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| ***Business structure – geographic and trading links*** |

**Introduction:**

* Local, national and international businesses
* Multinational businesses

In your previous studies, you **classified** businesses according to their **sec\_\_\_\_\_\_r** (public/private) or **ind\_\_\_\_\_\_\_\_\_y** (pharmaceuticals, sportswear or cosmetics) or **own\_\_\_\_\_\_\_\_p** (sole trader, PLC).

We can now add**GEOGRAPHIC** (place) to the list.

Let’s start by naming (or describing) a few examples of businesses.

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| **Local** | **National** | **International** |
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**Local businesses** – do not have an expansion objective

**National** – not interested in establishing operations in other countries

**International** –operate in more than one country

(Regional) similar to local businesses but may operate in a whole province(s)

**Multinational** businesses (‘Multinationals’ or ‘MNCs’/’MNEs’)

*KEY DEFINITION OF MULTINATIONAL BUSINESS*

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**‘Firms have their headquarters (HQ) in one country and operate branches, factories and assembly lines and plants in others.’**

They are **more than** just importers and exporters: they produce their goods and services in more than one country.

Because of their size, they can be very powerful and influential (consider Apple, Coca-cola, Microsoft) and so can sometimes cause problems with nations (countries).

A **typical multinational** has its head offices in a Western European country or the USA but has **operations** (manufacturing, production, processing) in less developed countries which may have smaller economies such as India, Vietnam, Thailand, Brazil or Mexico. **Why do you think this is?**

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**Why** become a multinational? (p.34)

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| **1: Closer to main markets** |  |
| **2: Lower costs of production** |  |
| **3: Avoid import restrictions** |  |
| **4: Access to local natural resources** |  |

Potential **problems** for multinationals:

There are some risks and potential problems for multinationals:

*Communication links*

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*Language, legal and culture differences*

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*Coordination with other plants/assembly lines/offices*

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*Lower skills levels of labour force*

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*Liability of foreignness/CDBA (Cost of Doing Business Abroad)*

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(LOF)The social costs arise from the unfamiliarity, relational, and discriminatory hazards that foreign firms face over and above those faced by local firms in the host country. There are economic costs too.

**Benefits** and **disadvantages/impact** to a ‘host’ country that opening up to multinationals (MNC) brings:

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| Benefits | Disadvantages |
| * Increase employment opportunities * Increase standard of living by giving better **p**\_\_\_ and conditions * Inward Investment/ Foreign Direct Investment (FDI) leads to improvements in host factories, technology and infrastructure * Increased taxes from 1) purchases 2) profits 3) wages and 4) products exported * Ethical considerations may see ‘fair’ wages paid as Corporate Social Responsibility (CSR) is increasingly both demanded by consumers and provided by businesses * MNCs reduce distribution costs when they set up factories where they sell their products and can reduce taxes legitimately if they produce within a Customs/Economic Union * Foreign exchange earnings * Increase local firms’ competitiveness * Raise GDP | * Non-CSR MNCs may seek only to exploit developing countries in order to **maximize** profits.They often set up ‘sweatshops’ -FoxConn * MNCs might locate in countries with **less strict** employment laws * MNCs can sometimes **sellgoods** which don’t meet EU/US safety standards in developing countries * **Natural resources** can be more readily exploited (often via **corruption**) and any environmental impact of operations is ignored * Governments often become **reliant** on tax income MNCs generate and overlook any **unlawful** activity * MNCs can sell items from one part of a business to another (in another country) and manipulate the price in order to reduce its tax liabilities. This is called **‘Transfer Pricing’** and is unethical (but mostly legal providing with restrictions )   ***Transfer pricing*** *is a profit* ***allocation*** *method used to attribute a corporation's net profit or loss before tax to tax jurisdictions.*  ***Transfer prices*** *are the charges made between controlled (or related) legal entities i.e. within the same group.*  *Legal entities considered under the control of a* ***single corporation*** *include branches and companies that are wholly or majority owned ultimately by the parent corporation. Certain jurisdictions consider entities to be under common control if they share family members on their boards of directors.* |

An important form of business is the **JOINT VENTURE**. You studied it last year. International Joint Ventures (IJVs) are combining two international companies for a particular project(s). You can use the **term (JV)** although many business research journals use **IJV** to denote international joint ventures.

‘A Joint Venture (JV) is a business agreement in which the parties agree to develop, for a finite time, a new entity and new assets by contributing equity’

* A business where (otherwise unacceptable) risk is **shared** by both sides. It is common for firms investing abroad to seek local partners. Foreign firms provide technical expertise, but locals have **advantages** with **local business practices**, **local marketing** and **dealing** with the **government** and the **labour** force.

Can you name any **International Joint Ventures** (IJVs) in China?

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For example, the Chinese government has long **favoured** (and often demanded) **joint ventures** for foreign companies wishing to enter China. Many existing MNCs in China started trading as an **IJV** with a local firm: **KFC** for example (in 1987)

For some companies, JVs may just produce a **one-off** product. For some, it’s a **long term** strategy. Car companies are very typical of JV/IJVs, as are telecommunications such as Sony (Japan) Ericsson (Sweden)& Nokia (Finland) and Siemens (Germany)

**Benefits include:**

* Sharing expertise, risk, knowledge, strengths, markets and resources are some of the benefits.

However, there is a **risk** that one company steals IP (Intellectual property) and know-how. Other risks include ***management styles***, ***cultural differences*** and **blaming** each other for errors.

Companies such as **ZTE** and **Huawei** may look to establish IJVs with foreign companies. Do you have any suggestions for a potential IJV for them? Why?

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**Nature and scope of international trading links:**

All countries engage in international trade with other countries. Why do you think they do?

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International trade: can be **positive**: improves *political* and *social* links – resolve differences

**Negative:**

* Loss of output from **dom**\_\_\_\_\_\_\_ firms that cannot effectively compete with imported goods
* Decline due to imports of **‘strategic’** goods such as coal, foodstuffs – a risky position to be in
* Switch to a **‘comparative advantage’** good may take time
* May restrict **‘infant industries’** (consider China’s development and foreign companies ’expertise – one has to allow the Chinese companies a chance to establish themselves domestically without being ‘crushed’)
* Some importers may ‘**dump’** goods at below cost price in order to eliminate competition from domestic firms/or unfair subsidies. **This is known as ‘dumping’.** A recent case was China **‘dumping’** solar panels in the EU. China responded with a threat for imported wine. All settled now.
* Value of imports **exceeds** value of exports: loss of foreign exchange.

***Infant industries are:***

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***Worksheet summary quiz and activity:***

1. Explain two reasons for the **growing importance** of international trade.

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1. List **three** examples of an MNC in China.

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True or False (Mark an **X**)

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| I will choose a random student to answer a question | **True** | **False** |
| 1. **MNCs** have their headquarters (HQ) in one country and operate branches, factories and assembly lines and plants in others |  |  |
| 1. There are many Chinese businesses in Africa because they just like the sun and wild animals |  |  |
| 1. **Hai’er** risk the **liability of foreignness** by expanding into the USA |  |  |
| 1. It is **effective** and **easy** to communicate across countries within an MNC. |  |  |
| 1. MNCs **always** value the labour, customs and resources of their host country. |  |  |

**Summary of the worksheet in your own words (in English and Chinese):**

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*Vocabulary check:*

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| **English** | **Chinese** |
| **Domestic** |  |
| **Influential** |  |
| **Sweatshop** |  |
| **Transfer pricing** |  |
| **Infant industries** |  |
| **Dumping** |  |
| **Unlawful** |  |