renaissance college of commerce & management

SYLLABUS

Class: - B.B.A. IV Semester

Subject: - International Business

UNIT – I	**An Overview of International Business:** Framework of International Business, Types of International Business, International Business Approaches, Global Marketing Theory of Competitive Advantages, Neo-Classical, Modern Approach to International Business, Problems of Trade and Aid to Developing Countries.
UNIT – II	**International Business Decision** : Mode of Entry, Marketing Mix, Factors Affecting decision For International Business,
UNIT – III	**Role Of International Institutions**: GATT, WTO, ECM, IMF, IBRD, IDA, IFC, UNCTAD, In International Business. Recent Trends in World trade, Multi National Corporations and the Trade
UNIT – IV	**Recent Trends in India's Foreign Trade**: Export and Import Policy, Trade Policy, Balance of Payment, Custom and Tariff Rationalization. Identifying Foreign Markets and Overseas markets, Product Development in international markets, Transfer Logistics and Distribution Channels, Role of Documentation in International Trade, Export Pricing, Methods of International Payments.
UNIT – V	**International Capital Movement**: Risk in International Operations, International Investment, Financing of Foreign trade, Factor Mobility and Direct Foreign Investment. Export Finance, Pre and post Shipment credit, Introduction to FEMA, Insurance. Role of ECGC and export Promotion Councils, Eurocurrency Market
UNIT – VI	**Regional Economic Groupings**: Major Trading Blocks, Globalization with Social responsibility, Introduction to International Monetary and Financial System

UNIT- 1

DEFINITION

International business is a term used to collectively describe all commercial transactions (private and governmental, sales, investments, logistics, and transportation) that take place between two or more nations. Usually, private companies undertake such transactions for profit governments undertake them for profit and for political reasons.

WHY STUDYING INTERNATIONAL BUSINESS:

- Most companies are either international or compete with international companies.
- Modes of operation may differ from those used domestically.
- The best way of conducting business may differ by country.
- An understanding helps you make better career decisions.
- An understanding helps you decide what governmental policies to support.

TYPES OF INTERNATIONAL BUSINESS COMPANIES

The company's approach to global expansion needs to fit in to its corporate agenda, and be in tune with the industry and time. Cross national business have been labeled into tour types in terms of organizational structure buy researchers.

Multi-domestic Organization: It is one that exports to/imports from organizations in other countries with primarily domestic production. The subsidiaries develop into decentralized decision-making units, make use of local resources to create a self-sufficient entity. Ex: GM, is a firm with subsidiaries extending over Europe that stand along as self-contained units.

International Organization: It has its assets centralized at its headquarters. The knowledge base is developed at the center, and from there it is dispersed to overseas locations. Subsidiary units are expected to leverage their local capabilities. Here core competencies are central, parent company capabilities are used, and knowledge disseminates from center outwards. Ex: Microsoft, Core product is developed at center, and the subsidiaries take care of localizing the product to fit the customer requirements that are regional or local.

Global Organization: It is one that is centralized but scaled globally, with knowledge retained at the center. Control is retained at the center. The subsidiary units have to furnish information to the center and comply with the headquarters control. Subsidiary units must draw from the best practices and experiences of all the subsidiary units and adopt the most efficient strategies from the entire company.Ex: Intel, keeping performance up to global standards and taking advantage of the learning, drawn from experience to show in terms of low costs and location advantages.

Transnational: Refers to an enterprise where national boundaries get blurred. Both centralized and decentralized methods are adopted in this model. While units are specialized, interdependence of units is also a characteristic feature. The subsidiary units abroad play an active role in the development of the firm's capabilities and share knowledge with worldwide locations. This model enables a firm to "think globally and Act locally". Ex: Caterpillar Inc., has set up manufacturing units in certain locations for many identical components. It however has assembly units in each of its major markets, so that the product can be made to suit local needs.

INTERNATIONAL BUSINESS APPROACHES / EPRG frame work

The foreign marketing involvement of a manufacturing company may widely vary from a state of no direct involvement to a state of total involvement. Several types of involvement are generally observed, even though they are not mutually exclusive nor sequentially progressive.

Depending on the kind and degree of its involvement in foreign marketing, a firm has to re-orient and re-organize its activities to cope with different levels of operational responsibilities inherent in such involvement. To throw some light on the issue, some guidelines are available from what is called EPRG orientation. The EPRG framework attempts, four broad types of orientation of a firm towards foreign marketing. They are:

1. ETHNOCENTRIC ORIENTATION : The ethnocentric orientation of a firm considers that the products, marketing strategies and techniques applicable in the home market are equally so in the overseas market as well. In such a firm, all foreign marketing operations are planned and carried out from home base, with little or no difference in product formulation and specifications, pricing strategy, distribution and promotion measures between home and overseas markets. The firm generally depends on its foreign agents and export-import merchants for its export sales.
2. REGIOCENTRIC ORIENTATION : Inregiocentric approach, the firm accepts a regional marketing policy covering a group of countries which have comparable market characteristics. The operational strategies are formulated on the basis of the entire region rather than individual countries. The production and distribution facilities are created to serve the whole region with effective economy on operation, close control and co-ordination.
3. GEOCENTRIC ORIENTATION : In geocentric orientation, the firms accept a world wide approach to marketing and its operations become global. In global enterprise, the management establishes manufacturing and processing facilities around the world in order to serve the various regional and national markets through a complicated but well co-ordinated system of distribution network. There are similarities between geocentric and regiocentric approaches in the international market except that the geocentric approach calls for a much greater scale of operation.
4. POLYCENTRIC OPERATION : When a firm adopts polycentric approach to overseas markets, it attempts to organize its international marketing activities on a country to country basis. Each country is treated as a separate entity and individual strategies are worked out accordingly. Local assembly or production facilities and marketing organizations are created for serving market needs in each country. Polycentric orientation could be most suitable for firms seriously committed to international marketing and have its resources for investing abroad for fuller and long-term penetration into chosen markets. Polycentric approach works better among countries which have significant economic, political and cultural differences and performance of these tasks are free from the problems created primarily by the environmental factors.

CONCLUSION : The involvement decision is conditioned by a variety of internal and external factors such as firms' export policy, resources and product range, volume of export business, regulatory and procedural conditions to be fulfilled both from exporting and importing angle.
From the foregoing, it will be evident that the scope of international marketing for a firm will be determined by its decisions regarding the means of entry into foreign markets as well as by the kind of involvement the firm wishes to have in its international marketing operations. It cannot be said that one kind of operation/orientation is better than the other, as each has its own advantage and disadvantage depending on the operating environmental factors.
However, a firm can adopt a policy of common or differential approaches in respect of different marketing decision areas.

TRADE LIBERALIZATION
The removal or reduction of restrictions or barriers on the free exchange of goods between nations. This includes the removal or reduction of both tariff (duties and surcharges) and non-tariff obstacles (like licensing rules, quotas and other requirements). The easing or eradication of these restrictions is often referred to as promoting "free trade."

Role of MNC's - According to an ILO repot, "the essential nature of multinational enterprises lies in the fact that its managerial headquarters are located in one country (home country) while enterprises carries out operations in number of other countries as well. (host countries).

DominanceofMNC's - Through liberalization there has been expansion & growth of MNC's. The GDP has increased from about 5% in beginning of 1980's to nearly 7% at end of 1990's. The MNC's are estimated to employ directly, at home and abroad around 73 billion people. For example, the US footwear company Nike currently employees 9000 people, while nearly 75,000 people are employed by its independent sub-contractors located in different countries.

Merits of MNC's- The important arguments in favour of MNC's are given below:-
MNC's help the host countries in following ways:-
1) MNC's help to increases the investment level & thereby the income & employment in host country.
2) The transnational corporations have become vehicles for the transfer technology, especially to developing countries.
3) They also kind a managerial revolution in host countries through professional management and employment of highly sophisticated management techniques.
4) The MNCs enable that host countries to increases their exports & decreases their import requirements.
5) They work to equalize cost of factors of production around the world.
6) MNC's provide and efficient means of integrating national economies.
7) The enormous resources of multinational enterprises enable them to have very efficient research & development systems. Thus, they make a commendable contribution to inventions & innovations.
8) MNC's also stimulate domestic enterprise because to support their own operations, the MNC's may encourage & assist domestic suppliers.
9) MNC's help to increase competition & break domestic monopolies.

Demerits:-
1) MNC's may destroy competition & acquire monopoly powers.
2) The transfer pricing enables MNC's to avoid taxes by manipulating prices on intra-company transactions.
3) Through their power and flexibility , MNC's can evade national economic autonomy & control, and their activities may be inimical to national income interests of particular countries.
4) MNCs retard growth of employment in home country.
5) MNCs technology is designed for world-wide Profit maximization, not the development needs of poor countries. In general, it is asserted, the imported technologies are not adopted to (a) Consumption needs (b) size of domestic markets (c) resource availabilities (d) stage of development of many of developing countries

THEORIES OF INTERNATIONAL BUSINESS
1) Classical theory : According to the classical theory of international trade, every country will produce their commodities for the production of which it is most suited in terms of its natural endowments climate quality of soil, means of transport, capital, etc. It will produce these commodities in excess of its own requirement and will exchange the surplus with the imports of goods from other countries for the production of which it is not well suited or which it cannot produce at all. Thus all countries produce and export these commodities in which they have cost advantages and import those commodities in which they have cost disadvantages.

2)Absolute Advantage Theory : In economics, the principle of **absolute advantage** refers to the ability of a party (an individual, or firm, or country) to produce more of a good or service than competitors, using the same amount of resources. Adam Smith first described the principle of absolute advantage in the context of international trade, using labor as the only input.

Definition of 'Absolute Advantage' -The ability of a country, individual, company or region to produce a good or service at a lower cost per unit than the cost at which any other entity produces that good or service.

Investopedia explains 'Absolute Advantage' - Entities with absolute advantages can produce something using a smaller number of inputs than another party producing the same product. As such, absolute advantage can reduce costs and boost profits.
Since absolute advantage is determined by a simple comparison of labor productivities, it is possible for a party to have no absolute advantage in anything;[7] in that case, according to the theory of absolute advantage, no trade will occur with the other party.[8] It can be contrasted with the concept of comparative advantage which refers to the ability to produce a particular good at a lower opportunity cost.

Origin of the theory - The main concept of absolute advantage is generally attributed to Adam Smith for his 1776 publication *An Inquiry into the Nature and Causes of the Wealth of Nations* in which he countered mercantilist ideas. Smith argued that it was impossible for all nations to become rich simultaneously by following mercantilism because the export of one nation is another nation's import and instead stated that all nations would gain simultaneously if they practiced free trade and specialized in accordance with their absolute advantage.

Features of this theory: A country that has an absolute advantage produces greater output of a good or service than other countries using the same amount of resources. Smith stated that tariffs and quotas should not restrict international trade; it should be allowed to flow according to market forces. Contrary to mercantilism Smith argued that a country should concentrate on production of goods in which it holds an absolute advantage. No country would then need to produce all the goods it consumed. The theory of absolute advantage destroys the mercantilist idea that international trade is a zero-sum game. According to the absolute advantage theory, international trade is a positive-sum game, because there are gains for both countries to an exchange.

Condition: The theory that trade occurs when one country, individual, company, or region is absolutely more productive than another entity in the production of a good. A person, company or country has an absolute advantage if its output per unit of input of all goods and services produced is higher than that of another entity producing that good or service.

Problems of Absolute Advantage: There is a potential problem with absolute advantage. If there is one country that does not have an absolute advantage in the production of any product, will there still be benefit to trade, and will trade even occur? The answer may be found in the extension of absolute advantage, the theory of comparative advantage.

Example -The principle was described by Adam Smith in the context of international trade. Now I am describing some of them below :
A country has an **absolute advantage** over another in producing a good, if it can produce that good using fewer resources than another country. For example if one unit of labor in India can produce 80 units of wool or 20 units of wine; while in Spain one unit of labor makes 50 units of wool or 75 units of wine, then India has an absolute advantage in producing wool and Spain has an absolute advantage in producing wine. India can get more wine with its labor by specializing in wool and trading the wool for Spanish wine, while Spain can benefit by trading wine for wool. (Adam Smith, *Wealth of Nations*, Book IV, Ch.2.)
The benefits to nations from trading are the same as to individuals: trade permits specialization, which allows resources to be used more productively.

3) Comparative Advantage Theory :
Definition of 'Comparative Advantage' : The ability of a firm or individual to produce goods and/or services at a lower opportunity cost than other firms or individuals. A comparative advantage gives a company the ability to sell goods and services at a lower price than its competitors and realize stronger sales margins.
Investopedia explains 'Comparative Advantage' : Having a comparative advantage - or disadvantage - can shape a company's entire focus. For example, if a cruise company found that it had a comparative advantage over a similar company, due ito its closer proximity to a port, it might encourage the latter to focus on other, more productive, aspects of country.
Origins of the theory - The idea of comparative advantage has been first mentioned in Adam Smith's Book *The Wealth of Nations*: "If a foreign country can supply us with a commodity cheaper than we ourselves can make it, better buy it of them with some part of the produce of our own industry, employed in a way in which we have some advantage." But the law of comparative advantages has been formulated by David Ricardo who investigated in detail advantages and alternative or relative opportunity in his 1817 book *On the Principles of Political Economy and Taxation* in an example involving England and Portugal.
Ricardo's Theory of Comparative Advantage -David Ricardo stated a theory that other things being equal a country tends to specialize in and exports those commodities in the production of which it has

maximum comparative cost advantage or minimum comparative disadvantage. Similarly the country's imports will be of goods having relatively less comparative cost advantage or greater disadvantage.

1. Ricardo's Assumptions:-
Ricardo explains his theory with the help of following assumptions:-
1. There are two countries and two commodities.
2. There is a perfect competition both in commodity and factor market.
3. Cost of production is expressed in terms of labor i.e. value of a commodity is measured in terms of labor hours/days required to produce it. Commodities are also exchanged on the basis of labor content of each good.
4. Labor is the only factor of production other than natural resources.
5. Labor is homogeneous i.e. identical in efficiency, in a particular country.
6. Labor is perfectly mobile within a country but perfectly immobile between countries.
7. There is free trade i.e. the movement of goods between countries is not hindered by any restrictions.
8. Production is subject to constant returns to scale.
9. There is no technological change.
10. Trade between two countries takes place on barter system.
11. Full employment exists in both countries.
12. **Perfect occupational mobility** of factors of production - resources used in one industry can be switched into another without any loss of efficiency
13. **Perfect occupational mobility** of factors of production - resources used in one industry can be switched into another without any loss of efficiency
14. **Constant returns to scale** (i.e. doubling the inputs in each country leads to a doubling of total output)
15. **No externalities** arising from production and/or consumption
16. **Transportation costs are ignored**
17. If businesses exploit **increasing returns to scale** (i.e. economies of scale) when they specialize, the potential gains from trade are much greater. The idea that **specialization** should lead to increasing returns is associated with economists such as **Paul Romer**and **Paul Ormerod.**

Ricardo's Example:- On the basis of above assumptions, Ricardo explained his comparative cost difference theory, by taking an example of **England** and **Portugal** as two countries &**Wine** and **Cloth** as two commodities. As pointed out in the assumptions, the cost is measured in terms of labor hour. The **principle of comparative advantage** expressed in labor hours by the following table.

	1 Unit Of Wine	*1 Unit of Cloth*
England	120	100
Portugal	80	90

Portugal requires less hours of labor for both wine and cloth. One unit of wine in Portugal is produced with the help of 80 labor hours as above 120 labor hours required in England. In the case of cloth too, Portugal requires less labor hours than England. From this it could be argued that there is no need for trade as Portugal produces both commodities at a lower cost. Ricardo however tried to prove that Portugal stands to gain by specializing in the commodity in which it has a greater comparative advantage. Comparative cost advantage of Portugal can be expressed in terms of cost ratio.

Effects on the economy -Conditions that maximize comparative advantage do not automatically resolve trade deficits. In fact, many real world examples where comparative advantage is attainable may require a trade deficit.

Considerations
Development economics -he theory of comparative advantage, and the corollary that nations should specialize, is criticized on pragmatic grounds within the import substitution industrialization theory of development economics, on empirical grounds by the Singer–Prebisch thesis which states that terms of trade between primary producers and manufactured goods deteriorate over time, and on theoretical

grounds of infant industry and Keynesian economics. In older economic terms, comparative advantage has been opposed by mercantilism and economic nationalism.

Free mobility of capital in a globalize world - Ricardo explicitly bases his argument on an assumed immobility of capital:" ... if capital freely flowed towards those countries where it could be most profitably employed, there could be no difference in the rate of profit, and no other difference in the real or labor price of commodities, than the additional quantity of labor required to convey them to the various markets where they were to be sold."

Criticism of theory
1. Applicability- Economist Ha-Joon Chang criticized the comparative advantage principle, contending that it may have helped developed countries maintain relatively advanced technology and industry compared to developing countries
2. Assumption rather than discovery - Philosopher and Professor of Evolutionary Psychology Bruce Charlton has argued that comparative advantage is a metaphysical assumption, rather than a discovery. In addition to falsifiable nature of the principle, he notes that the principle relies on several assumptions that are not necessarily operative.

Comparative advantage exists when a country has a **margin of superiority** in the production of a good or service i.e. where the **opportunity cost** of production is lower.
Ricardo's theory of comparative advantage was further developed by Heckscher, Ohlin and Samuelson who argued that countries have different **factor endowments** of labor, land and capital inputs. Countries will **specialize** in and **export** those products which use intensively the factors of production which they are most endowed.
Worked example of comparative advantage .Consider the data in the following table:

Pre-Specialization	CD Players	Personal Computers
UK	2,000	500
Japan	4,000	2,000
Total Output	6,000	2,500

To identify which country should specialize in a particular product we need to analyses the internal **opportunity cost** for each country. For example, were the UK to shift more resources into higher output of personal computers, the opportunity cost of each extra PC is four CD players. For Japan the same decision has an opportunity cost of two CD players. Therefore, Japan has a comparative advantage in PCs.
Determinants of comparative advantage
Comparative advantage is a **dynamic concept**. It can and does change over time. Some businesses find they have enjoyed a comparative advantage in one product for several years only to face increasing competition as rival producers from other countries enter their markets.
For a country, the following factors are important in determining the relative costs of production:

- The **quantity and quality of factors of production available**: If an economy can improve the quality of its labor force and increase the stock of capital available it can expand the productive potential in industries in which it has an advantage.
- **Investment in research & development** (important in industries where patents give some firms significant market advantage .An appreciation of the exchange rate can cause exports from a country to increase in price. This makes them less competitive in international markets.
- **Long-term rates of inflation** compared to other countries. For example if average inflation in Country X is 4% whilst in Country B it is 8% over a number of years, the goods and services produced by Country X will become ***relatively more expensive*** over time. This worsens their competitiveness and causes a switch in comparative advantage.
- **Import controls such as tariffs and quotas** that can be used to create an artificial comparative

advantage for a country's domestic producers- although most countries agree to abide by international trade agreements.

- **Non-price competitiveness of producers** (e.g. product design, reliability, quality of after-sales support)

Interpreting the Theory of Comparative Advantage

A better way to state the results is as follows. The Ricardian model shows that if we want to maximize total output in the world then,

First, fully employ all resources worldwide;

Second, allocate those resources within countries to each country's comparative advantage industries; and

Third, allow the countries to trade freely thereafter.

Importance:

The good in which a comparative advantage is held is the good that the country produces most efficiently. Therefore, if given a choice between producing two goods (or services), a country will make the most efficient use of its resources by producing the good with the lowest opportunity cost, the good for which it holds the comparative advantage. The country can trade with other countries to get the goods it did not produce.

3) The Heckscher-Ohlin Trade Model

The Heckscher-Ohlin (HO hereafter) model was first conceived by two Swedish economists, Eli Heckscher (1919) and Bertil Ohlin. Rudimentary concepts were further developed and added later by Paul Samuelson and Ronald Jones among others. There are four major components of the HO model:

1. Factor Price Equalization Theorem,
2. Stolper-Samuelson Theorem,
3. Rybczynski Theorem, and
4. Heckscher-Ohlin Trade Theorem.

Definition: Heckscher–Ohlin theorem is one of the four critical theorems of the Heckscher–Ohlin model. It states that a country will export goods that use its abundant factors intensively, and import goods that use its scarce factors intensively. In the two-factor case, it states: "A capital-abundant country will export the capital-intensive good, while the labor-abundant country will export the labor-intensive good."

The critical assumption of the Heckscher–Ohlin model is that the two countries are identical, except for the difference in resource endowments.

Initially, when the countries are not trading:

- The price of capital-intensive good in capital-abundant country will be bid down relative to the price of the good in the other country,
- The price of labor-intensive good in labor-abundant country will be bid down relative to the price of the good in the other country.

Features of the model - The **Heckscher–Ohlin model** (**H–O model**) is a general equilibrium mathematical model of international trade, developed by Eli Heckscher and Bertil Ohlin at the Stockholm School of Economics. It builds on David Ricardo's theory of comparative advantage by predicting patterns of commerce and production based on the factor endowments of a trading region. The model essentially says that countries will export products that use their abundant and cheap factor(s) of production and import products that use the countries' scarce factor(s).

Theoretical development of the model - The Ricardian model of comparative advantage has trade ultimately motivated by differences in labor productivity using different *technologies*. Heckscher and Ohlin didn't require production technology to vary between countries, so (in the interests of simplicity) the *H-O model has identical production technology everywhere*. Ricardo considered a single factor of production (labor) and would not have been able to produce comparative advantage without technological differences between countries. The H-O model removed technology variations but

introduced variable capital endowments, recreating endogenously the inter-country variation of labor productivity that Ricardo had imposed exogenously.
Extensions - The model has been extended since the 1930s by many economist.Notable contributions came from Paul Samuelson, Ronald Jones, and JaroslavVanek, so that variations of the model are sometimes called theHeckscher-Ohlin-Samuelson model or the Heckscher-Ohlin-Vanek model in the neo-classical economics.

Assumptions of the theory
Heckscher-Ohlin's theory explains the modern approach to international trade on the basis of following assumptions:-
1. There are two countries involved.
2. Each country has two factors (labor and capital).
3. Each country produce two commodities or goods (labor intensive and capital intensive).
4. There is perfect competition in both commodity and factor markets.
5. All production functions are homogeneous of the first degree i.e. production function is subject to constant returns to scale.
6. Factors are freely mobile within a country but immobile between countries.
7. Two countries differ in factor supply.
8. Each commodity differs in factor intensity.
9. The production function remains the same in different countries for the same commodity. For e.g. If commodity A requires more capital in one country then same is the case in other country.
10. There is full employment of resources in both countries and demand are identical in both countries.
11. Trade is free i.e. there are no trade restrictions in the form of tariffs or non-tariff barriers.

The 2×2×2 model
The original H-O model assumed that the only difference between countries was the relative abundances of labor and capital. The original Heckscher–Ohlin model contained two countries, and had two commodities that could be produced. Since there are two (homogeneous) factors of production this model is sometimes called the "2×2×2 model".
The model has *variable factor proportions* between countries: Highly developed countries have a comparatively high ratio of capital to labor in relation to developing countries. This makes the developed country capital-abundant relative to the developing nation, and the developing nation labor-abundant in relation to the developed country.

The original, 2x2x2 model was derived with restrictive assumptions. These assumptions and developments are listed here.
Both countries have identical production technology : This assumption means that producing the same output of either commodity *could* be done with the same level of capital and labor in either country. Another way of saying this is that the per-capita productivity is the same in both countries in the same technology with identical amounts of capital.
Countries have natural advantages in the production of various commodities in relation to one another, so this is an 'unrealistic' simplification designed to highlight the effect of variable factors. Ohlin said that the HO-model was a long run model, and that the conditions of industrial production are "everywhere the same" in the long run.

Production output must have constant Return to Scale : Both of the countries in the simple HO model produced both commodities, and both technologies have constant returns to scale (CRS). (CRS production has twice the output if both capital and labor inputs are doubled, so the two production functions must be 'homogeneous of degree 1').
These conditions are required to produce a mathematical equilibrium. With increasing returns to scale it would likely be more efficient for countries to specialize, but specialization is not possible with the Heckscher-Ohlin assumptions.

The technologies used to produce the two commodities differ : The CRS production functions must differ to make trade worthwhile in this model. For instance if the functions are Cobb-Douglas technologies the parameters applied to the inputs must vary. An example would be:

$$\text{Arable industry: } A = K^{1/3}L^{2/3}$$
$$\text{Fishing industry: } F = K^{1/2}L^{1/2}$$

Where A is the output in arable production, F is the output in fish production, and K, L are capital and labor in both cases.In**this example**, the marginal return to an extra unit of capital is higher in the fishing industry, assuming units of F(ish) and A(rable) output have equal value. The more capital-abundant country may gain by developing its fishing fleet at the expense of its arable farms. Conversely, the workers available in the relatively labor-abundant country can be employed relatively more efficiently in arable farming.

Labor mobility within countries - *Within* countries, capital and labor can be reinvested and re-employed to produce different outputs. Like the comparative advantage argument of Ricardo, this is assumed to happen costless.

Capital immobility between countries - The basic Heckscher–Ohlin model depends upon the relative availability of capital and labor differing internationally, but if capital can be freely invested anywhere competition (for investment) will make relative abundances identical throughout the world.
Differences in labor abundance would not produce a difference in *relative* factor abundance (in relation to mobile capital) because the labor/capital ratio would be identical everywhere.
As capital controls are reduced, the modern world has begun to look a lot less like the world modelled by Heckscher and Ohlin. It has been argued that capital mobility undermines the case for Free Trade itself, see: Capital mobility and comparative advantage Free trade critique. Capital is mobile when:

- There are limited exchange controls
- Foreign Direct Investment (FDI) is permitted between countries, or foreigners are permitted to invest in the commercial operations of a country through a stock or corporate bond market

Labor immobility between countries - Like capital, labor movements are not permitted in the Heckscher-Ohlin world, since this would drive an equalization of relative abundances of the two production factors.This condition is more defensible as a description of the modern world than the assumption that capital is confined to a single country.

Commodities have the same price everywhere - The 2x2x2 model originally placed no barriers to trade, had no tariffs, and no exchange controls. It was also free of transportation costs between the countries, or any other savings that would favor procuring a local supply.
If the two countries have separate currencies, this does not affect the model in any way (Purchasing Power Parity applies).

Perfect internal competition -Neither labor nor capital has the power to affect prices or factor rates by constraining supply; a state of perfect competition exists.

Econometric testing of H–O model theorems - Heckscher and Ohlin considered the Factor-Price Equalization theorem an econometric success. Modern econometric estimates have shown the model to perform poorly, however, and adjustments have been suggested, most importantly the assumption that technology is not the same everywhere.

Criticism against the Heckscher–Ohlin model - Although H-O model is normally thought to be basic for international trade theory, there are many points of criticism against the model.

Poor predictive power -The original Heckscher–Ohlin model and extended model such as the Vanek model performs poorly, as it is shown in the section "Econometric testing of H-O model theorem. Even when the HOV formula fits well, it does not mean that Heckscher–Ohlin theory is valid. Indeed, Heckscher–Ohlin theory claims that the state of factor endowments of each country determines the production of each country.

Factor equalization theorem -The factor equalization theorem (FET) applies only for most advanced countries. Heckscher–Ohlin theory is badly adapted to the analyze South-North trade problems. The assumptions of HO are unrealistic with respect to North-South trade. Income differences between North and South is the concern that third world cares most. The factor price equalization theorem has not shown a sign of realization, even for a long time lag of a half century.

Identical production function -The standard Heckscher–Ohlin model assumes that the production functions are identical for all countries concerned. This means that all countries are in the same level of production and have the same technology which is highly unrealistic. The standard Heckscher–Ohlin model ignores all these vital factors when one wants to consider development of less developed countries in the international context.[10] Even between developed countries, technology differs from industry to industry and firm to firm base.

Capital as endowment -In the modern production system, machines and apparatuses play an important role. What is named capital is nothing other than these machines and apparatuses, together with materials and intermediate
products. Capital is the most important of factors, or one should say as important as labor. By the help of machines and apparatuses' quantity is not changed at once. But the capital is not an endowment given by the nature. It is composed of goods manufactured in the production and often imported from foreign countries. In this sense, capital is internationally mobile. The concept of capital as natural endowment distorts the real role of capital.

Homogeneous capital -In the Heckscher–Ohlin model, the rate of profit is determined according to how abundant capital is. Before the profit rate is determined, the amount of capital is not measured. This logical difficulty was the subject of academic controversy which took place many years ago. In fact, this is sometimes named Cambridge Capital Controversies. Heckscher–Ohlin theorists ignore all these stories without providing any explanation how capital is measured theoretically.

No unemployment -Unemployment is the vital question in any trade conflict. Heckscher–Ohlin theory excludes unemployment by the very formulation of the model, in which all factors (including labor) are employed in the production.

No room for firms -Standard Heckscher–Ohlin theory assumes the same production function for all countries. This implies that all firms are identical. The theoretical consequence is that there is no room for firms in the HO model.

Unrealistic Assumptions -Besides the usual assumptions of two countries, two commodities, no transport cost, etc. Ohlin's theory also assumes no qualitative difference in factors of production, identical production function, constant return to scale, etc. All these assumptions makes the theory unrealistic one.

Restrictive -Ohlin's theory is not free from constrains. His theory includes only two commodities, two countries and two factors. Thus it is a restrictive one.

One-Sided Theory -According to Ohlin's theory, supply plays a significant role than demand in determining factor prices. But if demand forces are more significant, a capital abundant country will export labor intensive good as the price of capital will be high due to high demand for capital.

Static in Nature -Like Ricardian Theory the H-O Model is also static in nature. The theory is based on a given state of economy and with a given production function and does not accept any change.

Criticism -According to Wijnholds, it is not the factor prices that determine the costs and commodity prices but it is commodity prices that determine the factor prices.

Consumers' Demand ignored -Ohlin forgot an important fact that commodity prices are also influenced by the consumers' demand.

Haberler's Criticism -According to Haberler, Ohlin's theory is based on partial equilibrium. It fails to give a complete, comprehensive and general equilibrium analysis.

Leontief Paradox -American economist Dr. Wassily Leontief tested H-O theory under U.S.A conditions. He found out that U.S.A exports labor intensive goods and imports capital intensive goods, but U.S.A being a capital abundant country must export capital intensive goods and import labor intensive goods than to produce them at home. This situation is called Leontief Paradox which negates H-O Theory.

Other Factors Neglected -Factor endowment is not the sole factor influencing commodity price and international trade. The H-O Theory neglects other factors like technology, technique of production, natural factors, different qualities of labor, etc., which can also influence the international trade.

Importance -The critical assumption of the Heckscher–Ohlin model is that the two countries are identical, except for the difference in resource endowments. This also implies that the aggregate preferences are the same. The relative abundance in capital will cause the capital-abundant country to produce the capital-intensive good cheaper than the labor-abundant country and vice versa.

NOTE –FOR PORTER'S DIAMOND THEORY-PLEASE REFER THE TEXT BOOK OF IB.

UNIT II

MODES OF ENTRY INTO AN INTERNATIONAL BUSINESS

There are some basic decisions that the firm must take beforforien expansion like: which markets to enter, when to enter those markets, and on what scale.

Which foreign markets?

-The choice based on nation's long run profit potential.
-Look in detail at economic and political factors which influence foreign markets.
-Long run benefits of doing business in a country depends on following factors:

- Size of market (in terms of demographics)
- The present wealth of consumer markets (purchasing power)
-

Nature of competition
By considering such factors firm can rank countries in terms of their attractiveness and long-run profit.

Timing of entry:-It is important to consider the timing of entry. Entry is early when an international business enters a foreign market before other foreign firms. And late when it enters after other international businesses.The advantage is when firms enters early in the foreign market commonly known as first-mover advantages

First mover advantage;-

1. it's the ability to prevent rivals and capture demand by establishing a strong brand name.
2. Ability to build sales volume in that country.so that they can drive them out of market.
3. Ability to create customer relationship**.**

Disadvantage:

1. Firm has to devote effort, time and expense to learning the rules of the country.
2. Risk is high for business failure(probability increases if business enters a national market after several other firms they can learn from other early firms mistakes)

Various Modes of entry:--

1. Exporting
2. Licensing
3. Franchising
4. Turnkey Project
5. Mergers & Acquisitions:
6. Joint Venture
7. Acquisitions & Mergers
8. Wholly Owned Subsidiary

1.Exporting: It means the sale abroad of an item produced ,stored or processed in the supplying firm's home country. It is a convenient method to increase the sales. Passive exporting occurs when a firm receives canvassed them. Active exporting conversely results from a strategic decision to establish proper systems for organizing the export factions and for procuring foreign sales.

Advantages Of Exporting :

a. Need for limited finance; If the company selects a company in the host country to distribute the company can enter international market with no or less financial resources but this amount would be quite less compared to that would-be necessary under other modes.

b. **Less Risks**; Exporting involves less risk as the company understand the culture ,customer and the market of the host country gradually. Later after understanding the host country the company can enter on a full scale.
c. **Motivation for exporting**: Motivation for exporting are proactive and reactive. Proactive motivations are opportunities available in the host country. Reactive motivators are those efforts taken by the company to export the product to a foreign country due to the decline in demand for its product in the home country.

2. **Licensing :**In this mode of entry ,the domestic manufacturer leases the right to use its intellectual property (ie) technology , copy rights ,brand name etc to a manufacturer in a foreign country for a fee. Here the manufacturer in the domestic country is called licensor and the manufacturer in the foreign is called licensee. The cost of entering market through this mode is less costly. The domestic company can choose any international location and enjoy the advantages without incurring any obligations and responsibilities of ownership ,managerial ,investment etc.

Advantages;
1. Low investment on the part of licensor.
2. Low financial risk to the licensor
3. Licensor can investigate the foreign market without much efforts onhis part.
4. Licensee gets the benefits with less investment on research anddevelopment
5. Licensee escapes himself from the risk of product failure.

Disadvantages:
1. It reduces market opportunities for both
2. Both parties have to maintain the product quality and promote the product . Therefore one party can affect the other through their improper acts.
3. Chance for misunderstanding between the parties.
4. Chance for leakages of the trade secrets of the licensor.
5. Licensee may develop his reputation
6. Licensee may sell the product outside the agreed territory and after the expiry of the contract.

3.Franchising: Under franchising an independent organization called the franchisee operates the business under the name of another company called the franchisor under this agreement the franchisee pays a fee to the franchisor. The franchisor provides the following services to the franchisee.

1. Trade marks
2. Operating System
3. Product reoutation
4. Continuous support system like advertising , employee training ,reservation services quality assurances program etc.

Advantages:
1. Low investment and low risk
2. Franchisor can get the information regarding the market culture, customs and environment of the host country.
3. Franchisor learns more from the experience of the franchisees.
4. Franchisee get the benefits of R& D with low cost.
5. Franchisee escapes from the risk of product failure.

Disadvantages :
1. It may be more complicating than domestic franchising.
2. It is difficult to control the international franchisee.

3. It reduce the market opportunities for both
4. Both the parties have the responsibilities to maintain product quality and product promotion.
5. There is a problem of leakage of trade secrets.

4.Turnkey Project: A turnkey project is a contract under which a firm agrees to fully design , construct and equip a manufacturing/ business/services facility and turn the project over to the purchase when it is ready for operation for a remuneration like a fixed price , payment on cost plus basis. This form of pricing allows the company to shift the risk of inflation enhanced coststo the purchaser. Eg nuclear power plants ,airports,oil refinery , national highways , railway line etc. Hence they are multiyear project.

5.Mergers&Acquistions:A domestic company selects a foreign company and merger itself withforeign company in order to enter international business. Alternatively thedomestic company may purchase the foreign company and acquires itownership and control. It provides immediate access to internationalmanufacturing facilities and marketing network.

Advantages :
1. The company immediately gets the ownership and control over theacquired firm's factories, employee, technology ,brand name anddistribution networks.
2. The company can formulate international strategy and generate morerevenues.
3. If the industry already reached the stage of optimum capacity level orovercapacity level in the host country. This strategy helps the hostcountry
.
Disadvantages:
1. Acquiring a firm in a foreign country is a complex task involvingbankers, lawyers regulation, mergers and acquisition specialists fromthe two countries.
2. This strategy adds no capacity to the industry.
3. Sometimes host countries imposed restrictions on acquisition of localcompanies by the foreign companies.
4. Labour problem of the host country's companies are also transferred tothe acquired company.

6.Joint Venture : Two or more firm join together to create a new business entity that islegally separate and distinct from its parents. It involves shared ownership.Various environmental factors like social , technological economic andpolitical encourage the formation of joint ventures. It provides strength interms of required capital. Latest technology required human talent etc. andenable the companies to share the risk in the foreign markets. This actimproves the local image in the host country and also satisfies thegovernmental joint venture.

Advantages:
1. Joint venture provide large capital funds suitable for major projects.
2. It spread the risk between or among partners.
3. It provide skills like technical skills, technology, human skills ,expertise , marketing skills.
4. It make large projects and turn key projects feasible and possible.
5. It synergy due to combined efforts of varied parties.
Disadvantages:
1. Conflict may arise
2. Partner delay the decision making once the dispute arises. Then theoperations become unresponsive and inefficient.
3. Life cycle of a joint venture is hindered by many causes of collapse.
4. Scope for collapse of a joint venture is more due to entry ofcompetitors changes in the partners strength.
5. The decision making is slowed down in joint ventures due to theinvolvement of a number of parties.

7.Acquisitions& Mergers:A mergers is a voluntary and permanent combination of businesswhereby one or more firms integrate their operations and identitieswith those of another and henceforth work under a common name andin the interests of the newly formed amalgamations.
Motives for acquisitions:
1. Removal of competitor

2. Reduction of the Co failure through spreading risk over a widerrange of activities.
3. The desire to acquire business already trading in certainmarkets & possessing certain specialist employees &equipments.
4. Obtaining patents, license & intellectual property.
5. Economies of scale possibly made through more extensiveoperations.
6. Acquisition of land, building & other fixed asset that can beprofitably sold off.
7. The ability to control supplies of raw materials.
8. Expert use of resources.
9. Tax consideration.
10. Desire to become involved with new technologies &management method particularly in high risk industries.

8.Wholly Owned Subsidiary : Subsidiary means individual body under parent body. This Subsidiary or individual body as per their own generates revenue. They give their own rent, salary to employees, etc. But policies and trademark will be implemented from the Parent body. There are no branches here. Only the certain percentage of the profit will be given to the parent body.
A subsidiary, in business matters, is an entity that is controlled by a bigger and more powerful entity. The controlled entity is called a company, corporation, or limited liability company, and the controlling entity is called its parent (or the parent company). The reason for this distinction is that a lone company cannot be a subsidiary of any organization; only an entity representing a legal fiction as a separate entity can be a subsidiary. While individuals have the capacity to act on their own initiative, a business entity can only act through its directors, officers and employees.
The most common way that control of a subsidiary is achieved is through the ownership of shares in the subsidiary by the parent. These shares give the parent the necessary votes to determine the composition of the board of the subsidiary and so exercise control. This gives rise to the common presumption that 50% plus one share is enough to create a subsidiary. There are, however, other ways that control can come about and the exact rules both as to what control is needed and how it is achieved can be complex (see below). A subsidiary may itself have subsidiaries, and these, in turn, may have subsidiaries of their own. A parent and all its subsidiaries together are called a group, although this term can also apply to cooperating companies and their subsidiaries with varying degrees of shared ownership.
Subsidiaries are separate, distinct legal entities for the purposes of taxation and regulation. For this reason, they differ from divisions, which are businesses fully integrated within the main company, and not legally or otherwise distinct from it.
Subsidiaries are a common feature of business life and most if not all major businesses organize their operations in this way. Examples include holding companies such as Berkshire Hathaway, Time Warner, or Citigroup as well as more focused companies such as IBM, or Xerox Corporation. These, and others, organize their businesses into national or functional subsidiaries, sometimes with multiple levels of subsidiaries.

INTERNATIONAL MARKETING MIX
hen launching a product into foreign markets firms can use a standard marketing mix or adapt the marketing mix, to suit the country they are carrying out their business activities in. This article talks you through each element of the marketing mix and the arguments for and against adapting it suit each foreign market.

International Marketing Mix: Product
Basic marketing concepts tell us that we will sell more of a product if we aim to meet the needs of our target market. In international markets this will involve taking into consideration a number of different factors including consumer's cultural backgrounds, religion, buying habits and levels of personal disposable income. In many circumstances a company will have to adapt their product and marketing mix strategy to meet local "needs and wants" that cannot be changed. Mcdonald is a global player however, their burgers are adapted to local needs. In India where a cow is a sacred animal their burgers contain chicken or fish instead of beef. In Mexico McDonalds burgers come with chilli sauce. Coca-cola is some parts of the world taste sweeter than in other places.

The arguments for standardisation state that the process of adapting the product to local markets does little more than add to the overall cost of producing the product and weakens the brand on the global scale. In today's global world, where consumers travel more, watch satellite television, communicate and shop internationally over the internet, the world is a smaller than it used to be. Because of this there is no need to adapt products to local markets. Brands such as MTV, Nike, Levis are all successful global brands where they have a standardised approach to their marketing mix, all these products are targeted at similar groups globally. As you can see both strategies; using a standard product and ancustomised product can work just as well. The right approach for each organisation will depend on their product, strength of the brand and the foreign market that the marketing is aimed at.

International Marketing Mix: Place
The Place element of the marketing mix is about distributing a product or service to the customer, at the right place and at the right time. Distribution in national markets such as the United Kingdom will probably involve goods being moved in a chain from the manufacturer to wholesalers and onto retailers for consumers to buy from. In an overseas market there will be more parties involved because the goods need to be moved around a foreign market where business practices will be different to national markets. For example in Japan there are approximately five different types of wholesaler involved in the distribution chain. Businesses will need to investigate distribution chains for each country they would like to operate in. They will also need to investigate who they would like to sell their products and services to businesses, retailers, wholesaler or directly to consumers. The distribution strategy for each country a business operates in could be different due to profit margins and transportation costs.

International Marketing Mix: Pricing
Pricing on an international scale is a complex task. As well as taking into account traditional price considerations such as fixed and variable costs, competition and target an organisation needs to consider additional factor such asthe cost of transport tariffs or import dutiesexchange rate fluctuationspersonal disposal incomes of the target marketthe currency they want to be paid in andthe general economic situation of the country and how this will influence pricing.The internet has created further challenges as customers can view global prices and purchase items from around the world. This has increased the level of competition and with it pricing pressures, as global competitors may have lower operating costs.

International Marketing Mix: Promotion
As with international product decisions an organisation can either adapt or standardise their promotional strategy and message. Advertising messages in countries may have to be adapted because of language, political climate, cultural attitudes and religious practices. For example a promotional strategy in one country could cause offence in another. Every aspect of promotional detail will require research and planning one example is the use of colour; red is lucky in China and worm by brides in India, whilst white is worn by mourners in india and China and brides in the United Kingdom. Many organisation adapt promotion strategies to suit local markets as cultural backgrounds and practices affect what appeals to consumers.
The level of media development and availability will also need to be taken into account. Is commercial television well established in your host country? What is the level of television penetration? How much control does the government have over advertising on TV, radio and Internet? Is print media more popular than TV?
Before designing promotional activity for a foreign market it would be expedient to complete a PEST analysis so that you have a complete understanding of the factors operating in the foreign market you would like to enter.
Conclusion - Prior to designing an international marketing mix a business should carry out a PEST analysis for every country they would like to operate in. This will help them determine what elements of the marketing mix can be standardised and which elements will need adjustments to suit local needs. It may well be that a business is able to use a standard marketing mix in the majority of cases and only need to adjust it on the rare occasion. Or every country may need its own marketing mix.

FACTORS AFFECTING DECISION FOR INTERNATIONAL BUSINESS,
Environmental factors for international business comprise the external relations a firm will face in going global. These include, most importantly, the economic, political and legal environments, each of these always entangled with the others.

Basic Issues - The central issues for the decision to go global are concerned with minimizing risk. A company, when considering the environment that it will deal with when entering a new market, has to deal with certain variables. These concern, for example, the cultural barriers to investment, the ability to reach a competitive edge with new investments and the strategic use of new technologies and natural resources that international investment might bring.
The Economic Environment - This element comprises the nature of the economic system and institutions of a particular country or region. It also takes into account the nature of human and natural resources within the target market. A firm will function very differently in a libertarian environment than within a highly statist one. Here, the activities and functions of local economic elites are also very important.

The Political Environment - Closely tied to the economic environment is the political one, itself also dealing with the nature of systems and institutions. Many variables to consider here are the stability of the political system, the existence of local or international conflict, the role of state enterprises and the nature of the bureaucracy.

The Legal Environment - The existence of bureaucratic systems and cultures is central in making the decision to invest globally. The nature of corruption, local values and assumptions that are built into national ideologies are major variables in this field. A great concern is the extent to which there is a culture of law or a culture of personal patronage, where negotiations are done on a personal rather than a legal basis. The impact of international lending agencies such as the International Monetary Fund or the World Bank is also important in creating a legal culture that a business will have to take seriously.

Social Structure - Experts such as Robert Brown and Alan Gutterman hold that social structure comprises the basic values of a people and transcends the institutions mentioned above. Issues such as the relation between the individual and the collective, religion, family life and even time concepts and gender roles are all significant in terms of dealing with a new population. Being sensitive to these might be the difference between success and failure.

Unit III

INTERNATIONAL INSTITUTIONS

International institutions are a central focus of international relations scholarship as well as of policymaking efforts around the world.

GATT - GENERAL AGREEMENT ON TARIFF AND TRADE

The **General Agreement on Tariffs and Trade** (**GATT**) was a multilateral agreement regulating international trade. According to its preamble, its purpose was the "substantial reduction of tariffs and other trade barriers and the elimination of preferences, on a reciprocal and mutually advantageous basis." It was negotiated during the Nations Conference on Trade and Employment and was the outcome of the failure of negotiating governments to create the International Trade Organization (ITO). GATT was signed in 1947, took effect in 1948, and lasted until 1994; it was replaced by the World Trade Organization in 1995.

The original GATT text (GATT 1947) is still in effect under the WTO framework, subject to the modifications of GATT 1994.

The GATT, was established on a provisional basis after the Second World War in the wake of other new multilateral institutions dedicated to international economic cooperation – notably the "Britton Woods" institutions now known as the World Bank and the International Monetary Fund.

The original 23 GATT countries were among over 50 which agreed a draft Charter for an International Trade Organization (ITO) – a new specialized agency of the United Nations. The Charter was intended to provide not only world trade disciplines but also contained rules relating to employment, commodity agreements, restrictive business practices, international investment and services.

In an effort to give an early boost to trade liberalization after the Second World War and to begin to correct the large overhang of protectionist measures which remained in place from the early 1930s-tariff negotiations were opened among the 23 founding GATT "contracting parties" in 1946. This first round of negotiations resulted in 45,000tariff concessions affecting $10 billion or about one-fifth – of world trade. It was also agreed that the value of these concessions should be protected by early and largely "provisional" acceptance of some of the trade rules in the draft ITO Charter. The tariff concessions and rules together became known as the General Agreement on Tariffs and Trade and entered into force in January 1948.

Although the ITO Charter was finally agreed at a UN Conference on Trade and Employment in Havana in March 1948, ratification in national legislatures proved impossible in some cases. When the United States' government announced, in 1950, that it would not seek Congressional ratification of the Havana Charter, the ITO was effectively dead. Despite its provisional nature, the GATT remained the only multilateral instrument governing international trade from 1948 until the establishment of the WTO.

Although, in its 47 years, the basic legal text of the GATT remained much as it was in 1948, there were additions in the form of "plural-lateral" voluntary membership agreements and continual efforts to reduce tariffs. Much of this was achieved through a series of "trade rounds".

The biggest leaps forward in international trade liberalization have come through multilateral trade negotiations, or "trade rounds", under the auspices of GATT – the Uruguay Round was the latest and most extensive.

The limited achievement of the Tokyo Round, outside the tariff reduction results, was a sign of difficult times to come. GATT's success in reducing tariffs to such a low level, combined with a series of economic recessions in the 1970s and early 1980s, drove governments to devise other forms of protection for sectors facing increased overseas competition. High rates of unemployment and constant factory closures led governments in Europe and North America to seek bilateral market-sharing arrangements with competitors and to embark on a subsidies race to maintain their holds on agricultural trade. Both these changes undermined the credibility and effectiveness of GATT.

WTO- WORLD TRADE ORGANIZATION

World Trade Organization came into existence in 1995 after the desolation of General Agreement on Tariff

and Trade (GATT).
*The WTO's overriding objective is to help trade flow smoothly, freely, fairly and predictably.*It does this by:
Administering trade agreements
Acting as a forum for trade negotiations
Settling trade disputes
Reviewing national trade policies
Assisting developing countries in trade policy issues, through technical assistance and training programs
Cooperating with other international organizations
The WTO has nearly 150 members, accounting for over 97% of world trade. Around 30 others are negotiating membership. Decisions are made by the entire membership. This is typically by consensus. A majority vote is also possible but it has never been used in the WTO, and was extremely rare under the

GATT and WTO trade rounds					
Name	**Start**	**Duration**	**Countries**	**Subjects covered**	**Achievements**
Geneva	April 1947	7 months	23	Tariffs	Signing of GATT, 45,000 tariff concessions affecting $10 billion of trade
Annecy	April 1949	5 months	13	Tariffs	Countries exchanged some 5,000 tariff concessions
Torquay	September 1950	8 months	38	Tariffs	Countries exchanged some 8,700 tariff concessions, cutting the 1948 tariff levels by 25%
Geneva II	January 1956	5 months	26	Tariffs, admission of Japan	$2.5 billion in tariff reductions
Dillon	September 1960	11 months	26	Tariffs	Tariff concessions worth $4.9 billion of world trade
Kennedy	May 1964	37 months	62	Tariffs, Anti-dumping	Tariff concessions worth $40 billion of world trade
Tokyo	September 1973	74 months	102	Tariffs, non-tariff measures, "framework" agreements	Tariff reductions worth more than $300 billion dollars achieved
Uruguay	September 1986	87 months	123	Tariffs, non-tariff measures, rules, services, intellectual property, dispute settlement, textiles, agriculture, creation of WTO, etc	The round led to the creation of WTO, and extended the range of trade negotiations, leading to major reductions in tariffs (about 40%) and agricultural subsidies, an agreement to allow full access for **textiles** and clothing from developing countries, and an extension of intellectual property rights.
Doha	November 2001	?	159	Tariffs, non-tariff measures, agriculture, labor standards, environment, competition, investment, transparency, patents etc	The round is not yet concluded. Bali Package signed on the 7th December 2013.

WTO's predecessor, GATT. The WTO's agreements have been ratified in all members' parliaments.
The WTO's top level decision-making body is the **Ministerial Conference** which meets at least once every two years. Below this is the **General Council** which meets several times a year in the Geneva headquarters. The General Council also meets as the Trade Policy Review Body and the Dispute Settlement Body. At the next level, the **Goods Council, Services Council and Intellectual Property (TRIPS) Council** report to the General Council.
Numerous **specialized committees, working groups** and **working parties** deal with the individual agreements and other areas such as the environment, development, membership applications and regional trade agreements.
The WTO Secretariat, based in Geneva, has around 600 staff and is headed by a director-general. Its annual budget is roughly 160 million Swiss francs. It does not have branch offices outside Geneva. Since decisions are taken by the members themselves, the Secretariat does not have the decision-making role that other international bureaucracies are given with.
The WTO is run by its member governments. All major decisions are made by the membership as a whole, either by ministers (who meet at least once every two years) or by their ambassadors or delegates (who meet regularly in Geneva). Decisions are normally taken by consensus.

Difference between WTO and GATT:-
The World Trade Organization is not a simple extension of GATT; on the contrary, it completely replaces its predecessor and has a very different character. Among the principal differences are the following:

The GATT was a set of rules, a multilateral agreement, with no institutional foundation, only a small associated secretariat which had its origins in the attempt to establish an International Trade Organization in the 1940s. The WTO is a permanent institution with its own secretariat.
The GATT was applied on a "provisional basis" even if, after more than forty years, governments chose to treat it as a permanent commitment. The WTO commitments are full and permanent.
The GATT rules applied to trade in merchandise goods. In addition to goods, the WTO covers trade in services and trade-related aspects of intellectual property.
While GATT was a multilateral instrument, by the 1980s many new agreements had been added of a plural-lateral, and therefore selective, nature. The agreements which constitute the WTO are almost all multilateral and, thus, involve commitments for the entire membership.
The WTO dispute settlement system is faster, more automatic, and thus much less susceptible to blockages, than the old GATT system. The implementation of WTO dispute findings will also be more easily assured.

ECM- EURO CURRENCY MARKET
Eurocurrency is the term used to describe deposits residing in banks that are located outside the borders of the country that issues the currency the deposit is denominated in. For example: a deposit denominated in US dollars residing in a Japanese bank is a Eurocurrency deposit, or more specifically a Eurodollar deposit.
HOW IT ORIGINATED?
After the Second World War, the amount of U.S. dollars outside the United States increased enormously.
As a result, enormous sums of U.S. dollars were in custody of foreign banks outside the United States.
During the Cold War period, especially after the invasion of Hungary in 1956, the Soviet Union feared that its deposits in North American banks would be frozen as a retaliation.
It decided to move some of its holdings to the Moscow Narodny Bank, a Soviet-owned bank with a British charter.
The British bank would then deposit that money in the US banks. There would be no chance of confiscating that money, because it belonged to the British bank and not directly to the Soviets. On February 28 1957, the sum of $800,000 was transferred, creating the first eurodollars.
Gradually, as a result of the successive commercial deficits of the United States, the eurodollar market expanded worldwide.
Thus, the currencies involved in the Eurodollar market are in no way different from currencies deposited with banks in the home country. It is only that Eurodollar is not under the orbit or surveillance of the monetary policy, where the currency in their home country is under the regulation of the national monetary policy
FEATURES OF EUROCURRENCY MARKET
It is an international market and it is under no national control: It has come up as the most important channel for mobilizing and deploying funds on an international scale.
It is a short term money market:
Eurodollar markets are the time-deposit market. The deposits here have a maturity period ranging one day to several months. Eurodollar is the short-term deposit. It is a wholesale market:
It is so because Eurodollar is the currency that is dealt in only large units.
Size of individual transaction is usually above $1million.
It is highly competitive and sensible market:
High competitive: This market is characterized as highly competitive because the market is growing and accepted internationally.
Sensible: The Eurodollar market is said to be sensible because it responds faster to the changes in demand and supply of the funds and also reacts to changes in the interest rates.

PARTICIPANTS IN EUROCURRENCY MARKET
1. Government
2. International Organizations
3. Central Banks
4. Commercial Banks
5. Corporations

6. MNC
7. Traders
8. Individuals
9. Participants have contributed in the demand and supply of the fund, in the following way:

SUPPLY:
Central Banks of various countries are the suppliers; they channel the fund through BIS.
Increase in the Oil Revenue of the OPEC has added to the fund.
MNCs and the traders place their surplus funds for the short-term gains.

DEMAND:
Government demand for these funds to meet the deficit arising due to meet the deficit arising due to the deficit in Balance of Payment and the rise in the oil prices.
Commercial Banks needs extra fund for lending. Some also borrow for the better 'window dressing' in the year-end.

ADVANTAGES
It helped the economies to solve the liquidity problems:
It provided better investment opportunities.
Funds are also by the commercial banks of various countries for domestic credit creation and window dressing.
This facilitated the growth and development of various countries like Brazil, South Korea, Taiwan, and Mexico etc…
Its International acceptance has helped in the international trade to expand and accelerated the process of globalization.

DISADVANTAGES
For many economies it is a new concept.
For many economies also considered that the speed of its growth or expansion is TOO fast.
For many economies, they feel this market gives a chance to avoid many a regulations that they try to impose on their national money market.

IMF – INTERNATIONAL MONETARY FUND
INTERNATIONAL MONETARY FUND :-International Monetary Fund was established in 1947. Following were the main objectives of this fund is –

1. To promote exchange rate stability among the different countries.
2. To make an arrangement of goods exchange between the countries.
3. To promote short term credit facilities to the member countries.
4. To assist in the establishment of International Payment System.
5. To make the member countries balance of payment favourable.
6. To facilitate the foreign trade.
7. To promote The international monetary corporation.

Management Of Fund :-The twelve member executive committee manages the affairs of IMF. Five members are the representatives of U.K, U.S.A, China, France and India. The remaining are elected by the other members countries. Its head office in in U.S.A.
Source Of IMF :-The initial capital of IMF was 8.5 billion dollar which was contributed by the 49 members. The quota of each member country was fixed in proportion to the national income and volume of foreign trade. Every country was required to pay in the form of gold and domestic currency.
FUNCTIONS OF IMF FUND
Merchant Of Currencies :-IMF main function is to purchase and sell the member countries currencies.
2. Helpful For The Debtor Countries :-If any country is facing adverse balance of payment and facing the difficulty to get the currency of creditor country, it can get short term credit from the fund to clear the debt. The IMF allows the debtor country to purchase foreign currency in exchange for its own currency upto 75%

of its quota plus an addition 25% each year. The maximum limit of the quota is 200% in special circumstances.

3. Declared Of Scarce Currency :-If the demand of any particular country currency increases and its stock with the fund falls below 75% of its quota, the IMF can declare it scare. But IMF also tries to increase its supply by these methods.

Purchasing: - IMF purchases the scare currency by gold.

Borrowing: - IMF borrows from those countries scare currency who has surplus amount.

Permission: - IMF allows the debtor countries to impose restrictions on the imports of creditor country.

4. To promote exchange stability :- The main aim of IMF is to promote exchange stability among the member countries. So it advises the member countries to conduct exchange transactions at agreed rates. On the other hand one country can change the parity of the currency without the consent of the IMF but it should not be more than 10%. If the changes are on large scale and IMF feels that according the circumstances of the country these are essential then it allows.

5. Temporary aid for the devalued currency :- When the devaluation policy is indispensable or any country then IMF provides loan to correct the balance of payment of that country.

6. To avoid exchange depreciation :- IMF is very useful to avoid the competitive exchange depreciation which took place before world war 2.

IBRD-INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

The **International Bank for Reconstruction and Development** (**IBRD**) is an international financial institution which offers loans to middle-income developing countries. The IBRD is the first of five member institutions which compose the World Bank Group and is headquartered in Washington, D.C., United States. It was established in 1944 with the mission of financing the reconstruction of European nations devastated by World War II. Together, the International Bank for Reconstruction and Development and its concessional lending arm, the International Development Association, are collectively known as the World Bank as they share the same leadership and staff.[1][2][3] Following the reconstruction of Europe, the Bank's mandate expanded to advancing worldwide economic and eradicating poverty. The IBRD provides commercial-grade or concessional financing to sovereign statesto fund projects that seek to improve transportation and infrastructure, education, domestic policy, environmental consciousness, energy investments, healthcare, access to food and potable water, and access to improved sanitation.

The IBRD is owned and governed by its member states, but has its own executive leadership and staff which conduct its normal business operations. The Bank's member governments are shareholders which contribute paid-in capital and have the right to vote on its matters. In addition to contributions from its member nations, the IBRD acquires most of its capital by borrowing on internationalcapital markets through bond issues. In 2011, it raised $29 billion USD in capital from bond issues made in 26 different currencies. The Bank offers a number of financial services and products, including flexible loans, grants, risk guarantees, financial derivatives, and catastrophic risk financing. It reported lending commitments of $26.7 billion made to 132 projects in 2011.

IDA- INTERNATIONAL DEVELOPMENT ASSOCIATION

The **International Development Association** (**IDA**) is an international financial institution which offers concessional loans andgrants to the world's poorest developing countries. The IDA is a member of the World Bank Group and is headquartered inWashington, D.C., United States. It was established in 1960 to complement the existing International Bank for Reconstruction and Development by lending to developing countries which suffer from the lowest gross national income, from troubled creditworthiness, or from the lowest per capita income. Together, the International Development Association and International Bank for Reconstruction and Development are collectively generally known as the World Bank, as they follow the same executive leadership and operate with the same staff.

The association shares the World Bank's mission of reducing poverty and aims to provide affordable development financing to countries whose credit risk is so prohibitive that they cannot afford to borrow commercially or from the Bank's other programs. The IDA's stated aim is to assist the poorest nations in growing more quickly, equitably, and sustainably to reduce poverty. The IDA is the single largest provider of funds to economic and human development projects in the world's poorest nations. From 2000 to 2010, it financed projects which recruited and trained 3 million teachers, immunized 310 million children, funded $792 million in loans to 120,000 small and medium enterprises, built or restored of 118,000 kilometers of paved roads, built or restored 1,600 bridges, and expanded access to improved water to 113 million people and improved sanitation facilities to 5.8 million people. The IDA has issued a total $238 billion USD in loans and grants since its launch in 1960. Thirty six of the association's borrowing countries have graduated from their eligibility for its concessional lending. However, eight of these countries have relapsed and have not re-graduated

IFC- INTERNATIONAL FINANCE CORPORATION

The International Finance Corporation (I.F.C) is an affiliated institution of World Bank. It was established on July 20, 1956 with the object of assisting private enterprises in developing countries by providing them with risk capital. The World Bank grant loans only to member governments or private enterprises with the guarantee of member government concerned. Again theWorld Bank provides only loan to private enterprises. Infact the development of private enterprises is held up for lack of adequate risk capital. Hence there was an urgent need for some international finance institution which would be willing to provide risk capital to the private industrial undertaking in developing countries. The I.F.C was set up to meet the participation requirement of private industrial undertakings.

OBJECTIVES OF THE I.F.C

The main objectives of the I.F.C is to accelerate the pace of economic development of the member countries in the under developed areas of the world in these ways.

- By investing in private productive enterprises in association with private investors and without any government guarantee of repayment.
- By bringing together investment opportunities, private capital, both foreign and domestic and experienced management.
- By stimulating productive investment of private capital, both foreign and domestic, in the developing countries for productive purposes.

MEMBERSHIP OF THE I.F.C-As already pointed out that the I.F.C is an affiliate of the World Bank. Its membership is separate from that of the World Bank. But it is only the members of the World Bank who can become members of the I.F.C. It is not essential that all the members of the World Bank should also be the members of the I.F.C, is optional for the members of the World Bank. Total membership of the I.F.C at present is 161.

ORGANIZATION OF THE I.F.C-All the powers of the I.F.C have been vested in the Board of Governors. There is one Governor from ach member country nominated by government of that country. The Board of Governors normally meets once a year to chalkout the general policy of the corporation. The general business of the I.F.C is carried on by the Board of Directors which meets at least once a month. There are 21 Executive Directors who constitute the Board of Directors of the corporation. The President of the World Bank is ex-officio Chairman of the Board of the Directors of I.F.C. Subject to this over all supervision, the day-to-day routine working of the corporation is conducted by the Executive Vice-President.

CAPITAL OF THE I.F.C-The Corporation was started in July 1956 with an authorized capital of 100 million dollars. The capital has been increased from time to time to meet the increasing requirements of the corporation. The Board of Directors has decided to double the authorized capital of I.F.C to 1,300 million dollars. The corporation has also been borrowing funds from the World Bank to supplement its financial resources.

INVESTMENT CRITERIA OF THE I.F.C-While extending financial assistance to enterprises the Corporation keeps following points in view.

The borrowing enterprises should be expected to make profits in course of time. Infect profitability is an essential criterion for loans to be made by the I.F.C.

The borrowing enterprises should be such as to make a definite contribution to

the economic development of the country in which it is located.
The corporation is prevented by its Charter to invest more than 22 million dollars in any single venture.
4. The corporation can make investment in a private enterprises only if more than 50 percent of the capital is forth from that enterprise itself.
So far as the equity is concerned the Corporation cannot provide more than 25 percent of the aggregate capital of the borrowing enterprise.

UNCTAD – UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

The **United Nations Conference on Trade and Development** (**UNCTAD**) (French *Conference des Nations unison le Commerce et le Développement (CNUCED)*) was established in 1964 as a permanent intergovernmental body.
UNCTAD is the principal organ of the United Nations General Assembly dealing with trade, investment, and development issues. The organization's goals are to: "maximize the trade, investment and development opportunities of developing countries and assist them in their efforts to integrate into the world economy on an equitable basis."
The primary objective of UNCTAD is to formulate policies relating to all aspects of development including trade, aid, transport, finance and technology. The conference ordinarily meets once in four years; the permanent secretariat is in Geneva.
One of the principal achievements of UNCTAD has been to conceive and implement the Generalised System of Preferences (GSP). It was argued in UNCTAD that to promote exports of manufactured goods from developing countries, it would be necessary to offer special tariff concessions to such exports. Accepting this argument, the developed countries formulated the GSP scheme under which manufacturers' exports and some agricultural goods from the developing countries enter duty-free or at reduced rates in the developed countries. Since imports of such items from other developed countries are subject to the normal rates of duties, imports of the same items from developing countries would enjoy a competitive advantage.
The creation of UNCTAD in 1964 was based on concerns of developing countries over the international market, multi-national corporations, and great disparity between developed nations and developing nations. The United Nations Conference on Trade and Development was established to provide a forum where the developing countries could discuss the problems relating to their economic development. The organisation grew from the view that existing institutions like GATT (now replaced by the World Trade Organization, WTO), the International Monetary Fund (IMF), and World Bank were not properly organized to handle the particular problems of developing countries. Later, in the 1970s and 1980s, UNCTAD was closely associated with the idea of a New International Economic Order (NIEO).
The first UNCTAD conference took place in Geneva in 1964, the second in New Delhi in 1968, the third in Santiago in 1972, fourth in Nairobi in 1976, the fifth in Manila in 1979, the sixth in Belgrade in 1983, the seventh in Geneva in 1987, the eighth in Cartagena in 1992 and the ninth at Johannesburg (South Africa) in 1996.
Currently, UNCTAD has 194 member states and is headquartered in Geneva, Switzerland. UNCTAD has 400 staff members and a bi-annual (2010–2011) regular budget of $138 million in core expenditures and $72 million in extra-budgetary technical assistance funds. It is a member of the United Nations Development Group. There are non-governmental organizations participating in the activities of UNCTAD.

Objectives - The objective of UNCTAD is (a) to reduce and eventually eliminate the trade gap between the developed and developing Countries, and (b) and to accelerate the rate of economic growth of the developing world.

Functions: The main Functions of the UNCTAD are:

- To promote international trade between developed and developing countries with a view to accelerate economic development.
- To formulate principles and policies on international trade and related problems of economic development.
- To make proposals for putting its principles and policies into effect, (iv) To negotiate trade agreements.
- To review and facilitate the coordination of activities of the other U.N. institutions in the

field of international trade.
- To function as a centre for a harmonious trade and related documents in development policies of governments.

Activities: The important activities of UNCTAD include (a) research and support of negotiations for commodity agreements; *(b)* technical elaboration of new trade schemes; and (c) various promotional activities designed to help developing countries in the areas of trade and capital flows.

RECENT TRENDS IN INTERNATIONAL BUSINESS/WORLD TRADE

The 1990s and the new millennium clearly indicate rapid internationalization and globalization. The entire globe is passing at a dramatic pace through the transition period. Today, the international trader is in a position to analyze and interpret the global social, technical, economic, political and natural environmental factors more clearly.

Conducting and managing international business operations is a crucial venture due to variations in political, social, cultural and economic factors, from one country to another country. For *example,* most of the African consumers prefer less costly products due to their poor economic conditions whereas the German consumers prefer high quality and high priced products due to their higher ability to buy. Therefore, the international businessman should produce and export less costly products to most of the African countries and vice versa to most of the European and North American countries. High priced and high quality Palmolive soaps are marketed in European countries and the economy priced Palmolive soaps are exported and marketed in
developing Countries like Ethiopia, Pakistan, Kenya, India, Cambodia etc.

International business houses need accurate information to make an appropriate decision. Europewas the most opportunistic market for leather goods and particularly for shoes. Bata based on theaccurate data could make appropriate decision to enter various European countries.International business houses need not only accurate but timely information. Coca-Cola couldenter the European market based on the timely information, whereas Pepsi entered later. Anotherexample is the timely entrance of Indian software companies into the US market compared tothose of other countries. Indian software companies also made timely decision in the case of'Europe.

The size of the international business should be large in order to have impact on the foreignEconomies. Most of the multinational companies are significantly large in size. In fact, theCapital of some of the MNCs is more than our annual budget and GDPs of the some of theAfrican countries. Most of the international business houses segment their markets based on thegeographic market segmentation. Daewoo segmented its market as North America, Europe,Africa, Indian subcontinent and Pacific markets.
International markets present more potentials than the domestic markets. This is due to the factthat international markets wide in scope varied in consumer tastes, preferences and Purchasingabilities, size of the population etc. For example, the IBM's sales are more in foreign countriesthan in USA, similarly, Coca-Cola's sales, Procter and Gamble's sales.

The size of the population, sometimes, may not determine the size of the market. This is due tothe backwardness of the economy and low purchasing power of the people, In fact, the size ofEritrea - an African country is roughly equal to that of the United Kingdom in terms of land areaand size of the population. But, in terms of per capita income it is one of the poorest countries inthe world with estimated per capita income of US $ 150 per annum. Therefore, the internationalbusiness houses should consider the consumers' willingness to buy and also ability to buy theproducts. In fact, most of the multinational companies, which entered Indian market after 1991,failed in this respect. They viewed that almost the entire Indian population would be thecustomers. Therefore, they estimated that the demand for consumer durable goods would beincreasing in India after globalisation. And they entered the Indian market. The heavy inflow ofthese goods and decline in the size of Indian middle class resulted in a slump in the demand for
consumer durable goods.

Wider Scope: Foreign trade refers to the flow of goods across national political borders.Therefore, it refers to exporting and importing by international marketing companies pluscreation of demand, promotion, pricing etc. As stated earlier, international business is muchbroader in scope. It involves international marketing, international investments, and managementof foreign exchange, procuring international finance from IMF, IBRD, IFC, IDA etc.,management of international human resources, management of cultural diversity, internationalmarketing, management of international production and logistics, international strategic management and the like. Thus, international business is broader in scope and covers all aspects
of the system.

Inter-country Comparative Study: International business studies the business opportunities,threats, consumers' preferences, behavior, cultures of the societies, employees, businessenvironmental factors, manufacturing locations, management styles, inputs and human resourcemanagement practices in various countries. International business seeks to identify, classify andinterpret the similarities and dissimilarities among the systems used to anticipate demand andmarket products'. The system presents inter-country comparison and inter-continentalcomparison/comparative analysis helps the management to evaluate the markets, finances,human resources, consumers etc. of various countries. The comparative study also helps themanagement to evaluate the market potentials of various countries.
The study also indicates the degree of consumer acceptance of the product, product changes anddevelopments in different countries. Managements of international business houses can group thecountries with similar features and design the same products, fix similar price and formulate thesame marketing strategies. For example, Prentice Hall grouped India, Nepal, PakistanBangladesh, Sri Lanka etc. into one category based on the customers' ability to pay and designedthe same quality product and sell them at the same price in all these countries. Similarly, Dr.Reddy's Lab does the same for its products to sell in the African countries.

Differences in Government Policies, Laws and Regulations: Sovereign governments enactand implement the laws, and formulate and implement policies and regulations. The internationalbusiness houses should follow these laws, policies and regulations. MNCs operating in Indiafollow our labor laws, business laws and policies and regulations formulated by the IndianGovernment.

Host Country's Monetary System: Countries regulate the price level, flow of money,production levels etc. through their monetary systems. In addition, they regulate foreignexchange rates also through the monetary system. The tools of monetary system include bankrate, cash reserve ratio, statutory liquidity ratio etc. Governments also regulate remittance of theprofit of international business houses to other countries. International companies should obeythese regulations. The Indian Government introduced full convertibility on current account; infact, many Governments introduced full convertibility on current account as a part of economicliberalisation.

National Security Policies of the Host Countries: Every country formulates the policies for itsnational security. Multinational companies should abide by these national security policies. Forexample, USA is a free economy as far as carrying out the business compared to many othercountries in the world. However, USA also imposes restrictions regarding the businessoperations, which affect the national security.

Cultural Factors: Cultural and custom factors vary widely from one country to the. Thesefactors include dressing habits, eating habits, religious factors and the like. Multinationalcompanies should consider these factors of the host country while operating in that country. *Forexample,* the culture of the Fiji people is that they attend to the family activities at least three times a day. Therefore, the companies operating in that country allow their workers to go homethree times a day. **Also, see Article 1 in Box.**

Article 1: impact of culture of Switzerland housewives on marketing of dishwashers
In Switzerland, foreign dishwasher manufacturers expected the same rapid sales as they had firstobtained in other West European markets; but sales in Switzerland were so slow that researchhad to be done to find out why (this research should, of course, have been done before not aftermarket entry). The research showed that the Swiss housewife had a different set of values to, forexample, her French and English counterparts; she was very conscious of her role as strict andhardworking and her responsibility for the health of her family. To the Swiss housewifedishwashers simply made life easy, and this conflicted with her Calvinistic work ethic. As aresult of this research, dishwasher manufacturers had to change their advertising promoting,
instead of ease and convenience, hygiene and health. They did this by emphasizing that becausedishwashers used temperature higher than hand hot, the process was more hygienic than washingup by hand. Thereafter, they had no automatic dishwashers in Switzerland.

Language: language is an important factor in international business. Even though 'Englishlanguage' is a major language in business operations in the world, there are still a large numberof 'non-English' speaking countries. Therefore, international business houses should train theiremployees in the local language of the host country. Added to this, there would be manylanguages in use in many, countries like ours. Therefore, the business houses should train theiremployees in the local languages also.
Nationalism and Business Policy: Nationalism is a dominating factor of the social life of thepeople of the host countries. In fact, nationalism also affects the business operations of themultinational corporations dramatically and drastically. The US people used the slogan **'BeAmerican and Buy American made'**, when the US automobile industry failed to meet thecompetition of Japanese automobile companies operating in USA. Similar incidents are alsoobserved in developing countries. Therefore, international business houses should be cautious ofnationalism and its after effects.

MULTINATIONAL CORPORATIONS AND WORLD TRADE
Introduction- The total foreign affiliates of MNCs, only little were developed countries . Foreign investment has been growing substantially faster than world output and export . Multinationals have been emerging from the developing countries . The diversified corporations have many odds against them and focus strategy is more successful
Definition: Multinational Corporation - The essential nature of the multinational enterprises lies in the fact that its managerial headquarters are located in one country while the enterprise carries out operations in a number of other countries as well International Marketing .
Five Criteria of MNC
It operates in many countries at different levels of economic development
Its local subsidiaries are managed by nationals
It maintains complete industrial organizations, including R and D and manufacturing facilities, in several countries
It has a multinational central management
It has multinational stock ownership International Marketing
Organizational Transformation- MNC is now increasingly assuming the role of an orchestrator of production and transactions within a cluster, or network, of cross border internal-external relationships, which may or may not involve equity investment, but which are intended to serve its global interests.

Globalization of business- Globalization is a way of corporate life necessitated, facilitated and nourished by the transnationalisation of the world economy and developed by corporate strategies.
Dimensions of Globalization
Doing or planning of expand, business globally.
Giving up the distinction between the domestic and foreign market and developing a global outlook of the business.
Locating the production and other physical facilities on a consideration of the global business dynamics, irrespective of national considerations.
Basing product development and production planning on the global market consideration.
Global sourcing of factors of production i.e., raw materials, components, machinery/technology, finance etc. are obtained from the best source anywhere in the world

Global orientation of organizational structure and management culture.

Dominance of MNCs and global economy

„ The global liberalization has paved the way for fast expansion and growth of the MNCs

„ The economic clout of the MNCs is indicated by the GDP of most of the countries is smaller then the value of the annual sales turnover of the multinational giants

MNCs and international trade

The sale of foreign subsidiaries in the host countries are three to four times as large as total world exports Significant increase in the export intensity of the foreign affiliates of MNCs . The abilities of multinationals to manipulate financial flows by the use of artificial transfer prices is bound to be a matter of concern government.

Merits of MNCs

MNCs help increase the investment level and thereby the income and employment in host country.

The transnational corporations have become vehicles for the transfer of technology, especially to the developing countries.

They also kindle a managerial revolution in the host countries through professional management and the employment of highly sophisticated management techniques.

The MNCs enable the host countries to increase their exports and decrease their import requirements.

5.They work to equalize the cost of factors of production around the world.

MNCs provide an efficient means of integrating national economics.

The enormous resources of the multinational enterprises enable them to have very efficient research and development systems. Thus they make a commendable contribution to inventions and innovations.

MNCsalso stimulate domestic enterprise because to support their own operations, the MNCsmay encourage and assist domestic suppliers.

MNCs help increase competition and break domestic monopolies.

Demerits of MNCs

The MNCs technology is designed for world wide profit maximization, not the development needs of poor countries. The imported technologies are not adapted to

- consumption needs
- size of domestic markets
- resource availabilities
- stage of development of many of the LDCs.

Through their power and flexibility, MNCs can evade or undermine national economic autonomy and control and their activities may be inimical to the national interests of particular countries.

MNCs may destroy competition and acquire monopoly powers.

The tremendous power of the global corporations poses the risk that they may threaten the sovereignty of the nations in which they do business.

MNCs retard growth of employment in the home country.

The transnational corporations cause fast depletion of some of the non-renewable natural resources in the host country.

The transfer pricing enables MNCs to avoid taxes by manipulating prices on intra-company transactions.

Growth Perspective of MNCs

Increasing emphasis on market forces and a growing role for the private sector in nearly all developing countries.

Rapidly changing technologies that are transforming the nature of organization and location of international production.

The globalization of firms and industries

The rise of services to constitute the largest single sector in the world economy

Regional economic integration

Code of Conduct

A framework to allow developing countries as well as transnational corporations to benefit from direct investments on terms contractually agreed upon

Legislation

Cooperation by governments

Fiscal and other incentives and policies towards foreign investment

An international procedure for discussions and consultations

Multinationals in India- In India the government policy confined the foreign investment to the priority areas like high technology and heavy investment sectors of national importance and export sectors. Firms which had been established in non-priority areas prior to the implementation of this policy have, however, been allowed to continue in those sectors. Several Indian outfits of MNCs are in the low technology consumer goods sector. There are many MNCs which are in high technology area. Since the economic liberalization unshared in 1991, many multinationals in different lines of business have entered the Indian market.

UNIT IV

EXIM POLICY

Every country has to regulate its own international trade mainly due to the specific reasons:

(i) improving its balance of trade and balance of payments position. Most of the developing countries face balance of payments, problem and, therefore, they struggle hard to maintain the balance in their imports and exports,

(ii) Protecting its own industries against the competition in the international market or in domestic markets from foreign products, and

(iii) Exploiting its manpower and natural resources to the maximum extent possible so that country's economic development may be done at a faster speed. In order to attain these objectives, almost every country imposes certain restrictions on its international trade, i.e., imports and exports. These restrictions may be called trade barriers.

Trade barriers may be:

(i) Tariff barriers and

(ii) Non-tariff or protective barriers.

(1) **Tariff barriers.** Tariff have been one of the classical methods of regulating international trade. Tariffs may be referred to as taxes levied on the imports. It aims at restricting the inward flow of goods from other countries to protect the country's own industries by making the goods costlier in that country. Sometimes the duty on a product is so steep that it does not become worthwhile to import it. In addition, the duties so imposed provide a substantial source of revenue to the importing country.

In India, customs duty from a significant part of total revenue and, therefore, is an important element in preparing the budget. Some countries use this method of imposing tariffs and customs to balance its balance of trade. A nation may also use this method to influence the political and economic policies of other countries. It may impose tariffs on certain imports from a particular country as a protest against tariffs imposed by that country on its goods.

In order to ensure that the system of imposing custom duties is not discriminatory, a multilateral association comprising a number of countries of the world, has been formed to help formulate trade policies of the member countries. This association is popularly known as General Agreement on Tariff and Trade (GATT) discussed in question 2.1 and its main objective is to reduce duties and other import levies systematically through mutual negotiations. It ensures that every member country enjoys a status of Most Favored Nation (MFN) and a member country must charge the tariffs and customs duties at the lowest rate unless otherwise settled bilaterally.

Kinds of tariffs. Tariffs may be classified according to

(i) the purpose of taxes, and

(ii) how they are levied.

(i) As far as the purpose of taxes is concerned, tariffs may be classified into two categories,

(a) Revenue tariff, and

(b) Protective tariff.

Revenue tariffs are basically intended to raise the Government revenue without intending to protect any industry of the country. It is levied at a fairly low rate and does not obstruct the free flow of imports.

Protective tariffs, on the other hand, aim at protecting the domestic industries and the generally levied at a very high rate and, therefore, obstruct the free flow of imports. Its main purpose is not to increase revenue but to provide a safeguard to the domestic industries against foreign competitions in the local market.

Tariffs sometimes are levied to discriminate between countries, e.g., tariffs are imposed on certain goods having certain specifications which are imported from a particular country.

(ii) **On the basis of method how tariffs are computed** Tariffs may be put into two categories-
(a) Specific tariffs, and
(b) Ad valorem tariffs.

Specific duties or tariffs are imposed on the basis of per unit of any identifiable characteristics of merchandise such as per unit of weight, volume, length, number or any other unit of quality of goods. The duty schedules so specified must specify the rate of duty as well as the determining factor such as weight, number etc. and the basis of arriving at determining factor such as gross weight, net weight or fare weight etc.
Ad valorem tariffs are based on the value of imports and are charged in the form of a specify percentage of the value of goods. The schedule should specify how the value of the imported goods would be arrived at.

Other Tariffs. In order to protect the domestic industries against competition, some other tariffs are also imposed. Among them two are important-
(a) Anti dumping duty and
(b) Counteracting duties.

(a) Anti-dumping duties. Very often, exporters from developed countries are eager to sell their products in the foreign markets with a view to capture a large market, at a very low price not proportionate to their cost of production. This attempt to introduce their products in a large quantity into foreign market at a very low price, even lower than cost, is called 'dumping'.
The Government of the importing country, there, therefore, impose customs duty on such goods at a very high rate to counteract this unfair competition. This duty is known as 'anti-dumping duties'. Such duties are charged in addition to the normal customs duty on the product. This additional charge would cover at least the difference between the export price and the normal price or market price in the exporting country.

(b) Counteracting duties. These are similar to the anti-dumping duties, and are charged on goods, imported from countries where the manufacturer-exporter is paid, directly or indirectly, a subsidy as an incentive for export. The amount of duty normally does not exceed the estimated amount of subsidy.

NON-TARIFF BARRIERS
Over the last few years, GATT has been endeavoring to achieve a reduced and rationalized tariff structure for trade among its member countries As per terms of GATT, every member, country will accord MFN treatment to all other member countries while importing goods from them. At the same time, importing countries are also concerned with development of their own industries and trade. They will have to protect them against unfair competition with a view to giving the domestic industry a fair chance for survival. To meet the challenges, more and more countries are adopting non-tariff measures, regulate their imports. Such measures may be called 'non-tariff barriers'. Some of these non-tariff measures are-
(a) Quantity restrictions, quotas and licensing procedures;
(b) Foreign exchange restrictions;
(c) Technical and administrative regulations;
(d) Consular formalities;
(e) State trading; and
(f) Preferential arrangements.
We shall discuss these measures in brief hereunder-
(a) **Quantity restrictions, quotas and licensing procedures.** Under quantity restrictions, the maximum quantity of different commodities which would be allowed to be imported over a period of time from various countries is fixed in advance. The quantity allowed to be imported or quota fixed normally depends upon the relations of the two countries and the need of the importing country. There is, therefore, no effect of price level changes in foreign or domestic markets and the Government is in a position to restrict the imports to a desired level. Quotas are very often combined with licensing system to regulate the flow of imports over the quota period as also to allocate them between various importers and supplying countries. Under this system, a license or a permit is to be obtained from the Government to import the goods specifying the quantity and the country, from which to import, before concluding the contract with the supplier.

(b) **Foreign exchange restrictions.** Exchange control measures have been widely used by a number of developing countries in the post-war period to regulate their imports and keep the balance of payments in controllable limits. Under this system, the importer must be sure that adequate foreign exchange would be made available to him for the imports of goods by obtaining a clearance from the exchange control authorities of the country before concluding the contract with the supplier.

(c) **Technical and administrative regulations.** The another measure to regulate the imports is the imposition of certain standard of technical production, technical specifications etc. to which an importing commodity must conform. Such types of technical restrictions are imposed in case of pharmaceutical products, etc.

(d) **Consular formalities.** A number of countries demand that shipping documents must accompany the consular documents etc. Sometimes, it is also insisted that such documents should be drawn in the language of importing countries. In case the documentation is faulty or not drawn in the language of importing country, heavy penalties are imposed. Fees charged for such documentation are quite heavy.

(e) **State trading.** In most of the socialistic countries, foreign trade, i.e. import and export transactions, is exclusively handled or canalized by certain state agencies. Separate state agencies are set up for each class of products. The agencies carry on the international trade strictly according to the Government policies.

India is a good example where state trading is followed in a restricted sense. Some articles, as decided by the Government, are imported only through the State Trading Corporation (STC). Likewise, exports of raw materials such as iron ore, mica etc. are canalized only through Minerals and Metals Trading Corporation.(MMTC).

(f) **Preferential arrangement.** With the evolvement of multilateral trading system, a few member countries agree to a small advantageous group for their mutual benefit. The member countries of the group negotiate and arrive at a settlement preferential tariff rate to carry on trade amongst them. The rates are much lower than ordinary tariff rates and applicable only to the member nations of the small group. Such types of preferential arrangements are outside the purview of the GATT. Some of the small groups are EEC, ASEAN, and LAFTA etc.

Differences between Tariff and Non-tariff Barriers

The purpose of tariff and non-tariff barriers is to regulate the free flow of imports. However, the following differences may note in their operation.

(i) With tariffs the Government **receives the revenue** whereas no revenue is received by the Government by applying non-tariff measures. However, it is favored as an appropriate measure to meet the demand of the country and to protect the industry.

(ii) Non-tariff measures **protect the producers** and make them feel more secure than under a tariff. Producers are inclined to produce more for domestic as well as for international market under non-tariff barriers. Such incentives are not there under tariffs.

(iii) **Customs classification and valuation procedures** pose a problem before the customs authorities whereas under non tariff measures no such problem arises.

(iv) Non-tariff barriers to trade induce the domestic producers **to form monopolistic organization** with a view to keeping output low and prices high. This is not possible under an import duty. If the price of products continues to rise due to the operation of monopolistic tendencies, imports became attractive even after the import duty is paid. Thus non-tariff barriers remain ineffective monopolistic tendencies prevail in the country.

(v) Imposition of tariffs and amendments therein are subject to **legislative enactment and** therefore are more or less inflexible further, in many cases, the scope for adjustments especially an upward revision of tariffs is very limited due to the commitment under **GATT**. On the other hand, non-tariff measures are often more flexible than tariff because the grant of import license or release foreign exchange is a matter of official discussion in regard to the timing and quantity.

(vi) Under tariffs, **price differences** between the importing and exporting countries will be only equal to the costs of tariffs and transportation. If differences are more than this, they will be eliminated by competition. But the price differences will be greater in two countries in non-tariff measures are adopted because there no free flow of imports.

(vii) As because the difference in prices of the product in two countries is more than the costs of tariffs and transportation under non-tariffs. **The importers earn huge profits and it makes the business of importing more lucrative.** But under the tariff system, there are no such complications because flow of goods is not restricted and therefore the price difference cannot be more than the costs of tariffs and transportation for long. There are, therefore, no huge profits to imports.

(viii) From the point of view of **administrative conveyance** tariffs are more simple to operate. Tariff rates once fixed through legislation, require to individual allocation of licensing, quotas or exchange. There are, however, a number of authorities for the administration of non-tariff measures. It may result in some sort of political interference or corruption.

(ix) **Tariffs favor particularly to efficient firms** in the country because only they can bear the competition, whereas non-tariff measures benefit the established firm because they get quotas or import licenses on the basis of their past representation and, therefore, **non-tariffs discriminate against newcomers.**

Thus both the measures-tariffs and non-tariffs-are not free from defects and, therefore, one cannot be advantageous to adopt individually. Both the measures are to be operated simultaneously to eliminate the ill-effects of each other and to get the best for the economy.

Why have Non-tariff Barriers Become More Important

We may come to the conclusion from the above discussion that tariffs earn the revenue for the Government of importing country. It shields domestic industries from foreign competition and therefore provides them an opportunity to grow to contribute to the national economy. On the other hand, tariffs increase the price of the commodities imported but do not check the inflow of goods effectively.

Moreover, the arrangement under GATT (General Agreement on Tariff and Trade) does not permit a country to impose discriminatory rates of tariffs for member countries unless otherwise agreed upon bilaterally. Under the agreement, every member country should be given Most Favored Nation (MFN) treatment from other member nations and they should be charged tariffs at the lowest rates. GATT, more often, attempts to reduce systematically duties and other import levies. The developing countries, therefore, find it difficult in such arrangements to protect their own industries and trade against international competition. With a view to giving the domestic industry a fair chance for survival, these tariff barriers are considered very seriously especially by developing countries.

In order to combat these limitations effectively, more and more countries have been adopting a number of non-tariff measures aimed at regulating their import trade. The most common non-tariff measures adopted by less developed countries are introducing quota system and licensing procedures, foreign exchange restrictions and bilateral arrangements. Technical and administrative regulations, state trading and consular formalities are preferred only in restricted sense to achieve only certain desired goods.

In short, it may be concluded that recently non-tariff measures have became more important than tariffs regulating the imports of a country in the desired direction keeping in mind the balance of trade and balance of payment situations.

HIGHLIGHTS OF THE FOREIGN TRADE POLICY 2015-2020

A. SIMPLIFICATION & MERGER OF REWARD SCHEMES

Export from India Schemes:

1. Merchandise Exports from India Scheme (MEIS)

(a) Earlier there were 5 different schemes (Focus Product Scheme, Market Linked Focus Product Scheme, Focus Market Scheme, Agri. Infrastructure Incentive Scrip, VKGUY) for rewarding merchandise exports with different kinds of duty scrips with varying conditions (sector specific or actual user only) attached to their use. Now all these schemes have been merged into a single scheme, namely Merchandise Export from India Scheme (MEIS) and there would be no conditionality attached to the scrips issued under the scheme. The main features of MEIS, including details of various groups of products supported under MEIS and the country groupings are at Annexure-1.

(b) Rewards for export of notified goods to notified markets under 'Merchandise Exports from India Scheme (MEIS) shall be payable as percentage of realized FOB value (in free foreign exchange). The debits towards basic customs duty in the transferable reward duty credit scrips would also be allowed adjustment as duty drawback. At present, only the additional duty of customs / excise duty / service tax is allowed adjustment as CENVAT credit or drawback, as per Department of Revenue rules.

2. Service Exports from India Scheme (SEIS)

(a) Served From India Scheme (SFIS) has been replaced with Service Exports from India Scheme (SEIS). SEIS shall apply to 'Service Providers located in India' instead of 'Indian Service Providers'. Thus SEIS provides for rewards to all Service providers of notified services, who are providing services from India, regardless of the constitution or profile of the service provider. The list of services and the rates of rewards under SEIS are at Annexure-2.

(b) The rate of reward under SEIS would be based on net foreign exchange earned. The reward issued as duty credit scrip, would no longer be with actual user condition and will no longer be restricted to usage for specified types of goods but be freely transferable and usable for all types of goods and service taxdebits on procurement of services / goods. Debits would be eligible for CENVAT credit or drawback.

3. Chapter -3 Incentives (MEIS & SEIS) to be available for SEZs

It is now proposed to extend Chapter -3 Incentives (MEIS & SEIS) to units located in SEZs also.

4. Duty credit scrips to be freely transferable and usable for payment of custom duty, excise duty and service tax.

(a) All scrips issued under MEIS and SEIS and the goods imported against these scrips would be fully transferable.

(b) Scrips issued under Exports from India Schemes can be used for the following:-

(i) Payment of customs duty for import of inputs / goods including capital goods, except items listed in Appendix 3A.

(ii) Payment of excise duty on domestic procurement of inputs or goods, including capital goods as per DoR notification.

(iii) Payment of service tax on procurement of services as per DoR notification.

(c) Basic Customs Duty paid in cash or through debit under Duty Credit Scrip can be taken back as Duty Drawback as per DoR Rules, if inputs so imported are used for exports.

5. Status Holders

(a) Business leaders who have excelled in international trade and have successfully contributed to country's foreign trade are proposed to be recognized as Status Holders and given special treatment and privileges to facilitate their trade transactions, in order to reduce their transaction costs and time.

(b) The nomenclature of Export House, Star Export House, Trading House, Star Trading House, Premier Trading House certificate has been changed to One, Two, Three, Four, Five Star Export House.

(c) The criteria for export performance for recognition of status holder have been changed from Rupees to US dollar earnings. The new criteria is as under:-

Status category	Export Performance FOB / FOR (as converted) Value (in US $ million) during current and previous two years
One Star Export House	3
Two Star Export House	25
Three Star Export House	100
Four Star Export House	500
Five Star Export House	2000

(d) **Approved Exporter Scheme - Self certification by Status Holders**
Manufacturers who are also Status Holders will be enabled to self-certify their manufactured goods as originating from India with a view to qualify for preferential treatment under different Preferential Trading Agreements [PTAs], Free Trade Agreements [FTAs], Comprehensive Economic Cooperation Agreements [CECAs] and Comprehensive Economic Partnerships Agreements [CEPAs] which are in operation. They shall be permitted to self-certify the goods as manufactured as pertheir Industrial Entrepreneur Memorandum (IEM) / Industrial Licence (IL)/ Letter of Intent (LOI).

B. BOOST TO "MAKE IN INDIA"
6. Reduced Export Obligation (EO) for domestic procurement under EPCG scheme:
Specific Export Obligation under EPCG scheme, in case capital goods are procured from indigenous manufacturers, which is currently 90% of the normal export obligation (6 times at the duty saved amount) has been reduced to 75%, in order to promote domestic capital goods manufacturing industry.

7. Higher level of rewards under MEIS for export items with high domestic content and value addition.
It is proposed to give higher level of rewards to products with high domestic content and value addition, as compared to products with high import content and less value addition.

C. TRADE FACILITATION & EASE OF DOING BUSINESS
8. **Online filing of documents/ applications and Paperless trade in 24x7 environment:**
(a) DGFT already provides facility of Online filing of various applications under FTP by the exporters/importers. However, certain documents like Certificates issued by Chartered Accountants/ Company Secretary / Cost Accountant etc. have to be filed in physical forms only. In order to move further towards paperless processing of reward schemes, it has been decided to develop an online procedure to upload digitally signed documents by Chartered Accountant / Company Secretary / Cost Accountant. In the new system, it will be possible to upload online documents like annexure attached to ANF 3B, ANF 3C and ANF 3D, which are at present signed by these signatories and submitted physically.

(b) Henceforth, hardcopies of applications and specified documents would not be required to be submitted to RA, saving paper as well as cost and time for the exporters. To start with, applications under Chapter 3 & 4 of FTP are being covered (which account for nearly 70% of total applications in DGFT). Applicationsunder Chapter-5 would be taken up in the next phase.

(c) As a measure of ease of doing business, landing documents of export consignment as proofs for notified market can be digitally uploaded in the following manner:-
(i) Any exporter may upload the scanned copy of Bill of Entry under his digital signature.
(ii) Status holders falling in the category of Three Star, Four Star or Five Star Export House may upload scanned copies of documents.

9. Online inter-ministerial consultations:

It is proposed to have Online inter-ministerial consultations for approval of export of SCOMET items, Norms fixation, Import Authorisations, Export Authorisation, in a phased manner, with the objective to reduce time for approval. As a result, there would not be any need to submit hard copies of documents for these purposes by the exporters.

10. Simplification of procedures/processes, digitisation and e-governance

(a) Under EPCG scheme, obtaining and submitting a certificate from an independent Chartered Engineer, confirming the use of spares, tools, refractory and catalysts imported for final redemption of EPCG authorizations has been dispensed with.

(b) At present, the EPCG Authorisation holders are required to maintain records for 3 years after redemption of Authorisations. Now the EPCG Authorization Holders shall be required to maintain records for a period of two years only. Government's endeavour is to gradually phase out this requirement as the relevant records such as Shipping Bills, e-BRC are likely to be available in electronic mode which can be archived and retrieved whenever required.

(c) Exporter Importer Profile: Facility has been created to upload documents in Exporter/Importer Profile. There will be no need to submit copies of permanent records/ documents (e.g. IEC, Manufacturing licence, RCMC, PAN etc.) repeatedly with each application, once uploaded.

(d) Communication with Exporters/Importers: Certain information, like mobile number, e-mail address etc. has been added as mandatory fields, in IEC data base. This information once provided by exporters, would help in better communication with exporters. SMS/ email would be sent to exporters to inform them about issuance of authorisations or status of their applications.

(e) Online message exchange with CBDT and MCA: It has been decided to have on line message exchange with CBDT for PAN data and with Ministry of Corporate Affairs for CIN and DIN data. This integration would obviate the need for seeking information from IEC holders for subsequent amendments/ updation of data in IEC data base.

(e) Communication with Committees of DGFT: For faster and paperless communication with various committees of DGFT, dedicated e-mail addresses have been provided to each Norms Committee, Import Committee and Pre-Shipment Inspection Agency for faster communication.

(f) Online applications for refunds: Online filing of application for refund of TED is beingintroduced for which a new ANF has been created.

11. Forthcoming e-Governance Initiatives

(a) DGFT is currently working on the following EDI initiatives:

(i) Message exchange for transmission of export reward scrips from DGFT to Customs.

(ii) Message exchange for transmission of Bills of Entry (import details) from Customs to DGFT.

(iii) Online issuance of Export Obligation Discharge Certificate (EODC).

(iv) Message exchange with Ministry of Corporate Affairs for CIN & DIN.

(v) Message exchange with CBDT for PAN.

(vi) Facility to pay application fee using debit card / credit card.

(vii) Open API for submission of IEC application.

(viii) Mobile applications for FTP

D. Other new Initiatives

12. New initiatives for EOUs, EHTPs and STPs

(a) EOUs, EHTPs, STPs have been allowed to share infrastructural facilities among themselves. This will enable units to utilize their infrastructural facilities in an optimum way and avoid duplication of efforts and cost to create separate infrastructural facilities in different units.

(b) Inter unit transfer of goods and services have been allowed among EOUs, EHTPs, STPs, and BTPs. This will facilitate group of those units which source inputs centrally in order to obtain bulk discount. This will reduce cost of transportation, other logistic costs and result in maintaining effective supply chain.

(c) EOUs have been allowed facility to set up Warehouses near the port of export. This will help in reducing lead time for delivery of goods and will also address the issue of un-predictability of supply orders.

(d) STP units, EHTP units, software EOUs have been allowed the facility to use all duty free equipment/goods for training purposes. This will help these units in developing skills of their employees.

(e) 100% EOU units have been allowed facility of supply of spares/ components up to 2% of the value of the manufactured articles to a buyer in domestic market for the purpose of after sale services.
(f) At present, in a period of 5 years EOU units have to achieve Positive Net Foreign Exchange Earning (NEE) cumulatively. Because of adverse market condition or any ground of genuine hardship, then such period of 5 years for NFE completion can be extended by one year.
(f) Time period for validity of Letter of Permission (LOP) for EOUs/EHTP/ STPI/BTP Units has been revised for faster implementation and monitoring of projects. Now, LOP will have an initial validity of 2 years to enable the unit to construct the plant and install the machinery. Further extension can be granted by the Development Commissioner up to one year. Extension beyond 3 years of the validity of LOP, can be granted, in case unit has completed 2/3rd of activities, including the construction activities.
(g) At present, EOUs/EHTP/STPI units are permitted to transfer capital goods to other EOUs, EHTPs, STPs, SEZ units. Now a facility has been provided that if such transferred capital goods are rejected by the recipient, then the same can be returned to the supplying unit, without payment of duty.

(h) A simplified procedure will be provided to fast track the de-bonding / exit of the STP/ EHTP units. This will save time for these units and help in reduction of transaction cost.
(i) EOUs having physical export turnover of Rs.10 crore and above, have been allowed the facility of fast track clearances of import and domestic procurement. They will be allowed fast tract clearances of goods, for export production, on the basis of pre-authenticated procurement certificate, issued by customs / central excise authorities. They will not have to seek procurement permission for every import consignment.

13. **Facilitating & Encouraging Export of dual use items (SCOMET).**
(a) Validity of SCOMET export authorisation has been extended from the present 12 months to 24 months. It will help industry to plan their activity in an orderly manner and obviate the need to seek revalidation or relaxation from DGFT.
(b) Authorisation for repeat orders will be considered on automatic basis subject to certain conditions.
(c) Verification of End User Certificate (EUC) is being simplified if SCOMET item is being exported under Defence Export Offset Policy.
(c) Outreach programmes will be conducted at different locations to raise awareness among various stakeholders.

14 Facilitating & Encouraging Export of Defence Exports
(a) Normal export obligation period under advance authorization is 18 months. Export obligation period for export items falling in the category of defence, military store, aerospace and nuclear energy shall be 24 months from the date of issue of authorization or co-terminus with contracted duration of the export order, whichever is later. This provision will help export of defence items and other high technology items.
(b) A list of military stores requiring NOC of Department of Defence Production has been notified by DGFT recently. A committee has been formed to create ITC (HS) codes
for defence and security items for which industrial licenses are issued by DIPP.

15. e-Commerce Exports
(a) Goods falling in the category of handloom products, books / periodicals, leather footwear, toys and customized fashion garments, having FOB value up to Rs.25000 per consignment (finalized using e-Commerce platform) shall be eligible for benefits under FTP. Such goods can be exported in manual mode through Foreign Post Offices at New Delhi, Mumbai and Chennai.
(b) Export of such goods under Courier Regulations shall be allowed manually on pilot basis through Airports at Delhi, Mumbai and Chennai as per appropriate amendments in regulations to be made by Department of Revenue. Department of Revenue shall fast track the implementation of EDI mode at courier terminals.

16. Duty Exemption
(a) Imports against Advance Authorization shall also be eligible for exemption from Transitional Product Specific Safeguard Duty.

(b) In order to encourage manufacturing of capital goods in India, import under EPCG Authorisation Scheme shall not be eligible for exemption from payment of anti-dumping duty, safeguard duty and transitional product specific safeguard duty.

17. Additional Ports allowed for Export and import

Calicut Airport, Kerala and Arakonam ICD, Tamil Nadu have been notified as registered ports for import and export.

18. Duty Free Tariff Preference (DFTP) Scheme

India has already extended duty free tariff preference to 33 Least Developed Countries (LDCs) across the globe. This is being notified under FTP.

19. Quality complaints and Trade Disputes

(a) In an endeavour to resolve quality complaints and trade disputes, between exporters and importers, a new chapter, namely, Chapter on Quality Complaints and Trade Disputes has been incorporated in the Foreign Trade Policy.

(b) For resolving such disputes at a faster pace, a Committee on Quality Complaints and Trade Disputes (CQCTD) is being constituted in 22 offices and would have members from EPCs/FIEOs/APEDA/EICs.

20. Vishakhapatnam and Bhimavaram added as Towns of Export Excellence

Government has already recognized 33 towns as export excellence towns. It has been decided to add Vishakhapatnam and Bhimavaram in Andhra Pradesh as towns of export excellence (Product Category–Seafood)

BALANCE OF PAYMENT

Balance of payment of the most important statistical statement for any country. The balance of payments of the balance of international payments of a country is a systematic record of all international economic transactions of that country during a given period usually a year. It is principal fool for the analysis of the monetary aspects of international trade and other economic transaction between the residents of one country and residents to the rest of the world. The record is so prepared as to provide meaning and measure of the various components of a country's external economic transactions. The aim is to present an account of all receipts and payment on account of goods, service and capital movement. Balance of payment is used in two different senses. First, in the accounting sense, as an accountant or as a complete record of all economic transactions between one country and the rest of the world. In this sense, the balance of payment follows the accountant's rule namely that the balance payment must always balance. Credit must always equal debits. This is true when all transactions are taken together. Second in the economic sense.

Prof. Benham "The Balance of payment of country is a record of its monetary transaction over a period with the rest of the world."

Prof. Walter Krause "The balance of payment of a country is a systematic record of account economic transactions completed between its residents and residents of the rest of the rest of the world during a given period of time usually a year."

CHARACTERISTICS OF BALANCE FO PAYMENT

On the basis of all the above mentioned definitions, the main characteristics of the concept of balance of trade are as follow.

Systematic Record of Economic transaction – The balance of payment's a comprehensive and systematic record of all international economic transactions of one country with the rest of the world.

Related with a Given Period of Time – The balance of payments is recorded for a particular period and it is usually a year.

It is an Account or Statistical Statement – The balance of payment has two sides namely receipts and payments or credit and debit as we have in an account. So the balance of payment is presented in the form of an account or statistical statement.

It shows the Relations Between Receipts and Payments – The balance of payment shows the mutual relationship between all receipts and payments and this relationship on each item could be either plus or minus or the relationship could be of two types favourable and unfavorable.
More Comprehensive – The balance of payment is more comprehensive in comparison to balance of trade as it includes all items of international monetary transactions whether visibles or invisibles. Goods or Service, Income or Capital.
Use or Residents in Comprehensive Sense – The terms residents includes all parties whether individuals of firms companies or institutions government or private. It includes all economic units of a country.
Balance of payments always Balance – From the accounting of view, this statement is true because all credits or receipts must always equal to all debit or payments.

COMPONENTS / STRUCTURE / ITEMS OF BOP
It is usually composed of two accounts by all the countries; Current account and (ii) Capital account
Some countries have more accounts like goods account, services account, unilateral transfers account, long terms capital account, short terms capital account, international liquidity account, official reserve assets account etc, and in all these different accounts there are several items of receipts and payment. In our country the responsibility to keep the proper record of all international economic and monetary transactions has been entrusted to the central Bank. The Reserve Bank of India (RBI) designs the format of Balance Of Payment (BOP) and it also from time to time modify the format. We will analyse the different items of balance of payments according the format of RBI –

ITEMS OF BALANCE OF PAYMENT
The Current Account – The current account consists of two major items namely -
Merchandise Exports and Imports and
Invisibles
Merchandise Exports and Imports and – Merchandise exports and imports refer to the total value of export and imports in goods. This first and single largest item of the balance of payment is popularly known as "international trade". The difference or balance of export and imports of a country is called the "Balance of Trade". It the exports exceed imports the balance of trade is favourable. In the opposite side it is unfavorable.
Invisibles or Trade in Services – The invisibles account usually comprises the services, gifts or charities. The important services are
Tours and Travels – For business, education, health, pleasure, pilgrimage like Haj or international conventions.
International Transportations Services
Banking services
Insurance Services
technical and Consultancy services
communication services

In addition to various services in current account under invisible account we also include;
Investment Income – Receipts and payment of Dividends, rents, profit and other income.
Transfer Payments – Transfer payments represent unilateral receipts and payments by private individuals or by government and include such things as grants aid donations gifts or charities etc. It is also called as receipts and payments without considerations.
Transfer or unilateral payments received form abroad are credits and those made abroad are debits.
Official reserves – Official reserves represent the holdings by the government or official agencies of the means of payment that are generally accepted for the settlement of international claims.
Repayment of Commercial Credit
Contractual amortization and Depreciation of Direct investment
Government expenditure
Miscellaneous services like patent fees, royalties, membership and subscription to journals and periodicals etc.

Capital Account – The capital account shows the capital inflows and outflows. Capital inflow represents credits while capital outflow represents debit. This account consists of short-terms and long-terms capital transactions. The main items in this account includes -
External Assistance _ all assistance, aid form other countries and it also include borrowing from foreign countries under concessional rate.
Commercial Borrowings – It includes all borrowings which the Government of India and private sector borrows funds from world money markets.
Banking Capital
Short Terms Credits
NRI Deposits and Remittances
Foreign investment – Which includes foreign direct investment (FDI), foreign institutional investors (FIIs) and Euro Equities, Bonds and others.
Rupee Debt Service.
Other miscellaneous flows.
In addition to these two major accounts of current accounts and capital accounts, there are following important items which are also included in our balance of payments.
I.M.F.
SDR Allocation
Gold Movement
International Monetary Foreign Exchange Reserves
Errors and Omissions.

SIGNIFICANCE OF BALANCE OF PAYMENTS

The balance of payment is regarded as the most important statistical statement of a country which comprehensively depicts the entire external situation of that country as a recordsits all international monetary transactions its importance can be confirmed by analysing the following points or significance.

Knowledge of Country's Economic position – As Balance of payment provides the entire international economic transactions of a country so with the analysis of balance of payment we could get the knowledge of country's economic transactions.

Helpful in the Analysis and Solution of Economic Problems – By having the knowledge of economic position of the country and knowing the economic problems the economic by analysing the problems could suggest practical means of solutions of those economic problems.

Helpful formulation of appropriate Economic Policies – the help of analysis of balance of payment, several policies of the nation could be formulated and implemented. The balance of payment has larger in fluency on all the economic policies particularly the commercial or EXIM policy, Fiscal policy, Monetary policy, industrial policy etc.

INDENTIFYING OPPORTUNITIES IN FOREIGN AND OVERSEAS MARKETS

An SME contemplating global expansion needs to take two strategic decisions i.e. which markets to enter and how to enter the market chosen. Depending upon the competitive strength of the firm and market opportunities, the selection of the product or services to be offered in the international market and the target markets is being made.

Market Identification and Selection: Any firm wanting to internationalize its operations may adopt either a reactive or a proactive approach to market identification as described below:

*Reactive Approach to Market Identification:*Most firms internationalize as an unintended response to an international marketing opportunity in the form of unsolicited export orders. In doing so, the positive stimulus in terms of increased profitability, turnover, market share, or image leads to catering to overseas markets as a repeat activity. A firm takes up overseas marketing on a regular basis. Consequently, international marketing becomes an integral part of the firm's marketing strategy.

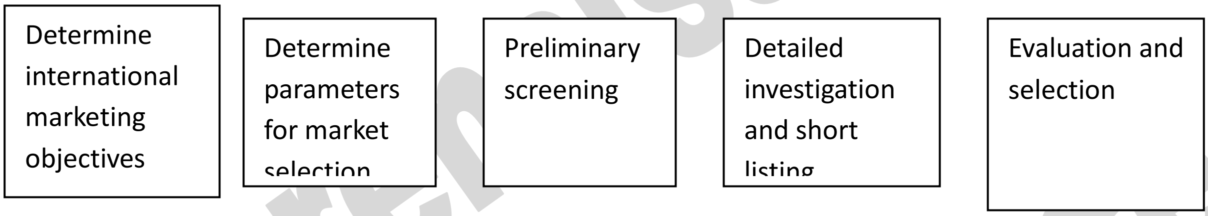
*Systematic Approach to Market Identification:*However, a systematic proactive approach is generally adopted by larger companies in selecting international markets. Since a firm ahs limited resources, it has to focus on a few foreign markets. Besides, proper selection of markets avoids wastage of the firm's time and resources so that it can concentrate on a few fruitful markets. A firm has to carry out preliminary screening of various countries before a refined analysis is carried for market selection.

The approach to enter into international markets can range from minimum investment with infrequent and frequent exporting to large investments of capital and management in order to capture and maintain a permanent, specific share of world markets. Depending upon the firm's objectives and market characteristics any of these approaches can be adapted.

Very often, entering international markets is not a matter of choice but of necessity to stay competitive in new and established markets. An executive involved in global marketing operations should have a thorough understanding of various entry modes. The major modes of entry into international markets adapted by firms are discussed in detail.

MARKET SELECTION PROCESS
The important steps involved in the market selection process are depicted in figure.

* **International Marketing Objectives**
  The first step in any management decision making process is to determine/ascertain the objectives. The market selected to serve a particular international marketing objective need not necessarily be the best suited to achieve some other international marketing objective. Various markets may have different degrees of attractiveness from the point of view of different objectives.
* **Parameters for Selection**
  For proper evaluation and selection of the markets, it is essential to clearly lay down the parameters and criteria for evaluation. Important parameters often used for market selection are shown in the evaluation matrix.



* **Preliminary Screening**

After determining the criteria for market selection, the next important step in market selection process is to conduct a preliminary screening of the markets. The objective of the preliminary screening process is to eliminate the markets which are obviously not potential enough as revealed by a cursory look.

The parameters used for the preliminary screening may vary from product to product. However, parameters like the size of population per capita income, structure of the economy, infrastructural factors, political conditions etc. are commonly used.

For example, in a country where there is no telecasting, there is obviously no market for T.V. sets. If the household income of the majority of a country with a small population is very low, the demand for costly consumer durables will be limited. There may be countries which should be omitted due to political reasons.

- **Short listing of Markets**

Preliminary screening enables one to eliminate markets which obviously do not merit consideration at the very outset. There would be a large number of markets left even after the preliminary screening. They are further screened with the help of more information than was used at the preliminary screening stage. The objective is to distill out a small number of markets which are likely to satisfy the company's criteria for market selection for a detailed analysis for ranking them and final selection.

- **Evaluation and Selection**

A thorough evaluation of the short listed markets is done with reference to the specific parameters and criteria and the markets are ranked of the basis of their overall attractiveness. One are more market (s) is/are selected from the rank list.

DETERMINANTS OF MARKET SELECTION

The market selection is normally based on two sets of factors, viz, the firm related factors and the market related factors.

a) Firm related factors
b) Market related factors

Firm related factors refer to such factors as the objective, resources, product mix, international orientation etc. of the firm.

a) Firm related Factors

A firm whose export objective is only to sell out a marginal surplus will select a foreign market suited to serve this purpose. Another firm with the same product, which wants to export a very large quantity, forming a very significant share of its total output, may have different consideration than the first firm in market selection. In the case of the second firm, as the total quantity involved is large and as it forms a significant share of its total output, market diversification would be important to minimize the risk. If we think of a third firm which also wants to export the same product as the first two firms but which wants to export several other products also, the market (s) which it selects may perhaps be different from what the first two firms have chosen; it would give more importance to the total exports of all its products than of any single product. Further, the market selection may be influenced by other objectives like growth. When business growth is an important objective, growth potential of the market will be an important criterion for selection.

The planned business strategy may also influence the market selection. For example, a market considered the most important from the point of view of exporting need not necessarily be the one that would be selected for locating production base or a sales office. A company that has plans for large expansion of foreign business may choose a market, to start with, which can serve as a hub of international business.

The market selection is also influenced by the international orientation.

Another very important determinant is the company resources comprising financial, human, technological and managerial factors.

The dynamism and philosophy of the top management and the internal power relations may also influence the market selection decision.

b) Market related Factors

The market related factors may be broadly grouped into general factors and specific factors. General factors are factors general to the market as a whole whereas the specific factors are factors which are specific to the industry concerned.

i) General Factors

1. **Economic Factors** : Include factors like economic stability, GDP growth trends, income distribution, per capita income, sectoral distribution of GDP and trends, nature of and trends in foreign trade and BoP, indebtedness, etc.
2. **Economic Policy** : Includes industrial policy, foreign investment policy, commercial policy, monetary policy, fiscal policy and other economic policies.

3. **Business Regulations** : Regulations of business like industrial licensing, restrictions on growth, takeovers, mergers etc, restrictions on foreign remittances, repatriations etc., tax laws; import restrictions and local content stipulations, export obligations and so on.
4. **Currency Stability** : Stability of the national currency is another very important consideration in the market selection.
5. **Political Factors** : Character of the political system including the nature and behaviour of the ruling party/parties and opposition party/parties, the government system etc, and political stability are among the most important determinants of market selection.
6. **Ethinic Factors** : Ethnic factors like ethinic characteristics, including ethnic deffereces, and their implication for the business, ethinic hamony etc. should also be analyzed.
7. **Infrastructur**e : Infrastructure facilities seriously affect business. For example power shortage could cause considerable production losses. Shipping and other communication bottlenecks could lot of delays and loss of business, in addition to high costs.
8. **Bureaucracy and Procedures** : The nature and behavior of the bureaucracy and the procedural system or styles are also important factors to be considered.
9. **Market Hub** : The ability of a market to act a hub, a base from where the company can operate in a contiguous region or countries, is a very important factor in the market selection of a company with plans for expansion of international business. South Africa, for example, could be such a hub for the entire sub Saharan Africa.

ii) **Specific Factors**

1. Trends in domestic production and consumption and estimates for the future of the products(s) concerned.
2. Trends in imports and exports and estimates for the future.
3. Nature of competition.
4. Government policy and regulations pertaining to the industry.
5. Infrastructure relevant to the industry.
6. Supply conditions of raw materials and other inputs
7. Trade practices and customs.
8. Cultural factors and consumer characteristics.
9. Market characteristics including the number and nature of market segments, price trends etc.

Evaluation Matrix

Attributes	***Weighting***	***Country A***		***Country B***		***Country C***	
	Factor	***Rs***	***WS***	***RS***	***WS***	***Rs***	***WS***
General							
Political Stability	10	10	100	7	70	10	100
Economic Stability	8	10	80	7	56	8	64
Currency Strength and Stability	8	9	72	7	56	8	64
Government policy	8	8	64	8	64	8	64
Infrastructural facilities	8	9	72	6	48	7	56
Ability to serve as marketing hub	10	8	80	5	50	6	60
Tax incentives	5	7	35	6	30	7	35
Ethnic factors	4	7	28	4	16	7	28
Bureaucracy and procedure	7	8	56	6	42	6	42
Sum of weighted scores			587		432		513
Specific							
Competition	8	4	32	7	56	8	64
Demand	10	10	100	6	60	8	80

Labour costs	7	7	49	8	56	7	49
Labour productivity	7	6	42	6	42	8	56
Infrastructure	8	8	64	6	48	8	64
Govt. policy & regulation	8	9	72	7	56	8	64
Incentives	5	6	30	5	25	6	30
Sum of weighted scores			389		343		407
Grand Total			976		775		920
Ranking Countries			1		3		2

Where, Rs – Raw Score, WS – Weighted Score (Weighting factors x Rs.)

PRODUCTION IN THE HOME COUNTRY: There are two possible ways of tapping overseas markets basing your operations in the home country. These are (a) indirect export and (b) direct export.

Indirect Export- The simplest form of indirect export one can think of is sales which are effected from the country when the foreign visitors purchase goods and in the process add to the foreign exchange earnings of the country. Foreign department stores or firms that have branch offices locally or agents who make purchases on behalf of their parent offices abroad also lead to one form of indirect export. Though resulting in foreign exchange earnings to the country, they are not the result of any deliberate effort on the part of locals to promote exports.The most important means of indirect export is through merchant exporters/export houses where the manufacturer entrusts the job of selling his products abroad to the specialist agencies which normally do engage in manufacturing.

Advantage of using an Export House / Merchant Exporter -Exporting through merchant exporter/export house can confer the following advantages:

The manufacturer avoids the problems of direct exporting such as investment of resources, collecting market intelligence, setting up of export department etc. and is served with instant foreign market knowledge.
Since the operational cost of export house / merchant-exporter will be spread over several parties, going through them will result in saving in unit cost.
In case the export house works on commission basis, there is possibility of expansion of exports, since there is incentive for the export house to expand sales.
In view of the fact that the export house will be effecting consolidated shipments there is a possibility of reduction in unit freight.
The reputation of export house will enable the manufacturer to get better representation for his products abroad. In case the export house is selling complementary products, sales might increase.

Disadvantage of using Export House / Merchant Exporter
The export house/merchant exporter, in order to earn more through commission, may take on too many unrelated lines resulting in the producer getting neither the expertise nor the attention he is looking for.
There is a possibility, under this arrangement, of the manufacturer continually depending on the export house and not developing export expertise himself.
There is also a possibility of both the manufacturer and the export house lacking personal involvement in the export business since either party may drop the other at any moment.
In view of the fact that the export house will be pushing the product abroad on its own name and reputation, the foreign customers may not associate the product with the manufacturer at all. This danger is more if the export house uses its letterhead and brand name.

Another form of indirect export is the consortium approach i.e., a limited number of manufacturers of the same product joining together and exporting it on a cooperative basis. In this type of arrangement, export management function is performed for several firms at the same time. There is closer cooperation and control as compared to merchant exporter or export house. Export orders will be procured on a joint basis and distributed amongst the constituent units. The individual units will be permitted to use their own letterheads and brand name. This arrangement confers more bargaining power on the consortium since the parties coming together can bargain over a position of strength. As in the case of exporting through export house, there is a possibility of saving in unit freight on account of consolidated shipment. Under-cutting is reduced to a great extent and all economies of scale associated with joint operation can be reaped.

The greatest disadvantage of consortium approach is that for this approach to succeed there should be perfect understanding among the members and each one should put in his best. As is well-known, cooperation can succeed only to the extent the individual members want it to succeed. Misunderstanding may arise over main issues and the presence of unscrupulous members is enough to spoil the business or the entire consortium.

Direct Export-When a manufacturer engages in direct export he takes more risks but gets more returns. More than anything else, direct export means more involvement for the manufacturer, more control and more expertise with the firm.

FOREIGN MANUFACTURING

There are various reasons for a company to go in for foreign manufacturing. Some of them are:
High cost of shipping of product to the export market;
Tariffs and non-tariff restrictions in the importing country;
Nationalist feelings in the country concerned not favouring import products;
Large size of the country, particularly regional groupings justifying establishment of manufacturing facilities in that country/region;
Greater scope to be in constant touch with the changing requirements of the foreign customer which is particularly true of fashion goods;
Lower production costs due to availability of cheaper/plentiful factor(s) of productions and
Advantages of acquiring an existing foreign product with all his facilities

Foreign manufacturing can take one or more of the following forms:
Assembly
Contract manufacture
Licensing
Joint Venture and
Wholly-owned foreign production (100% ownership)

OFFSHORE SOURCING, SUB-CONTRACTING AND MANUFACTURING

Although imports have always been important in some sectors, companies in more and more industries find offshore sources of components and finished products a means of increasing their profitability. As offshore sourcing has spread across industries, it has also spread to countries in Asia, South America and other developing areas.
The motivations for offshore sourcing are usually to obtain lower-cost products.

Selecting the form of Offshore Sourcing

Offshore Purchase

This is a relationship between independent buyers and sellers in which goods are exchanged for money.

Offshore sub-contracting

This term covers many different relationships between independent companies in which the buyer is more involved with the source than in a simple buyer-seller relationship. The buyer may provide detailed product specifications, technical assistance, raw materials or needed components or even some financing to the foreign manufacturers.

Joint Venture Offshore Manufacturing

This relationship involves the joint ownership with a foreign company of an offshore manufacturing enterprise.

Controlled Offshore Manufacturing

This relationship is that of a parent and wholly-owned foreign operation, generally a subsidiary corporation that supplies the parent's needs for a product.

Selection Criteria

Four important selection considerations are:

Company capabilities and resources

Availability and capabilities of suppliers or partners

Projected sourcing volumes and variability

Degree of integration of offshore sourcing with other operations.

Company Capability and Resources: Different forms of offshore sourcing demand different abilities on the part of enterprises and vastly different commitments of resources. Simple offshore purchasing requires little experience or investment, whereas controlled offshore manufacturing requires a considerable commitment of investment capital and management time.

*Availability and Capabilities of Suppliers or Partners***:** Whether acceptable suppliers and/or partners are available depends on the country, on the complexity of the production requirements, and on the size of the proposed operation. Small operations for relatively simple products may have a wide choice of suppliers or partners, whereas larger investments for more complex products will be more limited in this respect. This partly explains why more controlled offshore manufacturing exists in electronics than in the apparel industry.

Evaluating Products for Offshore Sourcing

Main Cost Tradeoffs

- Labour
- Materials and Components
- Factory Overhead
- Corporate Overhead
- Shipping and Duties

Products Available for Offshore Sourcing

- Labour Intensive Products
- Standardised Products
- Products with a predictable sales pattern
- Products that are easy to ship and face low import duties

Evaluating Sources and Partners

Capabilities for manufacturing and delivering acceptable products on time and acceptable costs

Willing to be good long term suppliers

A partner is expected to bring to the venture considerable expertise in addition to its capital investment.

The Selection of an International Market Entry Mode:

An SME needs to critically examine several factors while selecting the most appropriate entry mode for international markets. The major factors which need to be examined are as under:

Market size

Market growth

Regulatory framework

Structure of competition

Level of risks.

These factors should be carefully evaluated considering the willingness and strength of the organisation to commit its resources for global expansion. Since in the initial phase a company entering into the international market on the basis of its competitive strengths in technological and managerial skills, it may choose to enter by using multiple entry modes in different markets. Opportunistic market entry modes such as International Sub-Contracting and subsidiary routes may be looked into for markets with high entry barriers and high competitive intensity. For countries with substantial market size and high growth rate, a firm may consider using Strategic Alliance and Joint Venture for market entry. However, an in-depth detail analysis is required for the firm before a final decision is taken on an international market entry mode.

PRODUCT DEVELOPMENT IN INTERNATIONAL MARKETS

There is an ever growing desire for customers to have new products. Meanwhile, companies frequently use new product development as a means to refresh their competitive advantage and some even set it as a business objective. With respect to international business, faster new product development is essential for companies wishing to secure increased export involvement. Ceris Burns, international marketing specialist for the cleaning industry considers new product development for overseas markets and outlines the implementation process that should be followed to minimise risk.

Few products these days are revolutionary which means that companies need to be innovative in every aspect of their business in order to keep one step ahead. Most often new products refresh or reinforce a product range by complementing the existing offer as opposed to being a catalyst for business change. Companies should bear in mind that the time needed to copy products is shortening and as such fast and cost-effective simultaneous launch of new products across multiple markets can be prudent.

The process used to develop products for international markets is similar to that for domestic markets. The main steps include; idea generation, market screening, business analysis, product development, market testing, marketing and product launch. The major difference is the increased requirement to analyze a product's suitability for launch as several countries are to be targeted as opposed to one. In depth research and reliable local knowledge is crucial to ensure that local product needs are met and for products to be positioned correctly from the beginning.

The process for international product development should include:

Idea Generation-Make sure you use all resources available to you both internal and external for new idea generation. Get everyone involved from employees, R&D, competitors, customers, sales personnel and distributors through to external experts.

Market Screening -Develop tough criteria to test ideas for their suitability in all target regions or countries so opportunities and any country specific restrictions are not missed. What will work wonders in one country might not make it off the starting blocks in another. Also remember to assess the level of adaptation needed for the product to be accepted in each market.

Business Analysis -Establish criteria to measure launch success and failure and link these to your target markets. You should also make provision for contingencies and unexpected events that might just occur.

Product Development-All relevant functions from production to design should be involved in the product development process. Whether in-house or external R&D is used, it's important that key management has easy access to the technology experts. It might also be practical if R&D were located close to your key target markets.

Test Your Market-The test area must be representative of your key target markets if the results are to be trusted. Infrastructure for market research, advertising and distribution will need to be established and you should remember to consider how your competitors may respond in your test market and globally.

Product Launch-Prepare a launch plan for either sequential launches where your primary focus is on lead markets or for a simultaneous launch where all countries are entered at the same time. Be ready for your competitors to react. If serious players they shouldn't give up their slice of the market without a challenge.

Protect Your Competitive Advantage-Think about your competitor's ability to copy and launch similar products. You should protect your Intellectual Property by taking out patent protection. Establishing a licensing agreement could also protect your position by enabling fast widespread distribution of your product on a regional or even worldwide basis.

Timing Is Everything-Finally, timing is critical for new product development to succeed. Get it right and you'll be able to fully exploit opportunities or competitor weaknesses. It is also important to keep your time to market i.e. from idea generation to full market distribution, to a minimum.

DISTRIBUTION CHANNEL AND TRANSFER LOGISTICS

The Importance of Distribution: Most producers use intermediaries to bring their products to market. They try to develop a **distribution channel** (**marketing channel**) to do this. A **distribution channel** is a set of interdependent organizations that help make a product available for use or consumption by the consumer or business user. **Channel intermediaries** are firms or individuals such as wholesalers, agents, brokers, or retailers who help move a product from the producer to the consumer or business user.

A company's channel decisions directly affect every other marketing decision. Place decisions, for example, affect pricing. Marketers that distribute products through mass merchandisers such as Wal-Mart will have different pricing objectives and strategies than will those that sell to specialty stores. Distribution decisions can sometimes give a product a distinct position in the market. The choice of retailers and other intermediaries is strongly tied to the product itself. Manufacturers select mass merchandisers to sell mid-price-range products while they distribute top-of-the-line products through high-end department and specialty stores. The firm's sales force and communications decisions depend on how much persuasion, training, motivation, and support its channel partners need. Whether a company develops or acquires certain new products may depend on how well those products fit the capabilities of its channel members.

Some companies pay too little attention to their distribution channels. Others, such as FedEx, Dell Computer, and Charles Schwab have used imaginative distribution systems to gain a competitive advantage.

Functions of Distribution Channels
Distribution channels perform a number of functions that make possible the flow of goods from the producer to the customer. These functions must be handled by someone in the channel. Though the type of organization that performs the different functions can vary from channel to channel, the functions themselves cannot be eliminated. Channels provide time, place, and ownership utility. They make products available when, where, and in the sizes and quantities that customers want. Distribution channels provide a number of logistics or physical distribution functions that increase the efficiency of the flow of goods from producer to customer. Distribution channels create efficiencies by *reducing the number of transactions* necessary for goods to flow from many different manufacturers to large numbers of customers. This occurs in two ways. The first is called **breaking bulk**. Wholesalers and retailers purchase large quantities of goods from manufacturers but sell only one or a few at a time to many different customers. Second, channel intermediaries reduce the number of transactions by **creating assortments**—providing a variety of products in one location—so that customers can conveniently buy many different items from one seller at one time. Channels are efficient. The *transportation and storage of goods* is another type of physical distribution function. Retailers and other channel members move the goods from the production site to other locations where they are held until they are wanted by customers. Channel intermediaries also perform a number of **facilitating functions**, functions that make the purchase process easier for customers and manufacturers. Intermediaries often provide *customer services* such as offering credit to buyers and accepting customer returns. Customer services are oftentimes more important in B2B markets in which customers purchase larger quantities of higher-priced products.

The Internet in the Distribution Channel
By using the Internet, even small firms with limited resources can enjoy some of the same competitive advantages as their largest competitors in making their products available to customers internationally at low cost. E-commerce can result in radical changes in distribution strategies. Today most goods are mass-produced, and in most cases end users do not obtain products directly from manufacturers. With the Internet, however, the need for intermediaries and much of what has been assumed about the need and benefits of channels will

Wholesaling: Wholesaling is all activities involved in selling products to those buying for resale or business use. **Wholesaling intermediaries** are firms that handle the flow of products from the manufacturer to the retailer or business user.

Wholesaling intermediaries add value by performing one or more of the following channel functions:
Selling and Promoting
Buying and Assortment Building
Bulk-Breaking
Warehousing
Transportation

Financing
Risk Bearing
Market Information – giving information to suppliers and customers about competitors, new products, and price developments
Management Services and Advice – helping retailers train their sales clerks, improving store layouts and displays, and setting up accounting and inventory control systems.

Independent Intermediaries-**Independent intermediaries** do business with many different manufacturers and many different customers. Because they are not owned or controlled by any manufacturer, they make it possible for many manufacturers to serve customers throughout the world while keeping prices low.

Merchant Wholesalers-**Merchant wholesalers** are independent intermediaries that buy goods from manufacturers and sell to retailers and other B2B customers. Because merchant wholesalers take title to the goods, they assume certain risks and can suffer losses if products get damaged, become out-of-date or obsolete, are stolen, or just don't sell. At the same time, because they own the products, they are free to develop their own marketing strategies including setting prices. Merchant wholesalers include full-service merchant wholesalers and limited-service wholesalers. Limited-service wholesalers are comprised of cash-and-carry wholesalers, truck jobbers, drop shippers, mail-order wholesalers, and rack jobbers.

Merchandise Agents or Brokers-**Merchandise agents** or **brokers** are a second major type of independent intermediary. Agents and brokers provide services in exchange for commissions. They may or may not take possession of the product, but they never take title; that is, they do not accept legal ownership of the product. Agents normally represent buyers or sellers on an ongoing basis, whereas brokers are employed by clients for a short period of time. Merchandise agents or brokers include manufacturers' agents (manufacturers' reps), selling agents, commission merchants, and merchandise brokers.

Manufacturer-Owned Intermediaries-**Manufacturer-owned intermediaries** are set up by manufacturers in order to have separate business units that perform all of the functions of independent intermediaries, while at the same time maintaining complete control over the channel. Manufacturer-owned intermediaries include sales branches, sales offices, and manufacturers' showrooms. *Sales branches* carry inventory and provide sales and service to customers in a specific geographic area. *Sales offices* do not carry inventory but provide selling functions for the manufacturer in a specific geographic area.

Types of Distribution Channels: The first step in selecting a marketing channel is determining which type of channel will best meet both the seller's objectives and the distribution needs of customers.

Channel Length-Distribution channels can be described as being either short or long. A short channel involves few intermediaries. A long channel, on the other hand, involves many intermediaries working in succession to move goods from producers to consumers. In general, business products tend to move through shorter channels than consumer products due to geographical concentrations and comparatively few business purchases. Service firms market primarily through short channels because they sell intangible products and need to maintain personal relationships within their channels. Not-for-profit institutions also tend to work with short, simple, and direct channels. Please note Table 15.1 below that highlights the characteristics of short and long marketing channels.

TABLE 15.1 Factors Influencing Marketing Channel Strategies

	CHARACTERISTICS OF SHORT CHANNELS	CHARACTERISTICS OF LONG CHANNELS
Market factors	Business users	Consumers
	Geographically concentrated	Geographically dispersed
	Extensive technical knowledge and regular servicing required	Little technical knowledge and regular servicing not required
	Large orders	Small orders
Product factors	Perishable	Durable
	Complex	Standardized
	Expensive	Inexpensive
Producer factors	Manufacturer has adequate resources to perform channel functions	Manufacturer lacks adequate resources to perform channel functions
	Broad product line	Limited product line
	Channel control important	Channel control not important
Competitive factors	Manufacturing feels satisfied with marketing intermediaries' performance in promoting products	Manufacturer feels dissatisfied with marketing intermediaries' performance in promoting products

Consumer Channels-The simplest and shortest distribution channel is a direct channel. A **direct channel** carries goods directly from a producer to the business purchaser or consumer. One of the newest means of selling in a direct channel is the Internet. A direct channel may allow the producer to serve its customers better and at a lower price than is possible using a retailer. Sometimes a direct channel is the only way to sell the product because using channel intermediaries may increase the price above what consumers are willing to pay. Another reason to use a direct channel is control.

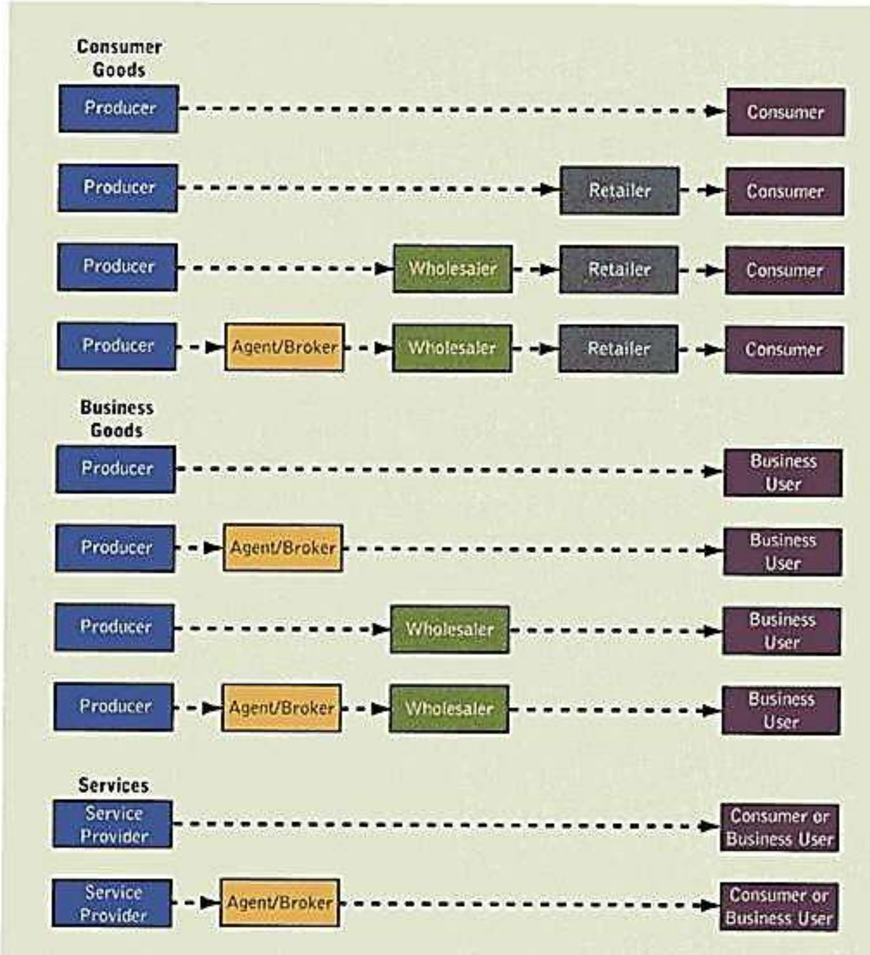
Many producers, however, choose to use **indirect channels** to reach consumers. Customers are familiar with certain retailers or other intermediaries and habitually turn to them when looking for what they need. Intermediaries also help producers fulfill the channel functions previously cited. By creating utility and transaction efficiencies, channel members make producers' lives easier and enhance their ability to reach customers.

The *producer-retailer-consumer channel* is the shortest indirect channel. GE uses this channel when it sells small appliances through large retailers such as Wal-Mart or Sears. The *producer-wholesaler-retailer-consumer channel* is another common distribution channel in consumer marketing.

Business-to-Business Channels-B2B distribution channels facilitate the flow of goods from a producer to an organizational customer. Generally, B2B channels parallel consumer channels in that they may be direct or indirect. The simplest indirect channel in industrial markets occurs when the single intermediary—a merchant wholesaler referred to as an *industrial distributor* rather than a retailer—buys products from a manufacturer and sells them to business customers.

Channels for Services-Because services are intangible, there is no need to worry about storage, transportation, and the other functions of physical distribution. In most cases, the service travels directly from the producer to the customer. Some services, however, do need an intermediary, often called an agent, who helps the parties complete the transaction. Examples include insurance agents, stockbrokers, and travel agents.
Note the alternative distribution channels for consumer goods, business goods, and services illustrated in Figure 15.2 below:

FIGURE 15.2
Alternative Marketing Channels



<u>Horizontal Marketing Systems-</u>A **horizontal marketing system** is a channel arrangement in which two or more companies at one level join together to follow a new marketing opportunity. By working together, companies can combine their financial, production, or marketing resources to accomplish more than any one company could alone.

<u>Multichannel Distribution Systems-</u>A **multichannel distribution system** is a distribution system in which a single firm sets up two or more marketing channels to reach one or more customer segments. This is also called a *hybrid marketing channel*.

Channel Strategy: Marketers face several strategic decisions in choosing channels and marketing intermediaries for their products. Selecting a specific channel is the most basic of these decisions. Marketers must also resolve questions about the level of distribution intensity, the desirability of vertical marketing systems, and the performance of current intermediaries.

<u>Marketing Channel Selection-</u>Marketing channel selection can be facilitated by analyzing market, product, producer, and competitive factors. A marketer could refer to Table 15.1 above for insights into whether the distribution channel should be short or long for the product in question. Then, he or she could refer to Figure 15.2 above and consider the alternative long or short channels for consumer goods, business goods, or services.

<u>Distribution Intensity-</u>**Distribution intensity** refers to the number of intermediaries through which a manufacturer distributes its goods. The decision about distribution intensity should ensure adequate market coverage for a product. In general, distribution intensity varies along a continuum with three general categories: *intensive distribution*, *selective distribution*, and *exclusive distribution*.

Intensive Distribution-An **intensive distribution** strategy seeks to distribute a product through all available channels in an area. Usually, an intensive distribution strategy suits items with wide appeal across broad groups of consumers, such as convenience goods.

Selective Distribution-**Selective distribution** is distribution of a product through only a limited number of channels. This arrangement helps to control price cutting. By limiting the number of retailers, marketers can reduce total marketing costs while establishing strong working relationships within the channel. Moreover, selected retailers often agree to comply with the company's rules for advertising, pricing, and displaying its products. Where service is important, the manufacturer usually provides training and assistance to dealers it chooses. Cooperative advertising can also be utilized for mutual benefit. Selective distribution strategies are suitable for shopping products such as clothing, furniture, household appliances, computers, and electronic equipment for which consumers are willing to spend time visiting different retail outlets to compare product alternatives.

Exclusive Distribution-**Exclusive distribution** is distribution of a product through one wholesaler or retailer in a specific geographical area. The automobile industry provides a good example of exclusive distribution. Though marketers may sacrifice some market coverage with exclusive distribution, they often develop and maintain an image of quality and prestige for the product. In addition, exclusive distribution limits marketing costs since the firm deals with a smaller number of accounts. In exclusive distribution, producers and retailers cooperate closely in decisions concerning advertising and promotion, inventory carried by the retailers, and prices.

Channel Conflict-The **channel captain** or **leader**, the dominant and controlling member of a distribution channel, must work to resolve conflicts between channel members. Conflicts can be *horizontal* and *vertical*.

Horizontal & Vertical Conflict-**Horizontal conflict** occurs among firms at the same level of the channel (i.e. between two retailers). **Vertical conflict** is conflict between different levels of the same channel (i.e. between a wholesaler and a retailer). Some conflict in the channel takes the form of healthy competition. Severe or prolonged conflict, however, can disrupt channel effectiveness and cause lasting harm to channel relationships.

Vertical Marketing Systems-A **vertical marketing system (VMS)** is a distribution channel structure in which producers, wholesalers, and retailers act as a unified system. One channel member owns the others, has contracts with them, or has so much power that they all cooperate. A **conventional distribution channel** consists of one or more *independent* producers, wholesalers, and retailers. A vertical marketing system, on the other hand, provides a way to resolve the channel conflict that can occur in a conventional distribution channel where channel members are separate businesses seeking to maximize their own profits—even at the expense sometimes of the system as a whole. The VMS can be dominated by the producer, wholesaler, or retailer. There are three major types of vertical marketing systems: *corporate*, *contractual*, and a*dministered*.

A **corporate VMS** is a vertical marketing system that combines successive stages of production and distribution under single ownership—channel leadership is established through common ownership. A little-known Italian eyewear maker, Luxottica, sells its many famous eyewear brands—including Giorgio, Armani, Yves Saint Laurent, and Ray-Ban—through the world's largest optical chain, LensCrafters, which it also owns.

A **contractual VMS** is a vertical marketing system in which independent firms at different levels of production and distribution join together through contracts to obtain more economies or sales impact than they could achieve alone. Coordination and conflict management are attained through contractual agreements among channel members. The **franchise organization** is the most common type of contractual relationship. There are three types of franchises:*manufacturer-sponsored retailer franchise system* (Ford Motor Co.), *manufacturer-sponsored wholesaler franchise system* (Coca-Cola bottlers), and *service-firm-sponsored retailer franchise system* (McDonald's). The fact that most consumers cannot tell the difference between contractual and corporate VMSs shows how successfully the contractual organizations compete with corporate chains.

An **administered VMS** is a vertical marketing system that coordinates successive stages of production and distribution, not through common ownership or contractual ties, but through the size and power of one of the parties. Manufacturers of a top brand can obtain strong trade cooperation and support from resellers (P&G). Large retailers such as Wal-Mart can exert strong influence on the manufacturers that supply the products they sell.

Logistics:Logistics is the process of designing, managing, and improving the movement of products through the *supply chain*. The **supply chain** is all the firms that engage in activities necessary to turn raw materials into a product and put it in the hands of the consumer or business customer. The difference between a supply chain and a distribution channel is the number of members and their function. A supply chain consists of those firms that supply the raw materials, component parts, and supplies necessary for a firm to produce a product ***plus*** the firms that facilitate the movement of that product from the producer to the ultimate users of the product—the channel members.

Physical Distribution-Logistics has the objective of delivering exactly what the customer wants—at the right time, in the right place, and at the right price. In planning for the delivery of goods to customers, marketers have usually looked at a process termed **physical distribution**, which refers to the activities used to move finished goods from manufacturers to final customers. Physical distribution activities include *order processing*, *warehousing*, *materials handling*,*transportation*, and *inventory control*. This process impacts how marketers physically get products where they need to be, when they need to be there, and at the lowest possible cost.

In logistics, the focus is on the customer. When planning for the logistics function, firms consider the needs of the customer first. The customer's goals become the logistics provider's goals. With most logistics decisions, firms must compromise between low costs and high customer service.

ROLE OF EXPORT DOCUMENTATION /DOCUMENTATION IN INTERNATIONAL BUSINESS

Export documentation plays a vital role in international marketing as it facilitates the smooth flow of goods and payments thereof across national frontiers. A number of documents accompany every shipment. These documents must be properly and correctly filled. Export documentation is, however, complex as the number of documents to be filled in is large, so also is the number of concerned authorities to whom the relevant documents are to be submitted. Moreover documents required differ from country to country.

Incorrect documents may lead to non delivery of goods to the importer. You may get the correct documents after some time but in the meantime storage charges may have to be paid. More important, the importer will think twice before importing from the same exporter.

It is therefore, advisable to take the help of shipping and forwarding agents who will obtain fill out the documents correctly as well as arrange for transportation. But every exporter should have an adequate knowledge about export documents and procedures.

On the basis of the functions to be performed, export documents can be classified under four categories:

Commercial Documents: These include commercial invoices, bills of exchange bills of lading, letters of credit, marine insurance policy and certificates etc.

2. Regulatory Documents: These are the documents which are required for complying with the rules and regulations governing export trade transactions such as foreign exchange regulations, customs formalities export inspection etc.

3. Export Assistance Documents: These are the documents which are required for claiming assistance under the various export assistance measures as may be in operation from time to time. Presently these refer to drawbacks of Central excise and customs duties, packing credit facilities etc,

4. Documentation required by importing Countries. These are the documents which are required by the importer in order to satisfy the requirements of his government. These include certificates of origin, consular invoice, quality control certificate etc.
Export documents could be classified into two categories depending upon the specific requirements satisfied by them: (1) Regulatory and (2) Operational.

Regulatory Requirements:
An exporter has to follow strictly the regulation of both the exporting country as well as that of the importing country. For example, there is exchange control in India. Therefore when we export goods, we have to give an undertaking to the RBI that we shall realize the foreign exchange in lieu of the goods exported. We do this by submitting GR form, and it is obvious that we cannot export unless we submit this document. Then there are certain commodities which are subject to export regulation. We have to obtain a licence for exporting the controlled commodities. Thus, another document has necessarily to be used. In order to build up an image of Indian goods abroad there is a system of compulsory pre-shipment inspection and quality control of a number of export goods. The exporter has to obtain an inspection certificate. This gives rise to still another document. There are a number of importing countries which stipulate that the exporter must submit certain specified documents duly certified by their missions in the exporting country. This condition makes it essential the use of the consular invoice and in some cases the use of the legalized invoice. There are countries specially the Commonwealth countries and also those developed countries which have offered concessions to the developing countries under the Generalized System of Preferences which demand that the exporters must submit a certificate of origin. Thus, the exporter has to submit GR form, export licence inspection certificate, consular invoice, legalized invoice and certificate of origin. These are examples of regulatory documents.

Operational Requirements:
The customs authorities are charged with the responsibility of verifying compliance on the part of the exporters with all types of regulations in force in the country. For their own record purposes, they have devised the Shipping bill. No shipping company or airline will accept any export cargo unless the customs authorities have granted their permission on the shipping bill. Along with the shipping bill, commercial invoices and packing lists are also to be submitted.
Common Import/Export Documents
There are many documents involved in international trade, such as commercial documents, financial documents, transport documents, insurance documents and other international trade related documents. In processing the export consignment, documentation may be executed in up to four contracts: the export sales contract, the contract of carriage, the contract of finance and the contract of cargo insurance. It is therefore important to understand the role of each document and their requirements in the international trade.

Commercial Documents

Document	Functions	Prepared by
Quotation	An offer to sell goods and should state clearly the price, details of quality, quantity, trade terms, delivery terms, and payment terms.	Exporter
Sales Contract (see Appendix II)	An agreement between the buyer and the seller stipulating every details of the transaction. It is a legally binding document. It is therefore advisable to seek legal advice before signing the contract.	Exporter and Importer
Pro Forma Invoice	An invoice provided by a supplier prior to the shipment of merchandise, informing the buyer of the kinds and quantities of goods to be sent, their value, and importation specifications (weight, size and similar characteristics). This is *not* issued for demanding payment but may be used when applying for an import licence/permit or arranging foreign currency or other funding purposes.	Exporter

Commercial Invoice	It is a formal demand note for payment issued by the exporter to the importer for goods sold under a sales contract. It should give details of the goods sold, payment terms and trade terms. It is also used for the customs clearance of goods and sometimes for foreign exchange purpose by the importer.	Exporter
Packing List	A list with detailed packing information of the goods shipped.	Exporter
Inspection Certificate	A report issued by an independent surveyor (inspection company) or the exporter on the specifications of the shipment, including quality, quantity, and/or price, etc; required by certain buyer and countries.	Inspection Company or Exporter
Insurance Policy/ Certificate	An insurance policy is an insurance document evidencing insurance has been taken out on the goods shipped, and it gives full details of the insurance coverage. An insurance certificate certifies that the shipment has been insured under a given open policy and is to cover loss of or damage to the cargo while in transit.	Insurer or Insurance Agent or Insurance Broker
Product Testing Certificate	A certificate to certify the products are conformed to a certain international/national technical standard, such as product quality, safety and specifications, etc.	Accredited Laboratories
Health Certificate	Document issued by the competent country when agricultural or food products are being exported, to certify that they comply with the relevant legislation in the exporter's country and were in good condition at time of inspection, prior to shipment and fit for human consumption.	Exporter / Inspection Authority
Phytosanitary Certificate	Frequently an international requirement that any consignment of plants or planting materials importing into a country shall be accompanied by a Phytosanitary Certificate issued by the exporting country stating that the consignment is found substantially free from diseases and pests and conforms with the current phytosanitary regulations of the importing country. Application of the certificate in Hong Kong should be made to the Agriculture and Fisheries Department.	Exporter
Fumigation Certificate	A pest control certificate issued to certify that the concerned products have been undergone the quarantine and pre-shipment fumigation by the approved fumigation service providers. It is mainly required by the US, Canada, Australia, New Zealand and UK's customs on solid wood packing material from Hong Kong and the Chinese Mainland.	Exporter or Inspection Company
ATA Carnet	An international customs document used to obtain a duty-free temporary admission for goods such as exhibits for international trade fairs, samples and professional equipment, into the countries that are signatories to the ATA Convention.	Exporter
Consular Invoice	A document required by some foreign countries, showing shipment information such as consignor, consignee, and value description, etc. Certified by a consular official of the importing country stationed in the foreign country, it is used	Exporter

	by the country's customs officials to verify the value, quantity and nature of the shipment.	

Transport Documents

Document	Functions	Prepared by
Shipping Order S/O	A document to give details of the cargo and the shipper's requirements. It is the basic document for preparing other transport documents such as bill of lading, air waybill, etc.	Shipper / Transport Companies
Dock Receipt D/R or Mate's Receipt	A receipt to confirm the receipt of cargo on quay/warehouse pending shipment. The dock receipt is used as documentation to prepare a bill of lading. It has no legal role regarding processing financial settlement.	Shipping Company
Bills of Lading (B/L)	An evidence of contract between the shipper of the goods and the carrier. The customer usually needs the original as proof of ownership to take possession of the goods. There are two types: a STRAIGHT bill of lading is non-negotiable and a negotiable or shipper's ORDER bill of lading (also a title document) which can be bought, sold or traded while goods are in transit and is used for many types of financing transactions.	Shipping Company
House Bill of Lading (Groupage)	A bill of lading issued by a forwarder and, in many cases, not a title document. Shippers choosing to use a house bill of lading, should clarify with the bank whether it is acceptable for letter of credit purpose before the credit is opened. Advantages include less packing, lower insurance premiums, quicker transit, less risk of damage and lower rates than cargo as an individual parcel / consignment.	Forwarder
Sea Waybill	A receipt for cargo which incorporates the contract of carriage between the shipper and the carrier but is non-negotiable and is therefore not a title document.	Shipping Company
Air Waybill (AWB)	A kind of waybill used for the carriage of goods by air. This serves as a receipt of goods for delivery and states the condition of carriage but is not a title document or transferable/negotiable instrument.	Airline
House Air Waybill (HAWB)	An air consignment note issued by an air freight agent to provide the cargo description and records. Again, it is not a title document.	Forwarding Agent
Shipping Guarantee	Usually a pre-printed form provided by a shipping company or the bank, given by an importer's bank to the shipping company to replace the original transport document. The consignee may then in advance take delivery of goods against a shipping guarantee without producing the original bill of lading. The consignee and the importer bank will be responsible for any loss or charges occurred to the shipping company if fault is found in the collection. It is usually used with full margin or trust receipt to protect the bank's control to the goods.	Importer's Bank / Shipping Company / Consignee
Packing List (sometimes as packing note)	A list providing information needed for transportation purpose, such as details of invoice, buyer, consignee, country of origin, vessel/flight date, port/airport of loading, port/airport of discharge, place of delivery, shipping marks / container number, weight / volume of merchandise and the	Shipper

	fullest details of the goods, including packing information.	

Financial Documents

Document	Functions	Prepared by
Documentary Credit D/C	A bank instrument began (issuing or opening bank), at the request of the buyer, evidencing the bank's undertaking to the seller to pay a certain sum of money provided that specific requirements set out in the D/C are satisfied.	The Issuing Bank upon an application made by the Importer
Standby Credit	An arrangement between customer and his bank by which the customer may enjoy the convenience of cashing cheques, up to a value. Or a credit set up between the exporter and the importer guaranteeing the exporter will pay the importer a certain amount of money if the contract is not fulfilled. It is also known as performance bond. This is usually found in large transactions, such as crude oil, fertilizers, fishmeal, sugar, urea, etc.	Exporter / Issuing Bank
Collection Instruction	An instruction given by an exporter to its banker, which empowers the bank to collect the payment subject to the contract terms on behalf of the exporter.	Exporter
Bill of Exchange (B/E) or Draft	An unconditional written order, in which the importer addressed to and required by the exporter to pay on demand or at a future date a certain amount of money to the order of a person or bearer.	Exporter
Trust Receipt (T/R)	A document to release a merchandise by a bank to a buyer (the bank still retains title to the merchandise), the buyer, who obtains the goods for processing is obligated to maintain the goods distinct from the remainder of his/her assets and to hold them ready for repossession by the bank.	Importer
Promissory Note	A financial instrument that is negotiable evidencing the obligations of the foreign buyer to pay to the bearer.	Importer

Government Documents

Document	Functions	Prepared by
Certificate of Origin (CO)	A certificate to certify the place of manufacture, the nature/quantity/value of the goods.	Trade and Industry Department and five Chambers of Commerce [1]
Certificate of Origin Generalized Systems of Preferences (GSP) Form A (or as Form A)	A C.O. to support the claim for preferential tariff entry (a reduced or zero rate) of the exporting country's products into the GSP donors under the GSP they operate. In general, a Form A is issued only when the goods concerned have met both the origin rules of the preference receiving country as well as the origin criteria of the respective donor country's GSP. Hong Kong is now a beneficiary under the GSP schemes operated by Canada and Norway, while China is beneficiary to countries like Australia, Canada, Czech Republic, European Union, Japan, Poland, Russia, Slovakia.	See Above
Import / Export Declaration	A statement made to the Director of Customs at port of entry/exit, declaring full particulars of the shipment, eg. the nature and the destination/exporting country of the ship's	Exporter/ Importer

	cargo. Its primary use is for compiling trade statistics.	
Import / Export Licence	A document issued by a relevant government department authorising the imports and exports of certain controlled goods.	Trade and Industry Department, Customs & Excise Department, etc
International Import Certificate (IIC)	A statement issued by the government of country of destination, certifying the imported strategic goods will be disposed of in the designated country. In Hong Kong, it is issued only to meet an exporting country's requirement.	Trade and Industry Department
Delivery Verification Certificate (DVC)	A statement issued by the government of country of destination, certifying a specific strategic commodity has been arrived in the designated country. In Hong Kong, it is issued only to meet an exporting country's requirement.	Trade and Industry Department
Landing Certificate	A document issued by the government of country of destination, certifying a specific commodity has been arrived in the designated country. In Hong Kong, it is issued by the Census and Statistics Department. Application requirements include letter stating the reason for the application, import declaration & receipt; bill of lading, sea waybill & land manifest; supplier's invoice; and packing list (if any).	Census and Statistics Department
Customs Invoice	A document specified by the customs authorities of the importing countries stating the selling price, costs for freight, insurance, packing and payment terms, etc, for the purpose of determining the customs value.	Exporter

EXPORT PRICING

Introduction - Pricing and costing are two different things and an exporter should not confuse between the two. Price is what an exporter offer to a customer on particular products while cost is what an exporter pay for manufacturing the same product.

Export pricing is the most important factor in for promoting export and facing international trade competition. It is important for the exporter to keep the prices down keeping in mind all export benefits and expenses. However, there is no fixed formula for successful export pricing and is differ from exporter to exporter depending upon whether the exporter is a merchant exporter or a manufacturer exporter or exporting through a canalizing agency.

Determining Export Pricing- Export Pricing can be determine by the following factors:

Range of products offered.
Prompt deliveries and continuity in supply.
After-sales service in products like machine tools, consumer durables.
Product differentiation and brand image.
Frequency of purchase.
Presumed relationship between quality and price.
Specialty value goods and gift items.
Credit offered.
Preference or prejudice for products originating from a particular source.
Aggressive marketing and sales promotion.
Prompt acceptance and settlement of claims.
Unique value goods and gift items.

Export Costing - Export Costing is basically Cost Accountant's job. It consists of fixed cost and variable cost comprising various elements. It is advisable to prepare an export costing sheet for every export product.
As regards quoting the prices to the overseas buyer, the same are quoted in the following internationally accepted terms which are commonly known as Incoterm.

METHODS OF PAYMENT IN INTERNATIONAL TRADE
To succeed in today's global marketplace and win sales against foreign competitors, exporters must offer their customers attractive sales terms supported by the appropriate payment methods. Because getting paid in full and on time is the ultimate goal for each export sale, an appropriate payment method must be chosen carefully to minimize the payment risk while also accommodating the needs of the buyer. As shown in figure 1, there are five primary methods of payment for international transactions. During or before contract negotiations, you should consider which method in the figure is mutually desirable for you and your customer.
New Payment Risk Diagram – To Be Created by Designer

	Least Secure	Less Secure		More Secure	Most Secure
Exporter	Consignment	Open Account	Documentary Collections	Letters of Credit	Cash-in-Advance
Importer	Cash-in-Advance	Letters of Credit	Documentary Collections	Open Account	Consignment

Figure: Payment Risk Diagram

Key Points
International trade presents a spectrum of risk, which causes uncertainty over the timing of payments between the exporter (seller) and importer (foreign buyer).
For exporters, any sale is a gift until payment is received.
Therefore, exporters want to receive payment as soon as possible, preferably as soon as an order is placed or before the goods are sent to the importer.
For importers, any payment is a donation until the goods are received.
Therefore, importers want to receive the goods as soon as possible but to delay payment as long as possible, preferably until after the goods are resold to generate enough income to pay the exporter.
Cash-in-Advance- With cash-in-advance payment terms, an exporter can avoid credit risk because payment is received before the ownership of the goods is transferred. For international sales, wire transfers and credit cards are the most commonly used cash-in-advance options available to exporters. With the advancement of the Internet, escrow services are becoming another cash-in-advance option for small export transactions. However, requiring payment in advance is the least attractive option for the buyer, because it creates unfavorable cash flow. Foreign buyers are also concerned that the goods may not be sent if payment is made in advance. Thus, exporters who insist on this payment method as their sole manner of doing business may lose to competitors who offer more attractive payment terms.
Letters of Credit- Letters of credit (LCs) are one of the most secure instruments available to international traders. An LC is a commitment by a bank on behalf of the buyer that payment will be made to the exporter, provided that the terms and conditions stated in the LC have been met, as verified through the presentation of all required documents. The buyer establishes credit and pays his or her bank to render this service. An LC is useful when reliable credit information about a foreign buyer is difficult to obtain, but the exporter is satisfied with the creditworthiness of the buyer's foreign bank. An LC also protects the buyer since no payment obligation arises until the goods have been shipped as promised.
Documentary Collections- A documentary collection (D/C) is a transaction whereby the exporter entrusts the collection of the payment for a sale to its bank (remitting bank), which sends the documents that its buyer needs to the importer's bank (collecting bank), with instructions to release the documents to the buyer for payment. Funds are received from the importer and remitted to the exporter through the banks involved in the collection in exchange for those documents. D/Cs involve

using a draft that requires the importer to pay the face amount either at sight (document against payment) or on a specified date (document against acceptance). The collection letter gives instructions that specify the documents required for the transfer of title to the goods. Although banks do act as facilitators for their clients, D/Cs offer no verification process and limited recourse in the event of non-payment. D/Cs are generally less expensive than LCs.

Open Account-An open account transaction is a sale where the goods are shipped and delivered before payment is due, which in international sales is typically in 30, 60 or 90 days. Obviously, this is one of the most advantageous options to the importer in terms of cash flow and cost, but it is consequently one of the highest risk options for an exporter. Because of intense competition in export markets, foreign buyers often press exporters for open account terms since the extension of credit by the seller to the buyer is more common abroad. Therefore, exporters who are reluctant to extend credit may lose a sale to their competitors. Exporters can offer competitive open account terms while substantially mitigating the risk of non-payment by using one or more of the appropriate trade finance techniques covered later in this Guide. When offering open account terms, the exporter can seek extra protection using export credit insurance.

Consignment - Consignment in international trade is a variation of open account in which payment is sent to the exporter only after the goods have been sold by the foreign distributor to the end customer. An international consignment transaction is based on a contractual arrangement in which the foreign distributor receives, manages, and sells the goods for the exporter who retains title to the goods until they are sold. Clearly, exporting on consignment is very risky as the exporter is not guaranteed any payment and its goods are in a foreign country in the hands of an independent distributor or agent. Consignment helps exporters become more competitive on the basis of better availability and faster delivery of goods. Selling on consignment can also help exporters reduce the direct costs of storing and managing inventory. The key to success in exporting on consignment is to partner with a reputable and trustworthy foreign distributor or a third-party logistics provider. Appropriate insurance should be in place to cover consigned goods in transit or in possession of a foreign distributor as well as to mitigate the risk of non-payment.

UNIT V

RISK IN INTERNATIONAL OPERATIONS

Business risk implies the possibility of some unfavorable happening. It is the possibility of loss due to same uncertain future occurrence. International business risk may be defined as the possibility of loss caused by some unfavorable or undesirable event in international business operations. Profit and growth rates in international business are higher but so are the attendant risk. Changes in international environment And difference in the economic systems, objectives and cultures of different countries are the main causes of international business risks. The degree of such risk differs from one company to another company and from one country to another country.

TYPES OF RISK -

Strategic Risk
(2) Operational Risk
(3) Political Risk
(4) Country Risk
(5) Technological Risk
(6) Environmental Risk
(7) Economic Risk
(8) Financial Risk
(9) Terrorism Risk

Strategic Risk: The ability of a firm to make a strategic decision in order to respond to the forces that are a source of risk. These forces also impact the competitiveness of a firm. Porter defines them as: threat of new entrants in the industry, threat of substitute goods and services, intensity of competition within the industry, bargaining power of suppliers, and bargaining power of consumers.

Operational Risk: This is caused by the assets and financial capital that aid in the day-to-day business operations. The breakdown of machineries, supply and demand of the resources and products, shortfall of the goods and services, lack of perfect logistic and inventory will lead to inefficiency of production. By controlling costs, unnecessary waste will be reduced, and the process improvement may enhance the lead-time, reduce variance and contribute to efficiency in globalization.

Political Risk: The political actions and instability may make it difficult for companies to operate efficiently in these countries due to negative publicity and impact created by individuals in the top government. A firm cannot effectively operate to its full capacity in order to maximize profit in such an unstable country's political turbulence. A new and hostile government may replace the friendly one, and hence expropriate foreign assets.

Country Risk: The culture or the instability of a country may create risks that may make it difficult for multinational companies to operate safely, effectively, and efficiently. Some of the country risks come from the governments' policies, economic conditions, security factors, and political conditions. Solving one of these problems without all of the problems (aggregate) together will not be enough in mitigating the country risk.

Technological Risk: Lack of security in electronic transactions, the cost of developing new technology, and the fact that these new technology may fail, and when all of these are coupled with the outdated existing technology, the result may create a dangerous effect in doing business in the international arena.

Environmental Risk: Air, water, and environmental pollution may affect the health of the citizens, and lead to public outcry of the citizens. These problems may also lead to damaging the reputation of the companies that do business in that area.

Economic Risk: This comes from the inability of a country to meet its financial obligations. The changing of foreign-investment or/and domestic fiscal or monetary policies. The effect of exchange-rate and interest rate make it difficult to conduct international business.

Financial Risk: This area is affected by the currency exchange rate, government flexibility in allowing the firms to repatriate profits or funds outside the country. The devaluation and inflation will also impact the firm's ability to operate at an efficient capacity and still be stable. Most countries make it difficult for foreign firms to repatriate funds thus forcing these firms to invest its funds at a less optimal level. Sometimes, firms' assets are confiscated and that contributes to financial losses.

Terrorism Risk: These are attacks that may stem from lack of hope; confidence; differences in culture and religious philosophy, and/or merely hate of companies by citizens of host countries. It leads to potential hostile attitudes, sabotage of foreign companies and/or kidnapping of the employers and employees. Such frustrating situations make it difficult to operate in these countries.

Although the benefits in international business exceed the risks, firms should take a risk assessment of each country and to also include intellectual property, red tape and corruption, human resource restrictions, and ownership restrictions in the analysis, in order to consider all risks involved before venturing into any of the countries.

INTERNATIONAL INVESTMENT AGREEMENT

n **International Investment Agreement (IIA)** is a type of treaty between countries that addresses issues relevant to cross-border investments, usually for the purpose of protection, promotion and liberalization of such investments. Most IIAs cover foreign direct investment (FDI) and portfolio investment, but some exclude the latter. Countries concluding IIAs commit themselves to adhere to specific standards on the treatment of foreign investments within their territory. IIAs further define procedures for the resolution of disputes should these commitments not be met. The most common types of IIAs are Bilateral Investment Treaties (BITs) and Preferential Trade and Investment Agreements (PTIAs). International Taxation Agreements and Double Taxation Treaties (DTTs) are also considered as IIAs, as taxation commonly has an important impact on foreign investment.

Bilateral investment treaties deal primarily with the admission, treatment and protection of foreign investment. They usually cover investments by enterprises or individuals of one country in the territory of its treaty partner. Preferential Trade and Investment Agreements are treaties among countries on cooperation in economic and trade areas. Usually they cover a broader set of issues and are concluded at bilateral or regional levels. In order to classify as IIAs, PTIAs must include, among other content, specific provisions on foreign investment. International taxation agreements deal primarily with the issue of double taxation in international financial activities (e.g., regulating taxes on income, assets or financial transactions). They are commonly concluded bilaterally, though some agreements also involve a larger number of countries.

FACTOR MOBILITY AND FOREIGN DIRECT INVESTMENT

INTRODUCTION - ***Factors of production*** represent inputs into the production process, such as labor, capital and know-how. Increasingly, those factors move internationally. In fact, a country's relative factor endowment may change because of factor movements. ***Foreign direct investment (FDI)*** occurs when an investor gains a controlling interest in a foreign operation either through acquisition or a start-up investment, i.e., ***FDI*** represents a company controlled through ownership by a foreign firm or individuals. Sales from foreign-owned operations are now about double the value of world trade.

FACTOR MOBILITY -

Why Production Factors Move

Factor mobility concerns the free movement of *factors of production*, such as labor and capital, across national borders. While capital is the most internationally mobile factor, short-term capital is the most mobile of all. Capital is primarily transferred because of differences in expected returns, although firms may also be responding to government incentives. People may also transfer internationally in order to work abroad, either on a temporary or a permanent basis. Often it is difficult to distinguish between economic and political motives for international labor mobility, because poor economic conditions often parallel repressive and/or uncertain political conditions.

Effects of Factor Movements

Neither international capital nor population movements are new occurrences. Immigrants bring human capital, thus adding to the base of a country's skills and enabling competition in new areas. Likewise, inflows of capital to those same countries can be used to develop infrastructure and natural resources, thus leading to its increased participation in the international trade arena.

The Relationship of Trade and Factor Mobility

Factor movement is an alternative to trade that may or may not be a more efficient allocation of resources. When factor proportions vary widely among countries, pressures exist for the most abundant factors to move to countries with greater scarcity.

Substitution. The inability to gain sufficient access to foreign production factors may stimulate efficient methods of domestic *substitution*, such as the development of alternatives for traditional production methods. In countries where labor is relatively abundant as compared to capital, workers tend to be poorly paid; many will attempt to go to countries that offer higher wages. Likewise, capital tends to move away from countries where it is abundant to those where it is relatively scarce. [See Figure 8.3]

Complementarity. Factor mobility via foreign direct investment may in fact stimulate foreign trade because of the need for equipment or components by a foreign subsidiary. Alternatively, trade may be restricted by local content laws or when FDI production leads to *import substitution*.

FOREIGN DIRECT INVESTMENT AND CONTROL

Firms naturally want to control their foreign operations in order to achieve their set objectives, but governments often worry the activities of foreign companies may reflect to decisions contrary to their countries' best interests.

The Concept of Control

If ownership is widely dispersed, then a small stake may be sufficient to establish effective managerial control of an investment. However, even sole ownership may not guarantee effective control if a local government dictates policies and procedures.

The Concern about Control

Government Concern. Many critics of FDI claim the host country's national interests may suffer if a multinational firm makes decisions from afar on the basis of its own overall corporate benefit.

Investor Concern. Multinationals want what is best for their overall corporate benefit, rather than what is best for a single operation in a specific country. Without control, firms are less likely to transfer technology and other competitive assets to foreign operations. With control, they are more likely to transfer strategic assets and also achieve lower overall operating costs. ***Appropriability theory*** concerns the idea of denying either potential or existing rivals access to a firm's strategic resources. ***Internalization*** represents the self-handling, i.e., the internal control, of business functions and operations, as opposed to the outsourcing of those activities.

COMPANIES' MOTIVES FOR FDI

Foreign direct investment is a way for firms to fulfill any one of three major operating objectives: to expand sales, to acquire resources and/or to minimize competitive risk. [See Table 8.1.]

Factors Affecting the Choice of FDI for Sales Expansion

The ***liability of foreignness*** represents the disadvantage a firm suffers relative to local companies when operating in a foreign country.

Transportation. When firms add the cost of transportation to those of manufacturing, some products become impractical to ship great distances. (When companies invest abroad in order to produce basically the same products they make at home, the investment process is called ***horizontal expansion.***)

Excess Capacity. When firms have excess capacity, they may be able compete in limited export markets in spite of additional transport costs. In such situations, firms may choose to determine foreign prices on the basis of variable rather than total costs. However, when firms need to add capacity in order to meet foreign demand, it is likely they will do so within or near the markets they intend to serve.

Scale Economies and Product Alterations. Firms that can achieve significant economies of scale will often centralize production activities and export to foreign markets. When they need to adapt products to individual markets, however, firms will be more likely to produce differentiated products in various foreign locations. The greater the adaptation, the greater the likelihood production will shift abroad.

Trade Restrictions. In spite of the progress to reduce barriers to trade through the GATT and the WTO, many restrictions still exist. In those instances, firms may be forced to invest in operations in foreign markets in order to overcome market imperfections.

Country-of-Origin Effects. Customers sometimes prefer (or are required) to buy domestic rather than foreign-produced products; in other instances they may prefer to source certain products (such as perfume or cars) from particular foreign countries, believing them to be of superior quality and/or value. In those instances, inherent benefits exist to producing nationally-based products in their traditional countries of origin.

Changes in Comparative Costs. Shifts in comparative production costs may cause firms to pursue resource-seeking investments.

Factors Affecting Motives to Acquire Resources through FDI

A firm may engage in foreign direct investment in order to source products from abroad.

Vertical Integration. ***Vertical integration*** represents a firm's ownership, and hence control, of either upstream suppliers (backward integration) and/or downstream customers (forward integration) in the value chain. Firms integrate vertically in order to assure that inputs, outputs and processes all flow efficiently and effectively. Because supplies and/or markets are better assured via integration, firms may be able to reduce inventories, spend less on promotion and avoid the costs of negotiating and enforcing contracts.

Rationalized Production. ***Rationalized production*** characterizes the situation in which different components or portions of a firm's product line are manufactured in different parts of the world in order take advantage of lower-cost labor, capital and/or materials. Another possible advantage of this strategy is smoother profits when exchange rates fluctuate across national currencies.

Access to Knowledge. A company may invest abroad in order to gain information for its organization as a whole.

The Product Life Cycle Theory. According to the *Product Life Cycle Theory,* production will move from the innovating country to other developed countries and then finally to developing nations. Ultimately a product may be imported by the country where it was initially developed.

Government Investment Incentives. In addition to restricting imports, governments frequently encourage direct investment inflows by offering tax concessions and/or other subsidies. Such incentives may shift a firm's least-cost production location. [See Chapter 12 for an in-depth discussion of this topic.]

Risk Minimization Objectives

Diversification through foreign direct investment is often a means of reducing risk.

Following Customers. In the organizational (industrial) sector, suppliers are often compelled to follow their downstream customers abroad if they wish to capture the associated potential business.

Preventing Competitors' Advantage. Firms in an oligopolistic industry may follow their competitors abroad to prevent their gaining a first-mover advantage. (***Oligopolistic industries*** consist of relatively few producers and sellers of a given product.)

Political Motives

Governments may provide incentives to their domestic firms to engage in foreign direct investment in order to gain access to strategic resources (such as oil) or to develop spheres of influence.

RESOURCES AND METHODS FOR MAKING FDI

Assets Employed

While ***FDI*** usually involves an international capital movement that crosses international borders with the expectation of a higher return, other types of assets such as managerial skills, technology, market information, etc. may be transferred as well. Some or all of the required capital may also be borrowed in the host country.

Buy vs. Build Decision

Firms can invest in foreign operations either through acquisition or through the construction of new facilities.

Reasons for Buying. The advantages of acquiring an existing operation include the avoidance of adding unneeded capacity to the industry, the acquisition of a trained workforce and the possibility of acquiring an existing brand. Thus, firms also avoid the inefficiencies of an initial start-up process and generate an immediate cash flow.

Reasons for Building. The advantages of building a start-up operation may include access to local financing, particularly if the firm plans to tap development banks. In addition, start-up may be the only viable investment option if no desirable company is available for acquisition; ill-conceived acquisitions can lead to serious carry-over problems.

INVESTOR'S ADVANTAGES

FDI can improve performance in several ways if a firm holds one or more advantages over its competitors. A ***monopoly advantage*** accrues to a firm if it is able to gain a unique advantage regarding technology, management skills, market access, etc. that is not available to local (either domestic or foreign) competitors. Some firms may be able to borrow capital at a lower interest rate than others, some may enjoy increased buying power because of currency fluctuations and others may gain from spreading the costs of product differentiation, R&D and advertising across markets. Still others hold advantages because of their patents, differentiated products, management skills and market access.

DIRECT INVESTMENT PATTERNS

The recent growth in foreign direct investment flows is the result of more receptive attitudes by governments, the process of *privatization* and the growing interdependence of the world economy.

Location of Ownership [See Table 8.2.]

Industrialized countries account for more than 90 percent of all direct investment outflows. This is because firms from those countries are more likely to have the capital, technology and managerial skills required for successfully investing abroad.

Location of Investment [See Figure 8.5]

The major recipients of ***FDI*** are developed countries, which received nearly 80 percent of the world's total in 2001. Their markets tend to be larger and better developed, they face less political turmoil and they tend to have liberal direct investment policies.

Economic Sectors of FDI

Over time, the portion of ***FDI*** accounted for by raw materials (including mining, smelting and petroleum) declined. At the same time, the portion devoted to resource-based production grew. Since the early 1970s, ***FDI*** has grown rapidly in the service sector (especially banking and finance), as has investment in technology-intensive manufacturing.

FDI IN COMPANIES' STRATEGIES

Foreign direct investment serves the goal of global efficiency by transferring resources to places where they can be used most effectively. While *marketing-seeking* investments generally favor *multi-domestic strategies, resource-seeking* investments generally lead to *vertical integration* or *rationalized production.*

ETHICAL DILEMMA:

Critics Debate the Ethics of FDI and Employment

Critics of FDI argue it is unethical for governments to lure operations away from existing locations by offering lucrative incentives. Critics also argue it is unethical for companies to accept those incentives. For their part, companies say they cannot decline such incentives because of competitive conditions. Nonetheless, newly unemployed workers suffer if they cannot find new jobs of equal pay, and large-scale under- or unemployment is a strain on any economy. Do governments in countries where production facilities are currently located have special ethical obligations to their citizens and firms to attempt to retain operations? Are such obligations any greater for those governments with burdensome environmental regulations and high taxes?

LOOKING TO THE FUTURE:

Will Factor Movements and FDI Continue to Grow Worldwide?

From year to year, FDI flows fluctuate both in their direction and rate of growth. The receptiveness of governments, the growing interdependence of the world economy and the increasing foreign experience of firms all encourage future growth. On the other hand, declining trade restrictions and new political realities (such as 9/11) serve to diminish the urgency of many import-substitution activities in the manufacturing sector. Since many barriers remain in the service sector, however, FDI may continue to grow in importance in that arena. At the same time, anti-immigration feelings appear to be curtailing international labor flows, regardless of the skills of the affected workers.

EXPORT FINANCE – PRE AND POST SHIPMENT CREDIT

INTRODUCTION

Export financing is another important area of export business. Export finance refers to the credit facilities extended to the exporters at pre-shipment and post-shipment stages. It includes any loan to an exporter for financing the purchase, processing, manufacturing or packing of goods meant for overseas markets. Credit is also extended after the shipment of goods to the date of realisation of export proceeds. In this unit, you will learn various schemes of finance available to exporters at pre-shipment and post-shipment stages. You will also be acquainted with the role of EXIM Bank in export finance.

INSTITUTIONAL FRAMEWORK

Institutional framework for providing finance comprises Reserve Bank of lndia, Commercia1 Banks, Export Import Bank of India and Export Credit and Guarantee Corporation. Reserve Bank of India, being the central bank of country, lays down the policy frame work and provides guidelines for implementation.

Finance short or medium term, is provided exclusively by the Indian and foreign commercial banks which are members of the Foreign Exchange Dealer's Association. The Reserve Bank of India function as refinancing institutions for short and medium term loans respectively, Provided by commercial banks. Export Import Bank of India, in certain cases, participates with commercial bank in extending medium term loans to exporters. Commercial banks provide finance at a concessional rate of interest and in turn are refinanced by the Reserve Bank! Export Import Bank of India at concessional rate. In case they do not wish to avail refinance, they are entitled for an interest rate subsidy. Export Credit & Guarantee Corporation (ECGC) also plays an important role through its various policies and guarantees providing cover for commercial and political risks involved in export trade.

PRE-SHIPMENT FINANCE

Pre-shipment finance is provided to the exporters for the purchase of raw materials, processing them and converting them into finished goods for the purpose of export. Let us discuss various pre-shipment advances available to the exporters.

PACKING CREDIT:-

The basic purpose of packing credit is to enable the eligible exporters to procure, process, manufacture or store the goods meant for export. Packing credit refers to any loan to an exporter for financing the purchase, processing, manufacturing or packing of goods as defamed by the Reserve Bank of India. It is a short-term credit against exportable goods. Packing credit is normally granted on secured basis. Sometimes clear advance may also be granted. Many advances are clean at their initial stage when goods are not yet acquired. Once the goods are acquired and are in the custody of the exporter banks usually convert the clean advance into hypothecation! pledge. Let us first discuss the detail procedure of packing credit.

Eligibility: Packing credit is available to all exporters whether merchant exporter, Export/ Trading/ Star Trading/ Super Star Trading Houses and manufacturer exporter. Manufacturers of goods supplying to Export/ Trading/ ST/ SST Houses and Merchant exporters are eligible for packing credit. The-foreign buyer through the medium of a reputed bank gives the credit to eligible exporters, for specified purposes against irrevocable letter of credit. It is also available against a confirmed or firm export order/contract placed by the buyer for export of goods from India.

Running Account Facility: The RBI has permitted banks to grant packing credit advances even without lodgement of-L/ C or firm-order/ contract under the scheme of Running Account Facility subject to, the fol1owing.conditions .

(i)The facility may be extended, J1rcwid.ed the need for Running Account facility has een established by the exporters to the' satisfaction of the bank.

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ii) The bank may extend this facility only to those exporters whose track record has been good.

iii) L/C or firm order is produced within a reasonable period of time. For Commodities under selective credit control, banks should insist on production of LlCs or firm orders within one month from the date of sanction.

iv) The concessive credit available ~in respect of individual pre-shipment credit should not go beyond

180 days.
Packing credit may also be given under the Red Clause letter of credit. In this method, credit' is given at the instance and responsibility of the foreign bank establishing the LIC. Here, the packing credit advance is made against a simple receipt and is unsecured.
Amount:-The loan amount is decided on the basis of export order and the credit rating of the exporter by the bank. Generally the amount of packing credit will not exceed FOB value of the export goods or their domestic value whichever is less. It can be to the extent of domestic value of the goods even though such value is higher than their FOB value provided the goods are entitled to duty draw back and also covered by the Export Production Finance Guarantee of the ECGC.
Period:-The packing credit can be granted for a maximum period of 180 days from the date of disbursement. The banks are authorised by RBI to extend this period. This period can be extended for a further period of 90 days, in case of non-shipment of goods within 180 days. The extension can be done provided the banks are satisfied that the reasons for extension are due to circumstances beyond the control of the exporters. Pre-shipment credit may be given for a longer period upto a maximum of270 days, if the banks are satisfied about the need for longer duration of credit.
Rate of Interest:-The interest payable on pre-shipment finance is usually lower than the normal rate, provided the credit is extinguished by lodging the export bills on remittances from abroad. If the exporter fails to do so they would not be able to avail concessional rate of interest.
In order to avail the packing credit; exporters are expected to make a formal application to the bank giving details of credit requirements along with the required documents.

ADVANCE AGAINST INCENTIVES

When the value of the materials to be procured for export is more than FOB value of the contract, the exporters may get packing credit advance more than the FOB value of the goods. The excess of cost of production over the FOB value of the contract represents incentives receivables. For example, when the domestic price of goods exceeds the value of export orders, the difference represents duty drawback entitlement. Banks can grant advances against duty drawback at pre-shipment stage subject to the condition that the loan is covered by Export Production Finance Guarantee of Export Credit Guarantee Corporation (ECGC). This guarantee enables banks to sanction advances at the pre-shipment stage to the full extent of cost of production. The extent of cover and the premium are the, same as for packing credit guarantee.

PRE-SHIPMENT CREDIT IN FOREIGN CURRENCY

This is an additional window to rupee packing credit scheme. This credit is available to cover both the domestic and imported inputs of the goods exported from India. The facility is available in any of the convertible currencies. The credit will be self-liquidating in nature and accordingly after the shipment of goods the bills will be eligible for discounting/ rediscounting or for post-shipment credit in foreign currency. The exporters can avail this finance under the following two options.
i)the exporters may avail pre-shipment credit in rupees and, then, the post-shipment credit either in rupees or in foreign currency denominated credit or discounting/ rediscounting of export bills.
ii) The exporters may avail pre-shipment credit in foreign currency and discounting/ rediscounting of the export bills in foreign currency.
PCFC credit will also be available both to the supplier units of EPZ/ EOU and the receiver units of EPZ/ EOU. The credit in foreign currency shall also be available on exports to Asian Clearing Union (ACU) Countries. This will be extended only °!l the basis of confirmed! firm export orders or confirmed L/Cs. The Running Account facility will not be available under the scheme.

POST-SHIPMENT FINANCE

It may be defined as "any loan or advance granted or any other credit provided by a bank to an exporter of goods from India from the date of extending the credit after shipment of goods to the date of realisation ion of export proceeds. It includes any loan or advance granted to an exporter on consideration of or on the security of, any duty drawback or any cash receivables by way of incentive from the government.
While granting post-shipment finance, banks are governed by the guidelines issued by the RBI, the rules

of the Foreign Exchange Dealers Association of India (FEDAI), the Trade Control and Exchange Control Regulations and the International Conventions and Codes of the International Chambers of Commerce. The exporters are required to obtain credit limits suitable to their needs. The quantum of credit depends on export sales and receivables. Post shipment finance is granted under various methods. The exporter may choose the type of facility as per his requirement. The Banks scrutinise the documents submitted for compliance of exchange control provisions like:

The documents are drawn in permitted currencies and payment receivable as permitted method of payment;

The relevant GR/PP form duly certified by the customs is submitted and particulars as stated in the GR/PP form are consistent with the documents tendered as well as the sale contract! firm order etc./ letter of credit;

The documents are submitted within the time limit stipulated and in case of delay suitable explanation is made;

The period of usance is in consonance with the time limit prescribed for realisation of export proceeds.

VARIOUS TYPES OF POST-SHIPMENT FINANCE.

1.Negotiation of Export Documents Under Letters of Credit

Where the exports are under letter of credit arrangements, the banks will negotiate the export bills provided it is drawn in conformity with the letter of credit. When documents are presented to the bank for negotiation under L/C, they should be scrutinized carefully taking into account all the terms and conditions of the credit. All the documents tendered should be strictly in accordance with the L/C terms. It is to be noted that the L/C issuing bank undertakes to honour its commitment only if the beneficiary submits the stipulated documents. Even the slightest deviation from those specified in the L/C can give an excuse to the issuing bank of refusing the reimbursement of the payment that might have been already made by the negotiating bank.

2.Purchase/Discount of Foreign Bills

Purchase or discount facilities in respect of export bills drawn under confirmed export contracts are generally granted to exporters who enjoy bill purchase/discounting limits sanctioned by the bank. As the security offered by the issuing bank under letter of credit arrangement is not available, the financing bank is totally dependent upon the credit worthiness of the foreign buyer. The documents, under the Documents against Payment (DIP) arrangements, are released through foreign correspondent only when payment is received. Whereas in the case of Documents against Acceptance (D/A) bills, documents are delivered to the overseas importers against acceptance of the draft to make payment on maturity. Since the financing banks are open to the risk of non-payment, ECGC policies issued in favour of exporters and assigned to banks are insisted upon. Under the policy, ECGC fixes limits and payment terms for individual buyers and the financing bank has to ensure that the limit is not exceeded so that the benefits of policy are available. Banks also secure a guarantee from ECGC on the post-shipment finance extended by them either on a selective or whole turnover basis. Banks sometimes do obtain credit reports on foreign buyers before they purchase the export bills drawn on the foreign buyer.

3.Advance against Bills Sent on Collection

Post-shipment finance is granted against bills sent on collection basis in the following situations:

i)when the accommodation available under the foreign bills purchase limit is exhausted ii)when some export bills drawn under L/ C have discrepancies.

iii)where it is customary practice in the particular line of trade and in the case of exports to countries where there are problems of externalisation.

Under the above situation, the bank may send the bill on collection basis and finance the exporter to some extent out of the total bill amount. The amount advanced will be liquidated out of the export proceeds of the export bill and the balance paid to the exporter.

Exporters may avail themselves on the forward exchange facility where they do not wish to be subjected to exchange risk on account of the new procedures for overdue export bills.

4.Advance against Goods Sent on Consignment

Sometimes exports are effected on consignment basis. In such condition payment is receivable to sale of goods. Goods are exported at the risk of exporter for sale. The banks may finance against such transaction subject to the exporter enjoying specific limit for such purpose. The overseas branch/ correspondent of the bank is instructed to deliver documents against Trust Receipt.

Advance against Export Incentives

Advances against the export incentives are given at the pre-shipment stage as well as the post-shipment stage. However, the major part of the advance is given at the post-shipment stage. The advance is granted to an exporter in consideration of or on the security of any duty drawback incentives receivable from the Government. The banks follow their own procedure in granting the advance. The most common practice is to obtain a power of attorney from the exporter executed in their favour by the banks. It is sent to the concerned government department like the Director General of Foreign Trade, Commissioner of Customs, etc. These advances are not granted in isolation. It is granted only if all other types of export finance are extended to the exporter by the same bank.

Advance against Undrawn Balances

In some of the export business, it is the trade practice that the bills are not drawn for the full invoice value of the goods. A small part of the bills is left undrawn for payment after adjustments due to difference in weight quality, etc. Advances are granted against such undrawn balances. In this case the export proceeds must be realised within 90 days.

The advances are granted provided the undrawn balance is in conformity with the normal level of balances left undrawn subject to a maximum of 5% of the full export value. The exporters are supposed to give an undertaking that they will surrender the balance proceeds within 6 months from the date of shipment.

Advance against Retention Money

Banks grant advances against retention money, which is payable within one year from the date of shipment. The advances are granted upto 90 days. If such advances extend beyond one year, they are treated as deferred payment advance which are also eligible for concessional rate of interest .

Post-shipment Export Credit Guarantee and Export Finance Guarantee

Post-shipment finance given to exporters by banks through purchase, negotiation or dis-count of export bills or advances against such bills qualifies for this guarantee. Exporters are expected to hold appropriate shipments or contracts policy of ECGC to cover the overseas credit risks.

Export Finance Guarantee cover post-shipment advances granted by banks to exporters against export incentives receivable in the form of duty drawback, etc.

Post-shipment Credit in Foreign Currency

The exporters have the option of availing of exports credit at the post-shipment stage either in rupee or in foreign currency. The credit is granted under the Rediscounting of Export Bills Abroad Scheme (EBR) at LIBOR linked interest rates. The scheme covers export bills with usance period upto 180 days from the date of shipment. Discounting of bills beyond 180 days requires prior approval from RBI. The exporters have the option to avail of pre-shipment credit and post-shipment credit either in rupee or in foreign currency. If pre-shipment credit has been availed of in foreign currency, the post-shipment credit necessarily to be under the EBR scheme. This is done because the foreign currency pre-shipment credit has to be liquidated in foreign currency.

EXPORTS UNDER DEFERRED PAYMENTS

You have learnt that all export proceeds must be surrendered to an authorised dealer within 180 days from the date of shipment. Exporters are required to obtain permission from the Reserve Bank through authorised dealers in the event of non-realisation of export proceeds within the prescribed period. However, realising the special needs of exports of engineering goods and projects, Reserve Bank has formulated special schemes permitting deferred credit arrangements. This will enable realisation of export proceeds over a period exceeding six months. Hence, contracts for export of goods and services against payment to be secured partly or fully beyond 180 days are treated as deferred payment exports. The credit extended is termed as deferred payment term credit.

For financing under deferred credit system a single point approval mechanism within a three tier system operates.

This system includes:

i)Commercial banks who are authorised dealers in foreign exchange in India, can provide in principle clearance for contracts valued uptoRs. 25 crores. They can avail refinance from EXIM bank.

ii)EXIM bank is empowered to give clearances for contracts of value of above Rs. 25 crores and uptoRs.) 100 crores.

iii)A working group considers proposals of contracts of value beyond Rs. 100 crores. The working group consists of representatives of all the above institutions to provide single window clearance.

Deferred credit facility is normally allowed only for export of engineering goods, turnkey projects involving rendering of services like designing, civil construction and erection and commissioning of plant or factory alongwith supply of machinery, equipment and materials. Project exports eligible for export finance are as follows:

i)**Turnkey projects**: These projects involve supply of equipment alongwith related services like design, detailed engineering, civil construction, erection and commissioning of plants, etc.

ii) **Construction projects:** involve civil works, steel structural works as well as associated supply of construction materials and equipment.

iii) **Technical and consultancy service contracts** involve provision of personnel, furnishing of knowhow, skills, operation and maintenance services and management contracts.

These services include:

a)Engineering services contracts involve supply of services such as design, erection, commissioning or supervision of erection and commissioning.

b) Consultancy services contracts involve preparation of feasibility studies, project reports, preparation of designs and advice to the project authority on specifications for plant and equipments.

DEFERRED CREDIT FACILITIES

Export of goods on deferred payment terms can be financed under suppliers credit or buyer's credit. Let us first understand what they are,

Supplier's Credit: The exporter extends credit directly to the overseas buyer and seeks refinance from commercial banks/EXIM bank.

Buyer's Credit: It is a loan extended by a financial institutions or a consortium of financial institutions to the overseas buyer for financing a particular contract. Let us discuss buyer's Credit in detail.

Under this scheme, credit is granted by EXIM Bank jointly with an authorised dealer to foreign buyers in connection' with export of capital goods and turnkey projects from India. The exporters are paid out of the buyer's credit on a non-recourse basis on their complying with the terms of the export contracts to be financed under the scheme. Before the exporter enters into any contract providing for credit terms to be financed under buyer's credit scheme, they should have detailed discussion with the bankers. While considering proposals under the scheme, the following factors are taken into account by EXIM Bank:

Competence and capability of Indian exporters in complying with the proposed commercial terms of the contract;

Justifiability of the contract on commercial considerations;

Economic viability of the overseas projects concerned of the importer and general economic

conditions of his country.

iv)credit worthiness of foreign borrower.

Reserve bank's permission is also required for the purpose of granting credit under the scheme since payment will have to be made to the exporter on behalf of non-resident buyer. The authorised dealer in Form DPX 6 should make application to the Reserve Bank for the purpose.

EXPORT IMPORT BANK OF INDIA: PRE- SHIPMENT

EXPORT CREDIT IN FOREIGN CURRENCY

In addition to the pre- shipment credit in foreign currency granted by the commercial banks, the Export-Import Bank of India (EXIM Bank) also offers the facility of pre- shipment export credit in foreign currency to only specified categories of the exporters unlike the PCFC offered by commercial banks to all categories of the exporters. The specified categories of exporters are as follows:

Export House/Trading House with annual export turnover exceeding Rs 10.00 crores.

Manufacturing units with minimum export orientation of 25% of production or export turnover exceeding Rs. 5 crores, whichever is lower. For this purpose only physical exports of commodities are taken into account. Such exports could be made either directly or through Trading Houses.

© The exporter should have satisfactory.

The Export Import Bank of India provides this facilities to the exporters through commercial banks. Such credit is granted to pay for the import of inputs required for export production. This credit is granted on the basis of the firm export order or the letter of credit.

Salient Features:-

The salient features of this scheme are as follows:

1.EXIM Bank raises short-term foreign currency funds on a revolving basis from one or more Syndicates of overseas lenders. Such funds are then made available by the EXIM Bank to the commercial banks in India who opt to avail of PCFC for on-lending to eligible exporter customers for import of eligible items. The commercial banks will, in turn, allocate PCFC limits to their customers on the basis of their assessment of import requi.rement for export production. The advances granted under PCFC to the exporters is ully liquidated from the export proceeds of the relative export bill.

The maximum period of an advance under PCFC will not generally exceed 180 days.

The applicable rate of interest on credit available to the exporter will be two per cent over and above the interest rate at which the funds are raised by the EXIM Bank. Exporters may also have to pay management fee, commitment, fee, etc, if applicable.

The repayment of the pre-shipment credit will be made out of sale proceeds of export shipment in respect of which the exporter availed of the facility.

ROLE OF EXPORT IMPORT BANK OF INDIA

Export-Import Bank of India was set up in 1982, for the purpose of financing, facilitating and promoting foreign trade of India. It is the principal financial institution in the country for coordinating working of institutions engaged in financing exports and imports. The major functions of EXIM bank are as follows;

Finance: The present focus of EXIM Bank is on export finance. The Bank finances export of Indian machinery, manufactured goods, consultancy and technology services on deferred payment terms. Exim Bank finance is also available at export production stages.

Services: EXIM Bank provides information, advisory services to enable exporters to evaluate the international risks, export opportunities and competitiveness.

Research & Analysis: Research & Analysis carried out on specific industry sub sectors with export potential, and international trade related subjects are provided to exporters. Look at Table 7.1 where details of various programmes offered by the EXIM Bank have been shown.

Table 7.1 lending and service programmes of EXIM Bank Programme	Use
For Indian Entities Export (Supplier's) Credit	Enables Indian exporters to extend term credit to Overseas importers, of eligible Indian goods
Financing of Rupee Expenditure for projects Export Contracts	Enables companies to meet cash flow deficits of projects being executed overseas on cash payment terms
Finance for Consultancy And Technology Services	Enables Indian exporters of consultancy and technology services to extend term credit to overseas Importers
Pre-shipment Credit	Enables Indian exporters to buy raw material and other Inputs for export contracts involving cycle time exceeding six months.
Finance for Deemed Exports	Enables Indian Companies to meet cash flow deficits of contracts secured in India and financed by multilateral funding agencies.
Foreign Currency Pre-shipment credit	Enables eligible exporters to access finance for import of raw materials and other inputs needed for export Production

FOREIGN EXCHANGE MANAGEMENT ACT **(FEMA),1999**

When a business enterprise imports goods from other countries, exports its products to them or makes investments abroad, it deals in foreign exchange. Foreign exchange means 'foreign currency' and includes:- (i) deposits, credits and balances payable in any foreign currency; (ii) drafts, travellers' cheques, letters of credit or bills of exchange, expressed or drawn in Indian currency but payable in any foreign currency; and (iii) drafts, travellers' cheques, letters of credit or bills of exchange drawn by banks, institutions or persons outside India, but payable in Indian currency.

In India, all transactions that include foreign exchange were regulated by Foreign Exchange Regulations Act (FERA),1973. The main objective of FERA was conservation and proper utilisation of the foreign exchange resources of the country. It also sought to control certain aspects of the conduct of business outside the country by Indian companies and in India by foreign companies. It was a criminal legislation which meant that its violation would lead to imprisonment and payment of heavy fine. It had many restrictive clauses which deterred foreign investments.
In the light of economic reforms and the liberalised scenario, FERA was replaced by a new Act called the Foreign Exchange Management Act (FEMA),1999.The Act applies to all branches, offices and agencies outside India, owned or controlled by a person resident in India. FEMA emerged as an investor friendly legislation which is purely a civil legislation in the sense that its violation implies only payment of monetary penalties and fines. However, under it, a person will be liable to civil imprisonment only if he does not pay the prescribed fine within 90 days from the date of notice but that too happens after formalities of show cause notice and personal hearing. FEMA also provides for a two year sunset clause for offences committed under FERA which may be taken as the transition period granted for moving from one 'harsh' law to the other 'industry friendly' legislation.
Broadly,the objectives of FEMA are: (i) To facilitate external trade and payments; and (ii) To promote the orderly development and maintenance of foreign exchange market. The Act has assigned an important role to the Reserve Bank of India (RBI) in the administration of FEMA. The rules,regulations and norms pertaining to several sections of the Act are laid down by the Reserve Bank of India, in consultation with the Central Government. The Act requires the Central Government to appoint as many officers of the Central Government as Adjudicating Authorities for holding inquiries pertaining to contravention of the Act. There is also a provision for appointing one or more Special Directors (Appeals) to hear appeals against the order of the Adjudicating authorities. The Central Government also establish an Appellate Tribunal for Foreign Exchange to hear appeals against the orders of the Adjudicating Authorities and the Special Director (Appeals). The FEMA provides for the establishment, by the Central Government, of a Director of Enforcement with a Director and such other officers or class of officers as it thinks fit for taking up for investigation of the contraventions under this Act.
FEMA permits only authorized person to deal in foreign exchange or foreign security. Such an authorized person, under the Act, means authorized dealer, money changer, off-shore banking unit or any other person for the time being authorized by Reserve Bank. The Act thus prohibits any person who:-
Deal in or transfer any foreign exchange or foreign security to any person not being an authorized person;
Make any payment to or for the credit of any person resident outside India in any manner;
Receive otherwise through an authorized person, any payment by order or on behalf of any person resident outside India in any manner;
Enter into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire, any asset outside India by any person is resident in India which acquire, hold, own, possess or transfer any foreign exchange, foreign security or any immovable property situated outside India.The Act deals with two types of foreign exchange transactions.

EXPORT GUARANTEE CORPORATION OF INDIA (ECGC)

The government of India set up the Export Risks Insurance Corporation (ERIC) in July 1957 in order to provide export credit insurance support to Indian exporters. To bring the Indian identity into sharper focus, the corporation’s name was once again changed to the present Export Credit Guarantee Corporation of India Limited in 1983. ECGC is a company wholly owned by the government of India.
Being essentially an export promotion organization, it functions under the administrative control of the Ministry of Commerce, Government of India. It is managed by a Board of Directors comprising representatives of the Government, RBI, Banking, Insurance and exporting community.

Role Of ECGC of India

ECGC was established in year 1957 by the Government of India to strengthen the export promotion drive by covering the risk on exporting credit. The goal of ECGC is to provide cost-effective insurance and trade related services to meet the needs and expectations of the Indian export market. It provides a range of credit risk insurance cover to exporters against loss in export of goods and services. ECGC also offers guarantees to banks and financial institutions to enable exporters to obtain better facilities from them.

Services provided by ECGC to exporters

To provide risk cover to the exporters against the risk associated in world market, viz., political risk and commercial risk.

To provide exporters information regarding credit-worthiness of overseas buyers.

Provides information on approximately 180 countries with its own credit ratings.

To help exporters to obtain financial assistance from commercial banks and other financial institutions.

To provide other essential services which are not provided by other commercial insurance companies.

To assists exporters in recovering bad debts.

To help exporter to develop and diversify their exports.

ECGC has also made a foray into information services by signing an alliance with M/s Dun &Bradsheet Corporation, the largest database company in the world, to provide information on domestic as well as foreign business companies, exporters, importers banks and other institutions.

Financial Guarantees issued by ECGC to banks-

In order to provide financial assistance to the exporters through commercial banks and other financial institutions, ECGC guarantees various loans provided by these financial intermediaries to the exporters. Due to the guarantees given by the ECGC, commercial banks can liberally lend money to the exporters. The nature of guarantees provided by the ECGC depends upon the purpose of finance.

Main Types of Guarantees offered:

Packing Credit Guarantee:- Any loan given by banks to an exporter at the pre-shipment stage against a confirmed export order or L/C qualifies for PCG. The guarantees assure the banks that in the event of an exporter failing to discharge his liabilities to the bank, ECGC would make good a major portion of the bank's loss; bank is required to be co-insurer to the extent of the remaining loss. Features of this guarantee are:

Any loan given to an exporter for the manufacture, processing, purchasing or packing of goods meant for export against a firm order or Letter of Credit qualifies for PCG.

Pre-shipment advances given by banks to parties who enter into contracts for export of services or for construction works abroad to meet preliminary expenses in connection with such contracts are also eligible for cover under the guarantee.

The guarantee, issued for a period of 12 months based on a proposal from the bank, covers all the advances that may be made by the bank during the period to an individual exporter within an approved limit.

Approval of ECGC has to be obtained if the period for repayment of any advance is to be extended beyond 360 days from the date of advance.

Whole-turnover Packing Credit Guarantee can be issued to banks which wish to obtain cover for packing credit advances granted to all its customers on all India basis. Under this option, premiums are lower and higher percentage of cover is offered.

Post shipment Export Credit Guarantee: Banks extend post-shipment finance to exporters through purchase, negotiation or discount of export bills or advances against such bills. The post-shipment credit guarantee provides protection to banks against non-realization of export proceeds and the resultant failure of the exporter to repay the advances availed. However, it is necessary that the exporter concerned should hold suitable policy of ECGC. The percentage of loss covered under this guarantee is 75%.

Features of this policy are:-

Individual Post-Shipment credit Guarantee can also be obtained for finance granted against L/C bills, even where an exporter does not hold an ECGC policy, provided that the exporter makes shipments solely against letters of credit.

This guarantee can also be issued on whole turnover basis wherein the percentage of cover under shall be 90% for advances granted to exporters holding ECGC policy. Advances to non-policyholders are also covered with the percentage of cover being 65%.

Export Production Finance Guarantee:- This guarantee enables banks to sanction advances at pre-shipment stage to the full extent of the domestic cost of production. Here again, the bank would be entitled to 66.67% of its loss from the corporation.

Export Finance Guarantee:- This guarantee covers post-shipment advances granted by banks to exporters against export incentives receivable in the form of duty drawback. The percentage of loss covered under this agreement is 75%.

Export Finance (Overseas Lending) Guarantee:- If a bank financing an overseas project provides a foreign currency loan to a contractor, it can protect itself from the risk of non-payment by obtaining Export Finance (Overseas Lending) Guarantee. The percentage of loss covered under this guarantee is 75%.

Export Performance Guarantee:- This is akin to a counter-guarantee to protect a bank against losses that it may suffer on account of guarantees given by it on behalf of exporters. Exporters are often called upon to furnish a bank guarantee to the foreign parties to ensure due performance or against advance payment or in lieu of retention money. The Export Performance Guarantee protects the banks against 75% of the losses. In the case of bid bonds relating to exports on medium/long term credit, overseas projects and projects in India financed by international financial institutions as well as supplies to such projects, guarantee is granted on payment on 25% of the prescribed premium. The balance of 75% becomes payable by the bankers if the exporter succeeds in the bid and gets the contract.

EXPORT PROMOTION COUNCIL

“The export promotion is basically **promoting, supporting and assisting** firms in entering international markets and achieving optimum opportunities from their international business activities and thereby encouraging exports in India”

In order to provide guidance and assistance to an exporter, the Government of India has setup several institutions, one of them is

Features of EPC

The EPCs are **non-profit organizations**

Registered under the **Indian Companies Act** or the **Societies Registration Act**

These Councils are also the registering authorities under the **Export Import Policy,1997-2002**

They are supported by financial assistance from the Government of India.

These Councils have been assigned the role and functions under the said Policy.

The Export Promotion Councils perform both **advisory** and **executive** functions

Each council is responsible for the promotion of a particular group of products, projects and services

FUNCTIONS/ROLES OF Export Promotion Councils

Providing information: To assist exporters to understand, interpret and implement the export policies and export assistance schemes of Government.

Providing assistance: To provide assistance in export promotional activities such as external publicity, participation in fairs and exhibitions, promotion of exclusive exhibitions and trade fairs of specific products.

Collecting data: To collect complete data on export growth, the problems faced by exporters, the specific help needed by the manufacturers and present the same to the Government in order to enable it to evolve appropriate export policies.

Acting as liaison: To carry on an effective liaison with industry and trade in order to identify the problems in export activities.

Sending trade delegations: To make arrangements for sending trade delegations and study teams to one or more countries for promoting the export of specific products and to circulate the reports of specific products and diversifying to new products.
Opening office abroad: To open offices abroad to help exporters in consolidating the existing exports and diversifying to new products.
Registering authority: To ct as registering authority under the import policy for registered exporters and to help them in expanding overseas market for their products.
Motivating exporters: To create consciousness among exporters through seminars, discussion and to motivate them for export promotion.
Co-operation with EIC: To provide co operation to the export inspection council on quality control and preshipment inspection of export goods.
Disposing applications: To provide assistance to members for speedy disposal of export assistance applications
Offering guidance: To offer guidance to member on various matters like utilization of GSP, export finance, insurance of goods and joint ventures aboard.
Indicating export opportunities: To collect and supply market information to exporter and thereby to help them to take benefits to take benefits of export opportunities available abroad.
Settling disputes: To help the member in settling their trade disputes through peaceful negotiations.
Solving transport problems: To help members to resolve their transport problems.
Concessions: To assist members in getting freight and other concessions for shipping conferences.
Issuing certificate of origin: To issue certificate of origin to Indian exporters certifying the origin of goods.
The EPCs helps Indian exporters through these functions in direct or indirect ways. They provide various services to Indian exporting communities. Each EPC has its working committee which elected by the members
EPCs do not provide financial or other type of direct assistance. They are purely advisory in character. All exporters of products, coming under the purview of council, are entitled to become member of the council. The members have to pay an annual subscription fee for the services rendered to them by the council. All members are given Registrations-Cum-Membership Certificate (RCMC) for the respective EPC. This certificate is useful for securing the benefits of various concessions and incentives offered by the government for export promotions.

EURO CURRENCY MARKETS

A Eurocurrencymarket is a money market that provides banking services to a variety of customers by using foreign currencies located outside of the domestic marketplace. The concept does not have anything to do with the European Union or the banks associated with the member countries, although the origins of the concept are heavily derived from the region. Instead, it represents any deposit of foreign currencies into a domestic bank. For example, if Japanese yen is deposited into a bank in the United States, it is considered to be operating under the auspices of the Eurocurrencymarket.
This market has its roots in the World War II era. While the war was going on, political challenges caused by the takeover of the continent by the Axis Powers meant that there was a limited marketplace for trading in foreign currency. With no friendly government operations within the European marketplace, the traditional economies of the nations were displaced, along with the currencies. To combat this, especially due to the fact that many American companies were tied to the well-being of business behind enemy lines, banks across the world began to deposit large sums of foreign currency, creating a new money market.

UNIT VI

REGIONAL ECONOMIC INTEGRATION

Regional economic integration has enabled countries to focus on issues that are relevant to their stage of development as well as encourage trade between neighbors.
There are four main types of regional economic integration.

- **Free trade area.** This is the most basic form of economic cooperation. Member countries remove all barriers to trade between themselves but are free to independently determine trade policies with nonmember nations. An example is the North American Free Trade Agreement (NAFTA).
- **Customs union.** This type provides for economic cooperation as in a free-trade zone. Barriers to trade are removed between member countries. The primary difference from the free trade area is that members agree to treat trade with nonmember countries in a similar manner. The Gulf Cooperation Council (GCC) [1] is an example.
- **Common market.** This type allows for the creation of economically integrated markets between member countries. Trade barriers are removed, as are any restrictions on the movement of labor and capital between member countries. Like customs unions, there is a common trade policy for trade with nonmember nations. The primary advantage to workers is that they no longer need a visa or work permit to work in another member country of a common market. An example is the Common Market for Eastern and Southern Africa (COMESA). [2]
- **Economic union.** This type is created when countries enter into an economic agreement to remove barriers to trade and adopt common economic policies. An example is the European Union (EU). [3]

In the past decade, there has been an increase in these trading blocs with more than one hundred agreements in place and more in discussion. A trade bloc is basically a free-trade zone, or near-free-trade zone, formed by one or more tax, tariff, and trade agreements between two or more countries. Some trading blocs have resulted in agreements that have been more substantive than others in creating economic cooperation. Of course, there are pros and cons for creating regional agreements.

Pros

The pros of creating regional agreements include the following:

- **Trade creation.** These agreements create more opportunities for countries to trade with one another by removing the barriers to trade and investment. Due to a reduction or removal of tariffs, cooperation results in cheaper prices for consumers in the bloc countries. Studies indicate that regional economic integration significantly contributes to the relatively high growth rates in the less-developed countries.
- **Employment opportunities.** By removing restrictions on labor movement, economic integration can help expand job opportunities.
- **Consensus and cooperation.** Member nations may find it easier to agree with smaller numbers of countries. Regional understanding and similarities may also facilitate closer political cooperation.

Cons

The cons involved in creating regional agreements include the following:

- **Trade diversion.** The flip side to trade creation is trade diversion. Member countries may trade more with each other than with nonmember nations. This may mean increased trade with a less efficient or more expensive producer because it is in a member country. In this sense, weaker companies can be protected inadvertently with the bloc agreement acting as a trade barrier. In essence, regional agreements have formed new trade barriers with countries outside of the trading bloc.
- **Employment shifts and reductions.** Countries may move production to cheaper labor markets in

member countries. Similarly, workers may move to gain access to better jobs and wages. Sudden shifts in employment can tax the resources of member countries.

Loss of national sovereignty. With each new round of discussions and agreements within a regional bloc, nations may find that they have to give up more of their political and economic rights. In the opening case study, you learned how the economic crisis in Greece is threatening not only the EU in general but also the rights of Greece and other member nations to determine their own domestic economic policies.

MAJOR TRADE BLOCKS

The concept of trade blocks is crucial in the context of international trade. Trade blocks are free trade zones designed to encourage trade activities across nations. The formation of trade blocks involves a number of agreements on tariff, trade and tax. The activities of trade blocks have huge importance in the economic and political scenarios of the contemporary world. Over the years trading blocks have played a major role in regulating the trend and pattern of international trade.

Regional Trade Blocks at a Glance

Regional trade blocks protect the interests of the member countries. The primary aim of trade block activities is to create a favorable economic framework for promotion of cross border trade among the member countries.

Different regional blocks have come up in the period of economic liberalization in various parts of the world. Some of the functionally active trading blocks are listed below:

NAFTA (North American Free Trade Agreement)
EU (European Union)
ASEAN (Association of Southeast Asian Nations)
MERCOSUR (Mercado Comun del Cono Sur)
CEFTA (Central European Free Trade Agreement)
GAFTA (Greater Arab Free Trade Area)
SAARC (South Asian Association for Regional Cooperation)
CEMAC (Economic and Monetary Community of Central Africa)
East African Community (EAC)
SACU (South African Customs Union)
PARTA or PIF (Pacific Regional Trade Agreement)
AEC (African Economic Community)
CACM (Central American Common Market)

A particular country may be a member of more than one regional trading block. However, in order to do away with overlapping, such nations are normally put within the most dynamic trade block.

Advantages of Trading Blocs

Access to larger markets leads to internal economies of scale.
External economies of scale due to improved infrastructure (e.g. transport and telecoms links)
Greater international bargaining power.
Increased competition between members.
More rapid spread of technology.

Disadvantages of Trading Blocs

Country may lose resources to more efficient members, or to geographical center, and become depressed region.
Firms may co-operate, collude and merge, leading to greater monopoly power.
Diseconomies of scale if firms become very large.
High administrative costs of trading bloc.

Trade Blocs-Opportunities

Elimination of trade barriers within the region would encourage the efficient firms to expand their business activities in all countries within the region.

Healthy competition within the region would help the less efficient firms in acquiring competencies in order to challenge the efficient firms.

The overall business performance in 'terms of productivity, quality, price,
Delivery and customer service will improve.

Consumers get better quality goods and services at competitive price

Employment opportunities in the region increase.

Trading Blocs – Threat

The removal of trade barriers provides opportunities to the efficient firms to enter the different markets within the region. This endangers the survival of the less efficient firms.

The resources of the less efficient countries are exploited by the firms from the advanced countries of the region.

The less developed countries of the region mostly become consumption centres while the advanced countries of the region become the production centres.

The less developed countries become still poorer whereas the advanced countries of the region become still richer.

It discourages trade with non-members as trade with non-members is subject to strict rules and trade barriers.

GLOBALISATION AND SOCIAL RESPONSIBILITY /SOCIAL RESPONSIBILITY IN INTERNATIONAL BUSINESS

INTRODUCTION -Ultimately, the concept of Corporate Social Responsibility derives from the study of ethics. Business ethics as defined by Crane and Matten (2010: 5) "is the study of business situations, activities and decisions where issues of right and wrong are addressed." "**Business Ethics** can be defined as the critical, structured examination of how people & institutions should behave in the world of commerce. In particular, it involves examining appropriate constraints on the pursuit of self-interest, or (for firms) profits, when the actions of individuals or firms affects others" (Business Ethics, 2008). One can then define business ethics as actions and activities of organisations that revolve around right and wrong; good and bad; acceptable and unacceptable. Crane and Matten were quick to add that this means only morally right and wrong and does not include such things as commercially, strategically or financially right or wrong.

Corporate Social Responsibility (CSR) is a subject with varied names. It is also called 'corporate sustainability, corporate citizenship, corporate social investment, the triple bottom line, socially responsible investment, business sustainability and corporate governance' (Partnerships, 2006). A popular definition of CSR comes from the World Business Council for Sustainable Development which states that it is "the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce, their families and the local community and society at large. (World Business Council for Sustainable Development, 1999)

CSR IN INTERNATIONAL BUSINESS

CSR initiatives engaged in by Multinational companies (MNCs) can be categorised thus:

CSR for global talent acquisition and retention

CSR for branding and reputation management

CSR as regulatory requirement

CSR as philanthropic engagement/initiative

CSR FOR GLOBAL TALENT ACQUISITION AND RETENTION

According to the former Deloitte CEO Jim Copeland (2003): "The best professionals in the world want to work in organizations in which they can thrive, and they want to work for companies that exhibit good corporate citizenship." The basis for CSR as a strategy for acquiring and retaining global talent for MNCs is that in both theory and practice "it has been observed that just as companies succeed in the market by fulfilling the needs of their respective customer base, they can manage their employees best by viewing them as internal customers, fulfilling their needs through a compelling menu of "job-products"

(Bhattacharya, Sankar, Korschun, 2007; see also William,1990; Gummesson,1987; Berry and Parasuraman, 1992; Varey, 1995; Ahmed and Rafiq, 2003). These job products include salary, health benefit, packages and job responsibilities and when designed properly, can contribute dramatically to job satisfaction, employee retention and productivity" (Bhattacharya et al, 2007). By engaging in CSR initiatives that are both specific and relevant, the values of a company are revealed and as such, its values can act as an "Employee Value Proposition" which is "the holistic sum of everything people experience and receive while they are a part of a company." This can be effective in building and sustaining a talented employee base (Bhattacharya et al, 2007).

According to research by Bhattacharya et al., some of the reasons why employees want to work in a company that engages in CSR include self enhancement, work-life integration, bridge to company, and reputational shield.Multinational companies in the modern era thrive on the diversity of their workforce bringing in the best minds and individuals from different parts of the world in a mix to give the organisation competitive advantage. A company as huge as PepsiCo has on its board a Director of Global Talent Acquisition. Business Link (n.d.) states that among other things, organisations gain from CSR as it gives

A good reputation making it easier to recruit employees.

Employees may stay longer, reducing the costs and disruption of recruitment and retraining.

Employees are better motivated and more productive

CSR FOR BRANDING AND REPUTATION MANAGEMENT - In discussing this, the major example which I intend to critique is the case of the Dutch company Shell and its activities in the Niger Delta region of Nigeria. This I have done already in the accompanying video presentation and as such have no further need to restate it here.

CSR AS REGULATORY REQUIREMENT- New laws like the carbon emission tax for airline operators currently in force in Europe is an example of how CSR initiatives can be pre-empted by government. As reported by Discovery News (2012), countries can avoid the tax by developing plans to reduce harmful emissions. This trend means that companies would have to engage in research and development to generate more innovations and products that are both commercially tenable and whose production, use and disposal is environmentally sustainable. CSR regulation by government may come in the form of requiring that Environmental Impact Assessment report be produced before any development that would have a major impact on the environment and communities around it is carried out detailing measures that would be taken to mitigate its adverse effects. This is a means of anticipating the effects of negative externalities of business. This law would have a far reaching effect on global airline companies who ply the European route as they would have to compulsorily contribute to 'making the air cleaner in Europe'. Already, China, India and the United States have made bold protests as an affront to the new law and have threatened reciprocal action as well as boycott of European routes. This would be of grave concern in international business as easy travel to various global destinations may be impeded as a result.

The UK took the case of CSR so importantly that during the successive Labour governments of Tony Blair and Gordon Brown, a Minister of Corporate Social Responsibility was appointed to oversee government's position on the issue of corporate sustainability and responsibility.

"A resolution adopted by the European Parliament on November 25, 2010 increased the likelihood that the days of CSR as a purely voluntary initiative are numbered" states Foley and Pasiponadya of the National Law Review "Approved by a margin of 480 votes to 48, the resolution on corporate social responsibility in international trade agreements calls on the European Commission to include a CSR clause in all of the European Union's trade agreements." A clause like this means that companies would have to prepare for the public domain, CSR balance sheets, "report on due diligence and seek free and informal consultations with local stakeholders" (Foley and Pasipondya, 2010)

In Nigeria however, a bill to make companies dedicate 3.5 per cent of their profits to CSR ventures is currently before the country's legislature for deliberation and passage. The bill which was brought before the parliament by the country's government seeks to make it mandatory for companies to engage in CSR initiatives. This would make Nigeria the first country to legislate on CSR. Taxes, however, do not fall under the remit of CSR as they are the responsibility of government. The law would apply to both local and multinational companies operating in the country. This law, however, would have several controversial areas as it requires 3.5 per cent of profit before tax as a blanket requirement for all companies, whether large ones or SMEs. This could discourage SMEs, who are already stretched for profit and lack the encouragement to continue in difficult economic times. The law however would ensure that companies engage in CSR, as a commission would be established to monitor and regulate it. Yet, it is likely that many nations are watching Nigeria, and waiting to find out if the CSR law works. "If this law does work, it is likely that many other countries might find similar laws proposed and implemented over time" (Chandranayagam 2009).

CSR AS PHILANTROPIC ENGAGEMENT/ INITIATIVE - Regarding philanthropy, top executives more often are caught up in the dilemma of having to choose between following critics who demand more corporate social responsibility investments and pressure from shareholders and investors who want the maximisation of short term profits. Philanthropy is now being used as a means of "public relations or advertising, promoting a company's image through high-profile sponsorships" (Porter and Kramer, 2002). Addressing the business context of charitable donations also helps a company leverage its capabilities and relationships. "Adopting a context-focused approach requires a far more disciplined approach than is prevalent today. But it can make a company's philanthropic activities far more effective" (Porter and Kramer, 2002)

With these, the context of CSR as a philanthropic engagement and initiative of charity can better be understood. CSR, as many have argued, is not corporate philanthropy as in giving money away just because of some sentimental reasons, given that there is an overflow of financial capabilities; CSR is about giving back to the community voluntarily and in a mutually beneficial way, yet not totally within the remit of business activities. CSR is an engagement in enlightened self-interest. Organizations make long-term investments usually buying intangible investments in the long run by making tangible payments in the near term. "Companies are finding an increasing need to depend on value adding activities such as corporate philanthropy in order to distinguish themselves from their competitors and cultivate goodwill amongst their stakeholders. The money they plough into philanthropic activities should not be viewed as a sunk cost. Instead companies should view it as an investment for the good of the overall firm" (Neryan 2009). If targeted well, a company can make its strategic CSR investments in areas where its potential customers can recognise its efforts. To show how vital this is for an organisation and its long term survival, at a CSR conference in Chicago in 2009, the firm Edelman presented the results of a global study of consumer attitudes that revealed that nearly seven in 10 (68%) consumers would remain loyal to a brand during a recession if it supports a good cause (Cmgrenier, 2009).

CSR for philanthropic engagement has been in use by various global businesses, for example MTN - the international telecommunications giant in Africa and the Middle East - which mandates its country operations to spend 1% of their profit after tax for philanthropic activities. In Nigeria, the MTN Foundation engages in philanthropic projects around health, education and empowerment of minorities.

CONCLUSION- As CSR becomes more and more popular, it has increasingly become a 'must do' rather than a 'nice to do'. Companies across the globe, from large brands as Coca Cola, MacDonald's and IBM to smaller ones doing business across boundaries are reaping the returns of improved visibility, positioning and rebuilding brand image and customer perception; talent acquisition and retention; and helping communities help businesses. CSR as a corporate strategy is indeed expedient for businesses, and more so MNCs, in the 21st century.

INTERNATIONAL MONETARY AND FINANCIAL SYSTEMS

International monetary systems are sets of internationally agreed rules, conventions and supporting institutions, that facilitate international trade, cross border investment and generally there allocation of capital between nation states.

International monetary system refers to the system prevailing in world foreign exchange markets through which international trade and capital movement are financed and exchange rates are determined.

The International Monetary System is part of the institutional framework that binds national economies, such a system permits producers to specialize in those goods for which they have a comparative advantage, and serves to seek profitable investment opportunities on a global basis.

Features that IMS should possess:-

Flow of international trade and investment according to comparative advantage.

Stability in foreign exchange and should be stable.

Promoting Balance of Payments adjustments to prevent disruptions associated with temporary or chronic imbalances.

Providing countries with sufficient liquidity to finance temporary balance of payments deficits.

Should at least try avoid adding further uncertainty.

Allowing member countries to pursue independent monetary and fiscal policies.

Stages in International Monetary System:-

Classic Gold Standards:-

22nd June 1816, Great Britain declared the gold currency as official national currency (Lord Liverpool's Act). On 1st May 1821 the convertibility of Pound Sterling into gold was legally guaranteed.

Other countries pegged their currencies to the British Pound, which made it a reserve currency. This happened while the British more and more dominated international finance and trade relations.

At the end of the 19th century, the Pound was used for two thirds of world trade and most foreign exchange reserves were held in this currency.

Between 1810 and 1833 the United States had de facto the silver standard. In 1834 (Coinage Act of 1834), the government set the gold-silver exchange rate to 16:1 which implemented a de facto gold standard.

In 1879 the United States set the gold price to US$ 20,67 and returned to the gold standard. With the "Gold Standard Act" of 1900, gold became an official instrument of payment.

From the 1870s to the outbreak of World War I in 1914, the world benefited from a well integrated financial order, sometimes known as **the First age of Globalization.** Money unions were operating which effectively allowed members to accept each other's currency as legal tender including **the Latin Monetary Union and Scandinavian monetary union**

In the absence of shared membership of a union, transactions were facilitated by widespread participation in the gold standard, by both independent nations and their colonies

Rules of the system:-

Each country defined the value of its currency in terms of gold.

Exchange rate between any two currencies was calculated as X currency per ounce of gold/ Y currency per ounce of gold.

These exchange rates were set by arbitrage depending on the transportation costs of gold.

Central banks are restricted in not being able to issue more currency than gold reserves.

Arguments in Favor of a Gold Standard

Price Stability:-

By tying the money supply to the supply of gold, central banks are unable to expand the money supply.

Facilitates BOP adjustment automatically:-

The basic idea is that a country that runs a current account deficit needs to export money (gold) to the countries that run a surplus. The surplus of gold reduces the deficit country's money supply and increases the surplus country's money supply.

In practice monetary authorities may not be forced to strictly tie their hands in limiting the creation of money.

Countries with respectable monetary policy makers cannot use monetary policy to fight domestic issues like unemployment.

Interwar Period (1918 – 1939)

The years between the world wars have been described as a period of de-globalization, as both international trade and capital flows shrank compared to the period before World War I. During World War I countries had abandoned the gold standard and, except for the United States.

The onset of the World Wars saw the end of the gold standard as countries, other than the U.S., stopped making their currencies convertible and started printing money to pay for war related expenses.

After the war, with high rates of inflation and a large stock of outstanding money, a return to the old gold standard was only possible through a deep recession inducing monetary contraction as practiced by the British after WW I.

The focus shifted from external cooperation to internal reconstruction and events like the Great Depression further illustrated the breakdown of the international monetary system, bringing such bad policy moves such as a deep monetary contraction in the face of a recession.

Conditions Prior to Bretton Woods:-

Prior to WW I major national currencies were on a system of fixed exchange rates under the international gold standards. This system had been abandoned during WW I.

There were fluctuating exchange rates from the end of the War to 1925. But it collapsed with the happening of the Great Depression.

Many countries resorted to protectionism and competitive devaluation. But depression disappeared during WW II

BRETTON WOODS (1945-1971):-

British and American policy makers began to plan the post war international monetary system in the early 1940s.

The objective was to create an order that combined the benefits of an integrated and relatively liberal international system with the freedom for governments to pursue domestic policies aimed at promoting full employment and social wellbeing.

The principal architects of the new system, John Maynard Keynes and Harry Dexter White

Bretton Woods is a little town in New Hampshire, famous mostly for good skiing. In July 1944, the International Monetary and Financial Conference organized by the U.N attempted to put together an international financial system that eliminated the chaos of the inter-war years.

The terms of the agreement were negotiated by 44 nations, led by the U.S and Britain. The main hope of creating a new financial system was to stabilize exchange rates, provide capital for reconstruction from the war and foment international cooperation.

Features of Bretton Woods System:-

The features of the Bretton Woods system can be described as a “gold-exchange” standard rather than a “gold-standard”. The key difference was that the dollar was the only currency that was backed by and convertible into gold. (The rate initially was $35 an ounce of gold)

Other countries would have an “adjustable peg” basically, they were exchangeable at a fixed rate against the dollar, although the rate could be readjusted at certain times under certain conditions.

Each country was allowed to have a 1% band around which their currency was allowed to fluctuate around the fixed rate. Except on the rare occasions when the par value was allowed to be readjusted, countries would have to intervene to ensure that the currency stayed in the required band.

The IMF was created with the specific goal of being the multilateral body that monitored the implementation of the Bretton Woods agreement.

Its role was to hold gold reserves and currency reserves that were contributed by the member countries and then lend this money out to other nations that had difficulty meeting their obligations under the agreement.

The borrowing was classified into tranches, each with attached conditions that became progressively stricter. This enabled the IMF to force countries to adjust excess fiscal deficits, tighten monetary policy etc, and force them to be more consistent with their obligations under the agreement.

Currencies had to be convertible: central banks had to exchange domestic currency for dollars upon request.
Although the adjustable exchange rate system meant that countries that could no longer sustain the fixed exchange rate vis-a-vis the dollar would be allowed to devalue their currencies, they could only do so with the consent of the other countries and the auspices of the IMF.
In a world with N currencies there are only N-1 exchange rates against the reserve currency. If all the countries in the world are fixing their currencies against the reserve currency and acting to keep the rate fixed, then the reserve country has no need to intervene.
Reserve currency country can use monetary policy for its own domestic policy purposes while other countries are unable to use monetary policy for domestic policy purposes. Therefore a decrease in the reserve country's money supply would cause an appreciation of the reserve currency and force the other central banks to lose external reserves.
So the reserve country can affect both the output in its country as well as output in other countries through changes in its monetary policy.

The Demise of the Bretton Woods System-

In the early post-war period, the U.S. government had to provide dollar reserves to all countries who wanted to intervene in their currency markets. Lead to problem of lack of international liquidity.
The increasing supply of dollars worldwide, made available through programs like the Marshall Plan, meant that the credibility of the gold backing of the dollar was in question. U.S. dollars held abroad grew rapidly and this represented a claim on U.S. gold stocks and cast some doubt on the U.S.'s ability to convert dollars into gold upon request.
Domestic U.S. policies, such as the growing expenditure associated with Vietnam resulted in more printing of dollars to finance expenditure and forced foreign governments to run up holdings of dollar reserves. Although they pursue this for a while a few countries began to become growingly less keen on holding dollars and more keen on holding gold.
In 1971, the U.S. government "closed the gold window" by decree of President Nixon.
The world moved from a gold standard to a dollar standard from Bretton Woods to the Smithsonian Agreement. Growing increase in the amount of dollars printed further eroded faith in the system and the dollars role as a reserve currency.
By 1973, the world had moved to search for a new financial system: one that no longer relied on a worldwide system of pegged exchange rates.
