.
3. **Expropriation** occurs when the local government seizes the foreign-owned assets of the MNC providing inadequate compensation, if any at all.
4. **Macropolitical risk** events are those that affect *all* foreign firms doing business in a country or region; e.g., terrorism, the use or threat of use of anxiety inducing violence for

political purposes. **Micropolitical risk** events are those that affect one industry or company or a few companies. **Terrorism** now poses a severe and random political risk.

5. The Political Risk Cont. : (see slide 1-28)

- a. Expropriation without prompt and adequate compensation
- b. Forced sale of equity to host country nationals, usually at or below depreciated book value
- c. Discriminatory treatment against foreign firms in applying laws and regulations
- d. Barriers to repatriation of funds (profits or equity)
- e. Loss of technology or intellectual property rights
- f. Interference in managerial decision making
- g. Dishonesty by government officials

C. Political Risk Assessment

1. International companies must conduct some form of political risk assessment in order to manage their exposure to risk and to minimize financial losses.
2. Risk assessment by multinational corporations usually takes two forms: the use of experts or consultants and the development of internal staff and in-house capabilities. Both means may be used. The focus must be on monitoring political issues before they become headlines. The ability to minimize negative effects on the firm or to be the first to take advantage of opportunities is greatly reduced once developments have been reported in the news.

Teaching Tip: The U.S. State Department issues travel warnings when it decides, based on all relevant information, to recommend that Americans avoid travel to a certain country. Have students compare the travel warnings with current country risk ratings. Warning and other travel information can be found on the Web at: <http://travel.state.gov/>.

Teaching Resource: The Website <http://money.cnn.com/> covers developments in Europe, Asia, Australia, and the Americas. Students can track issues by industry, region, or country. The State Department's Website provides country information at <http://www.state.gov>.

3. For autonomous international subsidiaries, most of the impact from political risks will be at the level of ownership and control of the firm. For global firms, the primary risks are likely to be from restrictions (on such things as imports, exports, and currency) with the impact of the local level of the firm's transfers of money, products, or component parts.

D. Managing Political Risk (see slide 1-29)

1. After assessing the potential political risk of investing or maintaining current operations in a country, managers face perplexing decisions on managing political risk. On one level, they can decide to suspend their firm's dealings with a certain country at a given point—either by the **avoidance** of investment or by the withdrawal of current investments (by selling or abandoning plants and assets). On another level, if they decide that the risk is relatively low in a particular country or that a high-risk environment is worth the potential returns, they may choose to start (or maintain) operations there and accommodate that risk through **adaptation** to the political regulatory environment. That adaptation can take many forms, each designed to respond to the concerns of a given local area.

2. Below are Taoka and Beeman suggested these means of adaptation:
 - a. **Equity sharing** includes the initiation of joint ventures with nationals to reduce political risks.
 - b. **Participative management** refers to actively involving nationals, including those in labor organizations or government, in the management of the subsidiary.
 - c. **Localization** of the operation by modifying the subsidiary's name, management style, and so forth, to suit local tastes. Localization seeks to transform the subsidiary from a foreign firm to a national firm.
 - d. **Development assistance** includes the firm's active involvement in infrastructure development (foreign-exchange generation, local sourcing of materials or parts, management training, technology transfer, securing external debt, and so forth).
3. In addition to avoidance and adaptation, two other means of risk reduction available to managers are dependency and hedging.
 - a. **Dependency**—keeping the subsidiary and host nation dependent on the parent corporation. It can be maintained with four methods:
 1. Input control—parent controls the key inputs.
 2. Market control—parent controls means of distribution.
 3. Position control—key positions in the hands of expatriate or home office managers.

Finally, even if the company cannot diminish or change political risks:
Hedging(minimizing losses associated with political events) can take place through political risk insurance and local debt financing..

E. Managing Terrorism Risk (see slide 1-30)

1. No longer is the risk of terrorism for global businesses focused only on certain areas such as South America or the Middle East. That risk now has to be considered in countries such as the United States, which had previously been regarded as safe. Eighty countries lost citizens in the World Trade Center attack on September 11, 2001. Many companies from Asia and Europe had office branches in the towers of the World Trade Center; most of those offices, along with the employees from those countries, were destroyed in the attack. Thousands of lives and billions of dollars were lost, not only by those immediately affected by the attack but also by countless small and large businesses impacted by the ripple effect; global airlines and financial markets were devastated. For many firms, however, the opportunities outweigh the threats, even in high-risk areas.

Teaching Tip: A number of firms offer political risk consulting services. You could have your students search the Web for some of these firms and report back the methodology that they employ.

F. Economic Risk (see slide 1-31)

1. A country's level of economic development generally determines its economic stability and therefore its relative risk to a foreign firm. Recently, the level of economic risk in Europe was a great concern around the world, in particular regarding concerns in the eurozone brought about by debt problems in Greece. In the 2014, Heritage Foundation Index of Economic Freedom, based on ten freedoms which reduce economic risk, Brazil, Russia, India, and China show a risk–return trade-off for investment.

2. A country's ability or intention to meet its financial obligations determines its economic risk. The economic risk incurred by a foreign corporation usually falls into one of two main categories (**see slide 1-32**); its investment in a specific country may become unprofitable if (1) the government abruptly changes its domestic monetary or fiscal policies, or (2) the government decides to modify its foreign-investment policies. The second situation would threaten the ability of the company to repatriate its earnings and would create a financial or interest-rate risk.
3. The risk of exchange-rate volatility results in currency translation exposure to the firm when the balance sheet of the entire corporation is consolidated and may cause a negative cash flow from the foreign subsidiary.

Teaching Tip: Ask students to choose a country and use the Website www.reuters.com (click investing, and then currencies) to find out how much of that country's currency they would receive if exchanging \$20. Then ask them to find out the cost of some basic items such as the cost of a combo meal at McDonald's, a movie ticket, and a Coca-Cola. How far does the money go there?

4. Currency translation exposure occurs when the value of one country's currency changes relative to another.
5. The four primary methods (**see slide 1-33**) of analyzing economic risk: *quantitative*, *qualitative*, *combination of both*, and the *checklist approach*.

Teaching Resource: CNN financial networks *world financial markets*—of particular interest is their real-time update of stock market indices from every major market in Africa, Asia, Europe, and Latin America. http://www.cnnfn.com/markets/world_markets.html.

III. Chapter Learning Goals & The Legal Environment (**see slides 1-34 & 1-35**)

- A. The prudent international manager consults both local and headquarters' legal services in order to comply with host country regulations and to maintain cooperative long-term relationships in the local area.
- B. Although the regulatory environment for the international manager consists of the many local laws and the court systems in those countries in which he or she operates, certain other legal issues are covered by international law. International law is the law that governs relationships between sovereign nations. The United Nations Convention on Contracts for the International Sale of Goods (CISG) applies to contracts for the sale of goods between countries that have adopted the convention.
- C. The manager of the foreign subsidiary or operating division will normally comply with a host country's legal system. There are three types of legal systems (**see slide 1-36**) in the world: common law, civil law, and Islamic law.
 1. Under common law, used in the United States and 26 other countries of English origin, past court decisions act as precedents to the interpretation of the law.
 2. Civil law is based on a comprehensive set of laws organized into a code. About 70 countries, predominantly in Europe, use civil law.
 3. Islamic countries use Islamic law, which is based on religious beliefs. It is used in 27 countries and combines in varying degrees, civil, common, and indigenous law.

D. Contract Law

1. A contract is an agreement by the parties concerned to establish a set of rules to govern a business transaction.
2. International managers recognize that they will be preparing a contract in a very different legal context from their own.
3. A contract in international business reflects the local legal system and political and currency risks in the country involved—legal consul in such matters is highly recommended.

E. Other Regulatory Issues (see slide 1-37)

1. Countries often impose protectionist policies, such as tariffs, quotas, and other trade restrictions, to give preference to their own products and industries.
2. Tax systems influence the attractiveness of investing in a given country and affect the relative level of profitability for the MNC. Tax issues include: foreign tax credits, holidays and exemptions, depreciation allowances, and profit or value added tax rates. Definitions of key items such as income and source vary across countries, as do reporting requirements.
3. The level of government involvement in the economic and regulatory environment varies a great deal among countries and has a varying impact on management practices.

Teaching Resource: Electronic Embassy—The Electronic Embassy provides information on all of the embassies in Washington, D.C., with links to embassy Websites. The site also includes an online newspaper, Embassy Flash, and an International Business Center for sponsors. This program also provides assistance to embassies and other international organizations in getting their information on the Web. <http://www.embassy.org/>

IV. Chapter Learning Goals & The Technological Environment (see slides 1-38 & 1-39)

Advances in information technology are bringing about increased productivity—for employees, for companies, and for countries. As noted by Thomas Friedman, technology, as well as other factors that are opening up borders—“the opening of the Berlin Wall, Netscape, work flow, outsourcing, offshoring, open-sourcing, insourcing, supply-chaining, in-forming”—have converged to create a more level playing field. The result of this convergence was the creation of a global, Web-enabled playing field that allows for multiple forms of collaboration—the sharing of knowledge and work—in real time, without regard to geography, distance, or, in the near future, even language.

- A. In a global information society, it is clear that corporations must incorporate into their strategic planning and their everyday operations the accelerating macro-environmental phenomenon of *technoglobalism*, in which the rapid developments in information and communication technologies (ICTs) are propelling globalization and vice-versa. Investment-led globalization is leading to global production networks, which results in global diffusion of technology to link parts of the value-added chain in different countries.
- B. The Internet is propelling electronic commerce around the world. In fact, the ease of use and pervasiveness of the Internet raises difficult questions about ownership of intellectual property, consumer protection, residence location, taxation, and other issues.
- C. New technology specific to a firm’s products represents a key competitive advantage to firms and challenges international businesses to manage the transfer and diffusion of proprietary

technology, with its attendant risks. Whether it is a product, a process, or a management technology, an MNC's major concern is the **appropriability of technology**—that is, the ability of the innovating firm to profit from its own technology by protecting it from competitors. Especially difficult is managing the transfer of technology to venture partners who might become future competitors.

- D. An MNC can enjoy many technological benefits from its global operations. Advances resulting from cooperative research and development (R&D) can be transferred among affiliates around the world, and specialized management knowledge can be integrated and shared. However, the risk of technology transfer and pirating is considerable and costly.
- E. Although firms face few restrictions on the creation and dissemination of technology in developed countries, less developed countries often impose restrictions on licensing agreements, royalties, and so forth, and have other legal constraints on patent protection.
- F. The most common methods of protecting proprietary technology are through patents, trademarks, trade names, copyrights, and trade secrets. The International Convention for the Protection of Industrial Property, often referred to as the Paris Union, is adhered to by over 80 countries for protection of patents.
- G. One of the risks to a firm's intellectual property is the inappropriate use of the technology by joint-venture partners, franchisees, licensees, and employees (especially those who move to other companies).
- H. Global managers will want to evaluate the **appropriateness of technology** for the local government—especially in less developed countries. Studying the possible cultural consequences of the transfer of technology, managers must assess whether the local people are ready and willing to change their values, expectations, and behaviors at work and to use new technological methods.

Under the Lens: The Global Role of Information Technology (see slide 1-40)

The city of Seoul—where nine of every 10 residents subscribe to a high-speed wireless Internet connection—is already one gigantic hot spot. “By 2015, when 80 percent of the residents are expected to carry smartphones or tablet PCs, wireless connectivity will be almost as free as it is ubiquitous: the municipal authorities are installing free Wi-Fi wireless hot spots in all the city's public spaces, including 360 parks, 3,200 intersections and 2,200 streets around shopping centers.” Every subway car, motel room, and street corner has high-speed Internet connectivity.

Making cities such as Seoul “smart” is intended to both improve productivity and attract businesses there. In addition, use of the Internet is propelling electronic commerce around the world (as discussed later in this chapter). Companies around the world are linked electronically to their employees, customers, distributors, suppliers, and alliance partners in many countries, resulting in increased communication and efficiency, as is described in the Procter and Gamble website: “P&G has more than 80 video collaboration studios globally. The immersive environment created by video studios allows employees to connect face to face from any part of the world—as if they were in the same room. These studios greatly reduce the need for travel—saving money, time, and reducing P&G's carbon footprint.”

- I. Global E-Business (see slide 1-41) is an important aspect of the changing technological environment. **E-business** is the integration of systems, processes, organizations, value chains, and entire markets using Internet-based and related technologies and concepts. It

enhances global competitiveness by providing efficiencies throughout the value chain. For instance, with a global portal, businesses can contact and negotiate with suppliers and buyers worldwide. **E-commerce** refers directly to the marketing and sales process via the Internet. The Internet and e-business provide a number of advantages in global business such as the following:

1. Convenience in conducting business worldwide; facilitating communication across borders contributes to the shift toward globalization and a global market
2. An electronic meeting and trading place, which adds efficiency in conducting business sales
3. A corporate Intranet service, merging internal and external information for enterprises worldwide
4. Power to consumers as they gain access to limitless options and price differentials
5. A link and efficiency in distribution

Although most of media attention has focused on e-commerce and the end consumer, greater opportunities exist in **B2B** (business-to-business) transactions. However, problems include internal obstacles and politics, difficulties in coordination and in balancing global versus local e-commerce, languages and cultural differences, and local laws. Barriers to e-business also include a lack of readiness of partners in the value chain, such as suppliers.

Teaching Tip: Websites like Forrester Research (www.forrester.com) and E-marketer (www.emarketer.com) provide regular updates on all facets of Electronic Commerce including statistics on the current state of B2B transactions online. Students can visit online or request updates delivered to their email accounts.

Teaching Resource: A Website of interest to students of international management is <http://globaledge.msu.edu>. The site contains a wealth of information and can be assigned with specific questions in mind.

Internet Resources

Visit the Deresky Companion Website at <http://www.pearsonhighered.com/deresky> for this chapter's Internet resources.

Chapter Discussion Questions

1-1. Poll your classmates about their attitudes toward “globalization.” What are the trends and opinions around the world that underlie those attitudes?

Learning Objective: 1; AACSB: Dynamics of the global economy

Opinions and comments will vary concerning the issue of globalization, and it is important that the differing opinions be allowed to be expressed. There is a concern that globalization destroys cultures, benefits only wealthy countries, hurts the environment, and lowers wage rates. Each of these issues could be addressed in a discussion of student opinions concerning globalization.

1-2. How has the economic downturn impacted trends in protectionism and nationalization?

Learning Objective: 1; AACSB: Dynamics of the global economy

As the fallout from the financial meltdown spread around the world in 2009, nationalist impulses gathered a storm as government maneuvers to take stakes in ailing industries were verging on partial or full nationalization—though, for the most part, not forcing it. Japan, for example, took a cue from the United States in taking majority stakes in major banks; while in Russia, the Kremlin was exploiting the economic crisis to establish more control over industries that it had long coveted, such as energy.

1-3. Discuss examples of recent macropolitical risk events and the effect they have or might have on a foreign subsidiary. What are micropolitical risk events? Give some examples and explain how they affect international business.

Learning Objective: 2; AACSB: Dynamics of the global economy

An event that affects all foreign firms doing business in a country or region is called a macropolitical risk event. In many regions, terrorism poses a severe and random political risk to company personnel and assets and can, obviously, interrupt the conduct of business. The increasing incidence of terrorism around the world concerns MNCs. In particular, the kidnapping of business executives has become quite common. In addition, the random acts of violence around the world have a downward effect on global expansion, not the least because of the difficulty in attracting and retaining good managers in high-risk areas, as well as the expense of maintaining security to protect people and assets and the cost of insurance to cover them. Companies that go ahead and invest in those high-risk areas do so with the expectation of a higher profit premium to offset risk.

An event that affects one industry or company or only a few companies is called a micropolitical risk event. Such events have become more common than macropolitical risk events. Such micro-action is often called “creeping expropriation,” indicating a government’s gradual and subtle action against foreign firms. This is a situation that occurs when you haven’t been expropriated, but it takes ten times longer to do anything. Typically, such continuing problems with an investment present more difficulty for foreign firms than do major events that are insurable by political-risk insurers.

1-4. What means can managers use to assess political risk? What do you think is the relative effectiveness of these different methods? At the time you are reading this, what countries or areas do you feel have political risk sufficient to discourage you from doing business there?

Learning Objective: 2; AACSB: Analytic skills

Risk assessment by multinational corporations usually takes two forms.

-One uses experts or consultants familiar with the country or region under consideration. Such consultants, advisers, and committees usually monitor important trends that may portend political change, such as the development of opposition or destabilizing political parties.

-They then assess the likelihood of political change and develop several plausible scenarios to describe possible future political conditions.

-A second and increasingly common means of political risk assessment used by MNCs is the development of internal staff and in-house capabilities. This type of assessment may be accomplished by having staff assigned to foreign subsidiaries, by having affiliates monitor local political activities, or by hiring people with expertise in the political and economic conditions in regions critical to the firm's operations. The effectiveness would depend on exactly what kind of risk the firm is facing; frequently, all means are used. The focus must be on monitoring political issues before they become headlines; the ability to minimize the negative effects on the firm—or to be the first to take advantage of opportunities—is greatly reduced once the news spreads through social media or CNN. No matter how sophisticated the methods of political risk assessment become, nothing can replace timely information from people on the front line. As of the end of 2012 the Arab Spring presents the greatest of the political risks where major corporations do business.

**1-5. Can political risk be “managed?” If so, what methods can be used to manage such risk, and how effective are they? Discuss the lengths to which you would go to manage political risk relative to the kinds of returns you would expect to gain?
Learning Objective: 2; AACSB: Analytic skills**

On one level, they can decide to suspend their firm's dealings with a certain country at a given point—either by the avoidance of investment or by the withdrawal of current investment (by selling or abandoning plants and assets). On another level, if they decide that the risk is relatively low in a particular country or that a high-risk environment is worth the potential returns, they may choose to start (or maintain) operations there and to accommodate that risk through adaptation to the political regulatory environment. Some of the methods used to manage political risk are as follows: equity sharing, participative management, localization of the operation, and development assistance. In addition to avoidance and adaptation, two other means of risk reduction available to managers are dependency and hedging. Multinational corporations also manage political risk through their global strategic choices. Many large companies diversify their operations both by investing in many countries and by operating through joint ventures with a local firm or government or through local licensees. By involving local people, companies, and agencies, firms minimize the risk of negative outcomes due to political events. The returns you would expect to gain would be the healthy continuation of your firm's business.

**1-6. Discuss the importance of contracts in international management. What steps must a manager take to ensure a valid and enforceable contract?
Learning Objective: 3; AACSB: Multicultural and diversity understanding**

Because international managers must operate in a variety of cultures and under a variety of legal systems, it is imperative that they prepare contracts carefully through consulting with experts in international law. Contracts reflect the local legal system and political and currency risks in the country involved, so allowances should be incorporated into foreign

contract agreements to take account of the social and business culture and the country's international reputation. The warranties or guarantees that a company offers with its products should be carefully designed and limited to conditions under its control. The firm must either incorporate political risk assumptions into the contract or make appropriate contingency plans.

- 1-7. Discuss the effects of various forms of technology on international business. What role does the Internet play? Where is this all leading? Explain the meaning of “appropriability of technology.” What role does this play in international competitiveness? How can managers protect the proprietary technology of their firms?**

Learning Objective: 4; AACSB: Use of information technology

Firms have globalized their supply chain, creating a higher level of inter-connectedness. This results in and creates a greater flow of technology transfer. At the same time, information technology has produced a more time-sensitive environment for international managers. The Internet has become a pervasive force in accelerating communications to and among businesses and consumers. E-commerce creates a global market opportunity for smaller companies. *Appropriability of technology* concerns the ability of the innovating firm to profit from its own technology by protecting it from competitors. Many legal clashes have come from disputes about the appropriability of technology, such as the battle between Texas Instruments and Fujitsu. The increased use of technology is moving us toward a faster, and in some cases, more fragmented marketplace. The most common methods of protecting proprietary technology are through patents, trademarks, trade names, copyrights, and trade secrets. The International Convention for the Protection of Industry Property, often referred to as the Paris Union, is adhered to by over 80 countries for protection of patents.

- 1-8. Discuss the risk of terrorism. What means can managers use to reduce the risk or the effects of terrorism? Where in the world, and from what likely sources, would you anticipate terrorism?**

Learning Objective: 1; AACSB: Analytic skills

Terrorism (the use or threat of use of anxiety-inducing violence for political purposes) is on the rise internationally, particularly in the form of kidnapping of business executives. The most common means of combating terrorism involve the use of political risk techniques and the implementation of contingency plans. Most firms operating abroad today, as well as many domestic firms, must plan for possible terrorism events and how the firm will be able to respond to its customers and employees in the event of such an event. Most students will probably identify Middle Eastern countries as most-likely sources of terrorism activity. Although this may be true, a significant internal threat exists in the United States and Europe as well.

Application Exercises

- 1-9. Do some further research on the technological environment. What are the recent**

developments affecting businesses and propelling globalization? What problems have arisen regarding use of the Internet for global business transactions, and how are they being resolved?

Learning Objective: 4; AACSB: Use of information technology

Technology is influencing global business as never before, and the rate of change is not expected to diminish any time soon. Technology is increasing the speed and quantity of information. Information can be sent instantly to almost any part of the world, and employees and customers have unprecedented access to information about companies. Technology has caused some convergence of tastes and preferences, making the marketing of products internationally easier. Increases in information and logistical abilities have made geographic borders less relevant. All of these advancements have propelled globalization. At the same time, the Internet has created the potential for a more democratic world, in which anyone with Internet access can express their opinions and voice their concerns. The increasing use of blogs has been a source of concern to some companies as disgruntled employees and customers have been able to negatively influence the public image of some companies. Companies are finding it necessary to manage this information flow and to take steps to counter these negative public listings.

1-10. Consider recent events and the prevailing political and economic conditions in the Russian Federation. As a manager who has been considering investment there, how do you assess the political and economic risks at this time? What should be your company's response to this environment?

Learning Objective: 2; AACSB: Dynamics of the global economy

The political and economic situation in Russia is troubling to many international managers, especially the recent political developments. Beginning with the Yukos action, confidence in the transparency and honesty of the Russian government has been called into question. The situation has only been made worse by recent allegations of misdeeds by the current government, including the murder of political opponents and critics. The energy resources of the country have allowed the government to act in a more aggressive manner, and it is anticipated that those resources will continue to allow such aggression for some time. It is prudent that international managers continually assess the political situation and take steps to avoid adverse actions. With the exception of the energy sector, Russia may not appear to be a good investment at this time. In some cases, partnering with reputable and powerful local businesspeople or businesses may be an acceptable means of reducing political risk. However, it is critical that the potential return from such investments match the increasing risk.

A good source of information on political risk, and an example of a company that assesses political risk can be found at: www.prsgroup.com .
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Experiential Exercises

Learning Objective: 2; AACSB: Dynamics of the global economy

There is no “right” answer to this exercise. It may be useful to begin a discussion of the benefits of a “China plus one strategy.” Using this framework, China is selected as a manufacturing location, but an additional Asian country is selected as protection against political risk. China is fast becoming the manufacturing hub of the world; however, China has had a long history of political and social disruption, especially when income disparity rises. The current disparity between urban and rural incomes is a source of concern. Rising costs in China are also a concern to potential investors. The emerging economies of Southeast Asia represent a desirable option. For example, Dell made a decision to invest \$1 billion in Vietnam instead of China due to Vietnam’s lower wage levels.

End-of-Chapter Case Study: Apple’s iPhone—Not “Made in America”

1-11. What is meant by the globalization of human capital? Is this inevitable as firms increase their global operations?

Learning Objective: 1; Analytic skills

Firms around the world have been offshoring manufacturing jobs to low-cost countries for decades. An increasing number of firms have been producing or assembling parts of their products in many countries; that is, outsourcing by contracting to a local firm, and then integrating them into their global supply chains. More and more firms are out-sourcing white-collar jobs to India, China, Mexico, and the Philippines: customer support, medical analysis, technical work, computer programming, form filling, and claims processing—all these jobs can now move around the globe in the same way that farming and factory jobs could move a century ago. Globalization of human capital is inevitable as companies look for the competitive edge that lower costs, a high energy workforce and globalized supply chains can provide.

1-12. How does this case illustrate the threats and opportunities facing global companies in developing their strategies?

Learning Objective: 1; Analytic skills

Opportunities: Companies can source product, technology, parts etc. from all over the world to get the best possible mix. Apple maintains that the large number of engineers and other skilled workers who could be accessed on short notice in China simply are not readily available in the United States; nor are the factories with the scale, speed, and flexibility that such a high-tech company needs.

Threats: Backlash concerning working conditions; possible breach of US laws concerning the use of toxic chemicals.

1-13. Comment on the Apple executive’s assertion that the company’s only obligation is making the best product possible: “We don’t have an obligation to solve America’s problems.”

Learning Objective: 2; Ethical understanding and reasoning abilities

To a large degree this is correct. Apple’s primary obligations are to its customers and shareholders. By producing excellent products at a reasonable price Apple is doing well to

both groups. Apple is not obligated to sacrifice either group to the vision of increasing America's employment numbers.

**1-14. Who are the stakeholders in this situation and what, if any, obligations do they have?
Learning Objective: 1; AACSB: Analytic skills**

Apple's stakeholders are their clients and shareholders – described above.
Foxconn's stakeholders are their workers, their owners and their clients – such as Apple, Dell etc. Foxconn's obligations are approximately the same as Apple's: to satisfy their clients, make profits for their owners but also to do well by their employees.

**1-15. How much extra are you prepared to pay for an iPhone if assembled in the United States? (See question 16)
Learning Objective: 1; AACSB: Analytic skills**

**1-16. How much extra are you prepared to pay for an iPhone assembled in China but under better labor conditions or pay? What kind of trade-off would you make?
Learning Objective: 1; AACSB: Analytic skills**

Both questions could only be answered on an individual basis, but it is important to remember that price is a factor in the purchase decision of a smart phone and therefore is a major component of competition. Even if you, as the reader/student, were willing to pay more how well would Apple be able to compete?

**1-17. To what extent do you think the negative media coverage has affected Apple's recent decision to ask the FLA to do an independent assessment and the subsequent decision by Foxconn to raise some salaries?
Learning Objective: 4; AACSB: Communication abilities**

It could be surmised that the negative reaction had a major impact on Apple's decision. It is well understood recently by many major corporations that sustainable business practices, which include fair treatment of employees, are valued by customers and shareholders. It may be assumed that Apple will continue to insist on fair treatment of employees by their subcontractors and validate that by third parties.

**Student Stimulation
Group or Class Learning Activities**

1. Students are often unaware of the physical distances involved in global business. A simple quiz or game can be an effective class exercise. Ask students to compare the distances between sets of U.S. cities and sets of international destinations.
 - a. Which is the greater travel distance?
New York to San Francisco OR Hong Kong to Singapore

Miami to St. Louis OR Paris to Moscow
Portland, Maine to Portland, Oregon OR Seoul, Korea to Hong Kong

- b. Which city is further south?
Monterey, Mexico OR Tampa, Florida
Mexico City OR Singapore
Paris OR New York

2. *Branding and Ethnocentrism*: Ask your students to identify the national origin of a variety of products/brands. After they have written their answers, show the correct ones. Ask why they thought certain brands came from the countries they originally named.

Some effective brands for this exercise include:

Disney (United States)
Michelin (France)
Bayer (Germany)
Shell Oil (Netherlands)
Nestle (Switzerland)
Outback Steakhouse (United States)
Burger King (UK)
Yoplait (United States)
SAAB (Sweden)
Volvo (United States—Ford)
Jaguar (United States—Ford)

3. *Experiencing currency translation exposure*: Ask students to imagine that they are employed by an American MNC in Europe. They are paid in Euros but in a few days they will be sent home to the United States and will need to change their earnings into dollars. Check the exchange rates on “payday” and again on the day they will “return home.” Did the rate change during those days? Did it benefit or harm the students in terms of the amount of dollars they were able to get in exchange for their euros?
4. *Assessing political risk activity*: Assign students three countries in relatively close proximity to each other (e.g., India, Pakistan, Nepal; or Thailand, Malaysia, and Singapore). Have the students use the format from Ex. 1.2 to develop a risk comparison of their three countries for presentation in the next class period. Discussion questions should probe learning experiences from both the process and the outcomes. *In terms of process*: To what extent was the information you desired readily available? Did the criteria allow you to differentiate between the countries? Could you envision other criteria that might also be important (students may mention terrorism, personal safety of executives)? *In terms of content*: Which country was the least risky? Most risky? Is risk alone an adequate criteria for foreign investment? How likely is it that the profile of the country you have chosen will be the same next year? Over the next five years?

Additional Stimulation Discussion Questions

1. A major issue in global business is the protection of intellectual property rights. Have you used Websites like audiogalaxy.com or morpheus.com? Are such uses a violation of intellectual property rights? Why or why not? How might such issues become relevant to global business?
2. What are some things you can do to prepare yourself for a business career involving international assignments?
3. What advantages does a bilingual or multilingual manager have over someone who is monolingual?
4. How might the computer revolution and other forms of information technology make it easier for companies to compete globally?
5. Do you feel prepared to work in a multicultural environment? Why or why not?
6. Do you see any advantages for small companies when competing against larger companies on a global scale?
7. If you had the opportunity to work abroad after graduation and could choose any country, which would you choose and why?
8. Would you be willing to accept a “plum” promotion overseas if it entailed possible exposure to terrorist activities, either directly or indirectly? What incentives and other inducements would an international company have to provide you in order for you to work in a politically unstable region?
9. What do you think would be some of the main difficulties of operating a Western company in an Islamic country under Muslim law? Would you be comfortable working in such a situation if you held what you considered to be an ideal job?

Web Exercise

The text describes how the financial crisis from 2008 has hit many industries hard, in fact crippling some and forcing others to retrench or downsize. The fact is that many companies have had to rethink what they previously assumed to be long-view growth patterns in terms of international strategy and global network structure. In addition to specific companies and industries, entire countries have also found that their position within the global business environment has changed—some for better, some for worse.

Look at the following Websites and develop an argument that shows how a financial crisis might completely change the thinking of global strategists in individual companies and in foreign governments?

East Asia Economics Forum

<http://www.eastasiaforum.org/tag/global-financial-crisis/>

The Economist

http://www.economist.com/world/asia/displaystory.cfm?story_id=14506580

Indian Economy

<http://www.economicshelp.org/blog/economics/indian-economy-2009/>

Newsweek

<http://www.newsweek.com/id/184621>

Mexico Economy

http://www.brookings.edu/opinions/2009/0304_mexico_martinez_diaz.aspx

BBC News

<http://news.bbc.co.uk/2/hi/business/8251164.stm>

Global Times

http://news.bbc.co.uk/2/hi/south_asia/7780040.stm



Facebook's Internet.org Initiative Serving the Bottom of the Pyramid?

Teaching Note

This teaching note was written by **Punithavathi Srikant**, Amity Research Centers Headquarter, Bangalore. It was prepared to accompany the Case **Facebook's Internet.org Initiative – Serving the Bottom of the Pyramid?** The case was compiled from published sources.

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Author: Punithavathi Srikant

Facebook's Internet.org Initiative – Serving the Bottom of the Pyramid?

Teaching Note

Prerequisite Conceptual Understanding

- ☞ Identifying Untapped Opportunities for Value Creation, “The Fortune at the Bottom of the Pyramid”, <http://www.csrwire.com/pdf/Prahalad-excerpt-001-022.pdf>, June 17th 2004
- ☞ Utilising emerging economies for growth, Sane Vivek and Kshatriya Anil, “Growing with The Masses–A New Approach to Bottom of The Pyramid”, <http://www.sibm.edu/FacultyResearch/pdf/growingmasses.pdf>, September 2011

Synopsis of the Case Study

The case, set in 2014, can be used in Post Graduate Business Management courses to teach Strategy and General Management. Facebook along with other technological companies had started Internet.org, an initiative to provide network access to millions of people in the developing world. Since its launch in August 2013, the initiative had brought basic internet facilities to the countries of Zambia, Paraguay, Indonesia, Kenya, Rwanda and Philippines with active support extended by the local governments. Mark Zuckerberg (Zuckerberg), Facebook's founder had realised that future growth for the company would come from emerging markets alone and had presented his initiative as a humanitarian effort for the economic betterment of people in those regions. Hailed as well as criticised by many, the Internet.org initiative did mix business with philanthropy and might create a monopoly thereby ignoring the principle of net neutrality. Called ‘venture humanitarianism’ and ‘Facebook's gateway drug’, this initiative was criticised as a strategy to rope in more users into Facebook ecosystem. Against this backdrop, the case study would look into the motives behind the launch of the novel initiative and examine how it served Facebook's business interests. While doing so, it will also analyse whether Internet.org was a canny business move dressed up to sound like charity to mine the fortunes at the bottom of the pyramid.

Teaching Objectives

The case study helps to understand and analyse:

- ☞ The significance of a ‘Connected World’
- ☞ Facebook's Internet.org Initiative
- ☞ Motives behind serving the BOP segment.

Teaching Plan:

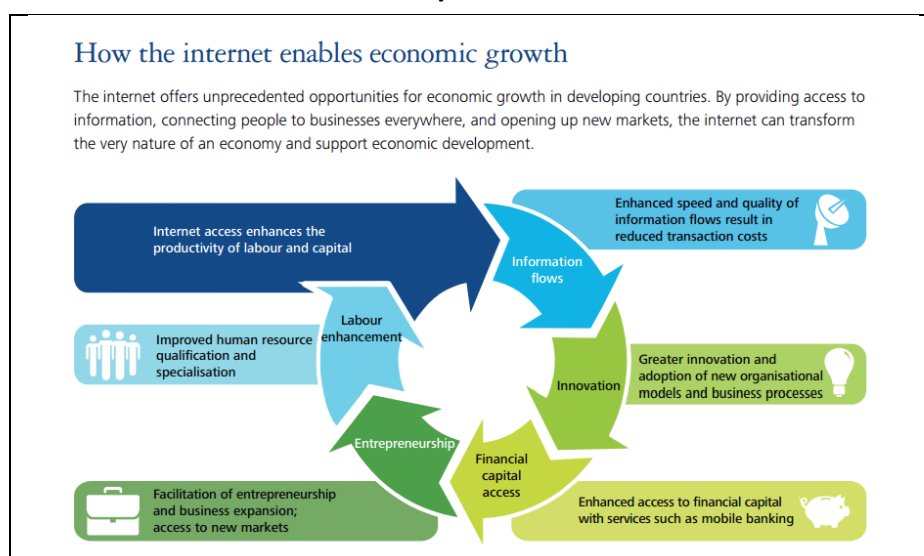
- ☞ The Teaching Note follows a sequential order as presented in the Suggested Teaching Plan [Annexure (TN) – I].

Case Analysis**Internet.org: Facebook's Game Plan****1 Give a brief outline of Facebook's Internet.org initiative.**

I initiated the discussion in the class by asking the students to share their views about the internet.org initiative of Facebook. Many felt that it was a noble cause perpetuated by Facebook. But some students were of the view that the initiative was started to further Facebook's business interests. On that note, I started analysing Facebook's internet.org initiative in detail. **[Paras 1 – 11 of the Section: "Internet.org: A Facebook Initiative", of the case study].**

- Internet.org was started to make internet accessible to everyone in the world.
- From **Exhibit I of the case study**, students identified the technological partners involved in the initiative.
- The Internet.org initiative was primarily a partnership between technological organisations, nonprofits, local communities and experts, and was intended to bring internet access to two thirds of global population who were not connected.
- Partners of Internet.org would work to find innovative business models by developing affordable technology and adopting best practices. The partners would invest in tools and software to efficiently transmit their data.
- Internet connectivity would prove to be a change agent for economic growth in developing countries and it would usher in prosperity by creating 140 million jobs, uplift the poor and improve infant mortality rates as net connectivity gave information about health, employment and local news. **[Exhibit (TN) – I].**
-

Exhibit (TN) – I
Internet Connectivity Drives Economic Growth



Source: "Value of connectivity Economic and social benefits of expanding internet access", https://fbcdn-dragon-a.akamaihd.net/hphotos-ak-ash3/t39.2365/851546_1398036020459876_1878998841_n.pdf, February 2014

- From **Exhibit II of the case study**, students found how internet.org had benefitted Zambian population.
- While in Philippines, it had increased the subscriber base by 25%.
- In Paraguay, 3 million people got connected, while the user base and their access to daily data had increased by 50%.
- Positive results were found in the countries of Indonesia, Tanzania and Kenya.
- In Rwanda, through Social EDU initiative students got access to online learning.
- In a developing country like India, internet.org was planning to tap lucrative rural regions where barriers like educational and cultural factors had proved to be challenging for net connectivity. So internet.org had collaborated with Unilever to reach the vast rural population of India.
- Facebook in collaboration with other partners was developing technology to overcome the challenges of connecting people in the developing world.
- Facebook's connectivity lab would use drones, radios, free space optics with technological expertise from NASA to meet the challenges of connecting the world.
- The connectivity lab's simulated conditions would help them to test their products and technology to that of the conditions existed in developing markets, so as to optimise their services offered.
- From **Annexure I of the case study**, students found the issues and challenges involved in connecting internet globally.
- Students realised how internet connectivity would improve the economic wellbeing of people in developing countries.

Then, the class furthered their discussion on how internet.org had brought in positive changes in the developing world.

Facebook's Two Faces!

2 Discuss the impact of Internet.org in emerging economies of the world.

The class discussed in detail how internet.org had impacted positively in emerging economies of the world. [**Paras 1, 2 and 7 of the Section: "A Solace for Emerging Economies or a Canny Business Move?"**, of the case study].

- Facebook founder Mark Zuckerberg had predicted that the internet.org initiative would empower the people of the emerging economies to decide what type of government they wanted, gave them access to healthcare and connected families that were miles apart.
- From **Exhibit III**, students understood the various barriers that inhibited internet connectivity to all.
- From **Exhibit IV** of the case study, students found the impact of internet.org in developing countries.
 - Internet connectivity in developing countries would increase the productivity by 25%, create nearly 140 million jobs and would increase the GDP by \$2.2 trillion.
- In India, improved connectivity would be made possible by offering regional language content.

- Internet.org had planned to reduce the cost of delivering data, expand wireless capacity and build more efficient apps.
- From **Exhibit V of the case study**, students realised how internet connectivity had improved the lives of Sardine Fishermen of Kerala, India by implementing common pricing practices. The initiative would accelerate the pace with which people were connected in developing countries.

Then the class discussed in detail, the much criticised and alleged business motive of Facebook backed internet.org initiative.

3 Was Internet.org initiative really about serving the bottom of the pyramid or was it more about Facebook trying to expand its reach? Analyse.

The class discussed how the initiative internet.org was meant to serve Facebook's business interests or it was a philanthropic move as claimed by Facebook. **[Paras 8 - 28 of the Section: "A Solace for Emerging Economies or a Canny Business Move?", of the case study].**

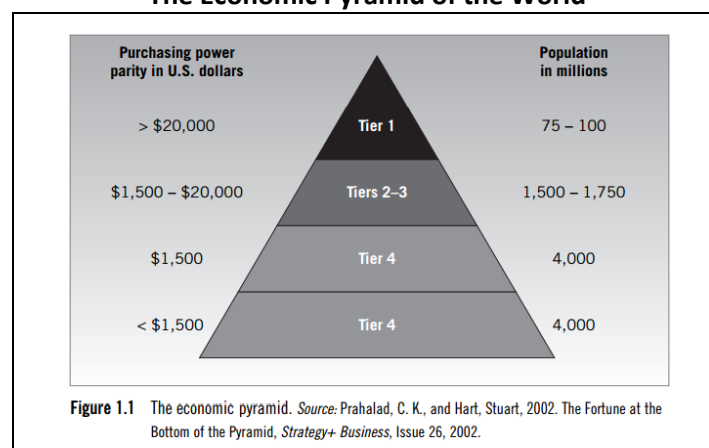
- Criticisms were raised against internet.org initiative.
 - The initiative was criticised as 'venture humanitarianism' in action and 'Facebook's gateway drug'.
 - Bill Gates opined that providing vaccines to the developing countries was more important than connecting the world through internet.
 - Global technological companies often portrayed their activities as efforts to solve world problems.
 - Internet.org offered only few basic apps for free and emerged as a middle man.
 - In countries of operation, internet.org used 'pay-as-you-app' model and charged various rates for different apps.
 - The initiative would bring other apps and websites into Facebook's ecosystem and would act as 'on-ramp to the Internet'.
 - This would influence users on their education, health and banking activities.
 - Facebook had ambitious plans to offer credits and identity infrastructure to its users.
 - Facebook also wanted to increase its revenue through growth coming from developing countries and that in effect curtailed the services offered by other providers.
 - Was also criticised as pseudo-humanitarian activity to promote its own profit motives.
 - Internet.org initiative's aim was to bolster the user base of Facebook and obtain data to serve its ads effectively.
 - People at the bottom of the pyramid had no choice and were lured to choose its services.
 - Critics also pointed out that Facebook wanted to be the first company to make customers in developing countries as its marketing targets, when they purchased their first Smartphones.
 - Criticised heavily as techno-colonialism and a Zombie war, the initiative was meant for expanding and consolidating Facebook's dominance of the world.
 - By this initiative, users became products from that of a customer.
- The initiative would prove to be beneficial to Facebook as India was a price sensitive market and would favour Facebook against other competitors.
- Net neutrality and internet freedom were affected.

- Zuckerberg had acknowledged that the initiative was an investment meant to reap benefits in the future for the company.
 - India was a crucial market for Facebook and it was geared to meet the challenges to promote its interests.
- Renowned Management Guru, C.K Prahalad (Prahalad) had stated that mining at the bottom of the pyramid (BOP) would offer new growth opportunities for organisations.
 - He also said treating people at the BOP as creative entrepreneurs and value-conscious consumers would be beneficial for organisations as it promoted innovation and sustained growth.
 - It helped them to come out of poverty and organisations should be restrained not to impose their solutions on them.
 - An example to that effect was Alibaba which was successful in rural China.
- Describing his agenda for Facebook's growth, Zuckerberg said that having connected one billion people, the next step would be to make 5 billion more connected. He elaborated how apart from making revenues, the company was building products so as to produce more entrepreneurs and promoted growth of ecommerce companies.
- Facebook's COO, Sheryl Sandberg said that the initiative was to connect unconnected people of the developing world in Facebook's second decade of operation and growth.
- But beneficiaries of internet.org felt that connecting through Facebook ecosystem was alright as they were not bothered about few advertisements that were creeping in while connecting their services.

But some analysts also felt that the initiative would become a win-win situation for both the people of developing world and Facebook and its allies. With its technological expertise, Facebook would solve the barriers and hurdles posed in developing countries for connectivity and also offered sustainable solutions to them. But caution should be exercised, as people interests and net neutrality should not be trampled upon by the business interests of these initiatives.

- From the PCU, "The Fortune at the Bottom of the Pyramid", the students understood how corporate could use the BOP and 'do well by doing good' to the consumers. **[Exhibit (TN) – II].**

Exhibit (TN) – II The Economic Pyramid of the World



Source: "The Fortune at the Bottom of the Pyramid",
<http://www.csrwire.com/pdf/Prahalad-excerpt-001-022.pdf>, June 17th 2004

- By engaging the people at the BOP through innovative means, and providing products and services, organisations could achieve a win-win situation and thereby make profits.
- BOP provided a latent market and they should be included in the core business of an organisation.
- Prahalad had brought out the changed logic of policy makers of India. **[Exhibit (TN) – III]**.

Exhibit (TN) – III
Changing Perspective about the Poor in India

From	To
The poor are a problem.	The poor represent a market.
	The private sector can and should participate effectively in this process. (A very selected subset of policy-makers goes one step further and recognizes that if large firms can service this Indian market, they could also access a global opportunity to serve 4–5 billion other people who are in a similar situation.)
Poor as wards of the state.	Poor as active consumers/entrepreneurs.
The poor do not appreciate new technology. Old technology solutions are acceptable.	Creative bundling of the most advanced technology with a local flavor.
Follow the Western model of development.	Selectively “leap-frog” and innovate.
Focus on resource constraints.	Focus on creativity and entrepreneurship.
Capital limitations.	Limitations of information and access. Imagination constraints.
Efficiency in a known model.	Innovation to develop a new model.
Adapted from C. K. Prahalad, <i>Strategies for the Bottom of the Pyramid: India as a Source of Innovations, Reflections</i> , Volume 3, Number 4, 2002.	

Source: “The Fortune at the Bottom of the Pyramid”,
<http://www.csrwire.com/pdf/Prahalad-excerpt-001-022.pdf>, June 17th 2004

- Creating a capacity to consume by focusing on affordability, accessibility and availability would ultimately prove beneficial to any organisation.
- Also from the PCU article, “Growing with The Masses A New Approach to Bottom of The Pyramid”, students found out the features to be focused for profitable growth while catering to the BOP segment. **Exhibit (TN) – IV**

Exhibit (TN) – IV
Strategies to Mine the Fortune at the BOP

- Lower price (affordability)
- Convenience and availability
- Brand power-biggest driver
- Adaptability as per the needs of the targeted customer.
- Use of technology to improve the systems.
- Driving away inefficiencies and making an all out effort to reduce the cost, and passing on the benefit to the customer.
- Volume driven market (Revenue per unit is less but the number of products being sold are more- Total sales increases).
- Greater turnover.
- It requires different types of marketing strategies to reach out to the target audience at the bottom.
- The most important feature of this business model is to understand the aspirations of the masses and then positioning the product accordingly. For e.g., the desire of the common man to fly by plane or a low income class woman trying to use a shampoo sachet at least once a week.
- It also requires different distribution channels and cannot depend upon the conventional channel of wholesalers and retailers. In many of the examples mentioned above NGO's (Non Government Organizations) or self-help groups have helped in distribution of products or creating awareness.

Source: Sane Vivek and Kshatriya, "Growing with The Masses A New Approach to Bottom of The Pyramid", <http://www.sibm.edu/FacultyResearch/pdf/growingmasses.pdf>, September 2011

Then, the class concluded stating that BOP provided vast opportunities for business growth and sustainability of an organisation.

Final Thoughts

Facebook backed internet.org was termed as an altruistic move by the founder Mark Zuckerberg, while its critics claimed that it was a ploy intended to bring more users into Facebook ecosystem. As markets in developed countries had matured riddled with stiff competition, organisations were looking for lucrative emerging markets from where explosive growth was predicted to happen. To tap these emerging markets, internet.org initiative was addressing the issue of cost than lack of infrastructure in those markets. Internet.org would give users a free preview of the internet services for a limited period and then would encourage spending more money on data packages offered by them. At the same time, connectivity would bring in economic growth and prosperity in developing regions of the world. By promoting its own platform, Facebook would emerge as the web for millions of people, while it may also ultimately defeat the principle of net neutrality, diversity and openness.

Additional Readings

1. Identifying Untapped Opportunities for Value Creation, "The Fortune at the Bottom of the Pyramid", <http://www.csrwire.com/pdf/Prahalad-excerpt-001-022.pdf>, June 17th 2004
2. Utilising emerging economies for growth, Sane Vivek and Kshatriya Anil, "Growing with The Masses–A New Approach to Bottom of The Pyramid", <http://www.sibm.edu/FacultyResearch/pdf/growingmasses.pdf>, September 2011 **Annexure (TN) – I**

Annexure (TN) – I
Suggested Teaching Plan

Prerequisite Conceptual Understanding

- ☞ Identifying Untapped Opportunities for Value Creation, “The Fortune at the Bottom of the Pyramid”, <http://www.csrwire.com/pdf/Prahalad-excerpt-001-022.pdf>, June 17th 2004
- ☞ Utilising emerging economies for growth, Sane Vivek and Kshatriya Anil, “Growing with The Masses–A New Approach to Bottom of The Pyramid”, <http://www.sibm.edu/FacultyResearch/pdf/growingmasses.pdf>, September 2011

The Big Picture
Innovative Growth Strategy

Detailed Teaching Plan Flow

Section – I Internet.org: Facebook’s Game Plan	Ideal Duration 30 Minutes
Description	
<ul style="list-style-type: none"> • Internet.org – An overview 	
Expected Learning Objective	
<ul style="list-style-type: none"> • internet.org Plans and Progress 	
Forward Linkage	
<ul style="list-style-type: none"> • Internet.org Project: Benevolent vs. Business Motive 	



Section – II Facebook’s Two Faces!	Ideal Duration 30 Minutes
Description	
<ul style="list-style-type: none"> • Impact of internet.org • Facebook’s internet.org - Enlightened self-interest or humanitarianism? 	
Expected Learning Objective	
<ul style="list-style-type: none"> • Innovative Growth Strategy of Facebook 	

Prepared by the Author