Global Marketing

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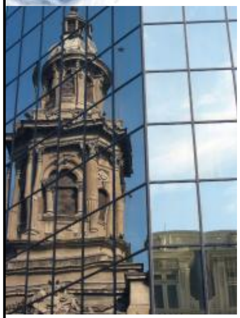
The Global Economic Environment
Chapter 2

Introduction



This chapter includes:
- An overview of the world economy
- A survey of economic system types
- The stages of market development
- The balance of payments

The World Economy—An Overview

- In the early 20th century economic integration was at 10%; today it is 50%
- EU and NAFTA are very integrated
- Global competitors have displaced or absorbed local ones

The World Economy—An Overview

- The new realities:
  - Capital movements have replaced trade as the driving force of the world economy
  - Production has become uncoupled from employment
  - The world economy, not individual countries, is the dominating factor

The World Economy—An Overview

The new realities, continued:
- The struggle between capitalism and socialism began in 1917 is over
- E-Commerce diminishes the importance of national barriers and forces companies to re-evaluate business models

Zeroing in on Economic Systems

- Globalization has made it harder to pigeonhole economies within the four-cell matrix
- Also consider:
  - Type of economy: advanced industrial state, emerging or transition economy, or developing nation?

Zeroing in on Economic Systems

– Type of Government: Monarchy, dictatorship, tyrant? One-party system? Dominated by another state? Democracy? Terrorist?
– Trade and capital flows: Free trade, part of trading bloc? Currency board or exchange controls?
– The commanding heights: Transportation, communications & energy sectors. State, private, or mixed ownership?

Zeroing in on Economic Systems

– Services provided by the state or state funded: Pensions, health care, education.
– Institutions: Country characterized by transparency, standards, absence of corruption? Standards ignored and court system compromised?
– Markets: Entrepreneurial high risk/high reward? Socialized market? Government dominated price and wage controls?

Economic Systems

Resource Allocation

Resource Ownership	Market	Command
Private	Market Capitalism	Centrally Planned Capitalism
State	Market Socialism	Centrally Planned Socialism

Market Capitalism

- Individuals and firms allocate resources
- Production resources are privately owned
- Driven by consumers
- Government's role is to promote competition among firms and ensure consumer protection

Western Market Systems

Type of System	Key Characteristics	Countries
Anglo-Saxon model	Private ownership; free enterprise economy; capitalism; minimal social safety net; highly flexible employment policies	United States, Canada, Great Britain
Social market economy model	Private ownership; "social partners" orientation that includes employer groups, unions, and banks; unions and corporations are involved in government, and vice versa; inflexible employment policies	Germany, France, Italy
Nordic model	Mix of state ownership and private ownership; high taxes; some market regulation; generous social safety net	Sweden, Norway

Centrally Planned Socialism

- Opposite of market capitalism
- State holds broad powers to serve the public interest; decides what goods and services are produced and in what quantities
- Consumers can spend only what is available
- Government owns entire industries and controls distribution
- Demand typically exceeds supply
- Little reliance on product differentiation, advertising, pricing strategy
- China, India, and the former USSR now moving towards some market allocation and private ownership

Centrally Planned Capitalism

- Economic system in which command resource allocation is used extensively in an environment of private resource ownership
- Example:
  - Swedish government controls 2/3s of all spending; a hybrid of CPS and capitalism (Market Socialism)
  - Swedish government plans move towards privatization

Economic Freedom

- Rankings of economic freedom among countries
  - “free” “mostly free” “mostly unfree” “repressed”
- Variables considered include such things as:
  - Trade policy
  - Taxation policy
  - Capital flows and foreign investment
  - Banking policy
  - Wage and price controls
  - Property rights
  - Black market

Economic Freedom—2013 Rankings

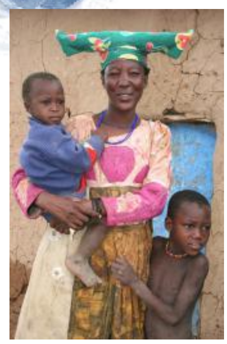
Free	Repressed
1. Hong Kong	169. Turkmenistan
2. Singapore	170. Equatorial Guinea
3. Australia	171. Dem. Rep. Congo
4. New Zealand	172. Burma
5. Switzerland	173. Eritrea
6. Canada	174. Venezuela
7. Chile	175. Zimbabwe
8. Mauritius	176. Cuba
9. Denmark	177. North Korea
10. United States	

Not ranked: Afghanistan, Iraq, Kosovo, Libya, Liechtenstein, Somalia, Sudan, Syria

Stages of Market Development

- The World Bank has defined four categories of development using Gross National Income (GNI) as a base
- **BEMs**, identified 10 years ago, were countries in Central Europe, Latin America, and Asia that were to have rapid economic growth
- Today, the focus is on **BRICS:** Brazil, Russia, India, China and South Africa

Low-Income Countries



GNP per capita of $1,025 or less

Characteristics
- Limited industrialization
- High percentage of population in farming
- High birth rates
- Low literacy rates
- Heavy reliance on foreign aid
- Political instability and unrest
- Concentrated in Sub-Saharan Africa

Lower-Middle-Income Countries

- GNI per capita: $1,026 to $4,035
- Characteristics
  - Rapidly expanding consumer markets
  - Cheap labor
  - Mature, standardized, labor-intensive industries like footwear, textiles and toys
- 50 bottom-ranked countries are LDCs—least developed countries
- India is the only BRIC nation

Upper-Middle-Income Countries

Chilean copper mine

GNP per capita: $4,036 to $12,475

Characteristics:

- Rapidly industrializing, less agricultural employment
- Increasing urbanization
- Rising wages
- High literacy rates and advanced education
- Lower wage costs than advanced countries

- Also called industrializing or developing economies
- BRICS: Brazil, China, Russia, South Africa
- Other countries: Malaysia, Chile, Venezuela, Mexico

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Newly Industrializing Economies (NIEs)

- Lower-middle and upper income economies with the highest sustained rates of economic growth
  - Greater industrial output that developing economies
  - Exports of manufactured and refined products
  - N-11 a new country grouping identified by Goldman Sachs
    - NIEs include Egypt, Indonesia, the Philippines, (lower-middle income) Mexico, and Turkey (upper-middle income)

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Marketing Opportunities in LDCs

- Characterized by a shortage of goods and services
- Long-term opportunities must be nurtured in these countries
  - Look beyond per capita GNP
  - Consider the LDCs collectively rather than individually
  - Consider first mover advantage
  - Set realistic deadlines

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Mistaken Assumptions about LDCs

1. The poor have no money.
2. The poor will not "waste" money on non-essential goods.
3. Entering developing markets is fruitless because goods there are too cheap to make a profit.
4. People in BOP (bottom of the pyramid) countries cannot use technology.
5. Global companies doing business in BOP countries will be seen as exploiting the poor.

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High-Income Countries

Tokyo

- GNI per capita: $12,476 or more
- Also known as advanced, developed, industrialized, or postindustrial countries
- Characteristics:
  - Sustained economic growth through disciplined innovation
  - Service sector is more than 50% of GNI
  - Households have high ownership levels of basic products

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High-Income Countries

- Characteristics, continued:
  - Importance of information processing and exchange
  - Ascendancy of knowledge over capital, intellectual over machine technology, scientists and professionals over engineers and semiskilled workers
  - Future oriented
  - Importance of interpersonal relationships

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G-8, the Group of Eight

- Goal of global economic stability and prosperity
  - U.S.
  - Japan
  - Germany
  - France
  - Britain
  - Canada
  - Italy
  - Russia (1998)

2013 G-8 Leaders in Lough Erne, Northern Ireland

G-20, Group of Twenty

- Established in 1999
- Finance Ministers and central bank governors of 19 countries and the EU

Russia hosted the 2013 summit.

OECD, the Organization for Economic Cooperation and Development

- 34 nations
- Post-WW II European origin
- Canada, U.S. (1961), Japan (1964)
- Promotes economic growth and social well-being
- Focuses on world trade, global issues, labor market deregulation
  - Anti-bribery conventions

The Triad

- U.S., Western Europe, and Japan
- Represents 75% of world income
- Expanded Triad includes all of North America and the Pacific Rim and most of Eastern Europe
- Global companies should be equally strong in each part

Product Saturation Levels

- The % of potential buyers or households who own a product
- India: 20% of people have telephones
- Autos: 1 per 43,000 Chinese, 21 per 100 Poles, 49 per EU adults, 8 per 1,000 Indians, 200 out of 1,000 in Russia, 565 out of 1,000 in Germany
- Computers: 1 PC per 6,000 Chinese; 11 PCs per 100 Poles; 34 PCs per 100 EU citizen

Balance of Payments

- Record of all economic transactions between the residents of a country and the rest of the world
  - Current account–record of all recurring trade in merchandise and services, and humanitarian aid
    - trade deficit—negative current account
    - trade surplus—positive current account
  - Capital account–record of all long-term direct investment, portfolio investment, and capital flows

Balance of Payments

TABLE 2-5 U.S. Balance of Payments, 2007–2011 (US$ millions)

	2007	2008	2009	2010	2011
A. Current Account	**–731,214**	**–668,854**	**–376,551**	**–470,898**	**–465,926**
1. Goods Exports	1,148,481	1,304,896	1,069,491	1,288,882	1,497,406
2. Goods Imports	–1,976,853	–2,139,548	–1,575,400	–1,934,006	–2,235,819
3. *Balance on Goods*	*–819,373*	*–834,652*	*–505,910*	*–645,124*	*–738,413*
4. Services: Credit	497,245	534,166	505,547	553,603	605,961
5. Services: Debit	–378,130	–398,266	–380,909	–403,216	–427,428
6. *Balance on Services*	119,115	135,850	124,637	150,387	178,533
7. *Balance on Goods and Services*	*–700,258*	*–698,802*	*–381,272*	*–494,737*	*–559,880*
B. Capital Account	**–1,842**	6,010	**–140**	**–152**	**–1,159**

U.S. Goods and Services Trade with BIC

TABLE 2-6 U.S. Goods and Services Trade with Brazil, India, and China, 2011 (US$ millions)

	China	India	Brazil	Russia
1. U.S. Goods Exports to	105,263	21,616	42,821	8,384
2. Goods Imports from	–400,642	–36,338	–31,549	–34,652
3. *Balance on Goods*	*–295,378*	*–14,722*	*11,272*	*–26,268*
4. U.S. Services Exports to	26,731	11,108	21,721	na
5. Services Imports from	–11,395	–16,921	–6,970	na
6. *U.S. Balance on Services*	*15,335*	*–5,814*	*14,751*	*na*
7. *U.S. Balance on Goods and Services*	–280,043	–20,536	26,022	na

Top Exporters and Importers, 2009

TABLE 2-7 Top Exporters and Importers in World Merchandise Trade, 2009 (US$ billions)

Leading Exporters	2009	Leading Importers	2009
1. China	$1,202	1. United States	$1,605
2. Germany	1,126	2. China	1,006
3. United States	1,056	3. Germany	938
4. Japan	581	4. France	560
5. Netherlands	498	5. Japan	552

Overview of International Finance

- Foreign exchange makes it possible to do business across the boundary of a national currency
- Currency of various countries are traded for both immediate (spot) and future (forward) delivery
- Currency risk adds turbulence to global commerce

Foreign Exchange Market Dynamics

- Supply and Demand interaction
  - Country sells more goods/services than it buys
  - There is a greater demand for the currency
  - The currency will appreciate in value

TABLE 2-8 Exchange Risks and Gains in Foreign Transactions

	$1,000,000 Contract		€1,100,000 Contract	
Foreign Contract Exchange Rates	U.S. Seller Receives	European Buyer Pays	U.S. Seller Receives	European Buyer Pays
€1.25 = $1	$1,000,000	€1,250,000	$880,000	€1,100,000
€1.10 = $1	$1,000,000	€1,100,000	$1,000,000	€1,100,000
€1.00 = $1	$1,000,000	€1,000,000	$1,100,000	€1,100,000
€0.85 = $1	$1,000,000	€850,000	$1,294,118	€1,100,000

Managing Economic Exposure

- ***Economic exposure*** refers to the impact of currency fluctuations on the present value of the company's financial performance.
- Occurs when sales are in a foreign currency
  - Nestlé generates 98% of sales outside home country
  - Euro zone companies GlaxoSmithKline, Daimler AG, BP, for example, generate 1/3 of sales in the U.S.

Managing Economic Exposure

- Numerous techniques and strategies have been developed to reduce exchange rate risk
  - ***Hedging*** involves balancing the risk of loss in one currency with a corresponding gain in another currency
  - ***Forward Contracts*** set the price of the exchange rate at some point in the future to eliminate some risk

Looking Ahead to Chapter 3

- The Global Trade Environment