# Unit-2 International Business Environment

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**International Corporations — Meaning**
An International corporation is a large commercial organization with operating affiliates in a large number of nations. A typical international corporation, also known as a multinational corporation, multinational enterprise or transnational enterprise functions with a headquarter based in one country, while its other facilities are located in other countries. Simply put, international corporations may produce, market, invest and operate across the world.

According to ILO (2010) Report, "The essential nature of a multinational company lies in the fact that its managerial headquarter is located in one country while the company carries out operations in a number of other countries as well"
According to Spero and Hart (1999), "A multinational corporation is a business enterprise that maintains direct investments overseas and that upholds value-added holdings in more than one country."

**Characteristics and Nature of MNCs**

Multinational Corporations are big and complex companies that operate in several countries. They conduct a large variety of production and distribution activities overseas. Hence it may be prudent for us to first understand its features.

**1. Origin:** MNCs have been in existence for past few centuries. The East India Company, England's flagship MNC was established in 1600. It was however post World War II, that the number of MNCs grew rapidly in Britain, USA. Germany, France and Japan and their presence expanded in the rest of the world.

**2. Profit Maximization:** Though MNCs may involve themselves in social welfare or employee welfare activities, the primary motive of MNCs is profit maximization.

**3. Multiple Objectives:** Though profit remains the core objective for most MNCs, many of them pursue multiple objectives such as sales and revenue maximization, long term survival, sustainable production, achieving cost efficiency and the like.

**4. Scope of Operation:** MNCs function in more than one country Their home country is where the headquarters is situated, whereas the foreign country ¡n which they operate are called as host countries.

**5. Activities:** MNCs can carry on several activities including but not limited to manufacture of goods and services, marketing, distribution, logistics and technology transfer among others. MNCs exist in almost all sectors such as pharmaceuticals, hospitality, automobile, petrochemicals, retail, insurance, banking, apparel, engineering, cosmetics, electronics and consumer goods

**6. Quality:** MNCs are big organizations. They compete not only with local rivals in their home country but also with foreign competitors in host countries. Hence, they place enormous value in providing quality products and services.

**7. Management:** Though different MNCs may have different management systems as far as leadership and hierarchy is concerned, many of them give importance to ideas that emanate across hierarchy. Many MNCs subsidiaries may also be completely handled by local executives.

**8. Importance to Branding:** A lot lies in the name and MNCs understand that McDonalds, Dominos, Nike and Levis invest enormous amounts to build, retain and expand their brand value. MNCs involve themselves in several brand building exercises to be ahead of their competitors.

**Role and Importance of Multi-National Corporations in International Business.**

**1. Filling the Saving Gap:** The most crucial contribution of M\JCs is that they help fill the saving gap. Developing countries suffer from saving and investment deficiency. Actual investment is lower than desired levels of investment If the country can fill this gap vith the help of foreign direct investments inflows made by MNCs, target economic growth rates can be achieved.

**2. Filling the Trade Gap:** Several MNCs produce in cheaper locations abroad (generally developing countries) and use the host country as an export hub. This results in expansion of exports for the host country and makes its Balance of Payments favourable.

**3. Filling Revenue Gap:** MNCs contribute to a nations tax collection. Government revenue increases as MNCs contribute by way of corporate taxes. This way, the government is able to mobilize funds to finance development activities in the country.

**4. Filling the Technology Gap:** MNCs not only bring in investment they also bring along technology and managerial skills which get disseminated in the host country over time. Such transfers are desirable for host country.

**5. Increase ¡n Employment Opportunities:** For conducting their operations, MNCs require a large number of skilled and low-skilled labour. This provides employment opportunities in a host country.

**6. Mass Production:** MNCs usually use advanced technologies and produce goods and services on a mass scale. They often are able to enjoy economies of scale due to large production levels, bringing down the costs of production significantly.

**7. Healthy international relations:** Commercial ties between countries especially with MNCs and subsidiaries strengthens international relations among countries.

**Foreign Direct Investment – Meaning, Concept, Importance.**

To understand Foreign Direct Investments, it may be prudent to first understand the types of foreign investment. Foreign or international investments are international capital movements that can be classified into the following two categories, namely Foreign Indirect investments and Foreign Direct investment.

**Foreign Indirect Investment (FU):** Popularly termed as Portfolio investments it includes purchase/acquisition of securities such as shares, bonds or debentures issued by domestic firms, institutions or companies by foreign institutional investors or individuals. Such investment is devoid of any control over the issuing firm's managerial or operational decisions.

**Foreign Direct Investment (FDI):** In Foreign Direct Investments unlike in portfolio investments, investing firm not only purchases an equity stake, but a power of control over the invested-in firms decision making. The decision making could be ¡n areas of informal managerial guidance, technical assistance, knowledge dissemination, sharing of marketing skills, networks expansion or may include vital decision making. The control may vary depending on the equity participation or strategic positioning of the investing firm. In simple words, FDI implies an investment a foreign firm's land, labour, capital and enterprise

**Definition of Foreign Direct Investment**

According to the Balance of Payment Manual of the IMF.. 'Foreign direct investment reflects the objective of obtaining a lasting interest by o resident entity in one economy (direct investor) in on entity resident in on economy other than that of the investor (direct investment enterprise)." The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence on the management of the enterprise.

**FDI CONCEPTS**

This section explains select concepts relating to Foreign Direct investments. It will discuss FDI Stock and FDI Flows. Components of FDI and Modes of FDI. Up to date statistics will help students to understand concepts better.

**IMPORTANCE OF FDI TO HOST COUNTRY**

The importance of Foreign Direct investments is not limited to international movement of capital. Along with capital, elements that are complementary to capital - such as skills, technolo9y, processes and management tend to get transferred from one country to the other.

There are many ways in which FDI benefits the host nation. Some of them have been discussed below:

**1. Increased Economic Growth and Employment Generation**
If capital inflows fill the investment gap in a developing country. creation of jobs becomes an important reason why countries attract FDL FDI inflows boost manufacturing as well as services sector. This in turn creates employment opportunities especially among the educated youth, skilled and unskilled labour. Increased employment leads to increased incomes. It provides the necessary purchasing power and expands the consumption of goods and services. This results in economic growth.

**2. Stimulation for Economic Development**
FDI is an important source of non-debt external capital. [t adds to the flow of goods and services in the host country. When a factory is constructed for production or a workspace is established to deliver services, at least some local labour, equipment and materials are utilised. It is argued that once construction is complete, it will employ few local employees and further demand local materials and services.

**3. Development of Backward Areas**
FDI is being considered as an important investment catalyst in a developing country. FDI enables transformation of remote and backward areas in a host country into accessible areas or even industrial hubs. For instance, area near the Hyundai unit at Sriperumbudur. Tamil Nadu in India exemplifies transformation of a backward area into an industrial hub Another example is the Japanese investment in soft and physical infrastructure in North-cast India. It has improved connectivity and logistics in the area. boosting social economy there.

**4. Human Resource Development**
Human resource development as an advantage derived through FDI inflows is often understated. Human resource sometimes referred to as human capital are the skills. knowledge and competence of the workforce. MNC fins invest heavily in skilling and capacity building of their staff. This improves the education and human capital quotient of the host country.

**5. Provision of Finance and Technology**
This is touted as the most important advantage of attracting FDI in a host country FDI is a non-debt finance, returns of which depend on ho'. the business Is operated by the foreign investor in India. Hence it is a low risk, equity-based financing mechanism of long run nature.

**6. Increase in Exports**
Many of the goods produced by FDI firms are meant for global markets and not for host country's domestic consumption. When the firm exports its goods globally, it increases host country's export earnings in foreign exchange.

**7. Exchange Rate Stability**
FDI inflows into a country translates into a continuous flow of foreign exchange. This helps the country's Central Bank maintain robust levels of reserves of foreign exchange. This can be used to finance imports and ensures stable exchange rates.

**8. Creation of a Competitive Market**
By allowing entry of foreign companies in the domestic market, FDI creates a competitive environment. It also helps in breaking presence of domestic monopolies. Competitive environment forces firms to constantly improve their processes and product offerings. thereby fostering innovation. Consumers are also benefitted as they gain access to a wider range of competitively priced goods and services.

**Legal Aspects of FDI from Indian Context.**

Foreign direct investment inflows brought by multinational corporations in India are subject to legal regimes. Foreign investment translates into enormous capital inflows in the country. This results in changing the dynamics of competition, consumer aspirations and business environment in general. It is for this reason, that Government shapes FDI policy and institutional regulations in a way that is supportive to the long-term growth and development objectives of the country.

When multinational corporations operate in India, they are obligated to function within the legal framework the legal aspects of FDI in the Indian context relate to 2 dimensions:

1, FDI Policy in India 2. Legal Concerns for MNCs

## 1. FDI Policy in India

India has witnessed a dramatic rise in the Foreign Direct Investment post economic reforms in 1991. The FDI inflows in India grew from a more 05$ 0.15 Billion in 1991-92 to 05$
74.4 billion in 2019-20. FDI inflows can largely be attributed to the openness in FDI policy and easing of FDI norms in India.
At present FDI is allowed in almost all sectors either through Automatic route (foreign investor does not require any approval from the Government of India for investment) or Approval route (also termed as Government Route, a foreign investor has to secure approval from the Government of India before making investments. The foreign investors’ proposal has to be cleared by the Government of India, concerned ministry and department If investment size is big. then approval has to be secured from Cabinet Committee also).

## 2. Legal Concerns for MNCs

MNCs functioning in India have to comply with all sectoral and industrial norms and legal regulations as framed from time to time. These may include legal rules relating to Product

safety standards. competition laws labour laws. environmental laws, protection of Intellectual Property Rights, advertisement and sales regulations, and contracts to name a few. This section discusses few of them and wherever possible. actual examples have been shared to make the text engaging.

1**. Product Safety Standards:** If damage. Injury or death is caused due to consumption of defective or damaged product a company can be held responsible for It and be made to compensate the customer as per Consumer Protection Act The intent is to provide protection to consumer against unfair trade practices. It also allows for effective and timely administration and settlement of consumer disputes.
Many MNCs to maintain their customer base and build brand image. ensure that faulty products are not sold. In some cases. if a fault is identified after selling, sorne companies have recalled their products.
An example Ii this regard Is BMW India Pvt. Ltd. In May 2020, the company due to a fault in the downstream catalytic converter oxygen sensor heating that led to d5abling of On board diagnosis, the specific model was recalled from all the relevant customers voluntarily. The part was replaced and customers satisfied.

**2. Protection of Intellectual Property Right (WR):** ¡PR arise from the use of some persons company’s special talent and abilities. These intellectual properties may include copyright, trademark patent GI Integrated Circuits, secret formula among others. Even though in India. laws for protection of PR are present enforcement of the same is not stringent. This has led to many MNCs being discouraged from investing in India.

**3. Competition Laws in India:** The Competition (Amendment) Act 2007. Implemented by the Competition Commission of India is aimed to eliminate any practice that can have an adverse effect on competition. The intent of the Law is to promote and sustain competition both by domestic and foreign players, to have a level playing field, which is in the interest of consumers. It prohibits any agreement among businesses which may result in collusion or formation of monopoly type formats in India.

**4. Labour Laws:** Labour laws have a colonial history in India. Over the years. they have evolved to suit the needs of a planned economic development and social justice to the lesser heard voices of society Labour is a subject in the Concurrent List, which means that Laws relating to Labour are made both by the central and state governments.

**5. Environmental Protection Laws:** Carbon emissions, thinning of ozone layer, water and air pollution are matters of global interest which are hotly debated. To reduce global effects, many countries including India, have entered into international treaties to protect the environment, All big-ticket foreign investors have to obtain permission and clearance from Ministry of Environment and Forests. Government of India.

## Cultural and Demographic Environment – Meaning and Importance in International Business

The success of an international business lies to a large extent on how it adjusts and adapts within the culture and demographic dynamics of countries in which it operates. Culture is often misunderstood as limited to cultural activities such as music, dance and drama. However, culture is a complex phenomenon. which also includes how members of a society or community behave, their way of life, language. sense of aesthetics etc.
Culture is a sum total of beliefs, thoughts. value systems. languages, customs and art which is shared by country men and women. It evolves over time but more importantly. culture assists in keeping the society well bound. Culture affects the way people think, behave and respond. It influences how people work, their attitude and pattern.
One of the big blunders while doing business internationally is being unaware of cultural differences.

**Importance of Cultural and Demographic Environment in International Business**

The understanding and appreciation of cultures and demographic environment for the gro'.th and success of international business cannot be overemphasized. International businesses can survive only if they are able to adapt to the cultures in which they function. Every business transaction in some way or the other involves interaction between people. It is in this context that understanding peoples way of thinking, belief systems, language, dressing, etiquettes, age related demands and preferences and way of life become a requisite to conducting success businesses.

The importance of culture and demographic environment has been listed below:

**1. Inclusion and Diversity at workplace:** International businesses operate in multiple countries. They often have employees who belong to different places. including home country, host country and other parts of the world. This results in immense diversity at workplace. A deeper understanding of cultures creates a conducive work environment, which is harmonious and encompasses inclusivity. This leads to increase in employee and business productivity.

**2. Unlearn and relearn:** Consideration towards people of different cultures helps businesses adapt to realities in new environments They unlearn their old ways of doing business, which may not be as useful in a certain environment and shift to new ways of doing business more conducive to new environments.

**3 Negotiation:** One of the fundamental applications of cultural understanding is for business negotiation. Whether it is during a joint venture negotiation, or discussion with clients and associates or dealing with local authorities in a host country. effective negotiation requires a perfect harmony and compatibility between business strategy and culture. Cross cultural understanding is particularly helpful at the time of problem solving and dispute resolution encountered by international business.

**4. Competitive advantage and culture:** International business can create a competitive advantage by steering its strategy and customizing its business model to suit cultural nuances and needs of the demographic environment. This could result into expanded national and international trade and commerce. Moreover. cultural and societal norms have a profound impact on the costs and modes of doing business. More often than not.. these norms have implications on the choice of countries. MNCs choose to operate in

**5. Understanding and Compassion:** Spreading of cross-cultural literacy among company employees can infuse compassion towards people in home country. Employees of international business, whether at managerial level or executive level can understand how cultural and demographic differences affect the practices of international business Many companies transfer their senior staff at regular intervals to different locations abroad. The purpose is to create a truly cosmopolitan and multi-cultural executive team. Being compassionate also helps in creating a positive attitude towards others.

**6. Understanding the Doc and Don’ts:** An understanding of cultures also helps to remove unwanted assumptions in a new country. Executives and senior managers of international business are often trained of the Das and Don’ts of different cultures before they interact with their foreign clients. This helps in avoiding conflicts and misunderstanding.

**7. Delivery of correct product and service delivery mix:** Every international business carefully studies the demographic nuances of a foreign country in which it plans to operate. Dimensions such as population size, age composition, incomes of different segments of population. tastes and preferences of people are carefully analysed. This helps a business to offer a correct mix of products and services which is most suited in a host country.