Part I

Globalization and the International Business Environment

The degree to which business is internationalized is a function of changes and developments in the world economy. Central to these developments in recent years is the process of globalization or increased global interdependence which many allege took place in the closing decades of the twentieth century. The globalization process is pervasive and provides the backdrop for many of the issues and ideas discussed throughout this volume. Not only globalization but also issues of the governance of international business and development, raised initially in this first part, recur in later chapters.

The opening chapter of this part discusses the characteristics of globalization, introduces various arguments about the uniqueness or otherwise of current trends and sets out some preliminary indicators that help assess the degree to which globalization has taken place. The remaining chapters are both important in their own right and are also presented in connection with their relationship to globalization. For example, regional integration has accelerated in recent years, a development that has significant implications for the regulation and governance of international business, trade and investment. It is legitimate to ask the question whether the renewed impetus towards regional integration complements the increasing integration at international level or whether it is a reaction to it. Even if the former is the case, is it possible that enhanced regional integration could still facilitate fragmentation of the marketplace if globalization begins to unravel?

Globalization has also thrown up new challenges for the world's international economic institutions like the World Trade Organization (WTO), the World Bank and the International Monetary Fund (IMF). The establishment of the WTO in 1995 represented a more extensive and legally grounded international trading system. The pressures of globalization imply a need for an even greater shift of regulation and powers to international institutions. Anti-globalization protestors single out international institutions as the servants of international business and the cause of many of the world's ills. Many of these ills are said to reside in the developing world which, according to globalization critics, is excluded from any benefits of greater international integration and, at worst, exploited for the benefit of wealthier countries. The final chapter of this part is on development and attempts to highlight some of the complexity of the arguments and theories surrounding development and identify how the development process interacts with international business activity.

Chapter 1

Globalization and the changing business environment

> No man is an island, entire of itself; every man is a piece of the continent, a part of the main.
>
> John Donne (1572–1631), *Meditations XVII*

OBJECTIVES

By the end of this chapter, you should be able to:

- define and distinguish between globalization and internationalization;
- identify and appraise the main drivers behind globalization;
- describe the extent of and limits to globalization;
- begin to identify how globalization impacts on business (you will have a much fuller view by the time you have worked your way through this book).

Towards the end of the twentieth century, it became apparent that fundamental changes were afoot in the world economy that profoundly affected business, politics, society, citizens and the ways in which various stakeholders interacted with each other. This process became known as 'globalization' – a frequently overused and contested term that came to mean all that was good or bad in the world economy. For those who welcomed the supremacy of markets and economic liberalism, globalization offered the possibility of boundless growth and prosperity, not only for developed countries but also for those developing countries brave enough to embrace rather than resist globalization in all its manifestations. For others, globalization threatened rising inequality, economic anarchy and a surrender of political control. In developed countries, job losses and the unravelling of social progress were anticipated as a result of greater competition from low-cost countries whereas developing countries feared that their former colonial subjugation had been replaced by the dominance of market forces and its agents in the form of multinational enterprises (MNEs). These negative perspectives of globalization were represented, both inside and outside the conference rooms, at the failed December 1999 World Trade Organization Ministerial Meeting in Seattle and, indeed, at most high-level meetings of international organizations in recent years (see Chapter 3).

The primary purpose of this chapter is to establish a context and platform for subsequent chapters. It begins with an exploration of the concept of globalization and discussion of some of the key drivers in the process. The analysis then highlights the main debates surrounding globalization, before attempting to measure key indicators of globalization with a view to linking the theoretical debate about globalization with what is actually happening in the world economy and the international business environment.

What is globalization?

Globalization is a complex phenomenon, contested in terms of its definition, extent and implications and therefore in terms of the most appropriate response to it. Economists, political scientists, sociologists, anthropologists and lawyers, among others, have all debated the meaning of the term within the context of their respective academic disciplines. The focus of this volume is on the implications of globalization for international business. In the process, these globalization debates are reflected in subsequent chapters in relation to their impact on business. In the mid-1990s, the IMF's World Economic Outlook defined globalization as 'the growing interdependence of countries world-wide through the increasing volume and variety of cross-border transactions in goods and services and of international capital flows, and also through the more rapid and widespread diffusion of technology'.

This definition is a useful starting point, highlighting interdependence, the increasing number and range of cross-border transactions and the important role played by technology. However, it is incredibly difficult to define such a multi-layered and complex phenomenon as globalization in one sentence or to reflect the significance of the different elements of the definition and how they spill over into non-economic areas. In order to understand globalization in terms of its deeper meaning and significance (or at least in terms of its implications for economic governance and business), it is essential to analyse the key, closely linked drivers behind the globalization process.

Globalization driver one: the changing economic paradigm – from demand management to neo-liberalism

The growing interdependence of economies referred to in the above definition of globalization has only taken place because of the increasing acceptance of economic liberalism as the preferred method of 'managing economies'. Indeed the idea of managing economies is a contradiction in terms in the context of neo-liberalism, an approach based on limiting the role of government to the provision of an environment in which businesses can flourish and which relies heavily on unleashing the forces of competition.

Liberal economic ideas initially took root in external economic policy. The philosophy of the General Agreement on Tariffs and Trade (GATT) set up in the aftermath of the Second World War was essentially liberal. GATT's objective was the progressive reduction of tariff barriers, a reaction to the damaging protectionist spiral that had occurred in the 1930s. As tariff removal gained ground, the removal of non-tariff barriers to trade became increasingly important within GATT and its successor organization, the WTO. Composed solely of developed countries upon its formation, the membership of the GATT/WTO subsequently expanded to include many countries to which GATT's philosophy had been alien. For example, during the 1990s, many former communist countries acknowledged the benefits of free trade by applying for membership. In December 2001, the landmark accession of communist China to this arch neo-liberal international economic organization took place. Algeria, which has long maintained a detached role in the international economic arena and exercised extensive state control over its domestic economy, is also in line for WTO membership.

By the end of the 1970s, liberal economic ideas had begun to permeate thinking about domestic economic policy management. During the 1950s and 1960s, the prevailing orthodoxy was based on Keynesian economics, particularly the belief that by managing demand, governments could exercise significant control over their economies. However, the international economic troubles of the 1970s challenged many basic assumptions about economic policy. Not surprisingly, the shift in policy occurred first in the United States, where the idea of competitive capitalism was strongest. Its main proponent was President Ronald Reagan whose primary domestic mission was to roll back the frontiers of the state. Indeed, the term 'Reaganomics' was invented to describe his programme of free market economics. Closely allied to this thinking and practice was the UK government of Margaret Thatcher which came to office in 1979. In many ways, the Thatcher government wrought a bigger shift in the UK than the Reagan government in the US as the state loomed much larger in UK economic life at the end of the 1970s than it had ever done in the US. Thatcherism swept away many economic sacred cows to such an extent that the Labour government elected in 1997 took as given many of the reforms that had been introduced so controversially in the 1980s. Although liberal economic thinking caught on most quickly and extensively in the US and the UK, it also started to influence economic policy in the rest of the developed world, albeit adapted to the specific political and cultural context of individual countries. By the mid-1980s, for example, liberalism had become so pervasive that it formed the basis of the EU's transformational single market programme.

Acceptance of free market ideology quickly spread beyond the advanced industrialized world. Countries like Hong Kong, Taiwan, Singapore and South Korea had long accepted the benefits of openness in external economic policy and had followed a development path of export promotion that took advantage of engagement with the global economy. However, this development also tended to be accompanied by extensive state direction and guidance of their economies – a grip that began to loosen somewhat towards the end of the twentieth century. Ideas about free trade and the introduction of liberal economic policies in the form of deregulation, privatization and a generally reduced role for the state began to be introduced, to varying degrees, in Latin America, parts of Africa and other parts of Asia (see Chapter 4). Economic liberalism rapidly replaced Communism following the fall of the Berlin Wall in 1989 and the disintegration of the Soviet Union in 1991. Most noteworthy of all has been the phased introduction of the market into China, the hitherto sleeping economic giant of Asia: this process began in the early 1980s and has occurred without the dismantling of the state and party apparatus that occurred in the former Soviet Union.

The extension of competitive liberalism into domestic economic policy has increased the complexity of interdependence and deepened the globalization that has taken place with significant implications for corporate strategies and behaviour. At one level, changing regulations and attitudes create additional and more secure investment opportunities, not only through traditional market entry modes like mergers and acquisitions and joint ventures (see Chapter 5) but also increasingly through participation in privatization programmes in developed countries, newly industrialized economies, transitional economies and in many developing countries. At a deeper level, the greater openness arising from the spread of liberal ideas and policies encourages the emergence of a mindset and a strategy that operates beyond traditional national market boundaries.

Globalization driver two: the spread of international governance and regulation

As economic liberal ideas were more widely adopted and barriers to cross-border business were eroded, questions came to be asked about the most appropriate location of policies to regulate the business environment. Increasingly, such policies were formulated at regional level (see Chapter 2) by organizations like the EU and/or at international level (see Chapter 3 and throughout). In itself, this development is a manifestation of the globalization trend and originated with the progressive reduction of tariff barriers among GATT contracting partners and later among WTO members. As integration through trade developed, other barriers to integration were thrown into the regulatory spotlight resulting in the emergence of a trade agenda with both a broader (for example, the Uruguay Round incorporated agriculture and services trade) and deeper scope. Technological developments, particularly the emergence of e-commerce, also pose new challenges to traditional governance structures.

The 2001 Doha Declaration that launched another round of multilateral trade talks includes policy integration in areas such as competition and environmental policy, which traditionally were not regulated at state borders like conventional GATT/WTO measures, but within the state itself as issues of domestic policy. The shift from what Prakash (Prakash and Hart, 2000) terms 'shallow' integration (trade-led integration brought about by tariff reductions) to deep integration (the need to harmonize or at least approximate domestic regulations) has not progressed as far at international as it has at regional level. In the case of the EU, which has experienced the deepest integration of all regional organizations, much of what is perceived as domestic policy, at least in market regulation terms, has already shifted from the nation state to the regional level by way of the SEM. However, as subsequent chapters demonstrate, the pressures for deep integration are present in several policy areas at the international level.

Moreover, the spectre of a shift to a higher level of governance on a number of erstwhile domestic issues has strengthened the argument that integrative trends are blurring national boundaries and eroding the sovereignty of nation states. Perspectives on desirable or likely outcomes vary, resulting in a number of complex questions. The answers to these questions are of utmost importance to business given that governance structures scope out the regulatory framework in which businesses operate and hence help shape their operating environment and the strategic options available to them. These questions, many of which are addressed in Chapter 3 in particular and throughout this volume, include:

- Is there a case, particularly given the emerging international regulatory gap, for greater global self-regulation?
- Is the world moving towards a system of multi-level governance in which national, regional and international interests work together to perform tasks traditionally performed by nation states?

- Does the tendency to shift part of the public policy agenda to an international level represent the death knell of national sovereignty or a redefinition of sovereignty that will enable greater regulation of MNEs' activities?
- Is the demise of the nation state exaggerated, given that the emerging multilateral international governance system is not supranational and is based on the nation state?

Globalization driver three: finance and capital spread

The additional trade and investment generated by globalization requires parallel movements of capital and finance (see Chapter 12). Deregulation, liberalization and technological change have indeed combined in recent decades to transform the finance sector to support the growing number of transnational transactions. Finance was traditionally always a heavily regulated, and hence fragmented, activity geographically, but change began in the 1960s with the emergence of the Eurodollar markets (markets in dollars held outside the US banking system and US control). A series of US reforms in the 1970s made it easier for US banks to operate abroad and for foreign banks to gain access to the US banking market. In 1975, the New York Stock Exchange abolished fixed commissions on dealing in securities and subsequent reforms of the US financial system have enabled banks to offer a much wider range of financial services. In the UK, the 'Big Bang' of 1986 ended the demarcation between banks and securities houses and allowed foreign firms entry to the stock exchange. Other European exchanges have undergone similar reforms. Within the broader context of the SEM, policies like the Second Banking Directive created the possibility of banks operating throughout the EU on the basis of a so-called 'single banking licence'. A key component of the SEM was the removal of the remaining controls on capital movements within the EU. Without such a measure, the additional trade, investment and industrial restructuring anticipated as a result of the SEM would have been severely inhibited. On a multilateral level, negotiations on liberalization of financial services continued after the end of the Uruguay Round with thirty countries reaching an interim agreement in 1995 to guarantee access to banking, securities and insurance.

The combination of more open markets with the adoption of new information and communications technologies (ICTs) has transformed international capital movements. In principle, capital can now be transferred around the world in an instant. In practice, although significantly reduced, regulatory barriers continue to prevent the full collapse of time and space for financial transactions. However, the potential for instantaneous financial transactions spanning the globe remains and is moving nearer to realization.

These developments have also increased both the complexity and volatility of international financial markets (see Chapter 12). A range of new financial instruments, many inherently volatile such as derivatives, has emerged to serve a broader marketplace. Although more mobile capital is clearly needed to support a more integrated international economic system and all parts of the production chain within multinationals, this mobility also brings with it more volatility. Individuals and institutions, for example, are able to transfer vast amounts rapidly around the globe to arbitrage between exchange and interest rates. Such movements can intensify crises and transmit crises from country to country, or even from region to region. The 1997 Asian financial crisis was a prime example of the potential for contagion in a more interdependent world (see Case Study 1.1).

A further consequence of these trends is a weakening of the link between currencies and their traditional locations – the nation state – and the multiplication of the forms of money. The former trend is particularly marked for the US dollar, which has become the currency of choice in a number of Latin America countries and elsewhere. Indeed, there are currently as many dollars in circulation outside as inside the United States. The birth of the euro on 1 January 1999 also reflects a movement away from the strong identification of currency with national territory and heralds the demise of such prominent currencies as the German mark, the French franc, the Italian lira and the Spanish peseta. The possibility of further regional currencies, albeit unlikely in the short term, cannot be ruled out. The link between national territories and means of payment is also further weakened by the cross-border use of credit cards and discussions about digital currencies within the context of the growth of electronic commerce.

Globalization driver four: the diffusion of information and communication technology

Technological innovation and its diffusion have clearly played a significant role in the redefinition and reorganization of commercial and economic space known as 'globalization', both facilitating restructuring of the manufacturing system and transforming the configuration of value-chains. Indeed, for companies in many sectors the development of new technology and/or its exploitation makes the difference between success and failure. This is increasingly the case not only in explicitly technological sectors but also, with the advent of e-commerce (see Chapter 13), in traditionally less technologically sensitive sectors such as retailing.

However, technology's precise significance in the globalization process is a subject of some controversy. Technological determinists such as Kevin Kelly (1999) argue that technology is the prime mover of change and that it makes globalization inevitable and irreversible. A more eclectic approach maintains that technological developments, although central to the transformation of intra- and inter-state and enterprise relationships, are not sufficient to bring about such change on their own account. Other social, political and economic factors, like the spread of neo-liberal economic philosophy with its themes of liberalization, deregulation and open markets, are also needed. In other words, technology is an important facilitator of change rather than its primary mover.

Even without the more extravagant claims for technology, it is possible to identify far-reaching effects of its diffusion. Transportation and telecommunications technologies have transformed space–time distances, reducing the effective economic distance among nations and organizations. Transportation technologies are concerned with the carriage of goods and people and, through progress from horsepower, sail and steam to the internal combustion engine and the jet engine, have significantly reduced the time taken to travel large distances. Communications technology, increasingly converging with computer technologies into ICTs, is concerned with the virtually instantaneous transfer of data and information to potentially anywhere in the world. Such technology has resulted in lower transaction and operational costs and given rise to e-commerce. This new form of business organization is potentially a prime agent of de-territorialization. However, cross-border payments, taxation and consumer protection issues, among others, require resolution before e-commerce fulfils its potential.

More generally, ICTs facilitate the emergence of denser and more effective networks within and between enterprises, especially across borders, a factor that underpins the contemporary debate about the 'new economy'. At the height of the dot.com frenzy, the new economy, a much over-hyped concept like globalization, threatened to take over from 'globalization' as the defining theme of the early twenty-first century. In practice, the new economy, with its emphasis on the intensification of networked organizations and relationships and on technology, can be viewed as a refocusing of the globalization debate, or at least as a closely linked variant of it.

Not only is this emphasis on networks of major importance for the management of MNEs, but it also has resonance for all organizations. For example, the high profile of and stronger links among NGOs, both nationally and internationally, as witnessed at the September 2000 fuel blockades in Europe and the December 1999 demonstrations at the WTO Ministerial in Seattle, are partially attributable to the spread and relative low cost of ICTs which enabled NGOs to utilize the Internet to inform and organize their supporters. Ironically, NGOs use one of the main drivers of globalization to facilitate their campaign to return to more localized social, political and economic forms of organization.

Globalization driver five: social and cultural convergence

A consequence of greater liberalization and the spread of global communications technology is a degree of social and cultural convergence, in itself a precondition for globalization. This does not imply that a global culture has replaced or is replacing the diversity of local and national cultures in the world. The range and deep-rootedness of beliefs, values, experience and symbols is too extensive for that. However, helped by the global consolidation of mass media, especially in broadcasting and by the power of the Internet, there is growing recognition of common symbols and experience. Such commonality does not need to be deeply embedded, or even much more than superficial, before it becomes useful for the development of a global mindset and hence global marketing. Social and cultural convergence across boundaries is only possible when there is no clash with more profoundly held cultural beliefs specific to a particular place or grouping, such as religion.

The emergence of a global consumer, or at least consumers with common preferences across a significant part of the globe, creates opportunities for the creation of global products – that is, homogeneous products that can be sold throughout the world on the basis of global marketing and advertising campaigns. Truly global products are relatively few and far between but where their existence is possible, they increase the viability and desirability of developing international production systems and value chains, with all the potential gains in terms of scale economies and utilization of different comparative advantages.

Divergent views of globalization

The debate about international economic integration is highly significant as it frames the business environment and shapes corporate strategies. However, globalization has proved to be a highly controversial process. The controversy centres upon interpretation of the strength and significance of the changes in the world economy. The most fundamental question concerns whether the economy is becoming truly global or simply more inter-national. A global economy implies a borderless economic space in which the integration of operations and markets takes place according to economic and market imperatives as opposed