from foreign goods in the interest of protecting local businesses and the jobs they offer. In the US, people question why the Japanese are allowed to set up auto plants in the US, while the country's farmers cannot sell rice in Japan even though imported rice would cost less than Japanese-produced rice.[12] In our country too, there is strong opposition to the import of anything. Infact, the controversy relating to *Videshi* (foreign) versus *Swadeshi* (domestic) was a major issue debated by political parties in the recently held general elections in our country.

Negotiations among countries to ease trade restrictions and prevent unfair trade practices are ongoing. The World Trade Organisation (WTO) is a major trade organisation that has been established to negotiate trade concessions among member countries. The members meet periodically and discuss the ways of minimising trade barriers.

Developing an International Perspective

Firms operating in cross border markets need to develop an international perspective. Three areas need special attention:experience, focus and attitude.[13]

Experience One way to acquire international perspective is to hire people with global exposure. A company cannot become a true MNC without having managers with an overseas perspective.

Focus The second way to develop an international orientation is by emphasising global orientation to human resource activities such as hiring, remunerating, performance appraisal, promotions and the like.

Attitude A third way to develop an international perspective is by changing the attitudes of managers towards their work. Companies should screen candidates carefully for overseas assignments and depute only individuals with the right attitudes.

Managing Diversity

Diversity is the outcome of globalisation. Workforce of any MNC comprises people from different countries. Within this diversity of national origins, there is even wider diversity of cultures, religions, languages and dialects, educational attainment, skills, values, ages, races, genders and other differentiating variables. Managing such a cosmopolitan workforce is a challenging task for any executive.

> Diversity has both benefits and problems. The problems are: absence of cohesion among workers, inaccurate communication stemming from assigning different meanings to words, sexual harassement, etc. Benefits of diversity include: enhancing creativity, better decision making, prevention of groupthink and better ideation

Before examining how to manage a multi-cultural workforce, it should be noted that diversity has both functional as well as dysfunctional consequences.

Among the potential problems associated with diversity is the likely absence of cohesion among workers. Where group lacks cohesion, members become less productive, and it becomes difficult to create a work environment that is conducive for efficiency and effectiveness. Another problem of diversity relates to inaccurate communication which may result from different meanings assigned to words; and different interpretations assigned to situations. Yet another problem resulting from diversity relates to sexual harassment. Many women are victims of sexual harassment in the workplaces. Sexual harassment consists of any unwanted sexual behaviour, including but not limited to suggestive looks, sexual jokes, touching, or

pressure for sexual favours. Finally, earnings gaps exist in multi-cultural work groups. Earnings gaps refer to discrepancies between the earning power of workers of similar educational backgrounds but different races. An American or a German is paid much more in an MNC than his/her Indian counterpart.

While there are some potential problems associated with diversity, there are a host of benefits to be gained. Culturally diverse groups can enhance creativity, lead to better decisions and result in more effective and productive performance. A significant benefit from diversity relates to prevention of group think, which is a social conformity and pressures on individual members of a group to conform and reach consensus. Another benefit of diversity stems from the possibility of generating more and better ideas. Because group members come from a host of different cultures, they are able to create a greater number of creative and unique solutions and recommendations.

To reap the benefits listed above, managers must take steps to manage the issue of diversity. Steps depend upon the stage of group development: entry, work and action. In the *entry stage*, the focus should be on building trust and developing team cohesion. This can be a difficult task for diverse teams, whose members are accustomed to working in different ways. In the *work stage* of development, attention needs to be directed more towards describing and analysing the problem or task that has been assigned. This stage is often fairly easy for managers of multicultural teams, because they can draw on the diversity of the members in generating new ideas. In the *action stage*, the focus is to shift to decision making and implementation. This can be a difficult phase as it demands consensus building among members. In achieving this objective, experienced managers work to help the diverse group recognise and facilitate the creation of ideas with which anybody can agree.

Fig.2.3 outlines seven specific spheres of activity that together help manage diversity more effectively.

Need to Maintain Good Corporate Citizenship

An MNC will be successful if only it creates and sustains the image of a good corporate citizenship as reflected in honesty and social responsiveness

As MNCs disperse their activities worldwide, they become highly visible and are required to operate under diverse compulsions such as cultural, political, economic and legal factors of different host countries. An international business will be successful if only it creates and sustains the image of a good corporate citizenship-the two hall marks of which are honesty and social responsiveness. Quite often, MNCs confront issues and conflicts of the type described below.

It was on December 2, 1984 that disaster struck residents of Bhopal. Deadly methyl isocyanite (MIC) leaked from the pesticide plant of Union Carbide killing 4000 in the night of December 2, and crippling for life more than 100,000 people.

The people of Bhopal are yet to get an answer as to why the Union Carbide Corporation set up an outmoded plant in Bhopal when they had already developed an advanced computerised safety system for their West Virginia plant in the U.S. The refrigeration system was faulty; the valve lines and vent lines in the Bhopal plant were old and worn out. Parts that should have been replaced had not been changed for more than two years.

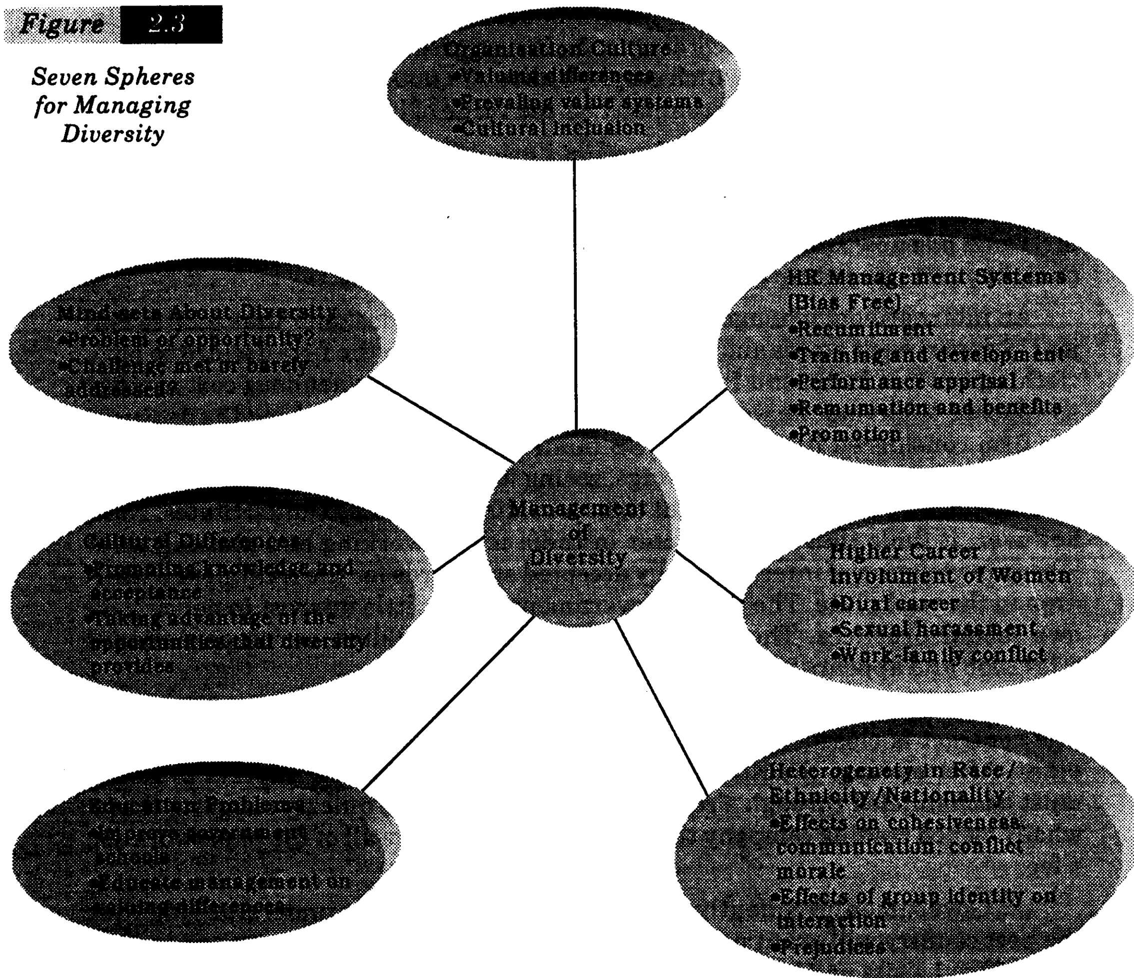

Figure 2.3

Seven Spheres for Managing Diversity

(**Source**: Stoner, et al., *Management*, p.199).

Though the accused in the criminal case linked to the Carbide disaster are facing the charge of "causing death not amounting to murder", citizens and activist groups continue to hold the multinational corporation guilty of "mass homicide" because, even though it was aware of the hazards of MIC and took safety precautions in its West Virginia plant, it did not take adequate steps here.

People here still want to know why the Government of India and the Government of Madhya Pradesh did not care to get adequate information about the hazardous nature of MIC and permitted Union Carbide to use such a deadly and lethal gas within city limits and store it in such huge quantities. At the time of the leak, more than 30,000 gallons of MIC had been stored. In contrast, the storage capacity in the West Virginia Plant was not more than 5000 gallons.

The Milan magistrates are now investigating Europe's 'biggest and spectacular' corporate scandal, where equivalent of some Rs.25,000 crores to Rs.50,000

crores cash assets in euros, have 'just vanished' from the company's Cayman Island (tax haven) accounts. According to the investigating Magistrates, the founder of the Parmalat Company, which employs about 39,000 staff, himself 'instigated fraud plan' which has led the company on the verge of bankruptcy.

The Italian authorities investigating Parmlat's slide into bankruptcy have accused Calisto Tanzi, its founder, of instigating a complex chain of financial schemes that has brought the huge dairy and food chain giant crushing down. Mr.Tanzi has now admitted misappropriating about euro 500 million over seven or eight years, according to Italian investigating authorities.

An international manager represents a US apparel designer that sells to major US department stores and retailers. Several years ago the firm decided to have clothing sewn in India and Pakistan, which resulted in tremendous cost savings as opposed to having the work done in the United States. In making the decision, the firm considered its impact on US families who depend on the income from these jobs. It opted for the cost savings, seeing its responsibility to produce a profit for shareholders as more important than providing jobs in the United States. Now, however, it finds that its contractor in India is overworking and abusing child labour in violation of internationally accepted standards for the treatment of children in the workplace. The Indian government shows little interest in policing its own labour practices. The sad story of the Indian children is run on national television and appears in the national press.

A firm enters into a contract to sell drilling equipment to a Korean company. The contract is closed while the Korean company president is visiting the US plant. After closing, the Korean executive points out that all imports to Korea must be channeled through a registered "local agent." He quickly suggests that a wholly owned trading company that be owns could handle all of the paperwork-for a fee.

US Government frequently gives aid as a bribe, with an understanding that the host country will grant political concessions in return. Governments use high level official visits and lobby aggressively for their home-based companies to help them gain foreign business. For example, US Government has paid for ministry heads to visit the United States when a U.S.Company is bidding or a contract, and has given scholarships to family members of officials that can provide business to US companies.

We will consider ethical dilemmas and issues relating to socially responsive actions later in this book.

The challenges of international business described above are daunting nodoubt. But the international managers are facing the challenges and are quite successful in their businesses. Successful global business managers adopt certain strategies, described in box 2.9 for their success.

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Box 2.9

Keys to Success

Know the Customer: The successful manager has detailed knowledge of what different international customers want and ensures that the company is flexible enough to customize products to meet those needs.

Emphasize Global Awareness: Good global managers ensure that the company designs and builds products and services for export from the beginning, not as an afterthought following the conquest of domestic markets.

Market a World-Class Product: Successful managers insist on high-quality products; they know that customers everywhere demand reliability.

Give Workers a Stake in the Company: The best global companies provide special incentives for employees who perform well.

Know How to Analyze Problems: Successful managers rarely start out with solutions. Instead, they tackle problems one piece at a time by experimenting and taking risks as necessary.

Understand Technology: The best managers find ways to match technology with the customer's environment. They do not, for example, make changes out of love for technology but will build new product lines using new and cheaper material when it becomes available.

Keep an Eye on Exchange Rates: The increasing popularity of using exchange rates to control trade means that global managers must constantly deal with shifts in currency values. In short, they must understand how exchange rates function.

QUESTIONS

1. Bring out the nature and causes for globalisation of industry.
2. What is an MNC. Name some Indian MNCs?
3. Bring out the benefits and limitations of MNCs.
4. Why is there strong opposition to the entry of MNCs into our country?
5. Bring out the impact of globalisation on culture.
6. Why do companies go international?
7. Bring out the challenges of globalisation.

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CHAPTER 3

Strategies for Going Global

CHAPTER OUTLINE

Strategies in Globalisation

- *Deciding whether to go global*
- *Deciding which markets to enter*
- *Deciding how to enter the market*
- *Learning to handle differences*
- *Adjusting the management process*
- *Selecting a managerial approach*
- *Deciding organisation structure.*

LEARNING OBJECTIVES

After reading this Chapter, you should be able to:

1. *Answer whether or not a company should go global*
2. *Determine which markets the company should enter*
3. *Deciding how the company should enter*
4. *Suggest ways of handling cultural and other differences*
5. *Select a managerial approach to manage an MNC*
6. *Design a suitable organisation structure for an MNC*

The previous chapter provided the theoretical backdrop to globalisation. Globalisation has come to stay. The issue before any businessperson is not whether or not to global but how to go about it. This chapter is devoted to a brief discussion of the strategies for going global.

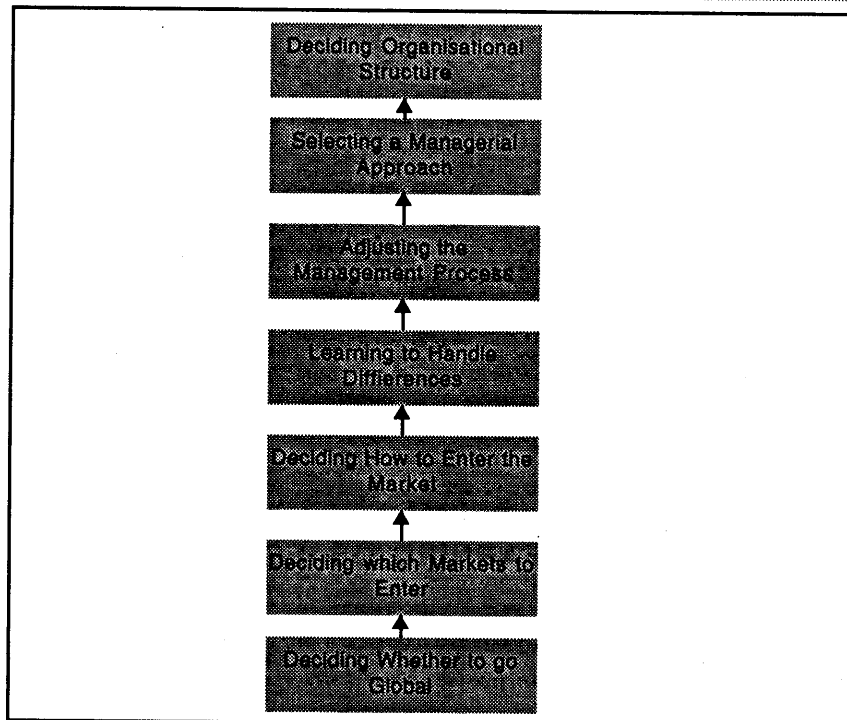
STRATEGIES IN GLOBALISATION

Globalisation involves decision-making on the following lines: (see also Fig. 3.1)

- Deciding whether to go global.
- Deciding which markets to enter.
- Deciding how to enter the market.
- Learning to handle differences.
- Adjusting the management process.
- Selecting a managerial approach.
- Deciding organization structure.

Figure 3.1

Globalisation Strategies



Deciding whether to go global

As stated above, globalisation has come to stay. Every manufacturer, whether producing tooth powder, herbal products, or software, is planning to take his products beyond the Indian shores. Open the newspaper or periodicals, you find profiles of companies fully illustrating joint venture deals with foreign companies or foreign investments flowing into power, roads and other infrastructural areas.

However, theoretically, it may be argued that deciding whether or not to go global is a difficult job, particularly when domestic market is vast as it is the case with our

country. For a long time, our businessperson enjoyed a sheltered and vast market where they could sell whatever they produced. But today's environment is different. Technological innovations, crumbling trade barriers, global flow of capital, revolution in the information technology, intensity of market competition, changing lifestyles and demand for new products are making internationalisation inevitable.

Local companies need to think about local markets.

However, not all companies need to go global. Local businesses, for example, do well to concentrate on local markets. Companies that operate in global industries,* on the other hand, must think and act globally. Thus, IBM must organize globally if it is to gain purchasing, manufacturing, financial and marketing advantages. Companies in the global industry must compete on a worldwide basis if they should succeed.

Before going international, the company must weigh several risks and answer many questions about its ability to operate globally. Can the company learn to understand the preferences and buying behavior of consumers in other countries? Can it offer competitively with foreign nationals? Do the company's managers have the necessary international experience? Has the management considered the impact of foreign regulations and political environments?

Because of the risks and difficulties of entering foreign markets, most companies do not act until some situation or event thrusts them into the global scene. Someone - a domestic exporter, a foreign importer, a foreign government - asks the company to sell abroad and the company is saddled with overcapacity, then it becomes important that the former must find additional markets for its goods.[1]

Deciding which markets to enter

This involves deciding on-

(i) volume of foreign sales,

(ii) number of countries to market in, and

(iii) the types of countries to enter.

Most companies start small when they go abroad. Some plan to stay small, viewing foreign sales as a small part of their business. Other companies have bigger plans, seeing foreign business as equal or even more important than their home business.

There is temptation for a company to spread its wings in as many countries as possible, but it makes better sense to operate in a fewer countries with a deeper market penetration in each.

The types of countries to enter depend on the type of product, geographical factors, income and population, political climate and other related factors (see Fig.3.2). It is advisable to rank the countries on specific factors. The goal is to determine the potential of each country. It goes without saying that the country which assures long run returns on investments must be selected for entering its market.

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*A global industry is one in which the strategic positions of competitors in given geographic or national markets are affected by their overall global positions.

Figure 3.2

Indicators of Market Potential

1. **Demographic Characteristics**
   - Size of population
   - Rate of population growth
   - Degree of urbanization
   - Population density
   - Age structure and composition of the population
2. **Geographic Characteristics**
   - Physical size of a country
   - Topographical characteristics
   - Climatic conditions
3. **Economic Factors**
   - GNP per capita
   - Income distribution
   - Rate of growth of GNP
   - Ratio of investment to GNP
4. **Technological Factors**
   - Level of technological skill
   - Existing production technology
   - Existing consumption technology
   - Education levels
5. **Socio-cultural Factors**
   - Dominant values
   - Life style patterns
   - Ethnic groups
   - Linguistic fragmentation
6. **National goals and plans**
   - Industry priorities
   - Infrastructure investment plans.

International businesses generally make political risk assessment before foraying into any foreign market.

Political risk is any governmental action or politically oriented event that could adversely affect fortunes of a company

Political Risk: Political risk is any governmental action or politically motivated event that could adversely affect the long-run profitability or value of a firm.[2] Political risk affects different firms in different ways. It can threaten the market of an exporter, the production facilities of a manufacturer, or the ability of a firm to repatriate its profits from a host country to its home country. Table 3.1 contains examples of political risks.

Political risk varies from nation to nation. It is very high in countries like Yugoslavia, Afghanistan, Turkey, Iraq, Algeria, Sudan, Nigeria,Somalia, Congo, Angola, Myanmar and Indonesia. Political risk is almost non-existent in the US, Canada, Denmark, Australia and Western European countries.

Distinction is often made between macro and micro risks. A macro political risk affects all international businesses in the same way. Expropriation, the seizure of assets by government with little or no compensation to the owners, is a macropolitical risk. Communist governments in Eastern Europe and China expropriated private firms following World War II. Fidel Castro did the same in Quba from 1958 to 1959. Recently, governments in Angola, Chile, Ethiopia, Peru, and Zambia have expropriated private firms. In all these cases international businesses were hard hit.

Table **3.1**

Examples of Political Risks and their Impact on International Business

Risks	*Impact*
(A) Macro Risks	
(i) Expropriation of corporate assets without prompt and adequate compensation	Loss of future profits
(ii) Barriers to repatriation of profits	No motivation to improve efficiency
(iii) Confiscation of properties	Loss of assets and future profits
(iv) Loss of technology or other intellectual property	Loss of future profits
(v) Compaigns against foreign goods	Loss of sales and increased costs of public relations campaigns
(vi) Mandatory labour legislations	Increased operating costs
(vii) Civil wars	Destruction of property, loss of sales, increased security cost, disrupted production runs
(viii) Inflation	Increased operating costs
(ix) Currency devaluations	Reduced values of repatriated earnings
(B) Micro Risks	
(i) Kidnappings, terrorist threats, etc.	Disrupted production, higher security costs, reduced productivity
(ii) Increased taxation	Reduced after tax profits
(iii) Officials' dishonesty	Loss of business, increased operating costs

Political boycotts also result in macropolitical risk. Since 1955, a number of Arab countries have boycotted firms with branches in Israel or companies that have allowed the use of their trade name there. Macropolitical risk can also come about because of indigenisation laws which bind international businesses accept equity participation by local citizens.[3]

Macro political risk has been changing in recent years. For example, Eastern European countries such as Poland, Hungary, and the Czech Republic are now inviting private investment, as does Russia. China's entry into WTO is a pointer to the changing environment in Asia. Vietnam's secret trade agreement with the US is another positive indicator. All these developments have certainly minimised the political risk but the risk continues to exist.

A micro political risk affects specific foreign businesses. Micro political risks include industry regulations, taxes, kidnapping and terrorist threats.

India's decision in 1975 to reduce foreign equity to 40% is a micro political risk

India's decision in 1975 to reduce foreign equity to 40 per cent and Peru's decision to nationalise its copper mines are examples of micro political risks. The US decision to tax textile imports is another instance. Yet another example is the bombing of Chinese embassy in Belgrade by NATO forces in 1997. In retaliation demonstrators in China trashed KFC stores but did not touch Pizza Hut stores though both were owned by a US based company. Chinese protestores did not attack Pizza Hut Stores thinking that it was Italian-owned.

Firms which have high visibility in host countries are targets of micro political risk. If agitation's cause is animosity between factories in the host country and the government of a foreign country, agitators may target only the most visible companies from that foreign country, like KFC.

Political Risk Assessment: International businesses must conduct some form of political risk assessment to manage risks. Typically, managers in host countries assess the potentially destabilising issues and evaluate their future impact on the firm, making suggestions for handling problems. Top management at head office then will establish guidelines for each host country managers to solve such problems.

Political risk assessment is made either by developing inhouse capabilities or by retaining the services of consultants

Risk assessment by international businesses usually takes two forms. One is through the use of experts or consultants familiar with the host country or region under consideration. Such consultants, advisers, and committees usually monitor important indicators that may portend political change. They then assess the likelihood of political change and develop several scenarios to describe alternative political conditions in the future.

A second and increasingly common means of political risk assessment used by international businesses is through the development of their internal staff and in-house capabilities. This type of assessment may be accomplished by having staff assigned to foreign subsidiaries or affiliates monitor local political activities or by hiring people with expertise in the political and economic conditions in regions critical to the firm's operations.

Whatever the method, timely information from the people on the front line should not be missed. Experts or consultants are no substitute for the line managers in the foreign subsidiaries, many of whom are host country nationals. These managers represent the most important resource for current information on the political environment and how it might affect their firm because they are uniquely situated at the meeting point of the firm and the host country. Prudent international businesses, however, weigh the subjectivity of these managers' assessments and also realise that similar events will have different effects from one country to another.[4]

Entry Strategies

Once the company has decided to go global, it must decide on the best mode of entry. The usual entry strategies are: (see also Fig. 3.3).

- Exports and imports
- Tourism and transportation
- Performance of services
- Use of assets
- Joint-ventures
- Wholly owned subsidiaries

As shown in Fig.3.3, the entry strategies are arranged in the order of their degree of presence in global markets and the extent of foreign investment.

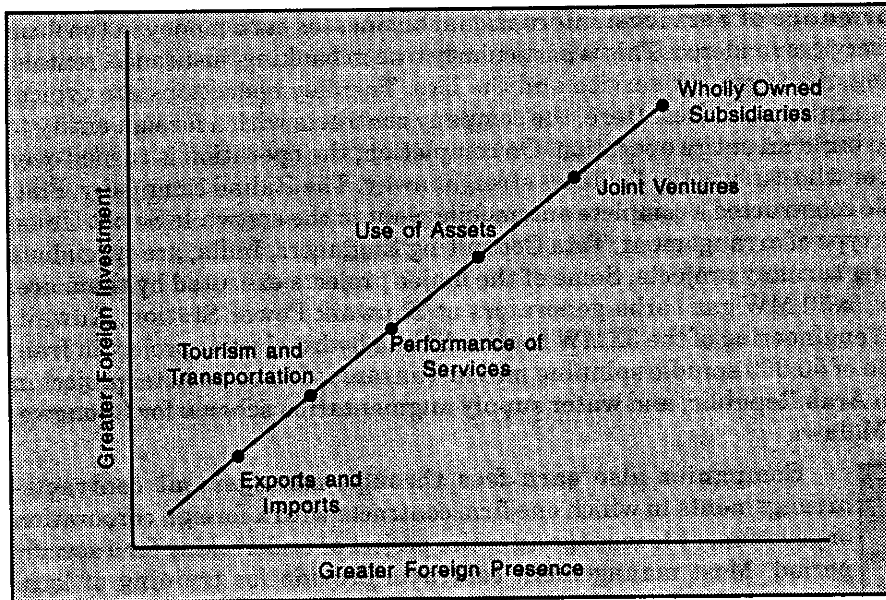


Figure 3.3 Entry Strategies

Exports or imports constitute the oldest mode of entry into a foreign market.

Exports and Imports: Exports are goods and services produced in one country but marketed in another country. Imports are goods and services produced in one country but bought by another country. Exports and imports do not take place only in tangible goods, but also include services such as those provided by international airlines, cruise lines, reservation agencies, and hotels. Infact, the trade in services is heavier than buying and selling of physical goods.

European Community (EC) is the world's single largest trading unit, followed by Asia and North America. The majority of this export and import activity is in the area of manufacturing such as industrial machinery, computers, cars, televisions, VCRs, and other electronic goods. But, as stated erlier, an increasing proportion of world trade is in services.

Though not a major player, India's presence in world business is steadily increasing. The exports from our country more than tripled from Rs.32,553 cr in 1990-91 to Rs.2,52,787 crore in 2002-2003. The country's imports also jumped from Rs.43,198 cr in 1990-91 to Rs.2,96,597 cr in 2002-2003. As a proportion of the GNP, foreign trade of India went up to 18.6 per cent as of today from 14.1 per cent from the beginning of 1990s.

Why do firms export? Reasons are not difficult to find. Expanding sales, gaining experience and building brand equity are the main reasons for firms selling goods and services in overseas markets.

Tourism and Transportation: Tourism and transportation are the routes of globalisation for such industries as shipping, airlines, hotel and travel agency. Some countries, Greece and Norway for example, depend on international tourism and transportation for employment, profits, and foreign exchange earnings. Earnings from foreign tourism are more important for the Bahamian economy than are earnings from export of merchandise. Similarly, in recent years the US has earned more from foreign tourism than from its exports of agricultural goods.

Performance of Services: International businesses earn money in the form of fees for services rendered. This is particularly true in banking, insurance, rentals, engineering, management service and the like. Turnkey operations are typical modes for earning such fees. Here, the company contracts with a foreign entity to design and build an entire operation. On completion, the operation is turned over to the owner who can use the facilities straight away. The Italian comnpany, Fiat, for example constructed a complete automobile plant in the erstwhile Soviet Union under this type of arrangement. Tata Consulting Engineers, India, are specialists in executing turnkey projects. Some of the major projects executed by them are: erection of 5x50 MW gas turbo-generators at Shuwaik Power Station, Kuwait, design and engineering of the 3XMW Derbendikhan hydro-electric project in Iran; installation of 50,000 spindle spinning mill in Tanzania; 180 room hotel project in the Yemen Arab Republic; and water supply augmentation scheme for Lilongwe, capital of Malawi.

Turnkey projects and management contracts are examples of service mode of entry into foreign markets

Companies also earn fees through management contracts-arrangements in which one firm contracts with a foreign corporation or government to manage an entire project or undertaking for a specific period. Most management contracts provide for training of local personnel who will eventually take over the management responsibilities. An example of this was Bell Canda's contract with the government of Saudi Arabia to manage the installation of modern transmission and switching equipment in Saudi Arabia's Telephone System. Similarly, under a management contract, for a ten year period (1969-1979), Citibank had lent its managerial expertise to Grindlays Bank. Disney receives management fees from managing theme parks in France and Japan.

Nearer at home, the late Aditya Birla was controlling his companies abroad through management contracts.

Licensing and franchising are examples for use of assets – one of the entry modes into foreign marekts

Use of Assets: Licensing and franchising are the modes which facilitate companies allow others to use their assets. Under a license agreement, one firm permits another to use its intellectual property for compensation called royalty. The firm that makes the offer is the licenser and the recipient firm is designated as the licensee. The property licensed generally includes such assets as patents, trade marks, copyrights, technology, technical knowhow, business skills, and the like. Licensing amounts to exporting intangibles.

Licensing has intutive appeal to many prospective global players. As a mode of globalisation, licensing requires neither capital investment nor detailed involvement with foreign customers. By generating royalty income, licensing provides an opportunity to exploit research and development already conducted. After initial costs, the licensee can reap benefits until the end of the license contract period. Licensing also reduces the risk of exproportion because the licensee is a local company that can provide leverage against government action. In recent years a number of host countries have demanded that MNCs license their assets rather than following only FDI routs.

The main disadvantage of licensing is that license fees are likely to be lower than FDI profits. Other disadvantages include:

- Possible loss of quality control
- Establishment of a potential competitor in third country markets
- Possible improvement of the technology by the local licensee, which then enters the licensor's home market
- Possible loss of opportunity to enter the licensee's market with FDI later
- Risk of technology being stolen
- High agency costs.

Multinational businesses do not typically use licensing of independent firms. On the contrary, most licensing arrangements have been with their own foreign subsidiaries or joint ventures. License fees are a way to spread the corporate research and development cost among all operating units and a means of repatriating profits in a form more acceptable to some host countries than dividends.

Another route of globalisation is **franchising**, which involves the granting of right by a parent company (the franchiser) to another (the franchisee) to do business in a prescribed manner. This right can take the form of selling the franchiser's products, using its name, production, and marketing techniques, or using its general business approach. Usually, franchising involves a combination of all these elements.

The major forms of franchising are manufacturer-retailer systems (such as a car dealership), manufacturer-wholesaler systems (such as soft drink companies) and service firm-retailer systems (such as lodging services, fast food outlets and hotel/motel industries).

Franchising is adaptable to the international arena, and with some minor adjustments for the local market, it can result in a highly profitable business. In fast foods, McDonald's Burger King, and Kentucky Fried Chicken have used franchise agreements to expand their markets from Paris to Tokyo and from Cairo to Carcas. In the hotel business, Le-Meridian among others has been very successful in gaining worldwide presence through the use of franchisees.

Franchise agreement typically requires the payment of a fee upfront and then a precentage on sales. In return, the franchiser provides assistance and, in some instances, may require the purchase of goods or supplies to ensure the same quality of goods or services worldwide.

> FDI allows the investors have a controlling interest in an overseas company. FDI can be a joint venture or a wholly owned subsidiary

Franchising can be beneficial to both the groups. It provides the franchiser with a new stream of income and the franchisee with a time proven concept and products that can be quickly brought to market.

Direct Investment: A direct investment is the one that allows the investor a controlling interest in a foreign company. Foreign direct investment (FDI) is another name for direct investment. FDI may take the form of a joint vernture or a wholly owned subsidiary.

A joint venture is a shared ownership in a foreign business. Generally, the venture is 50-50 ownership in which there are two parties, each of which holds a 50 per cent ownership stake and contributes a team of managers to share operating control. Fuji-Xerox is one of the most enduring and successful joint-ventures

between two companies of different countries. The world famous company-Rolls Royce-has 25 joint ventures across all its business activities.

There are 868 Indian joint ventures abroad, out of which 286 ventures are in operation and 582 are under different stages of implementation. The approved equity of these ventures amounts to $1097.68 million.

Indian joint ventures are predominantly in other developing countries like Malaysia, Indonesia, Singapore, Sri Lanka, Nigeria, Kenya, UAE, and Thailand. Joint ventures have been set up both by private entrepreneurs and public sector undertakings.

Indian Joint Ventures are located mainly in developing countries

In a wholly owned subsidiary, the company owns 100 per cent of the equity. At present there are 733 wholly owned Indian subsidiaries abroad, out of which 216 are in operation and 517 are at various stages of implementation. The approved equity of these subsidiaries amount to $820.59 million.

A wholly owned subsidiary can be set up in a foreign market in either of two ways. The company can set up a totally new operation or can acquire an established firm and use the firm to promote its products. The subsidiary that is established starting from the ground up (i.e. from a greenfield) is called a **greenfield investment**. Compared to green field investment, a cross-border acquisition has a number of benefits. First, acquisition is quicker than establishing a firm. Greenfield investment requires extended periods of physical construction and organisational development. By acquiring an existing firm, an international business can shorten the time required to gain a presence and facilitate competitive entry into the market. Second, acquisition may be a cost-effective way gaining competitive advantages such as technology, brand names, and logistical and distribution advantages, while simultaneously eliminating a local competitor. Third, international economic, political, and foreign exchange conditions may result in market imperfections allowing target firms to be undervalued. Many firms throughout Asia have been the target of acquisition as a result of the Asian economic crisis impact on their financial health. Many companies were in dire need of capital injections for competitive survival.

Greenfield investment involves setting up of operations newly. Such an investment is heavy and risky too.

There is the flip side to cross-border acquisitions. There is the possibility of paying too high a price. Meshing different corporate cultures can be traumatic experience. Managing the post-acquisition process is characterised by downsizing to gain economies of scale and scope in overhead functions. This results in unhealthy impacts on the firm as individuals attempt to save their own jobs. There are also difficulties arising from host governments intervening in pricing, financing, employee hiring, and nationalism and favouritism.

Direct investment, (or FDI) through joint venture or wholly owned subsidiaries, is the most preferred way of entering into foreign markets.

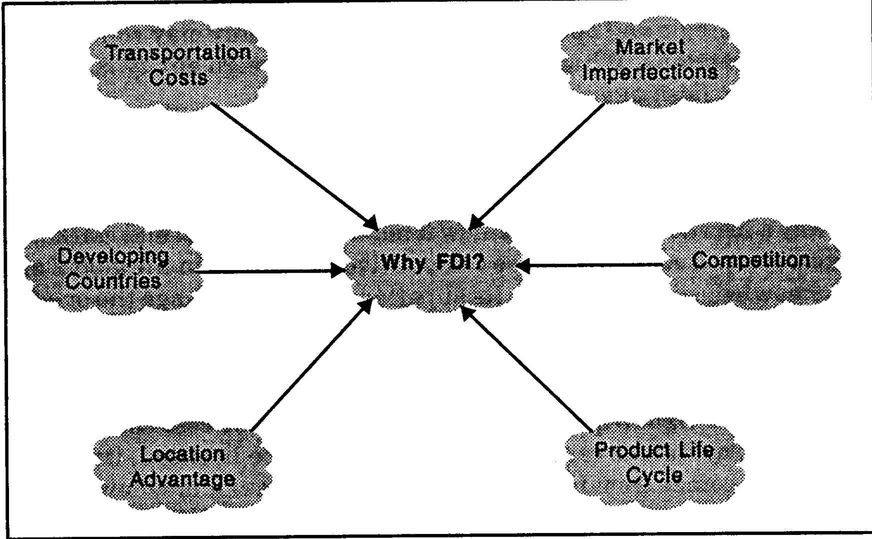
But, FDI is expensive and risky when compared to exporting and licensing. FDI is expensive because a firm must bear the costs of establishing production facilities in a foreign country or of acquiring a foreign enterprise. FDI is risky because of the problems associated with doing business in another culture where the "rules of the game" may be different. Yet, firms prefer to go all out to acquire enterprises abroad or establish subsidiaries in alien countries. Six factors explain such preference: (i) transportation costs, (ii) market imperfections, (iii) competition, (iv) product lifecycle, (5) location advantages, and (vi) developing countries.[5] (See Fig.3.4)

Though expensive and risky, yet FDI is preferred because of
(i) transportation costs
(ii) market imperfections
(iii) competition
(iv) product life cycle
(v) location
(vi) developing countries

Transportation Costs: From the transportation cost perspective, goods may be of low value to weight ratio type or the opposite, namely, high value to weight ratio type. In the former, (e.g. cement, soft drinks etc.) transportation cost is considerable and it is unprofitable to ship them over long distances. They can also be produced in almost any location. In products of this type, relative to either FDI or licensing, the attractiveness of exporting decreases. For products with a high value to weight ratio, however, transport costs are a minor component of total landed cost. Electronic components, personal computers, computer software, and the like belong to this category. In these products, transportation costs have little impact on the relative attractiveness of exporting, FDI, and licensing.

Figure 3.4

Reasons for the flow of FDI



Market Imperfections: The market imperfections theory offers a major explanation why firms prefer FDI to exporting or licensing. Alternatively called *internationalisation theory* in the literature on global business, this approach highlights two major *impediments:* barriers to exporting and barriers to the sale of know-how. These obstacles inhibit markets from working perfectly.

Barriers to exporting and barriers to the sale of knowhow prevent market perfections from happening

Impediments to the free flow of products between nations decrease the profitability of exporting, relative to FDI and licensing. Governments are the main source of impediments to the free flow of products between nations. By imposing tariffs on imported goods, governments can increase the cost of exporting relative to FDI and licensing. Similarly, by restricting imports through the imposition of quotas, governments increase the attractiveness of FDI and licensing.

Sale of know-how takes place through licensing. Impediments to the sale of know-how increase the profitability of FDI relative to licensing. Though licensing is less expensive and risky, firms do not prefer it because of three reasons. First, licensing may result in a firm giving away its know-how to a potential foreign competitor. For example, RCA Corporation licensed, in the 1960s, its leading-edge colour television technoilogy to a number of Japanese firms including Matsushita and Sony. At that time RCA saw licensing as a way to earn a good return from its technology in the Japanese market without the costs and risks associated with FDI. However, Matsushita and Sony quickly assimilated RCA's technology and used it to enter the US market to compete directly against RCA. As a result, RCA is now a minor player in its home market, while Matsushita and Sony have a much bigger market.

Secondly, licensing does not give a firm the right control over manufacturing, marketing, and strategy in a foreign country that may be required to profitably exploit its advantage in know-how. With licensing, control over production, marketing, and strategy is granted to a licensee in return for a royalty fee. However, for both strategic and operational reasons, a company may want to retain control over the functions. When tight control over a foreign entity is desirable, FDI is preferable to licensing.

Thirdly, a company's know-how itself may not be for licensing. This is particularly true of management and marketing know-how. It is one thing to license a foreign firm to manufacture a particular product, but quite another to license the way a firm does its business-how it manages its process and markets its product. Take Toyota, a company whose competitive advantage in the global auto industry is acknowledged to come from its superior ability to manage the overall process of designing, engineering, manufacturing, and selling automobiles; that is, from its management and organisational know-how. Toyota is credited with pioneering the development of a new production process, known as lean-production, that enables it to produce higher-quality automobiles at a lower cost than its global rivals. Although Toyota has certain products that can be licensed, its real competitive advantage comes from its management and process know-how, which cannot be licensed. Toyota is increasingly pursuing a strategy of FDI; moving away from its traditional exporting route.

Thus, when one or more of the following conditions prevail, markets fail as a mechanism for selling know-how and FDI is more profitable than licensing: (1) when the firm has valuable know-how that cannot be adequately protected by a licensing contract, (2) when the firm needs tight control over a foreign entity to maximise its market share and earnings in that country, and (3) when a firm's skills and know-how are not amenable to licensing.

Competition: FDI flows are often a reflection of rivalry among firms in the global market place. Assuming that three firms A, B and C dominate the market in the US (this situation is called oligopoly). Firm A established a subsidiary in France. Firms B and C reflect that if this investment is successful, it may affect adversely their export business to France and give firm A an advantage of early start. Furthermore, firm A might discover some competitive asset in France that, it could repatriate to its home country to harrow firms B and C in their native soil. Given these possibilities, firms B and C decide to follow firm A and establish operations in France.

First entry into the US by Honda then followed by Toyota and Nissan typify how competition casuses inflow of FDI into any country. As per the competition theory, firms resort to FDI when competitors do it first.

Expounded by F.T.Knickerbockers in the early 1970s, the competitors theory for FDI flow has evidence for support. For example, Honda undertook FDI in the US and Europe during the 1980s. Toyota and Nissan followed suit.

The Product Lifecycle Theory: This theory has been propounded by Raymond Vernon. Vernon argued that often the same firms that pioneer a product in their home markets undertake to produce a product for consumption in foreign markets. Thus, Xerox introduced the photocopier in the US, and it was Xerox that set up production facilities in Japan (Fuji-Xerox) and Great Britain (Rank-Xerox) to serve those markets.

Vernon's view is that firms undertake FDI at particular stages in the lifecycle of a product they have pioneered. They invest in other advanced countries when local demand in those countries grows large enough to support local production (as Xerox did). They subsequently shift production to developing countries when product standardisation and market saturation give rise to price competition and cost pressures. Investments in developing countries, where labour costs are lower, is seen as the best way to reduce costs.

Location Advantages: In addition to the various factors discussed till now, there are certain location-specific advantages that attract FDI. The location-specific advantages in particular, include natural resources such as oil and other minerals, which are by nature specific to certain locations. A firm must undertake FDI to exploit such endowments. This explains the FDI undertaken by many of the world's oil companies, which have to invest where oil is located. Another example is the valuable human resource, such as low-cost highly skilled labour force. The cost and skill of labour varies from country to country. A Canadian medium-sized plant is thinking in terms of renovating a plant near Warsaw in Poland as the price of labour in that country is fairly low. Other nearby countries have lower wage rates, but Warsaw, the company's specific choice, has a cadre of well trained factory workers who could be transferred to the renovated factory. Similarly, one major benefit of locating plants in Mexico is the highly skilled labour force that can be hired at fairly low wage rates. Additionally, manufacturing firms located in Mexico report high productivity growth rates and quality performance. France has been the target of much MNC activity. Daimler-Chrysler has recently built a new factory in France because of its faith in the workers' productivity and work ethic. Additionally, France's recent economic growth has impressed many MNCs.

Apart from theories, strong reasons why FDI flows into any country are location-specific. Some regions are endowed with rich resources which attract FDI

Hyundai, the automobile giant from South Korea, has chosen Chennai in India for its new car manufacturing plant. Skilled labour at low wages; location of auto parts manufacturers such as Wheels India, Brakes India, Sundaram Fasteners, Sundaram Brakes, Bimetal Bearings, Tafe, and India Pistons in and around Chennai; guaranteed power supply; cheap land and proximity to sea port have attracted the plant to the capital city of Tamil Nadu.

The argument that location-specific advantages attract FDI is propounded by the British economist John Dunning. Dunning believes that market imperfections make licensing and exporting difficult and thereby rendering FDI an obvious choice to globalisation.

FDI and Developing Countries: A developing country is characterised by low savings, low capital formation, and low investment. Such a country obviously looks for an external source to fill its resource gap.

In addition to the resource-gap, a developing country suffers from lack of advanced technology. As is well known, FDI brings, along with it, technology to the developing country. Besides, a developing country often needs to import rawmaterials that are not available domestically. The country needs foreign currency to pay for imports. FDI is of great help to the country in this respect.

FDI helps a developing country in another way also. When any MNC sets up its subsidiary in a developing country, along with capital and technology the parent company transfers its work culture, managerial concepts and skills, to the foreign affiliate (See Box 3.1 for an illustration). The recipient country benefits immensely from such transfer of managerial skills.

Box 3.1

Toyota's 'Milk Run'

For many years after it was founded in 1937, Toyota was derided as a company made up of "a bunch of farmers". Reason? It hired a lot of farmers to work its assembly lines and, in fact, the founding family's name Toyota meant "abundant rice field" in Japanese (the word Toyota, however, has no meaning in that language). Over the six decades, Toyota has come to acquire the most fearsome reputation in the industry for its exemplary manufacturing system, where costs and inefficiencies are pared not just every day, but every second.

Take a look at its low-fat Bidadi operations: the maximum amount of raw material at the factory at any point of time does not exceed two hour's production requirement; all finished cars leave the factory within 48 hours, and no dealer is sent more than 15 day's stock. So, just how does Toyota do it? The trick lies in its famous 'milk run', which involves picking up small quantities of supplies from vendors throughout the day. This is how it works: every morning small trucks leave a central stocking point (there is one each in Pune, Delhi, and Chennai), picking up supplies from the local vendors. These trucks then return to the hub, where the supplies are transferred to a bigger truck, which leaves for Toyota Plant at Bidadi every day. For vendors based in and around Bangalore, the milk runs are straight from the plant to the vendor and back.

(***Source:*** *Business Today*, October 28, 2001.)

Flow of FDI

FDI flows in all directions in the globe as Table 3.2 shows. Strictly speaking, developing countries should get major share of FDI inflow as these are the nations who are in need of foreign capital. But this is not happening as Table 3.2 shows. During 2002, for example, out of a total inflow of $651.2 billion, developed countries received 71 per cent ($460.3 billion) and the remaining 29 per cent ($162.1 billion) went to developing economies. India's share in the total inflow is negligible. The country received just $3.4 billion in 2002. The next chapter throws more light on the reasons why India is a poor cousin in terms of the receipt of FDI.

Table **3.2**

FDI Inflows to Major Economies, 2001 and 2002

(Billions of dollars)

Host Region / Economy	*2001*	*2002*
World	823.8	**651.2**
Developed countries	589.4	460.3
European Union	389.4	**374.4**
France	55.2	51.5
Germany	33.9	38.0
Luxembourg	..	125.6
United Kingdom	62.0	24.9
United States	144.0	30.0
Developing Economies	209.4	**162.1**
Africa	18.8	11.0
Algeria	1.2	1.1
Angola	2.1	1.3
Nigeria	1.1	1.3
South Africa	6.8	0.8
Latin America and the Caribbean	83.7	**56.0**
Argentina	3.2	1.0
Brazil	22.5	16.6
Mexico	25.3	13.6
Asia and the Pacific	106.9	**95.1**
China	46.8	52.7
Hong Kong, China	23.8	13.7
India	3.4	3.4
Korea, Republic of	3.5	2.0
Malaysia	0.6	3.2
Philippines	1.0	1.1
Singapore	10.9	7.7
Taiwan Province of China	4.1	1.4
Thailand	3.8	1.1
Central and Eastern Europe	25.0	**28.7**
Czech Republic	5.6	9.3
Poland	5.7	4.1
Russian Federation	2.5	2.4

(***Source:*** *World Investment Report*, 2003, p.7)

Learning to handle differences

Another stage in evolving a global strategy is learning to handle differences that persist across countries. Differences are often difficult to perceive but careful observation yields dividends in the form of new opportunities and new ways of reducing risks.

Economists are being employed by Indian companies also. The Tata Group has six economists, Mahindra and Mahindra two, DHL one and Aditya Birla Group two

MNCs must forecast economic conditions in the countries they operate. Large companies have their own staff of economists; smaller ones tend to rely on the general knowledge of non-specialised line managers and on forecasts supplied by private companies, agencies, governments and banks.

One of the most important things an MNC must know about any country where it does business is the exchange rate between its currency and the currency of other nations. Fluctuations in exchange rates will benefit or affect the fortunes of the MNC.

Political environment varies across countries. Two distinct political environments exist in the world — democracy and totalitarianism. Democracies provide stable business environments through laws protecting individual property rights. Totalitarian or authoritaranian regimes are marked by corruption, coups and bloodbaths. The international manager needs to study the political environment obtaining in the host country and modify the strategies to shift the local needs.

More pronounced are the cultural differences existing across the globe. Food habits, buying habits, languages, communication systems, body languages, gift-giving and negotiation systems vary from country to country. No product can be sold in the standardised form to all the buyers; no ad can be designed and exhibited in the same way in all the media of the world; no good can be packaged with similar colours and displayed in the retail stores of all countries; and no international manager can use same body language, and nuanas while sitting across a table to negotiate with an Arab, a Japanese, a Korean, or an Indian businessman. In general, international managers are successful when they employ the following six strategies:[6]

1. Managers see themselves as citizens of the world and not belonging to one country.
2. Managers develop integrated and innovative strategies that make it difficult and costly for others to replicate.
3. Managers implement their strategies aggressively and effectively supported by huge investments from their eemployers.
4. Managers are aware of the fact that the developed countries alone are not the countries of excellence fit enough to come out with innovations in technologies. What is a poor country today can become a potential candidate to attract R&D establishments as has been recently proved in India.
5. Managers develop a system that keeps them informed about political changes around the world and implications of these changes on the firm.
6. Managers seek to achieve culture strategy fit while strategising their activities.

Adjusting the management process

Management process, as is well known, involves planning, organising, staffing and controlling. Now, this process needs to be different for an MNC operating in an international environment (see Table 3.3).

Table 3.3

Managing Domestic and International Businesses

	Domestic enterprise (industrialized country)	*International enterprise*
Planning: Scanning the environment for threats and opportunities	National market	Worldwide market
Organising: 1. Organisation sturcture	Structure for domestic operations	Global structure
2. View of authority	Similar	Different
Staffing: 1. Sources of managerial talent	National labour pool	Worldwide labour pool
2. Manager orientation	Often ethnocentric	Geocentric
Leading: 1. Leadership and motivation	Influenced by similar culture	Influenced by divergent cultures
2. Communication lines	Relatively short	Network with long distances
Controlling: Reporting system	Similar requirements	Many different requirements

(**Source**: Heinz Weihrich, et al, *Management-A Global Perspective*, McGraw-Hill, 1994, p.94).

Managerial actions both at the macro level and micro level need to be oriented differently. At the macro-level, issues generally involved are - What special steps are needed in the planning and control systems of MNCs? Should organisations be structured and co-ordinated differently in different countries? How to recruit people and compensate them adequately? Should the performance appraisal system differ from country to country?

Management process at macro and micro levels needs to be oriented differently

At the micro-level, the decisions involved are: How should one individual interact with another from a different country? Should people in one country be managed differently from people in another country?

The thrust in adjusting the management process is to motivate people to think and act globally.

Selecting a managerial approach

What must be the appropriate managerial practices suitable for an MNC? For a long time, the popular belief was that the West European – American approach was ideal for any company, including a multi-national. Then came the Japanese management about which no manager or consultant stopped talking about. Which of these approaches is suitable for an MNC? Before answering this question, it is useful to know what these approaches specifically mean.

William Ouchi has contrasted Japanese organizations with American ones as shown in Fig.3.5. The contrast is, however, based on human resource management practices.

As seen from Fig.3.5, the American approach is highly individualistic in spirit and action and this may not suit the less developed countries where collectivism and not individualism, is the main trait. Western managerial practices likewise have individualistic orientation.

Figure 3.5

The Contrast

Japanese Organizations	Vs	American Organizations
Life time employment		Short term employment
Slow evaluation and promotion		Rapid evaluation and promotion
Non-specialised career paths		Specialised career paths
Implicit control mechanisms		Explicit control mechanisms
Collective decision making		Individual decision making
Collective responsibility		Individual responsibility
Holistic concern		Segmented concern

(***Source***: William Ouchi, *"Theory Z"*, p.58)

What is needed for an MNC then is the synthesis of the American and Japanese approaches. Infact, the most successful American and Japanese companies follow identical practices which are the result of fusion between the two approaches.

Fig 3.5 outlines management approaches unique to Japanese companies and American organisations. Do Indian companies have an approach of their own?

The answer is in the affirmative. Following features are common to most Indian businesses.

- Most decisions are made not by professional managers, but by family members.
- Most executives are second generation entrepreneurs — sons of fathers — known for extravagance, and flamboyance. If their businesses have been successful, it is mainly because of the general environment prevailing in the country till 1990s. It is doubtful whether these abrasive individuals will be successful in the emerging environment.
- Siblings quarrel for shares in the fortunes. Personal ambitions are more important than the fortunes of the organisations built up by their parents.
- Most decisions are made by intution or on the advise of astrologers, palmists or *vastu* consultants.

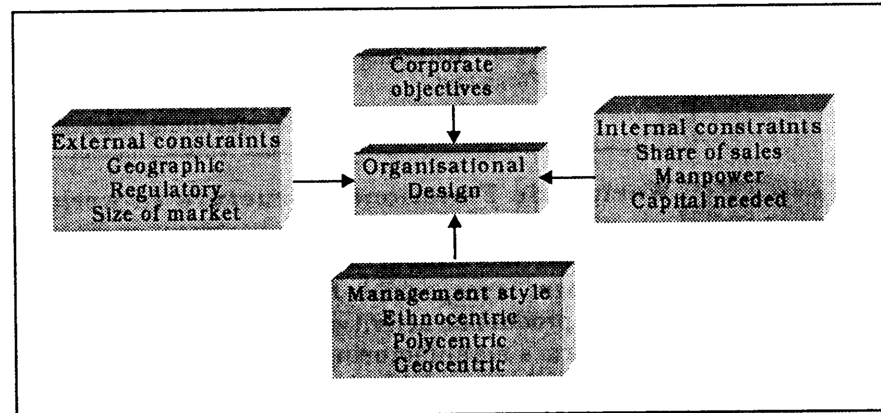
Deciding an organisation structure

Efficient operation of an MNC requires an effective organisational structure. A successful organisation should maintain smooth operating internal communication and control, as well as sensitive and flexible interaction with the dynamics of the international business environment.

Several factors affect organisational design of an MNC. They can be classified as corporate objectives, management style, external constraints and internal constraints as shown in Fig.3.6.

Figure **3.6**

Factors Affecting Organisational Structure



Ethnoculture management style expects centralisation in decision making. Polycentricism allows the opposite of ethnocentricsm. In geocentric organisations tend to become cosmopolitian

Management style can affect organisational design profoundly. The ethnocentric management style is characterised by strong control by the parent company. Its organisational structure reflects strong centralisation in decision making, and most of its managerial personnel are home country nationals. Polycentric management allows decentralisation of authority and decision making. Management personnel in foreign subsidiaries are largely of the host nationalities. In geocentric management, the organisational design is cosmopolitan, with little concentration of decision making and personnel in any particular nationality. The characteristics of these management styles are relevant not only in organisational design, but also in marketing, production, finance, personnel, control and business strategy.[7]

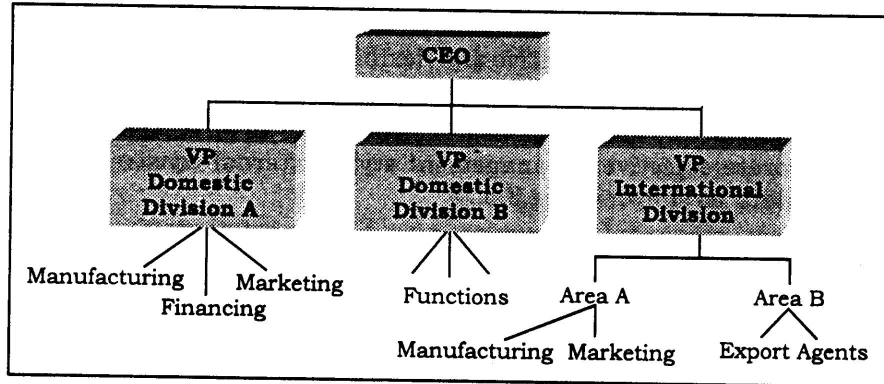
An MNC can adopt any of the six fundamental structures. These are international division structure, worldwide functional organisation, geographic area organisation, product organisation, mixed organisation and matrix organisation.[8]

International Division Structure In the international division structure, the overseas unit is an adjunct to the domestic business. It handles all the international activities, which may be organized by function, product or geographic area. All of the overseas subsidiaries are under the authority of the international division Vice-President who coordinates the entire foreign operation. As the international activities are under one head, control and communication are easy. The structure can also respond quickly to changes in the international business environment. As overseas opera-

tions expand and deversif•ty, this structure fails to cope with the new demands. Fig.3.7 illustrates the international division structure.

Figure 3.7

International Devision Structure

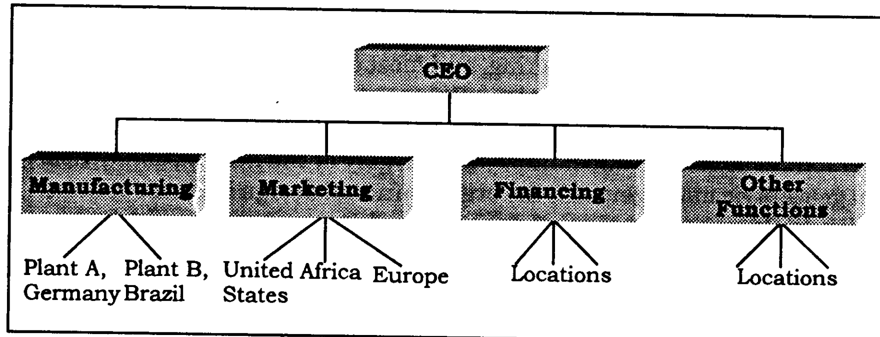


In worldwide functional structure, each department is responsible for its activities around the world.

Worldwide Functional Structure In worldwide functional organisation, each functional department or division is responsible for its activities around the world. For example, the manufacturing department is responsible for world-wide manufacturing activities. It plans production activities according to the needs and capabilities of the firm's manufacturing locations. Since each functional area deals with the global market, specialisation and concentration of functional expertise can be taken advantage of. Control of various functions can be accomplished relatively easily (see Fig.3.8).

Figure 3.8

Worldwide Functional Organisation



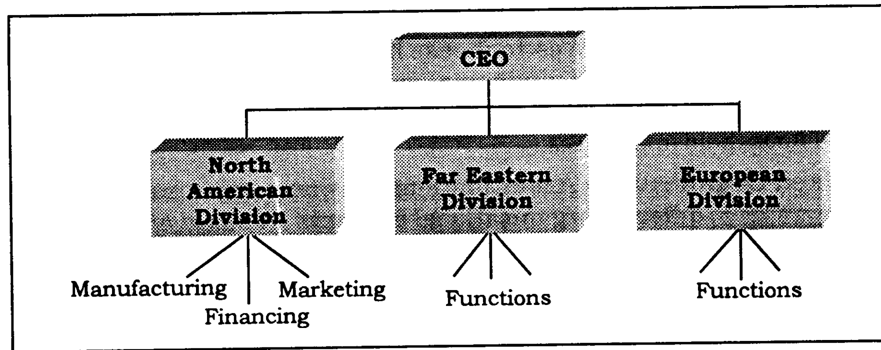
In this structure, each functional unit is responsible for its own worldwide operations and profitability. Communication among finance, marketing and manufacturing departments may become difficult since each department may have its operations in different foreign locations. Similarly, the mobility of expert managers or specialists within the company can be hindered because each of these people may be highly specialised only in the department or at one location.

Geographic area structure involves organisaiton of worldwide activities by spliting the globe into different geographic areas.

Geographic Area Structure According to geographic area organisation, worldwide activities are organised by dividing the globe into different geographic areas. The regional manager or Vice-President of each area is responsible for all business activities within that geographical area (see Fig.3.9).

Figure 3.9

Geographic Area Organisation

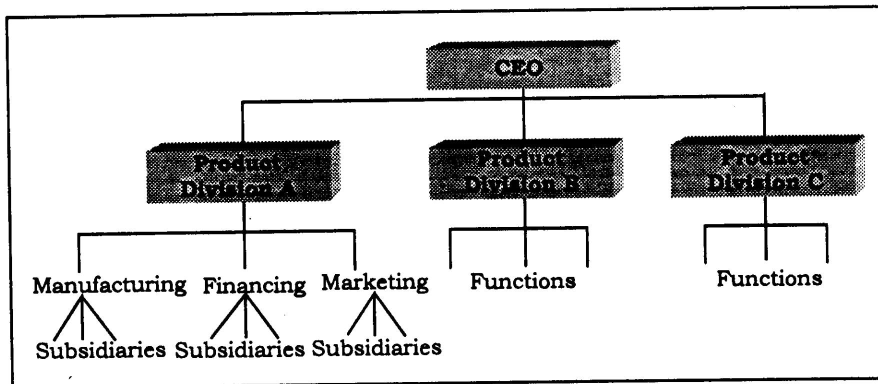


A geographic division can respond to the market conditions of a particular area much more efficiently than any other organisational structure. However, since there are different divisions covering different areas, there may be duplication of functions. There is also the problem or lack of communication among divisions. Since each division retains some degree of autonomy, each may abrogate its co-operation and co-ordination in production, marketing and other functions.

Product Organisation In product organisation, the company is divided into product divisions, as shown in Fig.3.10. Each product division has its own Vice-President or manager who is responsible for all functional departments, such as exporting, manufacturing, marketing and finance.

Figure 3.10

Product Organisation



In this organisation, the company responds to the market conditions in terms of product lines. For example, a tractor manufacturing company can alter the production and marketing of the agricultural machinery to cope with the increasing need in that market segment. In the international market, however, this type of organisation may not be efficient since each product division has its own international subdivisions. By breaking production, marketing, sales, and other functional activities into different product divisions, international activities can be seriously disintegrated, especially in the areas of coordination and control. Another problem is that a product manager, although expert in technical and production aspects, may have insufficient knowledge of and experience with international structure. Air France, Pan American and other international airlines have diversified into passenger airlines

> In product structure, the company is divided into product divisions. Each division is headed by a manager who is responsible for all functional departments

divisions, cargo divisions, hotel divisions and so on. Large manufacturing firms such as Siemens and Westinghouse have successfully organised their activities into different product divisions, including industrial machinery, transport equipment, telecommunication equipment, electrical power generation equipment and household appliances.

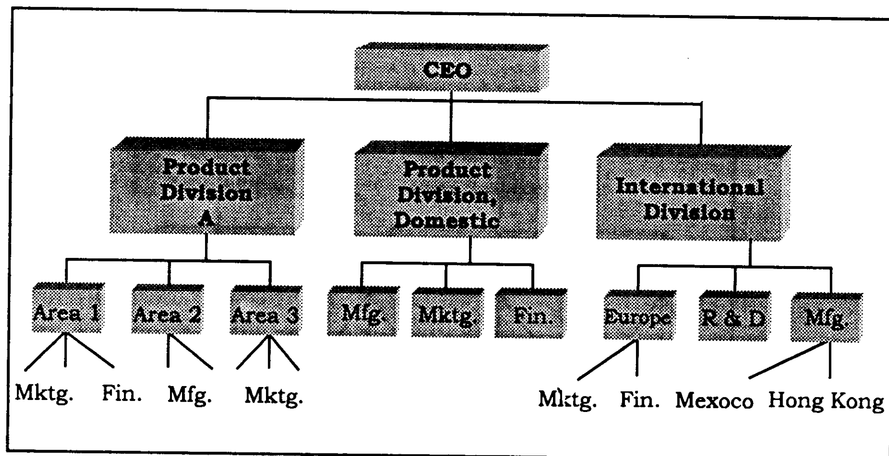
Mixed Organisation A multinational business organisation can be composed of different organisational elements. A mixed organisation can combine the structures of function, product and geographic formats. Such an organisation allows geographic flexibility, quick response to market conditions and functional efficiency.

Mixed organisation combines structures of functions, product and geographic formats. Uniliver is one example of an MNC which uses mixed structure

A firm can combine product organisation and international divisions, as shown in Figure 3.11. For example, the tractor manufacturing company mentioned previously might have two domestic product divisions, a construction machinery division, an agricultural tractor division, an international division for all products with functional departments and a separate agricultural machinery division for each of two large geographic regions such as Europe and Asia. A multinational manufacturer of household appliances such as Phillips Electric and Sanyo, with subsidiaries in many foreign countries could use a mixed structure to meet the specific conditions of each of its foreign markets and to maximise the firm's operational and distribution capabilities.

Figure 3.11

Mixed Organisation



Indeed, Uniliver PLC, the consumer products giant uses mixed structures. It uses a classic regional structure with local managers in three areas of the world: Africa/Middle East, Latin America and East Asia/Pacific. But in Europe and North America, where consumer preferences are more similar, the structure is different. The President of Lever Brothers Co. in New York, for example, reports to the Uniliver worldwide detergents-products coordinator in London.

Matrix Organisation A mixed organisation is just one form of matrix organisation. A matrix structure can be organised by combining regions, products

Figure 3.12

Matrix Organisation

	Region 1	Region 2	Region 3
Project A	Functions	Functions	Functions
Project B			
Project C			

Martrix structure involves overlying one structure on another – a totally differentstructure. In matrix structure subordinates report to matrix bosses and matrix bosses share subordinates

and functions. In the organisation shown in Figure 3.12, for example, the product A division in geographic region 1 has different functions, such as manufacturing, marketing, financing and so on. The matrix structure is flexible and responsive to the changing market needs. Matrix organisations are often utilised by high technology firms, turnkey firms and construction firms, including TRW, Bechtel, NEC and Siemens.

Need for Newer Models

The organisational structures discussed till now seem to fail to meet the requirements of contemporary global businesses. Thanks to advanced information technology, global managers sitting thousands of kilometers apart can interact and discuss face to face through effective communication networks. One of the biggest impacts of information technology is on the structural parameters of the corporation, as more and more areas of bureaucratic functions get automated and low-wage jobs get eliminated, and as the corporation becomes more skill-dominated and knowledge-oriented. The result of information technology is remarkable on the organisation of communication channels, flow of authority and decision-making inside and outside the corporation. The need for instantaneous and real-time decision-making means that the traditional ways of defining and designing an organisation's structure is no longer appropriate or even relevant.[9] For the maximized leveraging of organisational resources, newer models are necessary.

The suggested models for MNCs are:

- Each firm must create a *chain of networks* of different technological orders and magnitudes. There is also a realisation that employees need an open, non-hierarchical and participation-encouraging organisational structure which empowers them to decide and act. A network is a partnership of a group of firms (or employees) sharing common concerns and values.

  Dynamic networked partnerships are visualised as a low-cost alternative structure for achieving global excellence. Its characteristic feature is that unlike the known traditional terms, organisations here have full flexibility in changing their relationships to adjust themselves to the changes in the environment.

- Acquisition of smaller corporations/firms having an entrepreneurial spirit. The owner-manager may be allowed to function as an entrepreneur, creating, '*small-firm effects*' inside the big corporation.
- Allow the employees to leave the salaried jobs and work as '*extended hands*' of the organisation by helping them start their own small enterprises. The employees enjoy total freedom of running their own enterprises, while having the backing of a solid giant corporation. Reliance is understood to have embarked upon this strategy. So is the case with the Xerox Corporation.
- Alvin Toffler suggests a '*checkboard*' organisation. The concept emerges from Australia's political system after the Second World War. The two main political parties agreed that whoever won the elections would place a representative from the other party at the next post and so on for each alternate hierarchy. This type of structure can be profitably used in joint ventures, where at every second post, a manager from principal partners can be placed. This facilitates information dissemination and a remarkable degree of openness, leaving less scope for wariness of intentions between the partners.

Checkboard system, as suggested by Alvin Toffler, can be tried at joint venture

- Acquisitions are common among MNCs, as observed in the beginning of this book. For example, Siemens, the German electronics giant, purchased Nixdorf Computer of Great Britain, making Siemens the largest European-owned computer maker. When an acquisition takes place, the purchasing MNC needs to fashion a structural arrangement that promotes synergy while encouraging local initiative by the acquired company. The result is an organisation design that draws on the more traditional structures that have been examined earlier but still has a unique structure specifically addressing the needs of the acquirer and the acquired.
- Joint-ventures too are common among MNCs. In joint-venture agreements, each co-partner contributes to the undertaking but all co-ventures co-ordinate their efforts for the overall good of the enterprise. Samsung, the giant Korean MNC, has alliances with AT&T to create pen-based computers, with Toshiba to make 64-megabyte flash memory chips, with USA Video to create video file services, and with General Instruments to develop digital television.[10]

Any joint venture requires carefully formulated structure that allows each partner to contribute what it does best and facilitates efficient co-ordination of efforts of all co-ventures. In the case of Samsung, this calls for clearly spelling out the responsibilities of all parties and identifying the authority that each will have for meeting specific targets.

QUESTIONS

1. Discuss the issues involved in globalisation.
2. Describe the organisational structures suitable for an MNC.
3. Describe the entry strategies available to enter global markets.
4. Why are new models needed for multinational corporations?

5. Why has been the flow of direct investment uneven across the globe?
6. Why don't joint ventures last long?
7. How is a particular country selected for initial foraying?

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CHAPTER 4

From Domestic Market to Global Markets

CHAPTER OUTLINE

Historical Evolution of India's Global Trade

Investment Flows

- *Inward Flows*
- *Reasons for Poor Flows*
- *Inflows Encouraging*

Attracting Foreign Capital

Implications for Indian Industries

Destination India

LEARNING OBJECTIVES

After reading this Chapter, you should be able to:

1. *Trace the history of India's foreign trade*
2. *Detail investment flows into and out of India*
3. *Analyse causes for poor inflows*
4. *Suggest ways of attracting inflows and stress why India is a destination for any foreign investor*
5. *Analyse implications of globalisation to Indian industry.*

The last two chapters provided theoretical backdrop to globalisation. This chapter deals with India's entry into the global markets and the challenges lying ahead.

Globalisation is a new phenomenon to us. We were for a long time content in serving the internal market which has been vast. Domestic production was insufficient to feed the vast market. We were compelled to import in order to supplement domestic production. We were also exporting to other countries. Our exports were composed of traditional commodities and the direction was mainly towards the erstwhile communist block. Globalisation, as it is understood now, did hardly exist during the past four and half decades.

> Globalisation is not new to our country. We were exporting to other countries and importing as well.

There are other reasons too which made us remain within the country's boundaries. For a long time, we did not have industries of the number and magnitude to think of globalisation. Vibrant economy filled with robust industries is a pre-requisite for internalisation. This was lacking in our country.

Secondly, for nearly four and half decades, we followed an economic policy which did not encourage competitive spirit among our industrialists. In the name of self-reliance, import substitution, *swadeshi* and economic sovereignty, we encouraged domestic industries to prosper, however inefficient they were. We gave them licences, fixed quotas, imposed tariffs and offered subsidies generously. We did not stop at this. We put several restrictions on foreign companies desiring to enter the Indian soil. This type of environment hardly promotes globalisation.

Finally, immediately after attaining Independence, we adopted the command economy of the erstwhile Soviet model to guide our economic development. While it is unnecessary to debate about the success or failure of centralised planning, it is sufficient to state that the world's greatest MNCs were born in the US, West Germany, Japan and the U.K. which incidentally did not have centralised planning.

Came 1990s. Dramatic developments took place across the globle. Soviet Russia collapsed and along with it the concept of centralised planning got discredited. Several countries, particularly Singapore, Thailand, South Korea, and China have achieved unprecedented economic prosperity through the integration of their economies with the global economy. Our country could not afford to remain isolated and poor any longer. Further, new technologies, information explosion, new materials, bio-energy, super fast micro-chips and other developments facilitated globalisation in a big way. Then came the Industrial Policy, 1991 which paved the way for globalisation in our economy.

HISTORICAL PERSPECTIVE

But our contacts with the world date back to the Buddha period itself. The main exports then from India to the West were spices, perfumes, jewels and fine textiles, but lesser luxuries such as sugar, rice and ghee were also exported, as well as ivory, both raw and worked. Indian iron was much esteemed for its purity and hardness, and dyestuffs such as lac and indigo were also in demand. Another requirement was live animals and birds; elephants, lions, tigers and buffaloes which were exported from India in appreciable numbers for the wild beast shows of Roman emperors and provincial governors, though these larger beasts went mainly overland through the

desert trading city of Palmyra; smaller animals and birds, such as monkeys, parrots and peacocks, found their way to Rome in even larger quantities as pets of wealthy Roman ladies.

In return for her exports India, wanted little but gold. Pottery and glassware from the West found their way to India, and many sherds of Arretine and other wares, mass-produced in Western factories, have been found in the remains of a trading station at Arikamedu, near Pondicherry. There was some demand for wine, and the Western traders also brought tin, lead, coral and slave-girls. But the balance of trade was very unfavourable to the West, and resulted in a serious drain of gold from the Roman Empire.[1] (Also see box 4.1).

Box 4.1

India's Early Global Trade

The Yemerites, Nabataens, and Himyars had their share in Indian trade. Commercial relations existed between India, Rome and Greece, and the balance of trade was in favour of India from the very beginning, as a result of which Roman gold poured into India. The price of Indian goods was settled in Roman gold coins. The Romans also used Indian sesame oil in their food and indigo for colouring. Many kinds of Indian precious and semi-precious stones such as diamonds, onyx, sardonyx, agate, carnelian, crystal, amethyst, opal, cat's eye, ruby, turquoise and garnet were in great demand in Rome. India used to export at least three kinds of parrots to Rome, and Rome imported skins, pearls and coloured hides as well as wool for weaving shawls from India. Ivory from India and Africa was extensively used for inlay work. Indian ivory used to reach Rome by the land and sea routes and Indian made ivory figures also reached Rome (One such figure has been found in Pompeii). The Romans had a great liking for tortoise shells from the Indian Ocean and used to purchase pearls from the Gulf of Mannar, as the fashionable women of Rome were very keen to possess pearls. Rome also used to import silk and costly textiles by the silk routes. Shellac and some Indian herbs were used as medicines. But due to the difficulties of communication, the prices of these products were high. Black pepper had an important place in the trade between India and Rome. In addition to black pepper, India also exported ginger, cardamom, and cinnamon which the Romans used to use both as a spice and incense. The Greek traders imported the oils of lemon grass and ginger grass and the nard oil. The saffron costus produced in Kashmir was used in Rome for ointments and medicines and for perfuming the wings.

(**Source:** P.N.Agarwala, *A Comprehensive History of Business in India*, TMH, 2001, p.262.

While it is unnecessary to describe, in detail, what all has happened since the days when the Roman Empire became poorer because of the drain of gold, suffice it is to state that our country did have trade contacts with the rest of the world till the British invasion.

Even the so called MNC's in our country are not a sudden occurrence. They were there during the 18th century too. The first MNC that came to Indian shores was the East India Company. An aggressor in the most aggressive period of British empire-building process, it left a bad taste in the mouth for most Indians.

By the turn of the 19th century, managing agency systems was in full bloom and names like Bird and Hilgers, McKinnon McKenzie, Andrew Yule, Martin Burn Ltd. and Gallanders Arbuthnot became household names.

By the 1940s, many more MNCs joined the bandwagon. Be it Bata Shoes, Phillips Radio, Lever Brother's soaps, Huntley Palmer's biscuits or Reckitt and Colman's Dettol, MNCs were present in every household. The entire MNC culture received a major jolt in 1974 when the Foreign Exchange Regulation (FERA) was evoked.

International companies were forced to bring down their equity to below 40% in Indian companies and many an expert manager was replaced by Indians. This in fact, led to the creation of Indian companies with MNC linkages. The Indian Tobacco Company (ITC) being a classic case in point.

It was around this time that made-in-India brands started to show their aggressiveness in the market place. Nirma was taking on Surf, Godrej and Kelvinator were dominating the white goods market, the newly evolved IT industry is indigenous and the likes of Dabur, MTR Foods, Cavinkare, and Chandrika are showing the world that they are good in branding too.

Life, ofcourse, had come full circle with the liberalisation process, and MNCs back with a vengeance. While companies like Phillips, Levers, Siemens, P & G, Smithkline Beecham and Glaxo had always been keen on India and have indicated their deep commitment to be a part of India's economic development process, many more are coming to stay.

Coco Cola has forgotten the dark days of 1978 when they were made to leave the country and is back in strength as is IBM. Not to be left behind, Pepsi and Kelloggs are here to stay as is LeviStruss, McDonalds, Kentucky Fried Chicken, Heinz, Samsung, Sony and all the rest.

INVESTMENT FLOWS

Our business houses have chosen joint venture routes to go global

Our businessmen have realized the need for integrating their activities with the world economy and hence, crossed Indian shores in search of new potential markets. They have chosen the joint venture route for globalising their activities.

The number of joint ventures at present is 868, out of which 286 are in operation and 582 are under various stages of operation. The approved equity of these joint-ventures amounts to $1097.68 million. In addition, there are 733 wholly owned subsidiaries abroad of which 216 are in operation and 517 are under implementation. The approved equity of these wholly owned subsidiaries amounts to $820.59 million.

Indian joint-ventures are found predominantly in developing countries like Nigeria, Sri Lanka, Thailand, Singapore, Kenya, Indonesia, Malaysia and the like. Joint-ventures owned by Indian companies are found in developed countries also but they belong to IT sector as Table 4.1 shows.

Table 4.1

Top 15 IT Software and Service Providers and their Affiliates

Rank	Company	Selected locations of affiliates
1	Tata Consultancy Services	Belgium, China, Germany, Japan, Netherlands, Singapore
2	Infosys Technologies Ltd.	Australia, Canada, China, Singapore, United States
3	Wipro Technologies	Japan, Sweden, United Kingdom, United States
4	Satyam Computer Services Ltd.	Germany, United Kingdom
5	HCL Technologies Ltd.	Bermuda, Ireland, Netherlands, United States
6	Patni Computer Systems Ltd.	United Kingdom, United States
7	Mahindra British Telecom Ltd.	United States
8	iFlex Solutions	United States
9	HCL Perot Systems Ltd.	Singapore, United Kingdom
10	NIIT Ltd.	Germany, Switzerland, United States
11	Polaris Software	Germany, United States
12	Birlasoft Ltd.	United Kingdom, United States
13	Mphasis BFL Ltd.	China
14	Pentasoft Technologies Ltd.	Indonesia, United States
15	Hexaware Technologies Ltd.	Germany, Singapore, United Kingdom, Untied States

(***Source:*** UNCTAD, based on National Association of Software and Service Companies, India and various media sources.)

Inward Flows

The flow of FDI into India is less compared to the size and need of the country. India's share in FDI inflow is much less when compared to other developing countries as Table 4.2 shows.

Table 4.2

FDI Inflow into India

Inflow of FDI into India has been disappointing

	2001	2002	2005
			(Billions of dollars)
Brazil	22.5	16.6	–
Mexico	25.3	13.6	–
China	46.8	52.7	–
HongKong-China	23.8	13.7	–
Singapore	10.9	7.7	–
Czech Republic	5.6	9.3	–
Poland	5.7	4.1	–
India	3.4	3.4	5.5

(**Source:** *World Investment Report,* 2003, p.7 and *Business Today,* November 6, 2005, p.141)

Much smaller countries like Singapore (population 42 lakh) and Poland (400 lakh people) have received much higher share of FDI compared to India which has a population of ten thousand lakh. Reasons for poor inflow are many.

Reasons for Poor Flow

> Democracy about which we are so proud of, is itself an impedement to the flow of FDI

There are several barriers to foreign investment. And most of the barriers are the ones created with in the country. Among the factors hampering the flow of foreign investment is an increasingly visible distaste for democracy. As Indian democracy matures, it is throwing up situations and leaders that do not fit easily into old ideological patterns that the developed world is familiar with. The uncertainty of a political ethos that is not fully understood stands out in sharp contrast to the clarity of authoritarian regimes. Some investors even argue that since authoritarian regimes are more dependent on economic success to divert attention from political issues, they are more focused on the economy than democracies like India where other issues like religion, caste, language or even a Miss World Pageant take a major portion of a government's attention.

Nothing can be more illustrative than the way the proposed project to put up an international airport at Bangalore is put on hold for decades. In contrast, in the past decade, China has built atleast 12 major international airports. Similarly, the Government of Karnataka has been dithering for years and has not been able to lay an express road between Bangalore and Mysore-a distance of 143 km. But the Chinese Government has laid in the last decade 29,000 km of high quality four-lane highways.

Table 4.3 shows India's inward FDI performance index from 1988 to 2000. The inward FDI performance index is the ratio of a country's share in global FDI inflow to its share in GDP.

As shown in Table 4.3, India's performance index is very low-in fact it ranks 119th among the 140 countries listed in the *World Investment Report* 2002. However, India is the only country whose performance index shows an improvement in 1998-2000 over the decade 1988-90.

Table **4.3**

India's Inward FDI Performance Index Compared

1988-90	*1998-2000*	
India	0.1	0.2
Pakistan	0.6	0.2
Sri Lanka	0.5	0.4
Mongolia	0.8	0.5
Chinese Taipei	0.9	0.3
Brunei	0.0	0.1
Indonesia	0.8	-0.6
Malaysia	4.4	1.2
Myanmar	1.9	0.6
Philippines	1.7	0.6
Singapore	13.8	2.2
Thailand	2.6	1.3

(**Source:** *World Investment Report,* 2002, UNCTAD)

Apprehensions about investing in India have not been helped by the early record of joint ventures. American executives monitoring joint ventures in India believe that Indian partners are often not in a position to live up to their part of the deal. In some cases, this is the result of unrealistic expectations, in others it has to do with the liquidity crisis, making it difficult for smaller Indian partners to come up with their share of capital.

The sensitivity of foreign investors to these risks is heightened by the fact that India has less to offer than some other developing countries. The Indian market is proving to be smaller than investors may have believed. The earlier enthusiasm about a large middle class is tempered by the realisation that it does not have the purchasing power to absorb even items targeted at the lower middle class in the West. Western fast food chains, for instance, have become items of luxury consumption in India. The Indian market can be seen in perspective from one rather startling statistic. By 2001, the Indian demand for pagers was expected to grow rapidly to 1.7 million, but in that year, China's demand would be 73 million. Without the buffer of a large domestic market, the main attraction India can offer to foreign capital is its cheaper costs of production, particularly labour costs. But India is not the only country offering these advantages. Several smaller countries are already being preferred to India. Taken individually, each small country may not have the advantage of lower labour costs for long. A rush of foreign capital into each country will raise wages there and eat into its advantage in labour costs. But taken together foreign capital can move from one small country to another. Since some of the other countries like Indonesia are quite large, India would have a long wait before its competitors exhaust their low labour cost advantage. And other countries may also be able to offer advantages like less rigorous environmental standards.

> Foreign investores are not enthusiastic to invest in India

The ability to attract foreign investment can also be adversely affected if the inflow of foreign capital is not appropriately integrated into the economy. This could happen in different ways. Sometimes, the concessions offered to attract foreign capital can distort the local economy to such an extent that foreign capital no longer finds it worthwhile to invest. This has already happened in the stock markets. In the effort to woo foreign institutional investors, the small investor has been ignored. As a result, the kind of small investor participation that helped Reliance emerge as a major industrial house is no longer seen. Without the emergence of new giants with the help of the capital market, the number of companies that are actively traded remains small. This narrow base reduces the options that Foreign Institutional Investors (FIIs) have, dampening their enthusiasm to invest.

> We have not been able to integrate foreign capital into our economy

The tendency to ignore the consequences of the concessions that are being offered may soon become more visible in other sectors. In the eagerness to attract foreign investment in the infrastructure sector, the prices are being offered without sufficient attention being paid to whether the economy can absorb these higher prices. So when the project is completed, investors may find that they have overestimated the demand. The fast track power projects have tried to overcome this risk by getting guarantees of a fixed offtake of power. But such guarantees can hurt NTPC units, if in a relatively better power situation, they are asked to stop producing power so that the predetermined quantity of power can be evacuated from the foreign power plants. And if the

government tries to avoid this situation by not offering guarantees, foreign investment in the power sector can also slow down.

The ability to integrate foreign capital into the economy is also hampered by the project oriented approach to this task. With the focus being on individual projects, the linkage between individual projects and the rest of the economy is often not given sufficient attention. The value of a modern expressway, for instance, is eroded if the time saved on it is lost in going from the expressway to the city. Despite Bangalore's Electronic City being built on one such expressway, several computer firms are considering moving out of the city, citing poor infrastructure as the reason[2].

The linkage between individual projects and the rest of the economy is often overlooked. The value of a modern expressway is lost if it takes a long time to reach a city

Policy guidelines lack clarity between central and state governments. Most policy guidelines are laid down by the central government but are left to the state governments for implementation. Delays take place at the implementation stage.

NRIs, who (numbering 22 million scattered across the globe and possessing collective wealth of Rs.200,000 crore) once accounted for 30% of the direct investment flow, have their own woes. They complain of bureaucratic red tape and demanding officials trying to extract money at every stage. Consequently, their interest in Indian companies declined as shown in Table 4.4.

Table 4.4

NRIs Desert Indian Primary Market

Year	*No. of issues offered to NRIs on preferential basis*	*No. of issues subscribed*	*Percent*
1991-92	32	25	78
1992-93	125	73	58
1993-94	406	109	27
1994-95	410	120	29
1995-96	701	30	4
1996-97 (Apr-Dec)	384	0	0

(**Source**: *The Hindu*, December 19, 1996)

We have innumerable labour laws which come in the way of improved labour productivity and the firm's profitability. Labour laws are so strange that even perennially sick units are made to work and workers are paid salaries even if they have no work to do. Payment of bonus is mandated even for a loss making unit. Dismissal of an errant worker or closure of a perennially sick unit is almost impossible. Labour laws need to be streamlined in tune with the demands of the competitive environment.

Labour laws are highly rigid. Even sick units are made to pay regular wages and even bonus.

There are still caps on the percentage of equity holding in different industrial sectors. There are still two routes to setting up a project: an automatic route which requires no prior sanction and the FIPB (Foreign Investment Promotion Board) route. An investment exceeding US $120 million requires permission from no less than the Cabinet Committee on Foreign Investment. The route to take thus depends on the size of the investment, how much foreign equity is to be held and in which industrial sector.

The Confederation of Indian Industry (CII) estimated that a typical power project would require 43 clearances from the Central Government and 57 from provincial and municipal governments. The CII found that with such redtapeism and confusion, 55% of potential investors in 2000-2001 dropped out after obtaining the requisite FIPB approval.

India continues to be a mystery wrapped in an enigma in terms of business development to many foreign investors, particularly Japanese. To the Japanese, our country is a totally different world with communal riots, unhygienic conditions, severe poverty and many linguistic and caste conflicts unlike their own monoculture, single language country. Caste is something which they cannot grasp and religious conflicts frighten them as investors. And of course, India's last few decades of socialism have left their own negative impact.

The way Enron project was handled demonstates how political differences can hamper projects

Different political parties, wedded to their own ideologies, impede industrial progress particularly when they are voted to power. The case in point is repudiation of the Enron power project. Agreement to execute the power project was signed by the then ruling party in the State of Maharastra and the Enron Corporation. Later, a different party came to power in the state and it thought it fit, purely for political reasons though, to cancel the project. Such cancellations send wrong signals to foreign investors.

ATTRACTING FOREIGN CAPITAL

The process of liberalisation that began in 1991 will continue and India, as a result, will experience more growth and within the next generation, will assume its rightful place as one of the premier economies of the world. It is not just its size, it is not just the fact that it is going to experience the growth it should have had 50 years ago. It is also a unique role that India will play as a model which its founders hoped it would do. But perhaps it is going to play this role in a way in which its founders did not anticipate and that is to demonstrate to the rest of the world that democracy is compatible with economic growth and change and that India can begin with democracy and still make the internal changes that make possible great economic growth. In many other parts of the world, the nations that have grown very fast, have been those that have had authoritarian regimes or only semi-democratic regimes. They allow individual freedoms in terms of economics and that in turn, made possible more democratic reforms. India will begin to show the world that she can do it in reverse, that she can begin with democracy and still set the stage for greater economic growth.[3]

In order to attract foreign investment on a large scale, the government has taken several steps to remove the barriers which have hindered the flow of investment on a large scale. (see box 4.2)

Results Encouraging

The results of all these efforts are encouraging. As seen from Table 4.5, the inflow of foreign capital has been steadily rising from year to year, except in 1997-98.

Table 4.6 gives break-up of foreign direct investment approvals from August 1991 to June 1999.

Box 4.2

Measures to Attract FDI

Year	Measure
1992	Foreign firms obtained automatic rights over international brand names
1993	Requirement for industrial licensing in specified industries (white goods, entertainment electronics) abolished
	FIIs allowed to invest in new Mutual Fund schemes
1994	Banks allowed to set their own rates for lending
	Companies allowed to issue preferential equity to FIIs
1996	Overseas pension funds, charities, foundations qualify as FIIs
	FIIs allowed to invest in un-listed firms
	FIIs allowed to invest 100% of funds (previous 30%) in debt Instruments
1998	Further concessions to FIIs-now allowed to invest in Government securities, Treasury Bills, listed and un-listed debt securities
1999	FIIs allowed conditional forward foreign exchange cover
	FIIs could participate in open offers in accordance with take-over codes
2000	100% foreign equity allowed in infrastructure projects-ports, roads, highways
2002	Limited FDI in print media permitted

Table 4.5

Year	*Rs.crore*
1990-91	185
1991-92	326
1992-93	1,713
1993-94	13,026
1994-95	16,133
1995-96	16,327
1996-97	21,328
1997-98	18,520

(**Source**: *Handbook of Statistics on Indian Economy*, RBI [1998])

Expectations and Concerns

At a recently concluded conference on FDI held in New Delhi sponsored by UNCTAD, a consensus seemed to emerge amongst Indian participants:

1. FDI into India was nowhere near its needs or potential. FDI levels would have to triple in the next 5 years if India was to attain its targeted growth rate of 8% p.a.
2. There still remained vestiges of resistance to FDI within the Indian establishment and the public at large. There was a need for effective advocacy groups to allay fears and permit more informed public opinion. Only civil society organisations can help dispel the complexes left behind by the East India Company.

Table 4.6

Foreign Collaboration Aprovals

	No.of Approvals	Amt.Involved (Rs.million)
Fuels(power, oil refinery and others)	581	6,18,479
Telecommunications	517	3,58,297
Transportation Ind.	993	1,41,972
Service Sector	670	1,20,308
Metallurgical Ind.	561	1,18,959
Chemicals (other than fertilisers)	1,423	1,14,770
Electrical Equipment	2,664	1,09,207
Food Processing(Ind.)	722	84,231
Hotel & Tourism	356	41,258
Textiles	578	29,999

(**Source:** *The Economic Times*, Nov 9, 1999).

3. The Government could play a much more positive role by being transparent and proactive in policy pronouncements. An atmosphere of secrecy and a Government which sporadically alters policy hardly promotes confidence.
4. Whilst FDI was eminently desirable, what was perhaps more important was a policy and regulatory framework which attracted investment and industrialisation as a whole, irrespective of whether this was foreign or domestic. FDI tended to flow in where the industrial environment was favourable and where the economy was strong.

This is by no means comprehensive: several other measures, such as the repeal of the draconian Foreign Exchange Regulations Act in favour of FEMA (Foreign Exchange Management Act) served directly or indirectly as stimuli for foreign investment. The Government also periodically announced, by means of formal notifications, relaxations in the percentage of foreign equity permissible in different industries. The term 'relaxation' must be stressed: in no instance has there been a tightening or reversion.

Perhaps the most important of these relaxations from the foreign investor's viewpoint was the discontinuation in 2000 of the provision for 'dividend balancing' in 22 categories of industries (mainly consumer goods/consumer durables). Under this provision, dividends repatriated to the parent country had to be balanced by export earnings over a 7 year period, such exports being optionally from own production or merchant exports.

On occasion, external factors have forced relaxations in policy. In response to a U.S. complaint, the WTO ruled that the compulsion to raise the indigenous content of cars to prescribed levels was not permissible, and the Government of India had to withdraw this clause.

Over and above the inducements offered by the Central Government were the incentives offered by provincial governments. Land, for instance, was and still is offered at very low rates for foreign-owned factories. Waivers or concessions are routine: Ford obtained a 15 year holiday from local sales tax in Tamil Nadu. General Motors had a 30 Km stretch of road completely re-surfaced by the Government of Gujarat.

IMPLICATIONS FOR INDIAN INDUSTRY

Globalisation has serious implications for the Indian industry. For a long time, the Indian industry exhibited such characteristics as high cost, low productivity, junk machinery, outdated technology, inferior quality, high sickness and very low competitive spirit. With all these, industrialists were still making money because of the protected environment. Environment in future will not be the same thanks to economic reforms and globalisation. Catchwords from now onwards shall be competitiveness, efficiency, profitability, technology upgradation, foreign capital, safety net and golden handshake.

Globalisation has some lessons for Indian industries:
- be quality conscious
- change attitudes
- keep customer satisfaction uppermost

Specifically, globalisation shall herald the following challenges to our industry:

1. Customer satisfaction has been the greatest of the casualties in our country. This cannot continue. The manager must think of offering quality goods at reasonable prices to the customer.
2. Attitude of the Indian businessman must change. He must look beyond the boundaries of the country and set up his own enterprises or partnerships with other companies in overseas markets. What Socrates said centuries ago must come true in his case. "I am not an Athenian or a Greek", said Socrates, "but a citizen of the world."
3. Improve the quality of products to international standards. Global standards, quality certification and testing are a must.
4. In the advanced countries, total quality management (TQM) is almost byword-the latest philosophy. Our industry must not lose time in achieving this goal. Having started late, we must move fast.

Any engineering industry goes through some distinct stages while attaining total quality. In the first stage, the organization aims at conformance to the product specification. This would need standards, technical ability to adhere to standards, an inspection and quality assurance department, and the right type of culture within the organisation. Such organizations will have solid quality assurance systems and with some effort, they can qualify for obtaining the ISO 9000 system accreditation. In this stage, the organisation tries to sell the products it can make.

In the second stage, an organisation moves beyond just adhering to its own product specifications. It tries to meet what the customer needs.

Engineering sector passes through four stages to attain total quality
- conforming product specification
- meet cunstomer needs
- compare with the best
- TQM

The marketing departments try to ascertain market needs and trends and the engineering and manufacturing departments fulfil this need. This is a feature of an organisation with substantial market orientation. This stage provides an enterprise with a competitive edge. Of course the source of feedback is one's own customer.

Beyond this is the third stage wherein an organisation is not just satisfied with customer satisfaction. It tries to measure and compare its performance in all aspects with those of better performers. This is known as *bench marking*. An organisation directs its focus outside its own walls. It studies competition, learns from the superior-competitors who have satisfied more demanding customers. In this process, it aims at identifying and beating the best proposition for its benefit.

Total quality management, the last stage, goes beyond beating the best. It is a process and a means for maintaining the leadership position through continuous change, adaptation and improvement. Total quality management is to improve the quality of work of all the people at all the functional areas of the organisation. It uses the fundamental ideas of group activity, participation of all, application of statistical and other QC tools, self-development and creativity. It imbibes the philosophy that there is always a better way of doing things.

World over, the best organisations are moving towards total quality management. A majority of them would have already gone through the earlier stages. In the race towards international competitiveness, organisations in India may have to pursue all these stages simultaneously. Pursuing them sequentially would take too long a time and we have to compress the time needed. This will make our task more strenuous. Industry must be prepared to make the effort.

Best companies around the world practise TQM

5. Globalisation means more markets for our products. We must seize the opportunity and export our products on a large scale. Exports are necessary to earn foreign exchange. We cannot look to th government for its help in boosting exports. Government can only create a favourable environment and it is upto the Indian industry to use the environment to sell Indian products overseas on a massive scale.

6. Nearly 96 per cent of the top 500 private sector companies in our country are family controlled and secretive. Holding small portions of equity capital, family members treat limited companies as their fiefdoms. They believe that they have right to inherit and control.

   While family inheritance and control may not be wrong, the brawls erupting between brothers or cousins send wrong signals to business community.

Majority of our private sector companies are privately held and are secretive

7. The eighties saw the development of global corporations and the global competitive arena. The earlier battles among the European and American companies were joined by the Japanese and Korean companies. Current developments in the Indian regulatory environments are opening the Indian gates for the expansion of the arena into India. Already some companies have taken positions through memberships in consortia, consulting projects, minority joint ventures, product-based technology transfer agreements, component supply arrangements, R&D agreements and the like. Some of the existing subsidiaries of the multinationals are looking for new strategic directions and strengthening their muscles to face the battle. The extension of the global competitive arena to India is a source of both a threat and an opportunity. There is the threat of mergers and acquisitions, and the elimination of medium and small companies from the market place. There is also the opportunity to forge strategic alliances and even test one's own strengths *vis-a-vis* multinational competition.

8. One of the requisites for success in globalisation is to think global but to act local. What this implies is that one must have an open mind to accept what is good but not to forget one's own moorings. This is what Mahatma Gandhi told us long back. 'I don't mind', said he, 'to keep windows open, but I don't want the wind to blow me off my feet'. This is also

To be successful one should think global but act local

Box 4.3

Justice for all

The troubles of Kentucky Fried Chicken in India have made foreign investors nervous about investing in India. But there is one aspect of the episode that should give them strong encouragement. It has proved that in India, the legal system offers swift and effective recourse to foreign investors against arbitrary acts of politicians and bureaucrats. This is in stark contrast with conditions in China, India's major rival in seeking foreign investment. When McDonald's lease in Beijing was abruptly terminated by the authorities there, the unfortunate company had no way of seeking any legal remedy. The authorities were, fundamentally, not challengeable. But in India, KFC was able to approach the courts, both in Bangalore and New Delhi, and get a reversal of acts of politicians and bureaucrats.

This point must not be stretched too far. The Indian legal system is in a terrible mess, and the courts take forever to convict anybody. No ordinary case is settled for years, may be decades. This is why many observers (including this newspaper) have often declared that the justice system is moribund. However, the KFC episode reminds us that the justice system can still deliver efficient remedies in respect of writ petitions, if not in normal litigation. This can be particularly important for foreign investors worried about political risk. It is often said that companies want an efficient legal system to enforce contracts, and this is unquestionably true. What is often forgotten is that companies also need protection against arbitrary action by the authorities which may have nothing to do with contracts. The closure of KFC outlets was not a violation of contract, it was administrative high-handedness, which happened to be even more damaging than contract violation. India has proved that it is capable of giving foreign investors a difficult time, but it has also proved that it is capable of giving investors some forms of recourse that would be unimaginable in China. However, we must add that this is not good enough, and that the judicial system needs a thorough overhaul to deliver reasonably speedy justice in ordinary cases. We need this for our own citizens, and we need to worry about their needs for justice far more than in the case of foreign investors.

(**Source**: Leader Comment, *The Economic Times*, Dec 8, 1995)

the lesson which Japanese teach to the rest of the world. Japanese have accepted foreign technology but never forgot their local culture.

DESTINATION INDIA

As was stated earlier, India is emerging as the most attractive country for foreigners to invest. There are several strong points why MNCs must invest their funds in our country.

We offer, to investors from abroad, a large market, a strong legal system (See Box 4.4), well developed capital markets, a class of private sector partners, and a rare commodity in the developing world - English speaking managers who can manage (not just operate) business.

We also have well entrenched the democratic set-up and perhaps ours is the only country which has come out of the 40 year old socialist trap successfully. Most of Asia has done it at the cost of, or in the absence, of democracy. Most of Latin America is still to get there and Eastern Europe is still struggling (Also see Fig.4.1).

Obstacles notwithstanding, India is a destination for any foreign investor

Figure 4.1

Star Status of Countries

General Approval Requirements	China	India	Indonesia	Korea	Malaysia	Singapore	Taiwan	Thailand
Foreign Investment	YES	Yes, automatic under certain conditions	YES	Yes, automatic in few cases	YES	NO	YES	No,except for restricted industries
Industrial Licensing	YES	No, except for few restricted industries	YES	YES	YES	No,except for few industries	YES	YES
Repatriation of Profit	YES	YES	YES	No,if in accordance with approved remittance schedule	NO	NO	NO	NO
Repatriation of Capital	YES	YES	Notification required	YES	NO	NO	YES	NO
Imports	NO	No, except for few restricted items	YES	YES	NO	NO	NO	NO
Foreign Loans	YES	YES	NO	YES	YES	NO	YES	NO
Domestic Loans	YES	NO	YES	NO	No,except above certain levels	NO	NO	NO
Technical Collaboration	YES	Yes,automatic within laid down parameters	NO	Notification required	YES	NO	YES	NO
Expatriate Employment	YES	YES	YES	YES	YES	YES	YES	YES
Incentives	YES	NO	YES	YES	NO	YES	YES	YES

Box 4.4

India's Special Strengths & Weaknesses

STRENGTHS	Scale*	Rank**
Stock Market		
Stock market is important for new financing	5.42	13
Science and Engineering		
Schools excel in basic science and maths	5.27	16
Country has a large pool of competent scientists and engineers	6.37	1
Engineering as a profession greatly attracts young talent	6.26	1
Labour Force		
Country has first-class business schools to train managers	5.05	8
Country has an abundant labour force	6.77	1
Rule of Law		
Judiciary is independent of the government	5.40	9
Compliance with court ruling is high	5.37	14
Firms have recourse to courts for challenging government actions	5.56	19
WEAKNESSES		
Financial Markets		
Citizens prohibited from investing in foreign stocks, bonds, bank a/c's	1.60	53
Financial sector sophistication is lower than international norms	2.74	43
Venture capital is scarce	2.63	50
Public Administration		
Administrative regulations that constrain business are pervasive	2.90	47
Government subsidies keep old industries alive	2.68	52
Civil Service is subject to political pressures	2.65	43
Tax evasion is rampant	2.27	48
Infrastructure		
Overall infrastructure is far worse than major trading partners	1.92	53
Road infrastructure constrains business development	1.85	53
Port facilities are underdeveloped	2.18	53
Direct dial phone service is prohibitively expensive	2.94	53
Country suffers from severe power shortages	1.94	53
Research and Development		
The business sector spends little on R&D	2.11	52
Research collaboration does not exist between universities and industry	2.66	53
Firms fail to commercialize academic research	2.66	51
Companies are poorly adapted to absorbing new technologies	2.29	34
Labour Regulations		
Average workers are unproductive	2.94	51
Hiring and firing practices are severely restricted	2.16	53
Labour regulations impede adjustment of working hours to meet changes in demand	2.58	49
Corruption and Bribery		
Extra payments connected with permits and licenses are common	2.79	48

* All questions have scale from 1 (lowest) to 7 (highest)
** India's rank amongst 53 countries ranked in the 1998 GCR

(**Source**: 1998 Global Competitiveness Report)

India is also blessed with the exemplary characteristics associated with any booming economy - a huge and productive compliment of skilled manpower and excellent earnings growth providing attractive opportunities for international investors to diversify portfolio risks.

Our country's relatively good performance among Asian countries and the steady pace of economic reforms should attract more and more foreign capital. Box 4.4 contains SWOT analysis of India.

QUESTIONS

1. Bring out the implications of globalisation to our businessmen.
2. Point out the favourable and unfavourable factors about India as a market for foreign investment.
3. Why has been the flow of foreign capital into India poor?
4. Why should India be the destination for foreign investors?

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CHAPTER 5

India, WTO and the Trading Blocks

CHAPTER OUTLINE

Functions of WTO
Differences between GATT and WTO
Structure of WTO
The Final Act
Implications for India
- ***Arguments for Joining WTO***
- ***Arguments against Joining WTO***

Agenda for the Next Millennium
India's Commitments to WTO
Trading Blocks

LEARNING OBJECTIVES

After reading this Chapter, you should be able to:

1. *Describe the functions and structure of WTO and differentiate it from GATT*
2. *Describe the Final Act and what it contains*
3. *Implications of joining WTO to India*
4. *List the agenda lying ahead of WTO in the next millennium*
5. *List our commitments to WTO*
6. *Shortlist the leading trading blocks and India's membership of them.*

The World Trade Organisation (WTO) was established on 1st January 1995. Governments had concluded the Uruguay Round negotiations on 15th December 1993 and Ministers had given their political backing to the results by signing the Final Act at a meeting in Marrakesh, Morocco in April 1994. The '*Marrakesh Declaration*' of 15th April 1994, affirmed that the results of the Uruguay Round would '*strengthen the world economy and lead to more trade, investment, employment, and income growth throughout the world.*' The WTO is the embodiment of the Uruguay Round results and the successor to the General Agreement on Tariffs and Trade (GATT).

The WTO administers the trade agreements negotiated by its members, in particular the GATT, the GATS (General Agreement on Trade in Services), and the TRIPS (Trade Related Aspects of Intellectual Property Rights). The WTO builds on the organisational structure that had developed under GATT auspices of the early 1990s.

The WTO has larger membership than GATT, the number of members stands at 148 (Oct. 13, 2004). India is one of the founder members of the WTO. How the membership benefits India is worth examining. This chapter is devoted for the purpose. Before this, it is useful to understand more about the WTO itself.

Basic Principles of WTO

The WTO agreements are lengthy and complex as they are legal texts covering a wide range of activities. They deal with agriculture, textiles and clothing, industrial standards and product safety, food sanitation regulations, intellectual property and many more. Some basic principles run through all these documents. These principles are the foundation of the WTO. The fundamental principles are: non-discrimination, transparency, binding commitments, reciprocity and safety valves.[1]

WTO is founded on certain fundamental principles. They being: non-discrimination, transparency, binding commitments, reciprocity and safety valves.

Non-discrimination: This principle is based on the concept of **normal trade relations**-previously called the most-favoured-nation (MFN) rule. This rule requires that the WTO members extend the same favourable terms of trade to all members that they extend to any single member. For example, if Japan were to reduce its import tariff on German automobiles to five per cent, it must reduce the tariff it charges on imports from all other members to five per cent.

The normal trade relations principle applies unconditionally. Although exceptions are made for the formation of trading blocks (discussed latter in this chapter) and for preferential treatment of developing countries, the non-discrimination principle is basic pillar of the WTO. Because of this principle, importers and consumers will have the benefit of using low cost goods, irrespective of whichever country they are being produced.

The principle of non-discrimination has one more dimension: national treatment. National treatment enjoins all member countries to treat imported and locally produced goods equally. National treatment only applies only after a product, service or item of intellectual property has entered the market. Obviously, imposing customs duty on an import is not a violation of national treatment even if locally-produced products are not charged an equivalent tax.