International Business Management

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UNIT—5

GLOBALIZATION AND LIBERALIZATION

Globalization and liberation are directly linked with each other. It has allowed companies to increase their base of operations, expand their workforce with minimal investments and provide new services to a broad range of consumers.The process of globalization has been an integral part of the recent economic progress made by India. It has played a major role in export-led growth, leading to the enlargement of the job market in India.

Pre Liberalization Period and Globalization

From independence till the later part of the 1980s, India economic approach was mainly based on government control and a centrally operated market. The country did not have a proper consumer oriented market and foreign investments were also not coming in. This did not do anything good to the economic condition of the country and as such the standard of living did not go up.

In the 1980s, stress was given on globalization and liberalization of the market by the Congress government under Rajiv Gandhi. In his government tenure, plenty of restrictions were abolished on a number of sectors and the regulations on pricing were also put off. Effort was also put to increase the condition of the GDP of the country and to increase exports.

Even if the economic liberalization policies were undertaken, it did not find much support and the country remained in its backward economic state. The imports started exceeding the exports and the India suffered huge balance of payment problems. The IMF asked the country for the bailout loan. The fall of the Soviet Union, a main overseas business market of India, also aggravated the problem. The country at this stage was in need of an immediate economic reform.

Liberalization in the 1990s

It was in the 1990s that the first initiation towards globalization and economic liberalization was undertaken by Dr Manmohan Singh, who was the Finance Minister of India under the Congress government headed by P.V. Narasimha Rao. This is perhaps the milestone in the economic growth if India and it aimed towards welcoming globalization. Since the liberalization plan, the economic condition gradually started improving and today India is one of the fastest growing economies in the world with an average yearly growth rate of around 6-7%.

Impact of Globalization

It was in July 1991, when foreign currency reserves had tumbled down to almost $1 billion; inflation was at a soaring high of 17%, highest level of fiscal deficit, and foreign investors loosing confidence in Indian Economy. With all these coupling factors, capital was on the verge of flying out of the country and we were on the brink of become loan defaulters. It was at this time that with so many bottlenecks at bay, a complete overhauling of the economic system was required. Policies and programs changed accordingly. This was the best time for us to realize the importance of globalization.

When the Gillette company developed a superior stainless steel razor blade, it feared that such a superior product might mean fewer replacements and sales. Thus, the company decided not to market it. Instead, Gillette sold the technology to Wilkinson, a British garden tool manufacturer, thinking that Wilkinson would use the technology only in the production of garden tools. When Wilkinson Sword Blades were introduced and sold quickly, Gillette understood the magnitude of its mistake.

The transfer of technology is essential for attaining a high level of industrial capability and competitiveness. Multinational corporations are playing an increasingly important role in technology transfer because they invest abroad to expand production, marketing and research activities. There is also a growing consciousness amongst governments of the need to increase technology transfer to the developing countries to help stabilise their economic and social conditions.

In spite of the many differences in social, political, cultural, geographic and economic conditions, there are some common characteristics in the technological environments of developing countries. The most common technology transfer from industrialised to

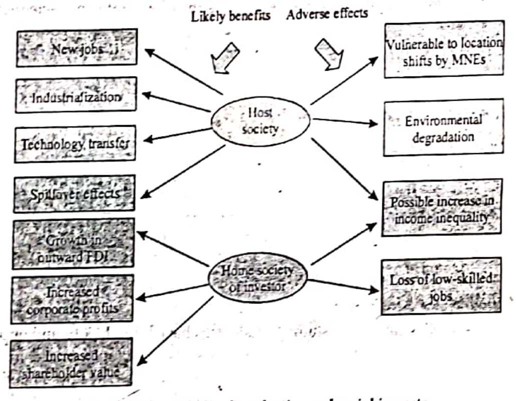

Figure 2.12: Globalized production and social impacts

Technology Environment

Technology can be defined as the method or technique for converting inputs to outputs in accomplishing a specific task. Thus, the terms 'method' and 'technique' refer not only to the knowledge but also to the skills and the means for accomplishing a task. Technological innovation, then, refers to the increase in knowledge, the improvement in skills, or the discovery of a new or improved means that extends people's ability to achieve a given task.

> "High technology has become like a force of nature. It transforms the economy, schools, consumer habits, the very character of modern life. Investors pour money into it; parents urge their children to study it; communities vie to attract its factories; decorators adopt it as a style; politicians push it as a panacea." (Source : Science Digest Magazine)

Technology can be classified in several ways. For example, blueprints, machinery, equipment and other capital goods are sometimes referred to as hard technology while soft technology includes management know-how, finance, marketing and administrative techniques. When a relatively primitive technology is used in the production process, the technology is usually referred to as labour-intensive. A highly advanced technology, on the other hand, is generally termed capital- intensive.

Changes in the technological environment have had some of the most dramatic effects on business. A company may be thoroughly committed to a particular type of technology, and may have made major investments in equipment and training only to see a new, more innovative and cost-effective technology emerge. Indeed, the managing director of a multinational organisation manufacturing heavy machinery once said that the hardest part of his job had nothing to do with unions, pay or products, but with whether or not to spend money on the latest technologically improved equipment.

Computer technology has had an enormous impact on education and health care, to name but two areas affected. The advancements in medical technology, for example, have contributed to longevity in many societies. In addition, the introduction of robots in many factories has reduced the need for labour, and the use of VCRs and microcomputers has become commonplace in many homes and businesses. Unfortunately, there is a negative side to technological progress. The introduction of nuclear weapons, for example, has made the destruction of the human race a frightening possibility. In addition, factories using modern technologies have polluted both air and water and contributed to various environmental and health-related problems.

Technology is a critical factor in economic development. Because of the advances of international communication, the increasing economic interdependence of nations, and the serious scarcity of vital natural resources, the transfer of technology has become an important preoccupation of both industrialised and developing countries. For many industrialised countries, the changes in the technological environment over the last 30 years have been immense particularly in such areas as chemicals, drugs, and electronics. It is vital that organisations stay abreast of these changes - not only because this will allow them to incorporate new and innovative designs into their products, but also because it will give them a firmer base from which to anticipate and counteract competition from other organisations.

Domestic laws govern marketing within a country, *e.g.*, the physical attributes of a product will be influenced by laws (designed to protect consumers) relating to the purity, safety or performance of the product. Domestic laws might also constrain marketers in the areas of product packaging, marking and labelling, and contracts with agents. Most countries also have certain laws regulating advertising, for example Britain does not permit any cigarette or liquor advertising on TV.

Different Legal Systems

The legal systems of most of the non-socialist countries can be grouped into common law and code law. Common law is generally based on precedents or past practices while a code, which is a comprehensive set of volumes having statutory force and covering virtually the whole spectrum of the country's law, is established by arbitrary methods - *e.g.*, a speed limit of 80 kph or a three-day period for cancelling a contract.

South Africa's commercial legal system has been influenced by English law. English courts create and follow precedents just as South African courts do. Furthermore, English cases are regularly cited as authority in our courts in situations where there is no domestic decision on the point and the particular case concerns an area of our law (such as insurance or negotiable instruments) which derives from, or was considerably influenced by, English law.

International Law

Buyers and sellers are at times also subject to international law, which may be defined as that body of rules which regulates relationships between countries or other international legal persons. There is neither an 'international parliament' empowered to create international law; nor an 'international police force' to enforce it.

The principal sources of international law are treaties and conventions. These are created when several countries reach agreement on a certain matter and bind themselves to it by authorising their representatives to sign a document embodying that agreement. Essentially, they have entered into a contract that obliges them to do something or to refrain from doing something. Failure to comply is the equivalent of breach of contract.

Other sources of international law are custom (*i.e.*, international practice that is accepted as law) and the general principles of law recognised by civilised nations or natural law (the basis of human co-existence). Although there is no organised body to 'enforce' international law, there is an International Court of Justice situated at The Hague in Netherlands. This court decides any matter which the parties regard as suitable for submission to it for adjudication. This means that a country approaches the court voluntarily; it cannot be brought to the court involuntarily.

Before a country is liable to comply with the provisions of a treaty or a convention, it must have signed the original protocol (*i.e.*, the original treaty document or minutes of the convention). Once a country has signed the protocol, the method of enforcement depends on the terms of the treaty or convention. A common way of bringing a defaulting country to heel is by imposing sanctions against it. Sanctions may take many different forms and can be applied with varying degrees of severity. Obviously, the more parties there are to the

Outsourcing

Outsourcing is a broad term which covers any contractual arrangement by which an organization (the client company) obtains goods or services it needs from another organization (the outsourcing company), rather than providing them itself in-house. Both the outsourcing contractor and the client company may be in the same country, but it is the growth in cross border outsourcing which is highlighted as an indicator of globalization.

A company may outsource some or even all its manufacturing process to one or more other firms. When it outsourcers the entire process, it becomes, in effect, a 'virtual' manufacturer. The manufacturing may be carried out under an agreed license, by which the manufacturers are allowed to legally use the trademark of the client company. The license may also provide for oversight of the process with respect to quality. Typically, these arrangements are adopted by companies in the developed world to make use of outsourced manufacturing in developing countries with a view to exporting the products to their home consumers or consumers in other developed markets. Contract manufacturers have prospered from outsourcing, growing into large, co-ordinated operations, able to shift factory production among different locations to achieve economies of scale (Buckley and Ghauri, 2004).

Business process outsourcing (BPO) has become common, usually due to the cost savings envisaged. For client companies, the rationale is that any function which is not core to its business can be shifted to an outside provider. In addition to IT services, back-office administration, call centres and help lines are candidates for outsourcing. The outsourcer is usually a specialist in the particular activity, and is able to achieve economies of scale, as it serves other customers as well. The client organization may well feel that handling these functions over to experts will give managers more time to focus on the company's main business. Outsourcing IT and accounting has thrived, and, as these are largely technical processes, they lend themselves to outsourcing. Outsourcing of HR functions has become popular, following BP's example in 1999. Its programme proved to be rather ambitious and had to be scaled back, but it has proceeded on an incremental basis since then. The outsourcing company may be in the same geographical region as the client company, but shifting functions abroad to a lower cost location, which is often called offshoring, is also taking place.

The term offshoring is applied to the contracting out of a function specifically to a low-cost country. The practice has grown dramatically, particularly in the services sector (UN, 2005). India has been a popular offshore location for companies from the US and the UK. In addition to call centres, Indian outsourcing companies now offer a range of back-office services to international companies. Offshoring has come to have negative connotations, implying that cost is the only factor in the decision to outsource and that the firm will inevitably cut jobs in the home country. Neither of these implications may apply to a particular outsourcing decision, but both are closely linked to the phenomenon in general. Not all outsourcing is o. shoring. HR and public sector outsourcing in the UK, for example, have tended to go to specialist domestic companies. In an ironic twist, half a million workers in India's state-owned banks went on strike in 2006, in protest at the outsourcing of back-office tasks to the country's own private outsourcing companies, which have prospered through offering just these services to global MNEs.

Outsourcing is sometimes criticized for its alleged transferring of jobs from advanced economies to cheaper locations, contributing to an international division of labour. It is argued that, while the company and its shareholders benefit, the employees in the home country lose out, as their jobs migrate to lower cost locations. In fact, the situation is much more complex than the critics suggest. Cost savings can be ploughed into upgrading the skills of workers, who are then able to take on more skilled jobs. The most vulnerable workers are in low-skilled jobs, in which the tasks are not dependent on being in the same location as the consumer. Researchers, however, face difficulties in quantifying the number of lost jobs. Millions of US jobs were lost due to the shift of manufacturing to East Asia and Mexico in the 1980s. It is estimated that the loss of jobs due to outsourcing is of a much lower magnitude, estimated at 473,000 in 2004 (Luce and Merchant, 2004).

Foreign Direct Investment (FDI)

FDI can be defined as investment by an organization in a business in another country, with a view to establishing production in the host country. The organization aims to gain control over this foreign production. There are various methods it can use to achieve its goals. It may simply buy a foreign business, becoming the new owner. Assuming the business is a growing concern, production continues under the new owners, who are likely to have new ideas on how to manage the business more efficiently. Alternatively, the company may take the bolder step of buying a Greenfield site in the foreign location and setting up a production unit to its own specification. This process will be longer and more complex for the company, but it will benefit from a unit designed specifically for its purposes and to its own specifications, and where its own technology can be incorporated from the outset. The greenfield option is often seen as the ideal, but this type of strategy is a high-risk one. In particular, it involves dealing directly with authorities in the host country for numerous permissions and services. As these processes are likely to be quite different from those in the home country of the investor, communication difficulties, delays and costs could mount before the project comes on stream. SX2.2 on Dyson is an example of this type of investment. The Dyson factory in Malaysia had been operating for two years before production was shifted there entirely.

A key aspect of FDI is the control which the investing company exerts over the overseas production. The joint venture involves give and take between partners, whereas the greenfield investor and the investor who has bought an existing company have the control which goes with ownership of their new assets. In all these cases, the investor establishes relations within the host environment. Hence, the investment is termed 'direct'. CS2.1 on Nokia illustrates expansion by FDI, transforming Nokia into a global company.

By comparison, investors who wish neither to have their products manufactured abroad nor to own and control foreign assets may still wish to invest overseas, for example by buying shares in a foreign company which seems to have good growth prospects. This type of investment is called portfolio investment, and is a financial investment only, not aimed at running the business. However, distinctions between the different types of investment may become blurred. A company may acquire a wholly owned subsidiary overseas, and leave the existing management to run the business, whereas another company may acquire only a minority stake in a foreign company's equity and proceed to exert control. The acquisition by Renault of a 37% stake in Nissan in 1999 is an example. New management introduced by Renault carried out radical changes, signifying a shift in control to the French company. It should also be remembered that ownership of shares in itself involves a role in decision-making, and even a stake of under 10% may be looked on

Improvement in Health Care Costs

Globalization has also positively affected the overall health care situation in the country. More and more medical innovations are coming in which are improving the health situation in India. The infant mortality rate and the malnutrition rate have significantly come down since the last decade. All these factors clearly prove that the globalization helped reduce the India poverty level.

Government Initiatives

To keep pace with the favorable effects of globalization, the government has taken a number of initiatives. A number of employment opportunities such as Prime Minister Rojgar Yojna and the CM Rojgar Yojna have been initiated to improve the employment situation in the rural areas. The Minimum Wages scheme has also been successfully implemented. In order to improve the quality of the workforce, effort is also being given to impact education to various sectors of the rural areas. Under these schemes, new schools are being opened up and attention is also being given to the welfare of the students. Likewise in the urban sector too, more and more employment opportunities are being opened up for the youth in a number of government sectors, banks and so on.

In order to foster communication and migration of workforce to various parts of the country to cater to the needs, the government has also developed infrastructure to a great extent. New roads and highways are being constructed to increase connectivity.

These processes are depicted in Figure 2.1. Global capital markets and growing economic integration vary significantly between countries. Trade and economic integration have surged ahead in the developed world and in some developing countries, but countries in much of Africa have seen little benefit.

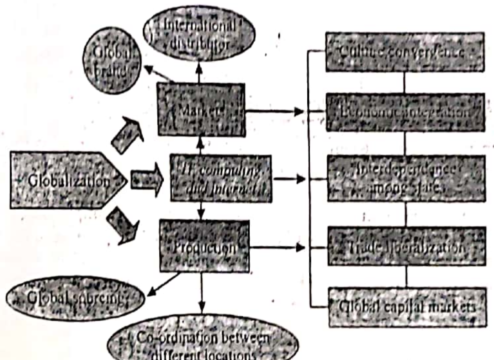

Figure 2.1: Globalization

Some globalization theorists predicted the demise of the nation-state, but national economies and national governments remain important players.