



Laying Foundations

PART 1

CHAPTERS

1. Globalizing Business
2. Understanding Formal Institutions:
Politics, Laws, and Economics
3. Emphasizing Informal Institutions:
Cultures, Norms and Ethics
4. Leveraging Resources and
Capabilities



C H A P T E R 1



Globalizing Business

Photo credit

O P E N I N G C A S E

Which Country Made This Book?

Let us start with a quiz: Which country made your book—yes, the very copy you are reading now? If you answer, “Of course, the United States!” sorry, you will only be given partial credit. Some of you will look at the copyright page (the second page after the title page) and point out the publisher, South-Western, and its address in Mason, Ohio (just outside Cincinnati), as evidence that this book is a US product. Well, not quite . . .

Not only is the nationality of our publisher difficult to track down, but it has also been *changing*. Founded in 1902, South-Western had been an independent US publisher until it was acquired in 1986 by the Thomson Corporation, an \$8 billion Canadian firm whose shares are listed in Toronto (TSX: TOC) and New York (NYSE: TOC). South-Western thus became a wholly owned subsidiary of Thomson. The book contract that I signed in 2005 was with Thomson (or specifically with Thomson Learning South-Western, a unit of Thomson Learning, which had been one of the four major divisions within Thomson with approximately \$2.47 billion in sales in 2006). So technically, the book had been Canadian—at least when it was conceived.

However, the winds of global change extensively discussed in this book have also directly impacted this book. In 2007 (before the book was finished), the Thomson Corporation sold its Thomson Learning division for \$7.75 billion to two private equity groups: the London-based Apax Partners and Toronto-based OMERS Partners.* Apax Partners is one of the oldest and largest private equity firms in the world with more than \$30 billion under its management. OMERS is one of the largest and most sophisticated asset management entities in Canada with over \$45 billion in assets. (Chapters 12 and 16 present more details on acquisitions and private equity.)

In July 2007, Thomson Learning, now under new British and Canadian ownership, changed its name to Cengage Learning. The name was based on being at the “center of engagement” for its customers worldwide. Cengage Learning is a multinational publisher with operations in 39 countries. In the academic marketplace, it serves elementary, secondary, and postsecondary students, teachers, professors, and learning institutions. Cengage will continue to emphasize its brands, including Heinle, Gale, Wadsworth, Delmar Learning, and our very own South-Western. In our own segment for business and economics college textbooks with the South-Western brand, Cengage Learning is number one in the world in terms of market share, followed by McGraw-Hill (with the Irwin brand) and Pearson (with the Prentice Hall brand). While Cengage is now UK and Canadian owned, Pearson is also UK owned and McGraw-Hill is US owned.

So, it appears that given the global nature of your publisher, Cengage, “Which country made this book?” is a very tricky question. Now, let us try a more straightforward one: Which country *produced* this book? In the jargon of publishing, “production” means the transformation of a manuscript into printable plates by a production house, which is neither a publisher nor a printer. (Actual printing is called “manufacturing.”) Although a portion of the production was indeed done in the United States (mostly involving proof-reading by the author and assistants), a majority of the production work for this book was done by a production house based in India. Everyone opening this book probably already knew that India has emerged as a leading global player in information technology (IT) and related services known as “business process outsourcing” (BPO). However, how many of you would have thought that the very book you are holding now had been produced in India?

* The Thomson Corporation used the proceeds of the sale of Thomson Learning as a part of its \$17 billion funds to acquire Reuters, a UK-based financial data and news service provider. The combined entity later became Thomson-Reuters.



LEARNING OBJECTIVES

After studying this chapter, you should be able to

1. explain the concepts of international business and global business
2. articulate what you hope to learn by reading this book and taking this course
3. identify one most fundamental question and two core perspectives that provide a framework for studying this field
4. participate in the debate on globalization with a reasonably balanced and realistic view and a keen awareness of your likely bias in favor of globalization
5. have a basic understanding of the future of the global economy and its broad trends

Now, the next question is: Why India for production? In two words: cost and quality. The cost to produce this book in India is only a fraction of the cost to do so in the United States. In the second half of 2007, our production house in India and I (and my team) followed a well-known practice in IT: “Chase the sun.” Every morning when I got up, I received files from India. Before I went to bed, I sent the revised files to India, where typesetters would get them the first thing in their morning. The next morning, the same pattern repeated itself, and such days went on until we eventually put the book “to bed.”

A few years ago, a majority of the Thomson textbooks were handled by US production houses. Since 2000, offshore outsourcing of support and services, primarily to Indian production houses, has been growing at 8% a year at Thomson (now Cengage). In response, US production houses fight back by becoming “Indian”—through subsidiary operations in India. In this very global business, Indian production houses not only need to fend for themselves against US rivals but also need to watch out for rivals from other emerging economies. For now, non-English-speaking competitors from Brazil, China, and Poland have a hard time winning contracts from Cengage. In the short run, the Philippines, with its large supply of low-cost, English-speaking professionals, seems determined to eat some of India’s lunch. In the long run, Bulgaria, China, and Pakistan may emerge as global contenders in IT/BPO. For managers at current and would-be competitors in these companies, there is no doubt that how to take advantage of the globalization of their business is their job number one.

Sources: Based on (1) author’s interviews with Cengage (formerly Thomson) executives, 2005, 2006, and 2007; (2) Cengage Learning, <http://en.wikipedia.org> (accessed August 16, 2007); (3) M. W. Peng, 2006, *Competing in and out of India*, *Global Strategy* (pp. 3–4), Cincinnati, OH: Thomson South-Western; (4) Thomson Investor Day presentations, October 6, 2005, and October 6, 2006; (5) <http://www.thomson.com>.

How do firms compete around the globe? For British, Canadian, Indian, and US firms involved in the production of your textbook, how do they strengthen their competitive advantage? For Brazilian, Bulgarian, Chinese, Pakistani, Philippine, and Polish firms that want to have a piece of the action, how can they overcome their disadvantage? What determines the success and failure of these firms around the world? This book will address these and other important questions on global business.

LEARNING OBJECTIVE 1

explain the concepts of international business and global business

international business

A business (firm) that engages in international (cross-border) economic activities or the action of doing business abroad.

multinational enterprise

defined as a firm that engages in foreign direct investments

foreign direct investment

investments in, controlling, and managing value-added activities in other countries.

INTERNATIONAL BUSINESS AND GLOBAL BUSINESS

Traditionally, **international business** (IB) is defined as (1) a business (firm) that engages in international (cross-border) economic activities and/or (2) the action of doing business abroad. Consequently, a previous generation of IB textbooks almost always takes the foreign entrant’s perspective, often dealing with issues such as how to enter foreign markets and how to select alliance partners. The most frequently discussed foreign entrant is the **multinational enterprise** (MNE), defined as a firm that engages in **foreign direct investment** (FDI) by directly investing in, controlling, and managing value-added activities in other countries.¹ As important as MNEs and their cross-border activities are, they only cover one side of IB—namely, the foreign side. Students educated by these books often come away with the impression that the other side of IB does not exist. Of course, the other side, consisting of domestic firms, does exist. Facing foreign entrants such as MNEs, domestic firms do not just sit around. They actively compete and/or collaborate with foreign entrants. In other words, focusing on the foreign entrant side captures, at best, only one side of the coin.²

It seems uncontroversial to suggest that there are two key words in IB: *international* (I) and *business* (B). However, previous textbooks all focus on “international”

(the foreign entrant) to the extent that the “business part” (that also includes domestic business) almost disappears. This is unfortunate because IB is most fundamentally about B before I. To put it differently, in the undergraduate and MBA curriculum at numerous business schools, the IB course is probably the *only* course with the word *business* in its title. All other courses are labeled as management, marketing, finance, and so on, representing one function but not the overall picture of business. Does it matter? Of course! It means that your IB course is an *integrative* course that has the potential to provide you with an overall business perspective (as opposed to a functional view) grounded in a global environment. Consequently, it makes sense that your textbook should give you both the I and B parts—instead of just the I part.

This is exactly why this book, which covers both I and B parts, is titled *Global Business*—not merely “international” business. **Global business**, consequently, is defined in this book as business around the globe. The activities include both (1) international (cross-border) activities covered by traditional IB books and (2) domestic business activities.

Such deliberate blurring of the traditional boundaries separating international and domestic business is increasingly important today because many previously national (domestic) markets are now globalized. In college textbook publishing, not long ago, competition was primarily on a nation-by-nation basis. South-Western (before its acquisition by Canada’s Thomson and more recently by Britain’s Apax Partners and Canada’s OMERS Partners), Prentice Hall (before its acquisition by Britain’s Pearson), and McGraw-Hill fought each other largely in the United States. A different set of publishers competed in other countries. Now, thanks to rising demand for high-quality business textbooks in English, Cengage (formerly Thomson), Pearson, and McGraw-Hill have significantly globalized their competition. It becomes difficult to tell in this competition what is international and what is domestic. *Global* does seem to be a better word to capture the essence of this competition.

Moreover, this book has gone substantially beyond competition in developed economies by devoting extensive space to competitive battles waged throughout **emerging economies**, a term that has gradually replaced the term *developing countries* since the 1990s.³ Another often used term is **emerging markets** (see Closing Case). How important are emerging economies? Shown in Figure 1.1, collectively, they now contribute approximately 50% of the global **gross domestic product** (GDP).⁴ Note that this percentage is adjusted for **purchasing power parity** (PPP), which is an adjustment to reflect the differences in cost of living (see In Focus 1.1). Using official (nominal) exchange rates without adjusting for PPP, emerging economies contribute about 26% of the global GDP. Why is there such a huge difference between the two measures? This is because cost of living in emerging economies, such as housing and haircuts, tends to be lower than

global business

business around the globe

emerging economies

A term that has gradually replaced the term *developing countries* since the 1990s. Another often used term is **emerging markets**.

gross domestic product

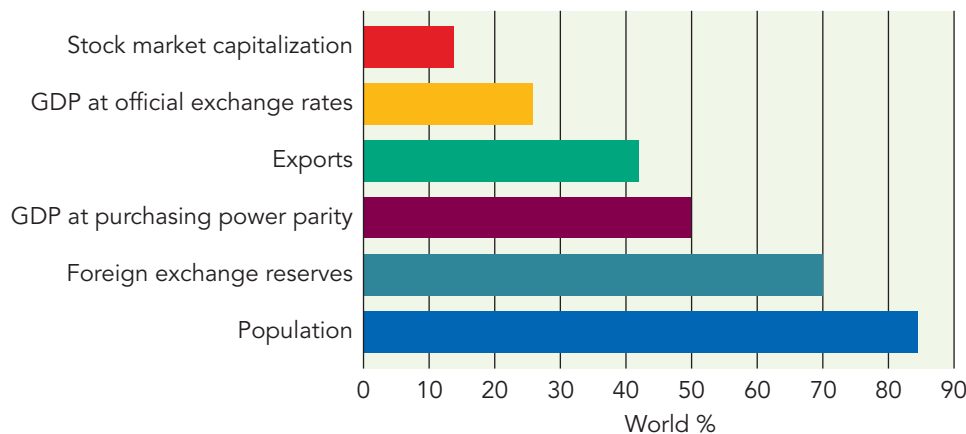
Note that this percentage is adjusted for purchasing power parity, which is an adjustment to reflect the differences in cost of living.

purchasing power parity

An adjustment made to the GDP to reflect differences in the cost of living.

FIGURE 1.1

THE CONTRIBUTIONS OF EMERGING ECONOMIES



Source: Adapted from *Economist*, 2006, Climbing back (p. 69), January 21: 69-70. Original data are from the International Monetary Fund’s World Economic Outlook database.

IN FOCUS 1.1 Setting the Terms Straight

GDP, GNP, GNI, PPP—there is a bewildering variety of acronyms that are used to measure economic development. It is useful to set these terms straight before proceeding. Gross domestic product (GDP) is measured as the sum of value added by *resident* firms, households, and government operating in an economy. For example, the value added by foreign-owned firms operating in Mexico would be counted as part of Mexico's GDP. However, the earnings of *nonresident* sources that are sent back to Mexico (such as earnings of Mexicans who do not live and work in Mexico and dividends received by Mexicans who own non-Mexican stocks) are not included in Mexico's GDP. One measure that captures this is **gross national product** (GNP). More recently, the World Bank and other international organizations have used a new term, **gross national income** (GNI), to supersede GNP. Conceptually, there is no difference between GNI and GNP. What exactly is GNI/GNP? It comprises GDP plus income from nonresident sources abroad.

Although GDP, GNP, and now GNI are often used as yardsticks of economic development, differences in cost of living make such a direct comparison less meaningful. A

dollar of spending in, say, Thailand can buy a lot more than in Japan. Therefore, conversion based on purchasing power parity (PPP) is often necessary (Chapter 7 has more details). The Swiss per capita GNI is \$54,930 based on official (nominal) exchange rates—*higher* than the US per capita GNI of \$43,740. However, everything is more expensive in Switzerland. A Big Mac costs \$5.20 in Switzerland versus \$3.41 in the United States. Thus, Switzerland's per capita GNI based on PPP becomes \$37,080—*lower* than the US per capita GNI based on PPP, \$41,950. On a worldwide basis, measured at official exchange rates, emerging economies' share of global GDP is approximately 26%. However, measured at PPP, it had doubled by 2005 to about *half* of the global GDP. Overall, when we read statistics about GDP, GNP, and GNI, always pay attention to whether these numbers are based on official exchange rates or PPP, which can make a huge difference.

Sources: Based on (1) *Economist*, 2007, The Big Mac index: Sizzling, July 7: 74; (2) *Economist*, 2006, Climbing back, January 21: 69; (3) *Economist*, 2006, Grossly distorted picture, February 11: 72; (4) World Bank, 2007, *World Development Report 2007*, Washington, DC: World Bank.

gross national product

measured as the sum of value added by *resident* firms, households, and government operating in an economy

gross national income

GDP plus income from nonresident sources abroad. GNI is the term used by the World Bank and other international organizations to supersede the term GNP.

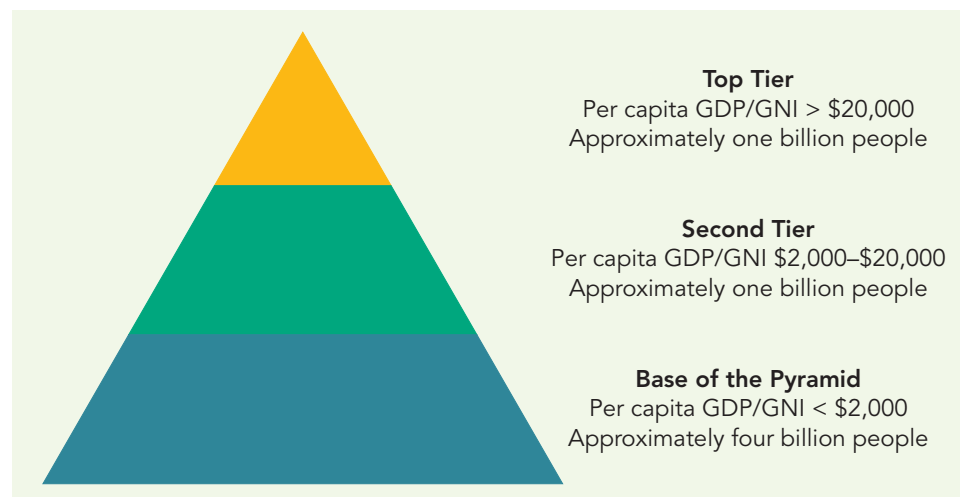
Triad

Three regions (North America, Western Europe, and Japan) of about one billion people with per capita annual income of \$20,000 or higher.

developed economies. For example, \$1 spent in Mexico can buy a lot more than \$1 spent in the United States. The rapid growth of some emerging economies is evident.⁵ A recent *Economist* survey of 555 executives from 68 countries reports that emerging economies command their utmost attention.⁶

The global economy can be viewed as a pyramid (Figure 1.2). The top consists of about one billion people with per capita annual income of \$20,000 or higher. They are mostly in developed economies in the **Triad**, three regions that consist of North America, Western Europe, and Japan. The second tier consists of another billion people making \$2,000 to \$20,000 a year. The vast majority of humanity, about four billion people, live at the base of this pyramid making less than \$2,000 a year. Most

FIGURE 1.2 THE GLOBAL ECONOMIC PYRAMID



Sources: Adapted from (1) C. K. Prahalad & S. Hart, 2002, The fortune at the bottom of the pyramid, *Strategy + Business*, 26: 54–67, and (2) S. Hart, 2005, *Capitalism at the Crossroads* (p. 111), Philadelphia: Wharton School Publishing.

MNEs (and most traditional IB books) focus on the top and second tiers. They end up ignoring the **base of the pyramid**.⁷ An increasing number of such low-income countries have shown a great deal of economic opportunities with rising income levels (In Focus 1.2). Today's students—and tomorrow's business leaders—will ignore these opportunities at the base of the pyramid at their own peril. This book will help ensure that you will not ignore these opportunities (see Closing Case).

base of the pyramid

The vast majority of humanity, about four billion people, live at the base of the pyramid and make less than \$2,000 a year.

WHY STUDY GLOBAL BUSINESS?

Global business (or IB) is one of the most exciting, challenging, and relevant subjects offered by business schools. In addition to the requirements at your business school that usually classify this course as a required (compulsory) or recommended course, there are at least two compelling reasons you should study it.

First, because many ambitious students aspire to join the top ranks of large firms, expertise in global business is often a prerequisite. Today, it is increasingly difficult, if not impossible, to find top managers at large firms without significant global competence. Of course, eventually, hands-on global experience, not merely knowledge acquired from this course, will be required.⁸ However, mastery of the knowledge of, and demonstration of interest in, global business during your education will set you apart as a more ideal candidate to be selected as an **expatriate manager**—a manager who works abroad, or “expat” in short—to gain such experience (see Chapter 15 for details).

Thanks to globalization, low-level jobs not only command lower salaries but are also more vulnerable. However, top-level jobs, especially those held by expats, are both financially rewarding and relatively secure. Expats often command a

LEARNING OBJECTIVE 2

articulate what you hope to learn by reading this book and taking this course

expatriate manager

A manager who works abroad (expat in short).

IN FOCUS 1.2 It's the Base of the Pyramid Calling

What magical device can boost entrepreneurship, provide an alternative to bad roads, widen farmers' and fishermen's access to markets, and allow swift and safe transfers of money? It is . . . a mobile (cell) phone! At the base of the global economic pyramid, where fixed-line phones are rare or nonexistent, mobile phones are often the very first telephone networks widely deployed. In a typical country at the base of the pyramid, an increase of ten mobile phones per 100 people reportedly boosts GDP growth by 0.6%. Not surprisingly, the most explosive growth is found in the poorest region of the world: sub-Saharan Africa. In 2006, subscriber growth rates in Chad, Liberia, and Zambia were 292%, 172%, and 138%, respectively. Of course, such growth was based on a very low penetration level: In sub-Saharan Africa, there were three mobile phones per 100 people in 2001. Now there are eight mobile phones per 100. In comparison, the ratio is above 50 mobile phones per 100 people in developed economies.

As the demand takes off at the base of the pyramid, mobile phone makers and service providers cannot be happier. The reason is simple: At the top of the pyramid, market penetration is reaching saturation. The “race to the bottom” is challenging because customers demand rock-bottom prices of \$50 or less per handset. For now, the only serious contenders for this segment, which is predicted to grow 100% annually for the next five years, are

Nokia and Motorola, the world's number one and number two makers, respectively. Their tremendous volume gives them hard-to-beat economies of scale. Samsung, LG, and Sony Ericsson have not yet announced plans to sell less-than-\$50 handsets, preferring to rake in profits at the high end. Chinese makers such as Bird and TCL find that their volume is not high enough to match the efficiencies enjoyed by Nokia and Motorola, so they lose money on low-end phones. Many customers at the base may be illiterate, but they are brand conscious. At the same price, they prefer Nokia and Motorola over unknown brands. Already, both Nokia and Motorola are further consolidating their position by making models for as little as \$25, while still maintaining margins at approximately 30%, which is comparable to their margin around the world. Overall, this is a win-win solution for numerous emerging economies eager to develop and for the few farsighted and capable mobile phone makers to do what C. K. Prahalad, a guru on the base of the pyramid, preaches: serving the world's poor, *profitably*.

Sources: Based on (1) *Business Week*, 2005, Cell phones for the people, November 14: 65; (2) *Economist*, 2005, Calling across the divide, March 12: 74; (3) *Economist*, 2006, Mobile phones in Africa, February 4: 94; (4) C. K. Prahalad & A. Hammond, 2002, Serving the world's poor, profitably, *Harvard Business Review*, September: 48–57; (5) C. K. Prahalad & S. Hart, 2002, The fortune at the bottom of the pyramid, *Strategy + Business*, 26 (1): 2–14.



What are some of the benefits you might enjoy as an expatriate worker?

international premium

A significant pay raise commanded by expats when working overseas.

significant **international premium** in compensation—a significant pay raise when working overseas. In US firms, their total compensation package is approximately \$250,000 to \$300,000 (including benefits; not all is take-home pay). To put it bluntly, if a 2,000-employee ball-bearing factory in Lima, Ohio is shut down and the MNE sets up a similar factory in Lima, Peru, only about ten to twenty jobs would be saved. Yes, you guessed it: These jobs are a few top-level positions such as the CEO, CFO, CIO, factory director, and chief engineer. These managers will be sent by the MNE as expats to Peru to start up operations there. Because it is regarded as a “hardship” assignment, the MNE has to give them many more perks in Peru than in Ohio. How about company-subsidized luxury

housing plus maid services, free tuition for children in American or international schools in Peru, and all-expenses paid vacation for the whole family to see their loved ones in Ohio? Moreover, these expats do not live in Peru forever. When they return to the United States after a tour of duty (usually two or three years), if their current employer does not provide attractive career opportunities, they are often hired by competing firms. This is because competing firms are also interested in globalizing their business by tapping into the expertise and experience of these former expats. And yes, to hire away these internationally experienced managers, competing firms will have to pay them an even larger premium. This indeed is a virtuous cycle.

This hypothetical example serves two purposes in motivating you: (1) Study hard, and someday you can become one of these sought-after, globetrotting managers. (2) If you do not care about being expats, do you really want to join the ranks of the unemployed due to such layoffs? If this scenario is too hypothetical, check out the 1998 movie *The Full Monty*. It portrays how laid-off steelworkers, to make a living, pick up an “alternative” line of work that my editors do not allow me to mention here—psst . . . it’s male strip dancing.

Second, even for graduates at large companies with no aspiration to compete for the top job and for individuals who work at small firms or are self-employed, you may find yourself dealing with foreign-owned suppliers and buyers, competing with foreign-invested firms in your home market, and perhaps even selling and investing overseas. Alternatively, you may find yourself working for a foreign-owned firm, your domestic employer acquired by a foreign player, or your unit ordered to shut down for global consolidation. This is a very likely scenario because approximately 80 million people worldwide, including 18 million Chinese, six million Americans, and one million British, are employed by foreign-owned firms. Understanding how global business decisions are made may facilitate your own career in such firms.⁹ If there is a strategic rationale to downsize your unit, you would want to be able to figure this out and be the first one to post your résumé on Monster.com. In other words, it is your career that is at stake. Don’t be the last in the know!

In short, in this age of global competition, “how do you keep from being Bangalored? Or Shanghaied?”¹⁰ (That is, have your job outsourced to India or China.) A good place to start is to study hard and do well in your IB course.

LEARNING OBJECTIVE 3

identify one most fundamental question and two core perspectives that provide a framework for studying this field

A UNIFIED FRAMEWORK

Global business is a vast subject area. It is one of the few courses that will make you appreciate why your university requires you to take a number of (seemingly unrelated) courses in general education. Here, we draw on major social sciences

that you have probably studied in general education, such as economics, geography, history, psychology, political science, and sociology, as well as a number of business disciplines such as finance and marketing. It is very easy to lose sight of the “forest” while scrutinizing various “trees” or even “branches.” The subject is not difficult, and most students find it to be fun. The number one student complaint (based on previous student feedback) is an overwhelming amount of information, which is also my number one complaint as your author.

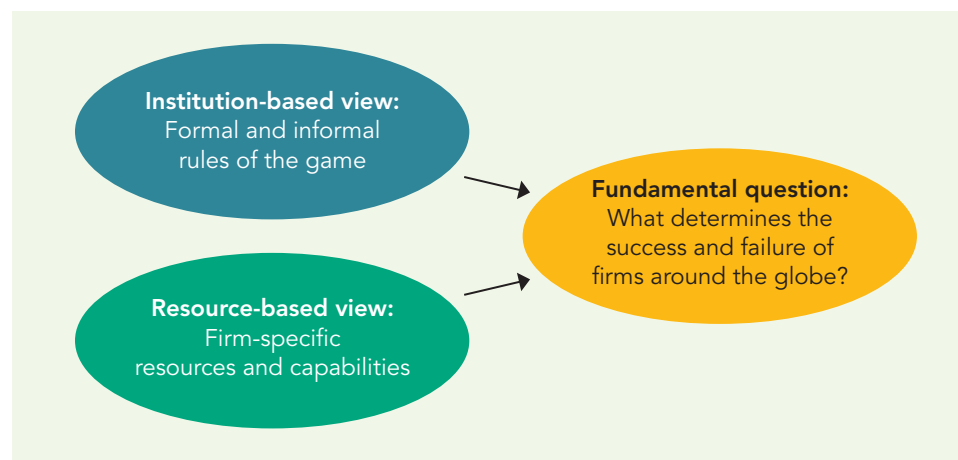
To proactively address your possible complaint and make your learning more manageable (and ideally, more fun), we will develop a unified framework as a consistent theme to cover *all* chapters (Figure 1.3). This will provide great continuity to facilitate your learning. Specifically, we will discipline ourselves by focusing on only one most fundamental question. A fundamental question acts to define a field and to orient the attention of students, practitioners, and scholars in a certain direction. Our “big question” is: *What determines the success and failure of firms around the globe?*¹¹ To answer this question, we will introduce only two core perspectives throughout this book: (1) an institution-based view and (2) a resource-based view. The remainder of this section outlines why this is the case.

One Fundamental Question

What is it that we do in global business? Why is it so important that practically every student in a business school around the world is either required or recommended to take this course? Although there are certainly a lot of questions to raise, a relentless interest in “what determines the success and failure of firms around the globe?” serves to unify the energy of our field. Global business, fundamentally, is about not limiting yourself to your home country and about treating the entire global economy as your potential playground (or battlefield). Some firms may be successful domestically. However, when they venture abroad, they fail miserably. Other firms successfully translate their strengths from their home market to other countries. If you were to lead your firm’s efforts to enter a particular foreign market, wouldn’t you want to find out what is behind the success and failure of other firms in that market?

Overall, the focus on firm performance around the globe, more than anything else, defines the field of global business. Numerous other questions all relate in one way or another to this most fundamental question. Therefore, the primary focus of this book is to answer this question: What determines the success and failure of firms around the globe?

FIGURE 1.3 A UNIFIED FRAMEWORK FOR GLOBAL BUSINESS



First Core Perspective: An Institution-Based View¹²

In layperson's terms, institutions are the "rules of the game." Doing business around the globe requires intimate knowledge about the formal and informal rules governing competition in various countries. It is difficult to imagine that ignorant firms not doing their "homework" to know the rules of the game in a certain country will emerge as winners. In a nutshell, an institution-based view suggests that success and failure of firms are enabled and constrained by the different rules of the game.

Some *formal* rules of the game, such as the requirements to treat domestic and foreign firms as equals, would enhance the potential odds for foreign firms' success. Hong Kong is well known to treat all comers, ranging from neighboring mainland China (whose firms are still technically regarded as "nondomestic") to far-away Chile, the same as it treats indigenous Hong Kong firms. It is thus not surprising that Hong Kong attracts a lot of outside firms. Other rules of the game, which may discriminate against foreign firms, would undermine the chances for foreign entrants. India's recent attraction as a site for foreign investment in IT/BPO (see Opening Case) was only possible after it changed its FDI regulations from confrontational to accommodating. Prior to 1991, India's rules severely discriminated against foreign firms. As a result, few foreign firms bothered to show up there, and the few that did had a hard time. For example, in the 1970s, Coca-Cola was confronted by the Indian government to either get out of India or hand over the recipe for its secret syrup, which it did not (and still does not) share even with the US government. Painfully, Coca-Cola chose to leave India. Its return to India since the 1990s speaks volumes about the changing rules of the game in India.

In addition to formal rules, *informal* rules such as cultures, ethics, and norms play an important part in shaping the success and failure of firms around the globe. For example, because founding new firms tends to deviate from the social norm of working for other bosses, individualistic societies, led by the English-speaking countries such as Australia, Britain, and the United States, tend to have a relatively higher level of entrepreneurship as reflected in the number of business start-ups. Conversely, collectivistic societies such as Japan often have a hard time fostering entrepreneurship; most people there refuse to stick their neck out to found new businesses, which is against the norm.¹³

Overall, an institution-based view suggests that the formal and informal rules of the game, known as institutions, shed a great deal of light on what is behind firm performance around the globe.¹⁴

Second Core Perspective: A Resource-Based View¹⁵

The institution-based view suggests that firms' success and failure around the globe are largely determined by their environments. This is certainly correct, as evidenced by, for example, the fact that India failed to attract much FDI prior to 1991 and that Japan does not nurture a lot of internationally competitive start-ups. However, insightful as this perspective is, there is a major drawback. If we push this view to its logical extreme, then firm performance around the globe would be entirely determined by their environments. The validity of this extreme version is certainly questionable.

In many ways, the resource-based view has emerged to overcome this drawback. While the institution-based view primarily deals with the *external* environment, the resource-based view focuses on a firm's *internal* resources and capabilities. It starts with a simple observation: In harsh, unattractive environments,

most firms either suffer or exit. However, against all odds, a few superstars thrive in these environments. For instance, despite the former Soviet Union's declared hostility toward the United States during the Cold War, PepsiCo had been successfully operating in the former Soviet Union starting in the 1970s (!). In the global airline industry, where most of the major airlines around the world have been losing money since September 11, 2001, a small number of players, such as Southwest in the United States and Ryanair in Ireland, have been raking in profits year after year. How can these firms succeed in highly unattractive and often hostile environments? A short answer is that PepsiCo, Southwest, and Ryanair must have certain valuable and unique *firm-specific* resources and capabilities that are not shared by competitors in the same environments.

Doing business outside one's home country is challenging. Foreign firms have to overcome a **liability of foreignness**, which is the *inherent* disadvantage that foreign firms experience in host countries because of their nonnative status.¹⁶ Just think about all the differences in regulations, languages, cultures, and norms. Against such significant odds, the primary weapon foreign firms employ is overwhelming resources and capabilities that after offsetting the liability of foreignness, still result in some significant competitive advantage. Today, many of us take it for granted that year in and year out, Toyota Camry is the best-selling car in the United States, Coca-Cola is the best-selling soft drink in Mexico, and Microsoft Word is the market-leading word processing software around the world. We really shouldn't take it for granted because it is *not* natural for these foreign firms to dominate nonnative markets. Behind such remarkable success stories, these firms must possess some very rare and powerful firm-specific resources and capabilities that are the envy of their rivals around the globe.

A Consistent Theme

Given our focus on the fundamental question of what determines the success and failure of firms around the globe, we will develop a unified framework by organizing the materials in *every* chapter according to the two core perspectives—namely, institution- and resource-based views. This is the *first* time a global business (or IB) textbook has developed such a consistent theme across all its chapters. Insightful as some of the previous books are, they probably collect too many “trees” or “branches” without assembling a coherent “forest.” Our unified framework—an innovation in IB books—guides our exploration of the global business “forest.”



liability of foreignness

The inherent disadvantage that foreign firms experience in host countries because of their nonnative status.

What are some factors that have contributed to this firm's success, despite a hostile business environment?

WHAT IS GLOBALIZATION?

The rather abstract five-syllable word **globalization** is now frequently heard and debated.¹⁷ Those who approve of globalization count its contributions to include higher economic growth and standards of living, increased sharing of technologies, and more extensive cultural integration. Critics argue that globalization undermines wages in rich countries, exploits workers in poor countries, and gives MNEs too much power. So, what exactly is globalization? This section (1) outlines three views of it, (2) recommends the “pendulum” view, and (3) introduces the idea of “semiglobalization.”

LEARNING OBJECTIVE 4

participate in the debate on globalization with a reasonably balanced and realistic view and a keen awareness of your likely bias in favor of globalization

globalization

The close integration of countries and peoples of the worlds.

Three Views of Globalization

Depending on what sources you read, globalization could be

- A new force sweeping through the world in recent times
- A long-run historical evolution since the dawn of human history
- A pendulum that swings from one extreme to another from time to time

An understanding of these views helps put things in perspective. First, opponents of globalization suggest that it is a new phenomenon since the late 20th century, driven by both the recent technological innovations and Western hypocrisy designed for MNEs to exploit and dominate the world. While presenting few clearly worked-out alternatives to the present economic order, other than an ideal world free of environmental stress, social injustice, and branded sportswear (allegedly made in “sweatshops”), pundits of this view nevertheless often argue that globalization needs to be slowed down if not stopped.¹⁸ Most antiglobalization protesters seem to share this view.

A second view contends that globalization has always been part and parcel of human history.¹⁹ Some historians are debating whether globalization started 2,000 or 8,000 years ago. MNEs existed for more than two millennia, with their earliest traces discovered in Assyrian, Phoenician, and Roman Empires.²⁰ International competition from low-cost countries is nothing new. In the first century A.D., so concerned was the Roman Emperor Tiberius about the massive quantity of low-cost Chinese silk imports that he imposed the world’s first known import quota of textiles.²¹ Today’s most successful MNEs do not come close to wielding the historical clout of some MNEs such as Britain’s East India Company during colonial times. In a nutshell, globalization is nothing new and will always march on.

A third view suggests that globalization is the “closer integration of the countries and peoples of the world which has been brought about by the enormous reduction of the costs of transportation and communication, and the breaking down of artificial barriers to the flows of goods, services, capital, knowledge, and (to a lesser extent) people across borders.”²² Globalization is neither recent nor one directional. It is, more accurately, a process similar to the swing of a pendulum.

The Pendulum View of Globalization

The third, pendulum view probably makes the most sense because it can help us understand the ups and downs of globalization. The current era of globalization originated in the aftermath of World War II, when major Western nations committed to global trade and investment. However, between the 1950s and 1970s, this view was not widely shared. Communist countries, such as China and the (former) Soviet Union, sought to develop self-sufficiency. Many noncommunist developing countries, such as Argentina, Brazil, India, and Mexico, focused on fostering and protecting domestic industries. However, refusing to participate in global trade and investment ended up breeding uncompetitive industries. In contrast, four developing economies in Asia—namely, Hong Kong, Singapore, South Korea, and Taiwan—earned their stripes as the “Four Tigers” by participating in the global economy. They become the *only* economies once recognized as less developed (low-income) by the World Bank to have subsequently achieved developed (high-income) status.

Inspired by the Four Tigers, more and more countries, such as China in the late 1970s, Latin America in the mid-1980s, Central and Eastern Europe in the late 1980s, and India in the 1990s, realized that joining the world economy was a must. As these countries started to emerge as new players in the world economy, they become collectively known as “emerging economies” (as discussed earlier).²³ As a result, globalization rapidly accelerated. For example, between 1990 and 2000,

while world output grew by 23%, global trade expanded by 80% and the total flow of FDI increased fivefold.²⁴

However, as a pendulum, globalization is unable to keep going in one direction. The 1990s, a period of very rapid globalization, saw some significant backlash against it. First, the rapid growth of globalization led to the historically inaccurate view that globalization is new. Second, it created fear among many people in developed economies because emerging economies not only seem to compete away many low-end manufacturing jobs but also increasingly appear to threaten some high-end jobs. Finally, some factions in emerging economies complained against the onslaught of MNEs, which allegedly not only destroy local companies but also local cultures and values as well as the environment. Many people in Indonesia, South Korea, and Thailand devastated by the 1997 Asian economic crisis bitterly resented the pre-1997 policies of rapid capital market liberalization, which made these countries subject to both the irrational exuberance and pessimism of the global investment community. They further resented the “rescue” policies of the International Monetary Fund (IMF) that might have exacerbated the downturns²⁵ (see Chapter 7).

Although small-scale acts of vandalizing McDonald’s restaurants are reported in a variety of countries, the December 1999 antiglobalization protests in Seattle and the September 2001 terrorist attacks in New York and Washington are undoubtedly the most visible and most extreme acts of antiglobalization forces at work. As a result, international travel was curtailed, and global trade and investment flows slowed in the early 2000s.²⁶

More recently, worldwide economic growth has again been humming on all cylinders. World GDP, cross-border trade, and per capita GDP have all soared to historically high levels. More than half of the world GDP growth now comes from emerging economies, whose per capita GDP grew 4.6% annually in the decade ending 2007. **BRIC** (a newly coined acronym for Brazil, Russia, India, and China) has become a new buzzword. Developed economies are also doing well, averaging 2% per capita GDP growth during the same period. *Fortune* in 2007 declared that “for your average globetrotting *Fortune* 500 CEO, right now is about as good as it gets.”²⁷ Yet, the same article cautioned, “Assuming history at some point proves yet again unkind . . . it pays to be vigilant.”

Overall, like the proverbial elephant, globalization is seen by everyone and rarely comprehended. All of us felt sorry when we read the story of a bunch of blindmen trying to figure out the shape and form of an elephant. Although we are not blind, our task is more challenging than the blindmen who study a standing animal. This is because we (1) try to live with, (2) avoid being crushed by, and (3) even attempt to profit from a rapidly moving (back and forth!) beast called globalization. We believe that the view of globalization as a pendulum is a more balanced and realistic perspective. Like the two-faced Janus (a Roman god), globalization has both rosy and dark sides.²⁸

Semiglobalization

Most measures of market integration (such as trade and FDI) have recently scaled new heights but still fall far short of complete globalization. In other words, what we have may be labeled **semiglobalization**, which is more complex than extremes of total isolation and total globalization. Semiglobalization suggests that barriers to market integration at borders are high but not high enough to completely insulate countries from each other.²⁹ Semiglobalization calls for more than one way for doing business around the globe. Total isolation on a nation-state basis would suggest localization (treating each country as a unique market) and total globalization would lead to standardization (treating the entire world as one market), but there is no single correct strategy in the world of semiglobalization, which results in a wide variety of experimentations.³⁰ Overall, (semi)globalization is neither to be opposed as a menace nor to be celebrated as a panacea; it is to be *engaged*.³¹

BRIC

A newly coined acronym for the emerging economies of Brazil, Russia, India, and China.

semiglobalization

A business strategy that suggests that barriers to market integration at borders are high but not high enough to completely insulate countries from each other.

LEARNING OBJECTIVE 5

have a basic understanding of the future of the global economy and its broad trends

GLOBAL BUSINESS AND GLOBALIZATION AT A CROSSROADS

The challenge confronting a new generation of business leaders in the 21st century is enormous. This book will provide you with a road map. As a backdrop for the remainder of this book, this section makes two points. First, a basic understanding of the world economy is necessary. Second, it is important to critically examine your own personal views and biases on globalization.

A Glance of the World Economy

The world economy at the beginning of the 21st century is an approximately \$48 trillion economy (total global GDP calculated at official, nominal exchange rates). Although there is no need to memorize a lot of statistics, it is useful to remember this \$48 trillion figure to put things in perspective.

A frequent observation in the globalization debate is the enormous size of MNEs. Table 1.1 ranks sales of the world’s largest MNEs alongside the GDP of the world’s largest countries. The size of these leading MNEs is indeed striking: 47 of the world’s top 100 economic entities are companies. If the two largest MNEs, US-based Wal-Mart and Exxon Mobil, were independent countries, they would be the 22nd and 23rd largest economies, respectively (their sales are smaller than

TABLE 1.1 TOP 100 ECONOMIES (GDP) AND COMPANIES (SALES)

Rank	Company	Country	US \$ Millions	Rank	Company	Country	US \$ Millions
1		United States	13,201,819	21		Indonesia	364,459
2		Japan	4,340,133	22	Wal-Mart Stores	(US)	351,139
3		Germany	2,906,681	23	Exxon Mobil	(US)	347,254
4		China	2,668,071	24		Poland	338,733
5		United Kingdom	2,345,015	25		Austria	322,444
6		France	2,230,721	26	Royal Dutch Shell	(UK/ Netherlands)	318,845
7		Italy	1,844,749	27		Norway	310,960
8		Canada	1,251,463	28		Saudi Arabia	309,778
9		Spain	1,223,988	29		Denmark	275,237
10		Brazil	1,067,962	30	BP	(UK)	274,316
11		Russian Federation	986,940	31		South Africa	254,992
12		India	906,268	32		Greece	244,951
13		South Korea	888,024	33		Iran	222,889
14		Mexico	839,182	34		Ireland	222,650
15		Australia	768,178	35		Argentina	214,058
16		Netherlands	657,590	36		Finland	209,445
17		Turkey	402,710	37	General Motors	(US)	207,349
18		Belgium	392,001	38		Thailand	206,247
19		Sweden	384,927	39	Toyota Motor	(Japan)	204,746
20		Switzerland	379,758	40	Chevron	(US)	200,567

AQ: We could not fit Table 1.1 across the page because of the way the text callout fell. We think because the columns simply snake and the tables is already split in two that running the table from one page to the next made sense. OK?

Table 1.1 (continued)

Rank	Company	Country	US \$ Millions	Rank	Company	Country	US \$ Millions
41		Portugal	192,572	71	AIG	(US)	113,194
42	Daimler Chrysler	(Germany)	190,191	72		Hungary	112,899
43		Hong Kong, China	189,798	73	China National Petroleum	(China)	110,520
44		Venezuela	181,862	74	BNP Paribas	(France)	109,214
45	Conoco Phillips	(US)	172,451	75	ENI	(Italy)	109,014
46	Total	(France)	168,351	76	UBS	(Switzerland)	107,835
47	General Electric	(U.S)	168,307	77		Egypt	107,484
48	Ford Motor	(US)	160,126	78	Siemens	(Germany)	107,342
49	ING Group	(Netherlands)	158,274	79	State Grid	(China)	107,182
50		Malaysia	148,940	80		Ukraine	106,111
51	Citigroup	(US)	146,777	81		New Zealand	103,873
52		Chile	145,841	82	Assicurazioni Generali	(Italy)	101,811
53		Czech Republic	141,801	83	J. P. Morgan Chase	(US)	99,973
54	AXA	(France)	139,738	84	Carrefour	(France)	99,015
55		Colombia	135,836	85	Berkshire Hathaway	(US)	98,539
56	Volkswagen	(Germany)	132,323	86	Pemex	(Mexico)	97,469
57		Singapore	132,158	87	Deutsche Bank	(Germany)	96,152
58	Sinopec	(China)	131,636	88	Dexia Group	(Belgium)	95,847
59		United Arab Emirates	129,702	89	Honda Motor	(Japan)	94,790
60		Pakistan	128,830	90	McKesson	(US)	93,574
61	Crédit Agricole	(France)	128,481	91		Peru	93,269
62	Allianz	(Germany)	125,346	92	Verizon	(US)	93,221
63		Israel	123,434	93	NTT	(Japan)	91,998
64		Romania	121,609	94	Hewlett-Packard	(US)	91,658
65	Fortis	(Belgium/Netherlands)	121,202	95	IBM	(US)	91,424
66	Bank of America	(US)	117,017	96	Valero Energy	(US)	91,051
67		Philippines	116,931	97	Home Depot	(US)	90,837
68	HSBC Holdings	(Britain)	115,361	98	Nissan Motor	(Japan)	89,502
69		Algeria	114,727	99	Samsung Electronics	(South Korea)	89,476
70		Nigeria	114,686	100	Credit Suisse	(Switzerland)	89,354

Sources: Adapted from (1) World Development Indicators database, World Bank, <http://www.worldbank.org> (accessed July 12, 2007) and (2) *Fortune*, 2007, The Fortune Global 500, <http://www.fortune.com> (accessed July 12, 2007). Numbers are rounded by the author. All numbers refer to 2006 data.

Indonesia's GDP but larger than Poland's). The sales of the largest EU-based MNE, Royal Dutch Shell, were larger than the GDP of Norway, Denmark, Greece, and Ireland—all EU members. The sales of the largest Asia-Pacific-based MNE, Toyota, were greater than the GDP of Malaysia, Singapore, and New Zealand.

In 2006, over 77,000 MNEs controlled at least 770,000 subsidiaries overseas.³² Total annual sales of the largest 500 MNEs exceed \$20 trillion (about 40% of global output). Table 1.2 documents the change in the makeup of the 500 largest MNEs. Figure 1.4 tracks the changes between 1996 and 2006, during which revenues nearly doubled. In general, over 80% of the 500 largest MNEs come from the Triad. Since 1990, the United States has contributed about one-third of these firms, the European Union has maintained a reasonably steady increase, and Japan has experienced the most dramatic variation (roughly corresponding to its economic boom and bust with several years of delay).

Among MNEs from emerging economies, those from South Korea and Brazil have largely maintained their presence in the *Fortune* Global 500. MNEs from China have come on strong—Beijing is now headquarters of 18 *Fortune* Global 500 firms, four fewer than New York City. Table 1.3 shows that in select industries, these MNEs, often regarded as “Third World multinationals” or “dragon multinationals,” have joined the top ranks.³³ Clearly, Western rivals cannot afford to ignore them, and students reading this book need to pay attention to these emerging multinationals.

The Globalization Debate and You

At the dawn of the 21st century, the seemingly one-directional march of globalization started to show its color as a pendulum, which has direct ramifications for you as a future business leader, a consumer, and a citizen. At least two sets of sudden, high-profile events have occurred that have significant ramifications for business around the world: (1) antiglobalization protests and (2) terrorist attacks. First,

TABLE 1.2 CHANGES IN THE *FORTUNE* GLOBAL 500, 1990–2006

Country/bloc	1990	1991	1992	1993	1994	1995	1996	1997
United States	164	157	161	159	151	153	162	175
European Union	129	134	126	126	149	148	155	155
Japan	111	119	128	135	149	141	126	112
Canada	12	9	8	7	5	6	6	8
South Korea	11	13	12	12	8	12	13	12
Switzerland	11	10	9	9	14	16	14	12
China	0	0	0	0	3	2	3	4
Australia	9	9	9	10	3	4	5	7
Brazil	3	1	1	1	2	4	5	5
Others	50	48	46	41	16	14	11	10
Total	500	500	500	500	500	500	500	500

large-scale antiglobalization protests began in December 1999, when more than 50,000 protesters blocked downtown Seattle in an attempt to derail a ministerial meeting of the World Trade Organization (WTO). The demonstrators were protesting against a wide range of issues, including job losses resulting from foreign competition, downward pressure on unskilled wages, and environmental destruction. Since Seattle, antiglobalization protestors have turned up at just about every major globalization meeting, and some protests have become violent. It is obvious that numerous individuals in many countries believe that globalization has detrimental effects on living standards and the environment. As shown throughout this book, the debate on globalization has numerous dimensions, and neither the proglobalization forces nor the antiglobalization forces have won the debate.³⁴

A second set of events center on terrorist attacks in New York and Washington on September 11, 2001, and the resultant war on terror in Afghanistan, Iraq, and elsewhere. Since then, terrorists struck Indonesia, Spain, and Britain. Terrorism, which used to be “a random political risk of relatively insignificant proportions,”³⁵ is now a leading concern for business leaders around the globe.³⁶ Heightened risk of terrorism has (1) reduced freedom of international movement as various countries curtail visas and immigration, (2) enhanced security checks at airports, seaports, and land border crossing points (see In Focus 1.3), and (3) canceled or scaled down trade and FDI deals, especially in high-risk regions such as the Middle East.

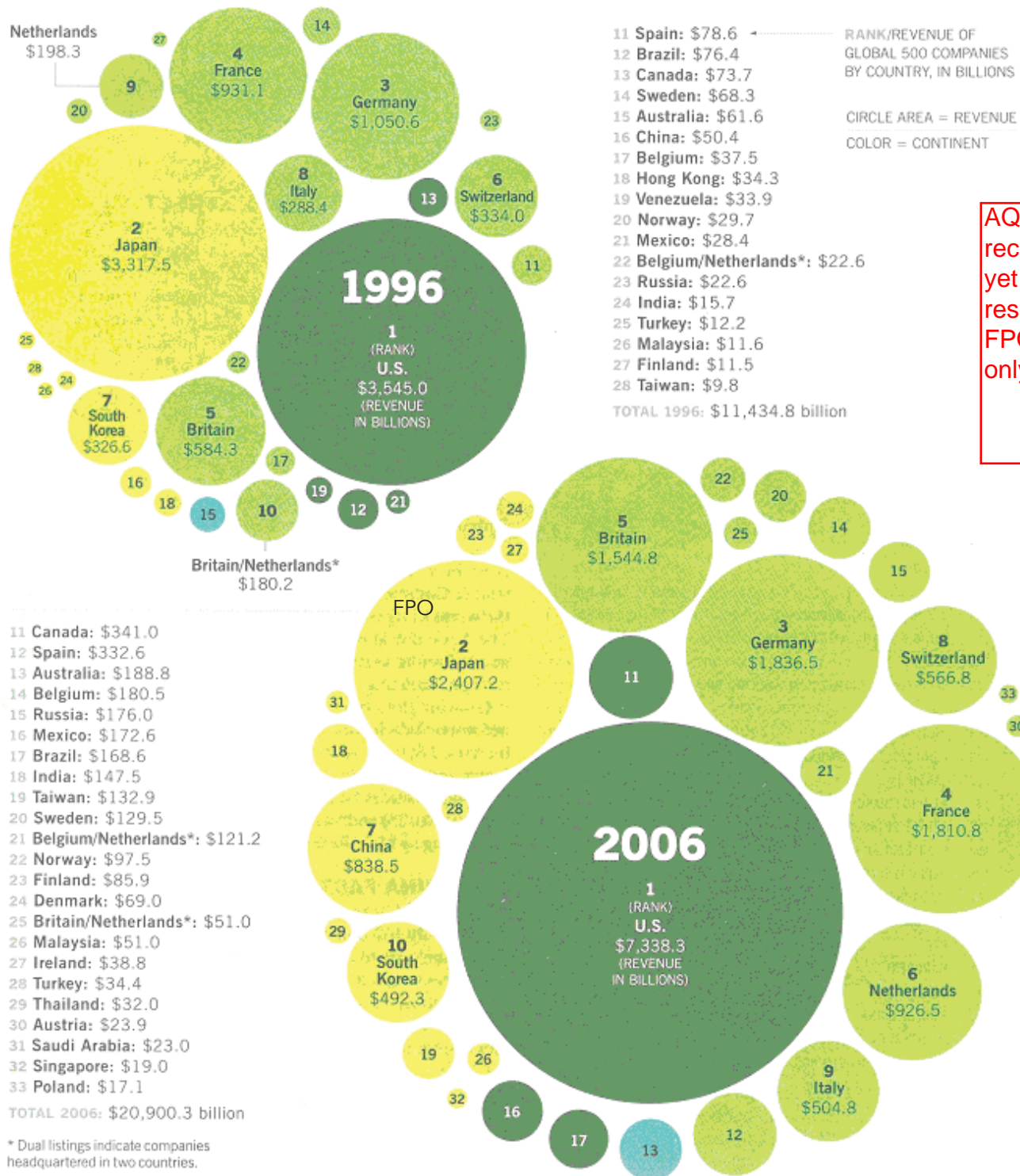
As a future business leader, you are not reading this book as a disinterested reader—as you would when reading a history book. The globalization debate directly affects *your* future.³⁷ Therefore, it is imperative that you participate in the globalization debate, instead of letting other people make decisions on globalization that will significantly affect your career, your consumption, and your country. Although this book does not advocate any particular view for your participation in the debate, it is important to know your own biases when joining the debate. By your very act of now taking an IB course and reading this book, you probably already have some proglobalization biases relative to nonbusiness majors elsewhere on campus and the general public in your country.

Table 1.2 (continued)

Country/bloc	1998	1999	2000	2001	2002	2003	2004	2005	2006
United States	185	179	185	178	192	189	176	170	162
European Union	156	148	136	139	150	147	161	165	165
Japan	100	107	95	88	88	100	81	70	67
Canada	12	12	13	5	14	12	13	14	16
South Korea	9	12	8	12	13	9	11	12	14
Switzerland	11	11	10	9	11	12	11	12	13
China	6	10	10	10	11	14	16	20	24
Australia	7	7	7	6	6	7	9	8	8
Brazil	4	3	3	4	4	3	3	4	5
Others	10	11	33	49	11	7	19	25	26
Total	500	500	500	500	500	500	500	500	500

Sources: Based on data from various issues of *Fortune Global 500*. Finland and Sweden are included as “others” prior to 1996 and as European Union after 1996.

FIGURE 1.4 THE FORTUNE GLOBAL 500



Source: Fortune, 2007, The world's largest corporations (p. 101), July 23: 100–103. Revenues of firms headquartered in one country are consolidated into one circle for 1996 and another one for 2006.

TABLE 1.3 TOP-TEN MNEs (BASED ON REVENUES) IN SELECT INDUSTRIES(Companies in **bold** typeface are based in emerging economies)

	Container shipping	Electronics	Mining	Petroleum refining	Steel
1	Moeller Maersk	Siemens	BHP Billiton	Exxon Mobil	Arcelor Mittal
2	Mediterranean	Hitachi	Alcoa	BP	Nippon Steel
3	CMA CGM	Matsushita	Alcan	Shell	JFE Steel
4	Evergreen	Samsung Electronics	Rio Tinto	Total	POSCO
5	Hapag-Lloyd	Sony	Vale do Rio Doce	Chevron	Baosteel
6	China Shipping	Toshiba	Phelps Dodge	Conoco-Philips	US Steel
7	APL	Tyco	Commercial Metals	Sinopec	Corus
8	Hanjin	LG Electronics	Furukawa	ENI	Nucor
9	COSCO	Royal Philips	Inco	CNPC	ThyssenKrupp
10	NYK	Mitsubishi Electric	Aluminum Corp. of China	Valero	Riva

Source: Adapted from United Nations, 2006, *World Investment Report 2006* (p. 123), New York and Geneva: United Nations.

You are not alone. In the last several decades, most elites in both developed and emerging economies—executives, policymakers, and scholars—are biased toward acknowledging the benefits of globalization.³⁸ Although it has long been known that globalization carries both benefits and costs, many elites have failed to take into sufficient account the social, political, and environmental costs associated with globalization. However, that these elites share certain perspectives on globalization does *not* mean that most other members of the society share the same views. Unfortunately, many elites fail to understand the limits of their beliefs and mistakenly

IN FOCUS 1.3 Terrorism, Protectionism, and Homeland Security

In 2004, in response to terrorist attacks, the US Department of Homeland Security awarded a major contract to Accenture LLP to design and implement the US Visitor and Immigrant Status Indicator Technology (US-VISIT) program, which would be deployed at the nation's more than 400 ports of entry. However, several members of Congress noted that Accenture LLP is *not* a US firm and argued that the contract should have been awarded to bona fide US firms—in other words, better homeland security protection calls for protectionism. Accenture LLP is the US-based subsidiary of Accenture Ltd., which is a global technology consulting firm with \$15 billion revenues in 2005. Accenture Ltd. has



123,000 employees in 48 countries, and 25,000 of them are in the United States. Despite Accenture Ltd.'s strong US roots (as part of the now-defunct Arthur Andersen until 1989) and its US stock listing (NYSE: ACN), it is incorporated in Bermuda, and its SEC filings disclose it as a "Bermuda holding company." The dilemma thus boils down to whether outsourcing US-VISIT to the US subsidiary of a Bermuda firm, as opposed to a "pure" US firm, compromises the effectiveness of the program.

Sources: Based on (1) J. Carafano, 2005, *Global terrorism and the global economy*, in *2005 Index of Economic Freedom*, Washington, DC: Heritage Foundation, <http://www.heritage.org>; (2) SEC filings by Accenture Ltd., 2005; (3) <http://www.accenture.com>.

nongovernment organizations

Organizations such as environmentalists, human rights activists, and consumer groups.

assume that the rest of the world is like “us.” To the extent that powerful economic and political institutions are largely controlled by these elites in almost every country, it is not surprising that some powerless antiglobalization groups end up resorting to unconventional tactics (such as mass protests) to make their point.

A lot of opponents of globalization are **nongovernment organizations** (NGOs), such as environmentalists, human rights activists, and consumer groups. Ignoring them will be a grave failure in due diligence when doing business around the globe.³⁹ Instead of viewing NGOs as opponents, many firms view them as partners.⁴⁰ NGOs do raise a valid point on the necessity of firms, especially MNEs, to have a broader concern for various stakeholders affected by their actions around the world.⁴¹ At present, this view is increasingly moving from the periphery to the mainstream (see Chapter 17).

It is certainly interesting and perhaps alarming to note that as would-be business leaders who will shape the global economy in the future, current business school students already exhibit values and beliefs in favor of globalization similar to those held by executives, policymakers, and scholars and different from those held by the general public. Shown in Table 1.4, relative to the general public, US business students have significantly more positive (almost one-sided) views toward globalization. While these data are based on US business students, my teaching and lectures around the world suggest that most business students worldwide—regardless of their nationality—seem to share such positive views on globalization. This is not surprising. Both self-selection to study business and socialization within the curriculum, in which free trade is widely regarded as positive, may lead to certain attitudes in favor of globalization. Consequently, business students may focus more on the economic gains of globalization and be less concerned with its darker sides.

Current and would-be business leaders need to be aware of their own biases embodied in such one-sided views of globalization. Since business schools aspire to train future business leaders by indoctrinating students with the dominant values managers hold, these results suggest that business schools may have largely succeeded in this mission. However, to the extent that there are strategic blind spots in the views of the current managers (and professors), these findings are potentially alarming. They reveal that business students already share these blind spots. Despite possible self-selection in choosing to major in business, there is no denying that student values are shaped, at least in part, by the educational experience business schools provide. Knowing such limitations, business school professors and students need to work especially hard to break out of this straightjacket.⁴²

TABLE 1.4 VIEWS OF GLOBALIZATION: AMERICAN GENERAL PUBLIC VERSUS BUSINESS STUDENTS

Percentage answering “good” for the question: Overall, do you think globalization is good or bad for	General public ¹ (N = 1,024)	Business students ² (N = 494)
• US consumers like you	68%	96%
• US companies	63%	77%
• The US economy	64%	88%
• Strengthening poor countries’ economies	75%	82%

Sources: Based on (1) A. Bernstein, 2000, Backlash against globalization, *Business Week*, April 24: 43; (2) M. W. Peng & H. Shin, 2008, How do future business leaders view globalization? *Thunderbird International Business Review* (in press). All differences are statistically significant.

To combat the widespread tendency to have one-sided, rosy views of globalization, a significant portion of this book is devoted to numerous debates. Beyond this chapter (which illustrates a big debate in itself), debates are systematically introduced in *every* chapter to provoke more critical thinking and discussion. Virtually all textbooks uncritically present knowledge “as is” and ignore the fact that the field is alive with numerous debates. No doubt, it is debates that drive practice and research forward. Therefore, it is imperative that you be exposed to cutting-edge debates and encouraged to form your own views when engaging in these debates.⁴³ In addition, ethics is emphasized throughout the book. A featured Ethical Dilemma and a series of Critical Discussion Questions on ethics can be found in every chapter. In addition, two full-blown chapters are devoted to ethics, norms, and cultures (Chapter 3) and corporate social responsibility (Chapter 17).

ORGANIZATION OF THE BOOK

This book has four parts. Part I is *foundations*. Following this chapter, Chapters 2, 3, and 4 deal with the two leading perspectives—institution- and resource-based views. Part II covers *tools*, focusing on trade (Chapter 5), foreign investment (Chapter 6), foreign exchange (Chapter 7), and global and regional integration (Chapter 8). Part III sheds light on *strategy*. We start with the internationalization of small, entrepreneurial firms (Chapter 9), followed by ways to enter foreign markets (Chapter 10), to manage competitive dynamics (Chapter 11), to make alliances and acquisitions work (Chapter 12), and to strategize, structure, and learn (Chapter 13). Finally, Part IV builds *excellence in different functional areas*: marketing and supply chain (Chapter 14), human resource management (Chapter 15), corporate governance (Chapter 16), and corporate social responsibility (Chapter 17).

In closing, most of you were probably surprised by the Opening Case on the global nature of your textbook. Globalization is fascinating, isn't it? This book will reduce the element of surprise by providing a road map as you embark on this journey. Welcome on board!

CHAPTER SUMMARY

1. Explain the concepts of international business (IB) and global business
 - IB is typically defined as (1) a business (firm) that engages in international (cross-border) economic activities and (2) the action of doing business abroad.
 - Global business is defined in this book as business around the globe.
 - This book goes beyond competition in developed economies by devoting extensive space to competitive battles waged in emerging economies and the base of the global economic pyramid.
2. Articulate what you hope to learn by reading this book and taking this course
 - To better compete in the corporate world that will require global expertise.
 - To enhance your understanding of what is going on in the global economy.
3. Identify one most fundamental question and two core perspectives that provide a framework for studying this field
 - Our most fundamental question is: What determines the success and failure of firms around the globe?
 - The two core perspectives are (1) the institution-based view and (2) the resource-based view.

- We develop a unified framework by organizing materials in *every* chapter according to the two perspectives guided by the fundamental question.
4. Participate in the debate on globalization with a reasonably balanced and realistic view and a keen awareness of your own likely bias in favor of globalization
 - Some view globalization as a recent phenomenon, and others believe that it is a one-directional evolution since the dawn of human history.
 - We suggest that globalization is best viewed as a process similar to the swing of a pendulum.
 5. Have a basic understanding of the future of the global economy and its broad trends
 - MNEs, especially large ones from developed economies, are sizable economic entities.
 - Current and would-be business leaders need to be aware of their own hidden proglobalization bias.

KEY TERMS

Base of the pyramid	7	Globalization	11	Liability of foreignness	11
BRIC	13	Gross domestic product (GDP)	5	Multinational enterprise (MNE)	4
Emerging economies (emerging markets)	5	Gross national income (GNI)	6	Nongovernment organization (NGO)	20
Expatriate manager (expat)	7	Gross national product (GNP)	6	Purchasing power parity (PPP)	5
Foreign direct investment (FDI)	4	International business	4	Semiglobalization	13
Global business	5	International premium	8	Triad	6

REVIEW QUESTIONS

1. What is the difference between international business and global business, as defined in this book?
2. Referring to Figure 1.1, how important are emerging economies in the overall global economy?
3. Referring to Figure 1.2, what observations can you make about the three tiers of people in the global economic pyramid?
4. What is your interest in studying global business? How do you think it might apply to your future?
5. If you were to work as an expatriate manager, where would you like to go and what would you like to do?
6. What is the fundamental question driving your study of global business, and why is it important?
7. How would you describe an institution-based view of global business?
8. How would you describe a resource-based view of global business?
9. After comparing the three views of globalization described in this book, which seems the most logical or sensible to you and why?

10. What is semiglobalization, and what factors contribute to it?
11. What do Table 1.2 and Figure 1.4 tell you about changes in the global economy over the last ten to fifteen years?
12. Why do some people protest against globalization? What point do they make that all people, whether for or against globalization, should consider?
13. What can people who are in favor of global business learn from NGOs such as environmentalists, human rights activists, and consumer groups?

CRITICAL DISCUSSION QUESTIONS

1. A classmate says: “Global business is relevant for top executives such as CEOs in large companies. I am just a lowly student who will struggle to gain an entry-level job, probably in a small domestic company. Why should I care about it?” How do you convince her that she should care about it?
2. In his book *The World Is Flat* (2005), Thomas Friedman suggests that the world is flattening—meaning it is increasingly interconnected by new technology such as the Internet. This can raise the poor from poverty, nurture a worldwide middle class, and even spread democracy. On the other hand, this presents significant challenges for developed economies, whose employees may feel threatened by competition from low-cost countries. How does this flattening world affect you?
3. ON ETHICS: What are some of the darker sides (in other words, costs) associated with globalization? How can business leaders make sure that the benefits of their various actions (such as outsourcing discussed in Opening Case) outweigh their drawbacks (such as job losses in developed economies)?
4. ON ETHICS: Some argue that aggressively investing in emerging economies is not only economically beneficial but also highly ethical because it may potentially lift many people out of poverty (see Closing Case). However, others caution that in the absence of reasonable hopes of decent profits, rushing to emerging economies is reckless. How would you participate in this debate?

VIDEO CASE

Watch “International Business” by Sir Bob Reid, Halifax Bank of Scotland.

1. How does the experience of the Nigerians in Japan illustrate what has been covered in this chapter regarding the “informal rules of the game?”
2. What did Sir Reid say which would suggest that “foreignness” is less an issue in West Africa than adaptability?
3. This chapter covered a range of economically developed nations but Sir Reid focused on West Africa—to what extent do his ideas apply to doing business in the highly developed economies?
4. Why did Sir Reid mention the importance of listening?
5. If your school has students from other countries, how can you apply this video to your interaction with those people?

C L O S I N G C A S E

Global Business and Emerging Economies

The bulk of international business takes place among developed economies—also described as high-income countries, Western (plus Japanese) economies, and the First World—which contribute approximately 74% of the global GDP by official (nominal) exchange rates. The UN defines these 44 countries as having per capita incomes in excess of \$9,000. Is it appropriate to continue to focus on them in the 21st century?

Referred to as developing economies, less developed countries, low-income nations, and the Third World, the term *emerging economies* has caught on since the 1990s. One side of the debate argues that emerging economies are the markets of tomorrow, and they are also frequently labeled “emerging markets.” This argument is certainly both true *and* false. Emerging economies consist of 156 countries in various stages of development, accounting for 84% of the world’s population but only approximately 26% of its GDP by official exchange rates. Some of them grow rapidly, whereas many others will be submerging in the years to come. In short, much of the base of the global economic pyramid will remain the base. Advocates for emerging economies concede that the relative economic firepower of even some of the largest emerging economies is limited. For example, Russia’s GDP is smaller than Italy’s and Mexico’s GDP is smaller than Texas’s.

However, what is exciting seems to be the growth potential of some (although not all) emerging economies, especially Brazil, Russia, India, and China—known as BRIC. During the Industrial Revolution, it took America and Britain 50 years to double their GDP. Today, China is achieving that in a single decade. Therefore, if Western firms want to grow, they will have to participate in such growth. For instance, demand for durables such as washers, dryers, and cars is primarily based on replacement needs in the West, whereas in many emerging economies, rising income levels afford numerous first-time purchases of these big-ticket items.

At present, FDI inflows to emerging economies command about one-third of global FDI inflows, \$334 billion of the global total of \$916 billion in 2006. Since FDI inflows to emerging economies trail those to developed economies, the argument goes, Western firms need to *disproportionately* invest in emerging economies. To support this argument, experts note that measured at purchasing power parity (PPP), emerging economies already command 50% of global GDP (see Figure 1.1). More than half of the world GDP *growth* now comes from emerging economies, whose per capita GDP grew 4.6% annually in the decade ending 2007 (developed economies averaged 2% per capita annual GDP growth during the same period). As a result, more and more job descriptions for CEOs in Western MNEs call for explicit business experience on the ground in emerging economies. Boards increasingly are looking for CEOs with passports showing frequent visits to BRIC.



On the other hand, strong arguments have been made against aggressively moving into emerging economies, given their uncertainties. Emerging economies often experience tremendous booms and busts. The Asian “miracle” was suddenly replaced by a major crisis in 1997. Central and Eastern Europe experienced the euphoria of the removal of communism in 1989, which was quickly replaced by a deep recession worsened by the Russian default in 1998. Since 1995, every major Latin America economy was hit by a significant crisis: Mexico (1995), Brazil (1998), Argentina (2002), and Venezuela (2006). China has been periodically hit by crises, ranging from SARS (2003) to the product safety mess (2007).

Overall, emerging economies represent the classic combination of high risk and high (potential) return. A sensible strategy for Western MNEs is to strike a balance between developed and emerging economies. Strong performance in emerging economies may significantly contribute to the worldwide corporate bottom line. Volkswagen, for instance, derives approximately one-third of its *worldwide* profits from China alone. For another example, consider water. General

Electric (GE) is working on water-desalination systems in the Middle East at \$0.001 per millimeter, which, according to GE's CEO Jeff Immelt, is "off-the-charts low cost." "We will never hit that in the US," Immelt continued, "But we'll hit it someplace outside. And the second we do, a huge market is going to open up inside as well." Likewise, GE is working in China on a magnetic resonance imaging (MRI) scanner that could cut price in half. "At the right cost point, you not only sell it in China," Immelt commented, "you open up a market among the 35% of US hospitals that today cannot afford to have an MRI scanner."

However, the expertise of Western MNEs, profiting from high-income customers at the top of the global pyramid, requires significant adaptation. For instance, bragging about shampoo-and-conditioner-in-one (otherwise known as 2-in-1) is of little relevance to customers who have never used shampoo or conditioner. Entering emerging economies with a warehouse-style retail format suitable for markets with a high level of car ownership (such as COSTCO and Sam's Club) is unlikely to reach the masses, who usually do not have cars.

Despite significant differences, emerging economies have enough common underlying logic to justify developing an alternative business model based on price/value trade-offs different from those in developed economies. General Motors and Honda are racing to develop \$5,000 entry-level cars for China. Given these MNEs' inability to profitably produce such models in the United States and Japan, imagine the profit potential these mod-

els developed in China may have back home where entry-level cars now sell for \$10,000.

To the extent Western MNEs often find it tough going in these unfamiliar territories, it is not surprising that some new MNEs from emerging economies—called Third World multinationals or "dragon multinationals"—well versed in such an alternative business model are capturing the hearts, minds, and wallets of customers in emerging economies. In India, Tata Motors is striving to unleash a "one lakh" car (one lakh equals 100,000 rupees, roughly \$2,500). In the Philippines, Jollibee beats the mighty McDonald's and is now venturing out to Southeast Asia and the Middle East. In Africa, Asia, and Central America, South African Breweries (now SABMiller) runs neck and neck with Anheuser-Busch, Carlsberg, and Heineken. Out of China, Lenovo aspires to become "king of the hill" in the PC battle. In a nutshell, there is money to be made in and out of emerging economies. The million (or billion) dollar challenge for global business in the 21st century is: How to make such money?

Case Discussion Questions

1. From an institution-based view, what determines firm performance in emerging economies?
2. From a resource-based view, what determines firm performance in emerging economies?
3. What are the main concerns that prevent Western MNEs from aggressively investing in emerging economies? What are the costs if they choose not to focus on emerging economies?

Sources: Based on (1) P. Aulakh, 2007, Emerging multinationals from developing economies, *Journal of International Management*, 13: 235–240; (2) L. Brouthers, E. O'Donnell, & J. Hadjimarcou, 2005, Generic product strategies for emerging market exports into Triad nation markets, *Journal of Management Studies*, 42: 225–245; (3) N. Dawar & A. Chattopadhyay, 2002, Rethinking marketing programs for emerging markets, *Long Range Planning*, 35: 457–474; (4) Economist Intelligence Unit, 2006, *Corporate Priorities for 2006 and Beyond*, London: *The Economist*; (5) *Fortune*, 2007, The greatest economic boom ever, July 23: 75–80; (6) S. Hart & T. London, 2005, Developing native capability, *Stanford Social Innovation Review*, summer: 28–33; (7) J. Mathews, 2006, Dragon multinationals as new features of globalization in the 21st century, *Asia Pacific Journal of Management*, 23: 5–27; (8) R. Wooster, 2006, U.S. companies in transition economies, *Journal of International Business Studies*, 37: 179–195; (9) M. Wright, I. Filatotchev, R. Hoskisson, & M. W. Peng, 2005, Strategy research in emerging economies, *Journal of Management Studies*, 42: 1–33.

NOTES

Journal acronyms: AME – *Academy of Management Executive*; AMJ – *Academy of Management Journal*; AMR – *Academy of Management Review*; APJM – *Asia Pacific Journal of Management*; BW – *Business Week*; CMR – *California Management Review*; HBR – *Harvard Business Review*; JIBS – *Journal of International Business Studies*; JIM – *Journal of International Management*; JM – *Journal of Management*; JMS – *Journal of Management Studies*; JWB – *Journal of World Business*; LRP – *Long Range Planning*; MIR – *Management International Review*; SMJ – *Strategic Management Journal*; TIBR – *Thunderbird International Business Review*

¹ This definition of the MNE can be found in R. Caves, 1996, *Multinational Enterprise and Economic Analysis*, 2nd ed. (p. 1), New York: Cambridge University Press; J. Dunning, 1993, *Multinational Enterprises and the Global Economy* (p. 30), Reading, MA: Addison-Wesley. Other terms are multinational corporation (MNC) and transnational corporation (TNC), which are often used interchangeably with MNE. To avoid confusion, in this book, we use MNE.

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