INTERNATIONAL BUSINESS

UNIT 1 INTRODUCTION

Objectives

- After reading this unit you should be able to:
- Define international business and highlight its importance
- Explain the historical developments of international business and its dimensions
- Understand the role of MNEs as Central actors in international business
- Appreciate the role of trade in services and the role of international trading houses and
- Understand the role of international business in the world economy and spread of global competition

Structure

1.1 CONCEPT OF INTERNATIONAL BUSINESS

The conceptual framework of international business starts with its definition. International business can be described as the business carried on across the national borders between two or more nations. The concept of international business stems from the business processes intersected by the national borders. Since the international business processes are not confined to the geopolitical boundaries in the conventional sense, the term `national border' is to be used in a wider perspective. A more flexible concept of the national border is the contact line between people and the multinational enterprises (MNEs) possessing a distinctive character attributable to their different social, cultural and economic environments.

A three-pronged approach may be adopted for understanding the concepts relating to international business. The first prong deals with the transmission of resources from one country to another in the form of shipment of goods, transfer of funds, and movement of people. The second prong is concerned with the relationship of the MNE with the host societies. The third prong involves the elements of conflict arising from the national sentiments and nationalistic attitudes guiding both the parent and the host countries. Here, the MNE has to grapple with the profitability aspects. It has also to grapple

with the question of how best to accommodate the interest of the parent and host nations.

Resource transmission is based on the mutual benefits expected from the trade flows between the trading nations and the investment activities undertaken by the MNEs abroad. The resource allocation, according to the Comparative Cost Doctrine propounded by Ricardo, benefits the countries engaging in trade. The state intervention may cause trade diversion, which may distort cost differentials and may direct resources to their inefficient uses. Trade across borders and investment in other countries (resource transmission) provide opportunities to the MNEs for taking advantage of their superior technology, innovativeness, and economies of scale.

The diverse business systems prevailing in different societies confront an MNE with the choices between conformity and innovation. A suitable growth strategy has to be adopted by introducing changes in a gradual manner, acceptable to the host governments, keeping in view the employment and welfare of the people. Despite the efforts of the MNEs to follow a balanced approach, areas of conflicts do arise because of different national interests. The MNEs are often seen as penetrating into the host country markets for exploiting their economies. The objectives of foreign investors and socio-economic objectives of the host governments may come in conflict. The conflicts relating to equity participation, use of local inputs, employment, expansion of exports, etc., may be resolved through negotiations.

A multi-national enterprise carries out its international operations in two ways. It may deal with the individual countries separately according to their politico-economic and social environments, taking care of the national interests of both the parent and the host countries. With different environmental factors prevailing in different countries, this approach may lead to a diversified and fragmented global pattern for the MNE.

Usually, an MNE operates simultaneously in many countries: The multi-country operations necessitate a suitable overall conceptual framework for international business. Here, some kind of conflict may arise between the need for specificity and the need for uniformity in managing multi-country operations. In the second approach, guided by the need for uniformity, an international firm considers the entire world as a global market, and attempts to use similar global strategies and goals in the diverse environments of different countries. The conflicts arising from pursuing discrete and uniform policies and strategies are related to problems such as product policy, logistic plans and ownership. Although it may appear difficult for an MNE to achieve unified policies in the face of its unique global characteristic due to different business laws in different countries, the success of the global firm lies in achieving a balance between fragmentation and unification. The thrust in the balance however may be towards unification.

1.2 NATURE AND IMPORTANCE OF INTERNATIONAL BUSINESS

The international business operations comprise many facets; and international trade is just one of these. Other aspects, such as licensing, joint[s] ventures and Foreign Direct Investment (FDI) of international business usually follow later, but not necessarily.

The United States is by far the largest investor and most of its investment is in the industrialised countries. The international trade and FDI, being integral parts of international business, are complementary to each other. A large part of the trade of the developed countries is among themselves, and investment is also mostly in each other. Earlier, the foreign investors invested their capital in activities like plantations and mines, but beginning from 50s, the major type of the FDI took place in the manufacturing industries, reflecting the steady development of the technology of the MNEs.

In recent years the reverse investment began in the case of the United States, and it became the most important and largest host country to the FDI. The increasing FDI into the United States is because of certain country-specific factors, namely, large market potential, abundant raw materials, declining labour costs as compared to other higher income countries, and the restricted trade policy for some products. Certain firm specific advantages gained by the European, Japanese and Canadian MNEs also encouraged them to invest in the United States.

Multinationals from the developing countries have also begun competing with the companies of the developed countries. Brazil, Argentina, Mexico, India, Hong Kong, Taiwan and South Korea are the important third world nations in some fields like construction contracts. The international companies from South Korea, Brazil, India and Taiwan have offered serious competition to the companies from the United States and even to the aggressive Japanese and German firms. Their advantage lies in their more adaptive attitudes, willingness to enter into joint ventures, partnerships, lower cost of production and lower profits and remittances.

The importance of a country in the world economy may be known by its share in international trade. The United States occupies the largest share in world trade followed by Germany, Japan and France. But, its share is declining continuously and that of the other developed countries increasing. The developing countries, especially the oil producing countries of the Middle East, have increased their share in the total world trade.

An interesting part of international trade is that some countries like Singapore, Hongkong and Taiwan have exports and imports substantially greater than their GNP. This happens due to the nature of their trade and their role as offshore assembly platforms (trade entrepots). Such trading countries export most of their production and allow export related imports.

International business is important because of its concern with (i) quantum, composition and direction of trade flows and FDI; and (ii) the effects of trade and foreign investment on the importing and exporting firms, and the world economies at large. In the absence of international business, the world could have remained stagnated as different countries would have been producing all the goods of their requirements by using their factor endowments at sub-optimal level. It was the merchandise trade in the initial stages and then the trade in services which provided the stimulus to gainful resource allocation according to the cost advantages. The imperfections and trade barriers in world market gave rise to licensing, joint ventures and FDI as other important forms of international operations. Therefore, the study of international business is significant in order to understand the intricacies behind the international trade and FDI and their effect on the world economic growth and welfare.

Activity 1

Contact some exporting company in your town, and ascertain the reasons for the increase, if any, in its exports.

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1.3 GROWTH OF INTERNATIONAL BUSINESS AND FDI

The genesis of international business may be traced to the ancient times when the Mesopotamian, Greek and particularly the Phoenician merchants carried out their trading activities in different parts of the world. The Phoenecians controlled the sea-borne trade and the goods procured by them from Egypt, Babylonia and Assyria were sold throughout the Mediterranean. They were doing foreign business even upto Cape Verde and the Azores Islands in the Atlantic, and for this purpose used the straits of Gibralter.

In those days, India's spices and textiles were also being traded by the Phoenicians to Egypt, Turkey, Greece, and Rome. The trading was mainly confined to the West Coast of India. Goods were landed in Southern Arabia through sea routes and transported to the Mediterranean ports for shipping to other trading places.

The Roman merchants were active in international business and played an important role in the development of the Roman empire by providing finance for the military expeditions. Trade was facilitated by the construction of roads and development of the banking system. The banks, owned by private entrepreneurs, accepted deposits for providing loans and credits to the merchants.

Rome was not only the centre of attraction for the merchants. They were operating as far as the Atlantic Coasts of Africa "and Europe and reached Germany upto the Baltic Sea. Some penetrated even to Turkestan to purchase Chinese goods.

The decay of the Roman empire and the rise of Turks and the Arab crusaders shifted the control of strategic ports into the hands of the Arabs and, subsequently, that of the overseas trade and markets. They purchased goods from India by establishing trading ports in Sind and dominated the trade on the Indian West Coast. During the 13th and 14th centuries, the Arabs spread their network in South-East Asian countries, notably in the present day Malayasia, Indonesia, Brunei and Southern Philippines.

The international business received stimulation from the events that happened at the beginning of the 11th century. The crusaders were forced to search out new avenues for trade. New commercial centres in Italy, such as Genoa and Venice sprang up and the Europeans, after losing their control of the sea routes to India through Red Sea and the Straits of Harmuz, had to circumnavigate Africa in order to obtain the Indian spices and textiles, which were in great-demand in Europe. Meanwhile, the European Renaissance led to voyages and the discovery of America by Columbus and the arrival of Vasco de Gama at Calicut in 1498.

The hurdle in the growth of international business was eased by the development of credit institutions and the introduction of methods of payments. The trade instruments like,. the bills of exchange and drafts facilitated the rapid increase in trade transactions, as there was no need for actual gold or silver to be delivered to settle the unfavourable balance of

trade. The bill of exchange assured the payment to the exporter on a specified date. Associated with this, the banking houses, functioning in the Eastern Mediterranean region in the 14th century, became important financial centres. By the 16th century, Holland developed into an international financial centre, and the Dutch banks financed the business all over Europe.

The considerable expansion of international business needed lots of money, and the individual investors were unable to cope with the situation. It became inevitable to pool capital together for carrying, out large transactions. The mechanism of joint stock company developed. Initially, the individual investors were returned their shares after the completion of a particular trade for which the capital was raised, but later on, the investors were permitted to keep their money with the company and earn dividends. The shareholders could sell their shares to the company depending upon their market value.

As a matter of fact, a great influence on the international business was brought about by the Industrial Revolution, which facilitated the application of machinery into the production process. The Industrial Revolution occurred in the U.K., and not only the production of manufacturing goods took place there but also these goods become cheaper. The excess production was exported and, in return, food-stuffs and raw materials were imported.

A series of innovations after, the Second Industrial Revolution in 1880 caused large scale production of a variety of .goods which required more raw materials from other countries. Capital began to flow out for the purpose of production of raw materials, which were mostly in the extractive industries, transport, communications and electric power. The world became interdependent; manufactured goods began to be exported by the European countries and food and raw materials by the less developed countries. The import of capital by some countries provided them an opportunity to develop their own industries and, thus, they became a part of the industrial world. Japan, in recent years, became an important industrial power by taking advantage of the capital inflows.

Emergence of Multinational Corporation

It was as early as the Fourteenth, century that the multinational companies were involved in foreign business. The trading firms in the Italian trade centres of Genoa and Venice operated across the border throughout the Eastern Mediterranean area. In Britain, trading companies were well-known for their foreign business during the reign of Queen Elizabeth I. The trading firms enjoyed monopoly powers in world markets, but they were surpassed by new forms of enterprises created by the Industrial Revolution. The need arose for' direct investment abroad in order to produce sufficient raw materials to meet the requirements of the manufacturing plants at home.

The outcome of this process was the formation of multinational companies making direct foreign investment for extraction, processing and transportation of raw materials to their parent countries. Some individuals were the forerunners in the. establishment of multinational enterprises. In 1865, Friedrick Bayer, a German. purchased some shares in New York just after two years of establishing a chemical plant in Germany. In 1876, he established dyestuff factories in Russia, in 1882 in France and, in 1908 in Belgium. According to Fortune Survey of 1990, this German firm "Bayer" ranked 39th among 500 world's largest companies in terms of their sales.

Alfred Nobel, a Swedish industrialist. established a plant at Hamberg, Germany in 1866. Similarly, the Singer company founded a plant at Glassgow, Scotland in 1887. In India, the commencement of the multinational corporate business may be assumed to have stated with the

establishment of the East India Company at the beginning of Seventeenth century. In 1788, Thomas Perry was the first to act as a free merchant in Madras followed by Jessop's predecessors, Breen & Co, in Calcutta.

Such trends in the FDI provided new dimensions to the international business activities. The payments for multinational business took the form of royalties, license fees and management fees in return for the use of patents, trade marks and technological know-how.

The United States' multinationals began their operations as early as 1850, when the United Fruit Company established its plants in Honduras and Nicaragua. As in the case of the others, the U.S. multinationals also developed in their early stages due to the need for new sources of raw materials. The U.S. foreign investment took place mainly in oil companies and mining. It was after the World War I that the U.S. first came on the international scene on a massive scale and industries, such as automotives, chemicals, petroleum and machine tools developed rapidly by supplying products to the allies. As the greater part of the 1920's saw a worldwide economic prosperity, the U.S. automotive industry, began dominating the world markets.

International Business in the Post-World War II Period

After suffering a setback following the 1930's severe recession in the world economy, the growth of international business in the post-World War II period, especially after 1950 was tremendous. Both the international trade and investment grew fast due to changes in the international economic arrangements like the proliferation of the bilateral investment treaties specifically meant for the promotion and protection of the FM. Other factors such as favourable political and economic environments of the host countries, prospects of profits and the developments of new forms of investments also provided a spurt to the growth of international business. After the production of merchandised goods, the MNEs also played a leading role in the international trade in services. In 1989, the contribution of the trade in services accounted for S 1000 billion out of the total world trade amounting to $ 3100 billion.

The new investment arrangements in the form of non-equity involvement in licensing agreements, turnkey contracts, management contracts, franchising, international sub-contracting and equity sharing in joint ventures have grown rapidly since the mid 1970s. The newly industrialized countries (NICs) entered into such contracts and, after attaining export capability, they began exporting technology abroad, both in the form of joint ventures and the FDI. Many OPEC nations are now having joint venture arrangements with the parent companies in their downstream processing, refining and distribution of related petroleum products. In the ASEAN countries, Japan is the major partner in the petrochemical joint ventures.

During the decades of the Fifties and Sixties, United States continued to be the major investor in foreign countries. The book value of the U.S. FDI increased from $ 11.8 billion in 1950 to $ 78.1 billion in 1970. The bulk of the U.S. foreign investment went to Canada and Western Europe, which received more than 50 per cent of the total U.S. FDI in 1970. The influx of American investment in Western Europe was mainly meant to take advantage of the emerging prosperity of the Common Market countries and to protect its export markets from their tariff barriers. The markets for Eurodollars and Eurobonds also developed in West Europe, promoting U.S. investments there. When the U.S. Government imposed restrictions on the American FDI, the U.S. MNEs continued to expand by using these markets.

The LDCs were not a large recipient of the U.S. direct investment during this period. The reason was America's lesser accent on investment in the extractive industries and greater accent on investment in manufacturing. The U.S. investment in Latin America in the manufacturing sector, increased only from $ 1.8 billion in 1950 to $ 4.6 billion in 1970. In Asia, during the same period the investment increased from $ 100 million to $ 150 million, indeed a meagre amount. The total U.S. direct investment in manufacturing increased from $ 6.4 billion to $ 32.3 billion over the same period. Thus, the U.S. multinationals changed their geographic as well as investment foci, resulting in very marginal or no development of LDCs.

In the 1970s, the developed countries invested relatively large amounts in the developing economies. In 1975, the U.S. foreign investment going to the developing countries amounted to about 47 per cent of its total international investment, and to Japan it was about 60 per cent. However, the trend was reversed in th 1980s and the developing countries again received relatively small amount of FDI. In 1986, the foreign investment by the U.S. and Japan to the developing countries was about 27 per cent and 33 per cent respectively.

The increase in FDI in the developing countries during the 1970s was in response to the optimism about the growth potential of these countries which did not continue in the 1980s. Some of the important reasons for this decline may be stated as the decreasing confidence in their credit worthiness due to the debt crisis in those countries, recession and macro economic instability (which further went to undermine the confidence of the investors), reduction in the attractiveness of large resource based projects, particularly petroleum owing to the nationalisation drive in the Middle East and the relative improvement in the profitability in the industrialised world itself.

The greater amount of Japanese investment is still being directed to the United States, but it has also shown an upward trend in Latin America and Asian countries, particularly the NICs. The interesting aspect of the international business during 1970s and 1980s is the decline in the dominance of the U.S. MNEs and the increase in the competitive strength of the European and, Japanese multinationals, and of even some MNEs of the developing countries. A reverse investment occurred in the U.S. The MNEs from Europe and Japan began investing large amounts of FDI in America. They have also provided competition to American firms in the overseas markets. A greater foreign investment took place in the manufacturing and service industries, showing a movement away from resource based projects.

Those of the LDC2s which have liberalized their economic policies have attracted relatively larger amount of FDI and have made good progress in their economies. Two lessons emerge from the investment behaviour in relation to FDI. One, the magnitude of FDI depends on the economic success of a nation. One would rarely find a case where foreign investors have taken interest in countries where unfavourable attitude to the international investment -and an uncongenial environment prevails. Two, infrastructural development is an essential prerequisite for attracting FDI. The prospects of the FDI in the LDCs, therefore, will depend upon the economic policies pursued by those countries with regard to the foreign investment and predictable political stability, and also the protection these countries can give to the trade marks.

Activity 2

From the above discussion about the growth of international business, list some important events which provided a spurt to the foreign trade and investment.

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1.4 DIMENSIONS OF INTERNATIONAL BUSINESS

International business has many dimensions. It is not merely the border crossing which is sufficient to comprehend the numerous problems faced by the MNEs in the overseas markets. Different countries follow different business laws, tax systems, and have different political, economic and cultural environments. The strategies of the MNEs aiming at efficient management and optimum returns are shaped by the external factors. An NINE, having company specific advantages on which it may have some control, has to confront and manage the foreign environments which may not be within its control. The formulation of policies to achieve efficiency in the functional areas, such as production, finance, marketing and human resource management, has to take into account all these realities.

Two types of theoretical issues are invoked in the international business management. The first type involves the study of trade and the FDI theories, and the second type is concerned with the financial matters which are, in turn, affected by the financial factors such as fluctuation in foreign exchange rates, changes in political and economic conditions and inflation. All these factors have to be taken into account while evaluating the fruitfulness of the foreign investment.

The MNEs are often criticised in their host countries. It is, therefore, advisable to maintain good relations with the host governments and convince them that their intention is not merely the pursuit of profit but directed at raising the level of growth and employment. It is important for an MNE to adopt an adjusting attitude towards the policies and programmes of the different host nations.

The international business also includes the study of international accounting, pricing, international management and marketing as they have a direct bearing on the operations of an MNE. Foreign competition is a continuing phenomenon, and this requires an MNE to make the necessary changes in its production techniques for lowering cost, raising productivity and improving the quality of its products, to exist in a globally-oriented business.

The various dimensions of international business may be summarised in Table 1.1.

Table 1.1

DIMENSIONS OF INTERNATIONAL BUSINESS

Host Country Environment Factors	MNE specific Advantages
International trade theory foreign exchange theory, Economic variables such as input, foreign exchange and balance of payments. Non economic variables, such as political, cultural and social systems	FDI theory adoption of entry methods and policies for risk management

Table 1.1

Host country laws about trade, foreign investment taxes and foreign exchange controls. International organisations such as IMF, GATT, UN Agencies and the international code of conduct.	Multinationals responses to the government policies, such as transfer price, tax planning foreign exchange exposure management. Functional Areas of MNE

Activity 3

From Table 1.1, mention : (i) the company specific advantages and the host country specific advantages; and (ii) also prepare a `task wheel', showing the controllable and non-controllable factors for an MNE.

Company Specific Advantages	Host Country Specific Advantages

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1.5 CENTRAL ACTORS IN INTERNATIONAL BUSINESS

The multinational enterprises are the central actors in` international business. An MNE-also known as Multinational Corporation (MNC), International Corporation (IC) and Transnational Corporation (TC)-conducts the business across the borders of a country and has been described in various manners. The U.N. Centre for Transnational Enterprises defines the Multinational Corporation as "enterprises which own or control production or service facilities outside the country in which they are based." Feyerweather defines them as "multicultural, multinational, global spanning systems". Rodriguez and Carter refer to a multinational firm as "a company with substantial operations (usually 30% or more of its total activity) carried on outside its own national borders. These activities may be trading or manufacturing"

According to Phatak (Arvind K. Phatak, Managing Multinational Corporation, Praeger Co., New York, 1974, pp 21-22) "A multinational company is an enterprise that has an interlocking network of subsidiaries in several countries, whose executives view the whole world as its theatre of operations, and therefore obtain and allocate financial, material, technical and managerial resources in a manner conducive to the achievement of total enterprise objectives." Like a firm doing business in a domestic market an MNE is also required to take decisions about the prospective returns. In addition, the MNEs may also have to take into the account the fluctuations in interest rates, exchange rates, impediments to trade, repatriation of funds and inflation in the countries where its subsidiaries operate.

Thus, the essence of multinationality is the international production. An MNE is that corporation, whose business operations are across the border, foreign to total sales (F/T ratio) is 30% or more and the attitude of management is geocentric, having a global orientation. The MNE is not supposed to adopt the ethnocentric approach as it is home-oriented, and it will not be called a true MNE even if it follows the polycentric approach which is merely the host nation oriented.

1.6 DIFFERENCES BETWEEN DOMESTIC AND INTERNATIONAL BUSINESS

Both the domestic and international businesses consist of consumers, producers and agencies purchasing goods and services. People in international business have also to resort to market surveys in order to know the customers' preferences for products, price promotion and distribution stategies. What then are the differences between the two? The striking differences in the domestic and international business are in terms of environmental factors affecting the decisions of the investors.

The economic and political risks confronted in the international business distinguish it from the domestic business. It is important for a multinational enterprise to study the prevailing economic and political conditions of the host country and also forecast the likely trends in them. The balance of payments position explains the performance of the external sector. A large deficit on current account of the balance of payments would mean dismal market opportunities. The rate of growth of the GNP, rate of growth of the labour force and labour productivity and per capita income are also indicators pointing out the future business possibilities in a particular country.

The political situation also influences the investment decisions. A change in the government may lead to the blockage of funds. In some cases, the political risk may be considered very high when expropriation of the foreign capital, an extreme step, may appear to be a possibility.

In the international business we have also to consider the variations in the exchange rates, inflation and policies of the government. The exchange rate changes involve the transaction, translation and operational risks. The volatility in the exchange rate affects the management of the working capital and the profitability of the international investment. A careful scanning of the environments of foreign economies is highly important in the decision making process for the international investment, its management, expansion of existing subsidiaries and the worthwhileness of the foreign investment.

1.7 TRADE IN GOODS AND SERVICES

It is important to understand the distinction between trade in goods (merchandise trade or visible trade) and trade in services (invisible trade). The merchandise, i.e., the imports and exports of raw materials and manufactured goods may show either trade deficit or surplus in the current account of a country's balance of payments. The invisible trade relating to the traditional services, such as shipping, aviation, communication, banking and insurance, plays a vital role. It supplements the trade in goods and may thus reduce the trade deficit. The trade in services has assumed a new trend, i.e., moving from the traditional services to the non-traditional services such as data processing, computer programming, scientific research, engineering, and consulting. The services are rapidly growing, and have opened new vistas for international trade. The developed countries are now orienting their economies from the industrial sector to the service sector, because foreign trade in services has become a critical factor for economic growth and employment.

In India, the trade in services has played a positive role, reducing our trade deficit and improving our foreign exchange position. Its role in India's Sixth and Seventh Five Year Plans may be summarized in Table 1.1.

Table 1.2

Key Indicators of India's Balance of Payments

(As per cent of GDP)

Year	Exports	Imports	Net Invisible	Trade Balance	Current Account Balance
1980-81	4.8	9.2	3.2	-4.4	-1.2
1981-82	4.9	8.7	2.4	-3.8	-1.5
1982-83	5.1	8.4	2.0	-3.2	-1.3
1983-84	4.9	7.7	1.7	-2.8	-1.1
1984-85	5.2	8.1	1.7	-2.9	-1.2
Average 1980-85	5.0	8.4	2.2	-3.4	-1.3
1985-86	4.4	8.1	1.4	-3.7	-2.3
1986-87	4.5	7.7	1.2	-3.2	-2.0
1987-88	4.9	7.7	0.9	-2.8	-1.9
1988-89	5.3	8.9	0.8	-3.5	-2.7
1989-90	6.4	9.3	0.6	-2.9	-2.3
Average 1985-90	5.1	8.3	1.0	-3.2	-2.2

Source : Government of India, *Economic Survey 1990-91*. p. *152*

Table 1.2 shows that the trade deficit in the Sixth plan averaged 3.4 per cent of the GDP, but it was brought down to 1.3 per cent on account of the surplus enjoyed by India in trade in services during this period averaging 2.2 per cent of the GDP. Although, the surplus in trade in services declined during the Seventh plan to 1.1%, it was still significant, as it lowered our trade deficit from 3.2 per cent to 2.2 per cent of the GDP.

Activity 4

Study the latest economic survey of the Government of India, and note the role of services on the current account of India's balance of payments. Attempt similar study of the data relating to some other developing countries. Compare the data and offer your comments.

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1.8 STATE TRADING IN INTERNATIONAL BUSINESS

State trading, as defined in the Havana Charter, means trading by the government or the government controlled enterprises.

According to Kostecki (in his book *State Trading, 1978), 20 to* 25 per cent of the international trade during the 1970s was carried out through the state trading. State trading has occupied an important place in the foreign trade of the developing countries, and ranges from 10 per cent (in the case of Brazil) to 90-100 per cent (in case of Egypt). As the foreign trade was the state monopoly in the erstwhile communist countries, usually the entire foreign trade transactions were carried out by way of state trading. In India, the share of public sector in total exports was 24.1 per cent in 1988-89. Most of the state trading in India is through the State Trading Corporation (STC).

The state engages in the international trade for achieving external and domestic objectives. The external objectives of the state trading are improvement in the international bargaining power and terms of trade, export expansion, fulfilment of the international obligations and linking of trade with socio-economic policies. The aim is improvement in the conduct of the international trade and increasing gains to the nation. The domestic objectives behind the state trading are protection of the domestic industry, achievement of price and distribution policies, augmenting of government revenue, health and the public security.

State trading would improve the welfare of the nation so long as it is employed to overcome the market imperfections. If it tends to distort the international trade flows like tariffs and quantitative restrictions, it may adversely affect the international welfare. Moreover, state enterprises have generally not been found operating as efficiently as private enterprises, and on this ground their contribution to the welfare of the nation is relatively lower.

1.9 INTERNATIONAL TRADING HOUSES

International trading houses are established to facilitate the trading activities at the global level.. The foremost function of an international trading house is to coordinate the exchange of goods and services between the importers and exporters of different countries.

Having a world-wide network of staff and communication units, these trading houses carry out market research in order to identify the potential buyers of different products supplied by different countries in the overseas markets. They also maintain trained personnel for assisting the exporters in procedural matters and the business laws of the trading partners. They also arrange the logistics, and accept financial liability for the shipments.

As a matter of fact, the international trading houses are extensions of export management companies (EMCs), which are independent businesses and act as the export departments of some other manufacturers who are not directly engaged in the export activity. In countries, such as Canada, certain manufacturers organise an export consortium for trading their exportable products. There are several trading houses operating in South Korea, Brazil and the United States, but most important are the large Japanese trading companies, known as Sogo Shoshas, which, after achieving success in various export markets, expanded their role from an international focus to a more global and multinational outlook.

These days, the international trading houses participate in joint ventures, provide finance for procurement of raw materials and assist in the third world country trade negotiations. With their pool of skilled and knowledgeable personnel in different parts of the world, they are well qualified to provide liaison function in multilateral negotiations, and can identify the potential participants in international joint ventures. In many cases, they serve' a banking role, which is made possible by their close connections with several: international banks.

1.10 INTERNATIONAL BUSINESS IN WORLD ECONOMY

Although many structural problems have occurred in the world economy,

especially after the 1973 oil crisis, international *business has* taken an upward trend. International trade has grown from $ 136 billion in 1960 to $ 2 trillion in 1980. During the 1980s, the world trade rose rapidly. According to the data in the 1991 edition of the IMF's *Direction of Trade-Statistics Year book,* international trade accounted for more than 3 trillion in 1990. The *value of* the world trade increased by about 14.6 per cent (in U.S. dollars) in 1990 compared to 8.1 per cent in 1989, and 14.5 per cent in 1988. However, the growth of trade in volume terms slowed by about 3.9 per cent in 1990 and 7.1 per cent in 1989 due to the decline-in global economic activities, disruption in trade among the central and East European countries and rise in the oil prices.

In 1990, the trade of the industrial countries grew at about the same rate as the world trade. Their exports rose by 15.3 per cent and imports by 14.8 per cent. Germany overtook the United States as the world's leading exporter. The exports and imports of the developing countries increased by 13.0 per cent and 15.3 per cent respectively in the same year. Among the developing countries, the Middle East recorded the fastest export growth in 1990 (23.9 per cent) mainly because of the higher oil prices. Its imports rose by 16.9 per cent the same year. The aggregate trade surplus of the Middle East shows the highest rise since 1981 (in US dollars).

The growth in the exports of the developing countries was 12.3 per cent in Asia, and it was outpaced by the rise in imports (14.3 per cent). The world trade flows are summarized in Table 1.2.

Table 1.3

World Trade Flows

(billion U.S. dollars)

Destination	With Industrial countries		With Developing countries		With USSR and select other countries[1]		Total	
Origin	Exp.	Imp.	Exp.	Imp.	Exp.	Imp.	Exp.	Imp.
Industrial countries								
1984	871.9	903.2	313.1	388.5	26.7	29.7	1224.5	1326.3
1989	1611.7	1651.6	463.4	544.2	35.1	30.0	2127.5	2238.9
1990	1867.1	1906.9	527.6	614.8	37.2	35.3	2452.4	2570.7
Developing countries								
1984	345.9	321.5	169.5	172.4	26.3	24.3	565.7	529.8
1989	478.0	469.5	251.2	250.0	32.2	28.4	785.3	763.3
1990	550.3	552.0	283.9	289.0	28.1	25.8	887.3	880.0

1— Albania, Bulgaria, Cuba, Czechoslovakia, former GDR, Democratic People's Republic of Korea and Mangolia.

Source : IMF, *Direction of Trade Statistics Yearbook, 1991.*

Activity 5

From Tale 1.3 ascertain the growth in foreign trade of (i) industrial countries and (ii) developing countries between 1984 and 1990 (in U.S. dollars).

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1.11 GLOBALISATION OF BUSINESS (SPREAD OF GLOBAL COMPETITION)

The United States enjoyed a considerable lead in the international business before and immediately after the World War II. The economic recovery of Western Europe and Japan in the early 1950s began eroding the U.S. domination, and created competition for global markets. One of the outcomes was that the number of the largest American companies in the 13 major industries of the world, such as aerospace, automotive, chemicals, electrical equipment, food products, paper petroleum, pharmaceuticals, textiles, got reduced from 11 in 1959 to 7 in 1976. Companies from Japan and Western Europe, particularly the German, Swiss and Dutch, have increased their share in the international trade and investment.

The spread of competition may be realised from the rise of the Japanese MNEs as a global force. In 1970, there was only one Japanese company among the 50 largest industrial companies in the world. The number increased to six by 1980. This trend continued, and in 1990 the Japanese have outstripped the United States in automobiles and steel. On the trade front also, the pattern shows a decreasing share for the United States and European countries, and a larger share for Japan. Even the multinationals from the developing countries are now in competition with each other in the international market.

The success of the European and Japanese multinationals in the face of the global competition can be attributed to their higher rates of savings, investment, technological development, improvement in management styles and higher productivity of labour. In view of the superiority gained by the multinationals of these nations, Lester Throw *(A Strategy for Revitalising American Industry,* Columbia Management Review, XXVII, No. 1 (Fall, 1984, p.9) lamented that unless the US corporations and government took urgent measures, its dominance as an industrial power would fast disappear, and it would be overtaken by Japan. In his words:

> "America faces a problem that is simply put. The huge technological edge enjoyed by America in the 1950s and 1960s has disappeared... We are now faced with competitors who may be in the process of achievements and may be with the process of moving ahead of us... when our effortless superiority has vanished, the American economy has been absorbed into a world economy. For most goods there is now a world market not just an American market. Competition is world-wide-not just American."

What Lester Throw has said may be taken as a warning by all those countries and governments, which are slack in upgrading their technologies and improving the quality of their products, but wish to compete at the world level where intense competition is a fact of life today.

1.12 WORLD'S LARGEST MULTINATIONALS

International trade and investment are now being dominated by the world's largest multinational companies. The United States which enjoyed a considerable lead before and immediately after World War II in the international business lost much of its share to European, Japanese, Canadian and even to the multinationals of the third, world countries. The relative performance and the number of the multinationals controlled by a particular country are indicative of its economic strength at the global level.

International Business