

# SL IB Business Management



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## 1.6 Multinational Companies (MNCs)

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### An Introduction to Globalisation

- **Globalisation** is the economic integration of different countries through increasing freedoms in the cross-border movement of people, goods/services, technology and = finance
- This **integration** of global economies has impacted **national cultures**, spread ideas, speeded up **industrialisation** in developing nations and led to de-industrialisation in developed nations
- Globalisation has been increasing for thousands of years - it is not a new phenomenon
- Improvements in technology and the **speed of global connections** have exponentially increased the **level of interdependence** between nations in the past 50 years
- Consumers now **source products globally** recognising **global brands** wherever they travel

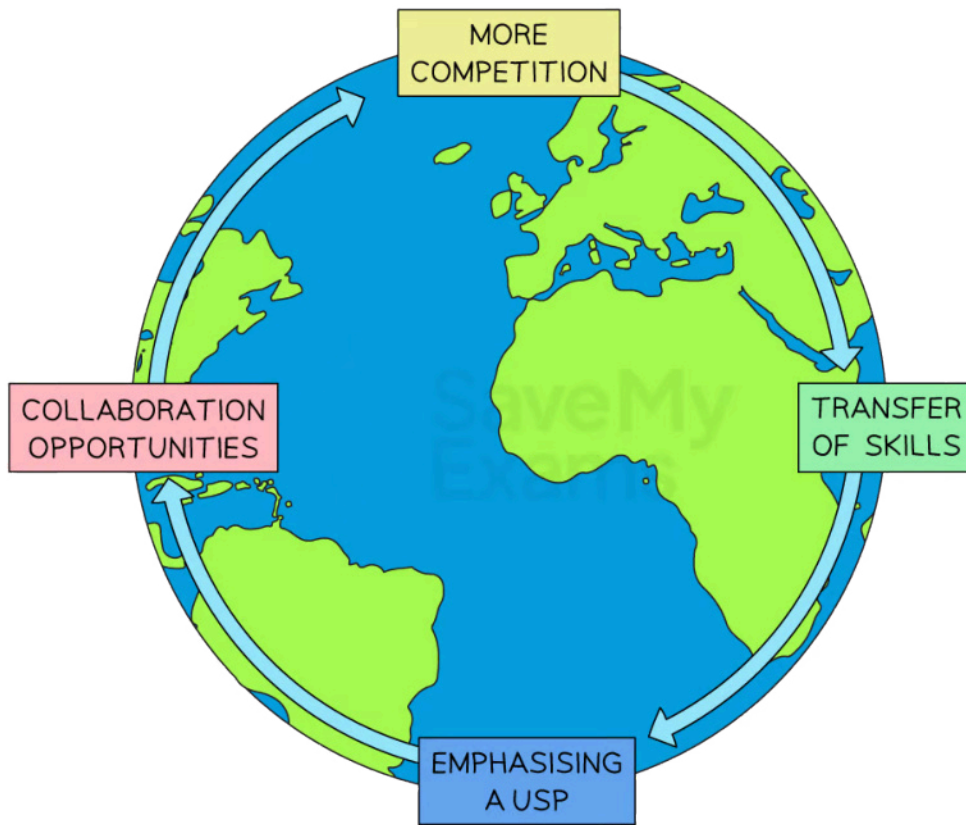
#### The Four Main Characteristics of Globalisation

1. Increasing foreign ownership of companies	2. Increasing movement of labour & technology across borders
3. Free trade in goods/services	4. Easy flows of capital (finance) across borders

- Globalisation has several impacts on domestic businesses that increasingly need to compete with global brands



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### ***Impacts of globalisation on domestic businesses***

- Domestic businesses face **increased competition** as a result of globalisation
  - This incentivises them to improve efficiency in order to remain competitive against global brands
  - Some domestic businesses may **drastically cut staffing** or require higher levels of productivity from workers
- The **transfer of skills** between global and domestic businesses can be mutually beneficial
  - Domestic workers can gain skills and knowledge from an international competitor
  - Global businesses will gain local knowledge, market insight and experience from domestic workers
- Domestic businesses can compete by developing or **emphasising a persuasive** unique selling point (perhaps the fact they are local)
- Both domestic and global businesses can benefit from **close collaboration** through joint ventures or strategic alliances



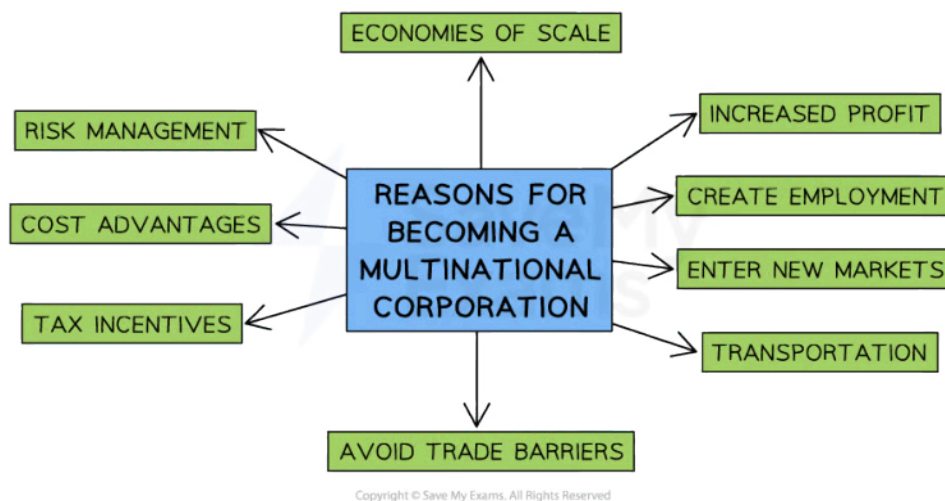
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## Reasons for the Growth of Multinational Corporations (MNCs)

- A **multinational company (MNC)** is a business that is registered in one country but has manufacturing operations/outlets in different countries
  - E.g. Starbucks headquarters are in Washington, USA but they have 32,000 stores in 80 countries
- Factors such as globalisation and deregulation have contributed to the growth of MNC's
  - **Globalisation** has made it easier for firms to do **business on a global scale** and the number and size of MNCs continues to increase
  - **Deregulation** through trade liberalisation and the harmonisation of financial and technical standards has made it easier for businesses to operate in diverse locations

## Reasons why Businesses want to Become Multinationals

- There are numerous reasons why businesses aim to grow to become multinationals



*There are many benefits to becoming a globally recognised brand*

1. **Economies of scale:** as they operate globally they are able to increase their output & benefit from lowered costs created by economies of scale
2. **Increased profit:** much of their profit is sent back to their home country. This point is debatable as many MNCs have offshore bank accounts and do not bring the profit back home
3. **Create employment:** new jobs are created in host countries each time a new facility is setup & this **raises income** which helps to improve the standard of living in that country
4. **New markets:** MNCs can identify potential markets & begin to sell there

5. **Transportation:** MNCs are able to setup facilities closer to their customers which reduces transportation costs
6. **Risk management:** by selling in many national markets, the **risk of failure** is reduced
  - If Egypt goes through a recession (with sales falling there), then this could be less impactful due to rising sales in a strong German market
7. **Tax incentives:** MNCs are able to increase their profits by setting up in countries with **low corporation tax** - or countries that offer MNCs a tax break (no tax) for their first 5–10 years of operation
8. **Cost advantages often related to labour:** many businesses choose to locate production facilities in countries where labour costs are low
  - Nike originates from the USA but 50% of their manufacturing takes place in China, Vietnam and Indonesia due to the **lower production costs** in these countries
9. **Avoidance of barriers to trade:** MNCs can establish bases in countries that are operating protectionist measures and by doing so, they avoid the measures e.g. A Chinese MNC may setup in the USA & produce there, thus avoiding import tariffs on their products exported from China to the USA



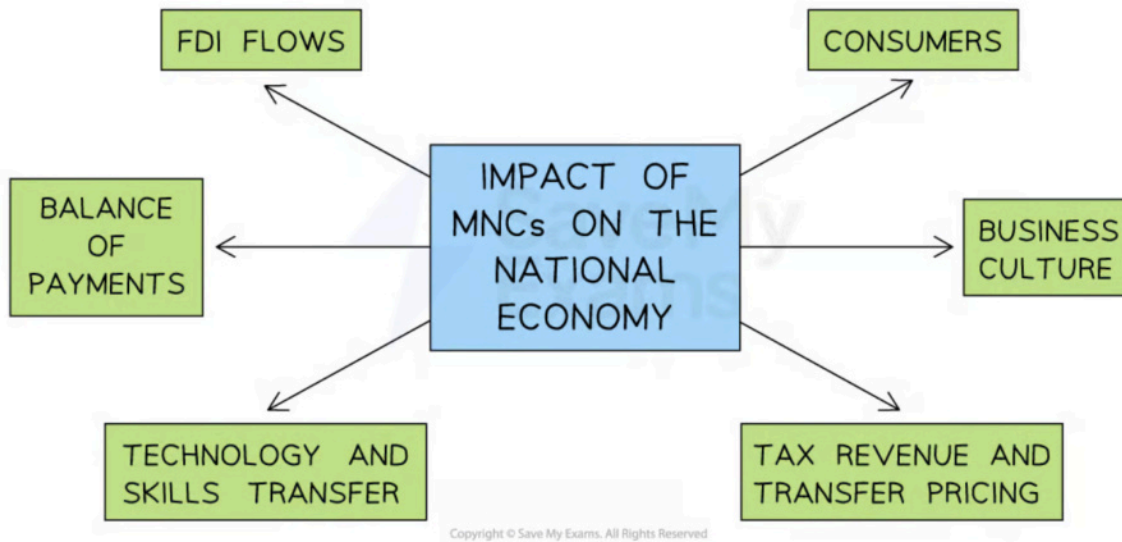
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## The Impact of MNCs on the Host Countries

- Many governments are in favour of MNCs establishing in their country as there are **benefits** to the wider economy



**MNCs impact several metrics in the national economy**

- MNCs offer both advantages and disadvantages for a host country with regard to:
  - Employment, wages and working conditions
  - The impact on local businesses
  - The impact on the local community and environment
  - The impact on the national economy

### Advantages and Disadvantages of MNCs to the Host Country

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>MNCs can help to <b>boost the local economy</b> creating <b>jobs</b> and opportunities for local businesses               <ul style="list-style-type: none"> <li>MNCs often offer <b>competitive wages</b> and <b>better working conditions</b> than local businesses</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>MNCs may exploit local workers if employment regulation is <b>weak or not enforced</b> and may <b>reduce the supply of workers</b> available to local businesses if they offer better pay and working conditions</li> </ul>



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- If the population is benefiting from higher wages, they may **spend more** on local business products
- MNCs may **utilise the services** of local businesses
- MNCs often invest to improve **infrastructure**
  - Better roads, transportation and access to water and electricity would help the local community in addition to helping the MNC operate more efficiently
- There is an **initial lump sum of money** and **ongoing tax revenue** which generates economic growth
  - This money **enriches local firms or citizens** who now have more money available to spend in the economy
  - If this money is **reinvested back into the local economy**, it may help to generate new jobs and boost economic growth
- Domestic businesses may be influenced by the business culture of MNCs
  - E.g. In the 1990s, UK businesses adopted the working practices of Japanese businesses such as Nissan
  - Workplaces became more open and employers started to copy ideas such as Kaizen and continuous improvement
- MNCs can bring new technologies and skills to local businesses
  - This will help to **improve efficiency and productivity**, helping domestic businesses to become **more competitive** in the national and international market
- Customers in countries which host MNCs benefit from
  - A **wider choice of goods** and services
  - **Lower prices** if MNCs pass their cost advantages on in the form of lower prices
  - **Better quality** of goods and services
- MNCs tend to establish production facilities in regions where labour costs are lower and **pay relatively low wages**
  - E.g. Bangladesh is used by many clothing brands to produce cheap clothes and many turn a blind eye to poor working conditions
  - This encourages local firms to **also ignore the working conditions**
- MNCs may not create jobs for local workers as they may **relocate workers from their own country** to work abroad (Chinese companies are notorious for this)
- If MNCs are able to produce at a lower cost and **compete with local businesses**, MNCs can **push domestic businesses out of the market** leaving customers with less choice and **higher prices**
- MNCs may cause **damage to the local environment** during and after the production process
  - E.g. Shell has a track record of **oil pollution** in vulnerable communities in Nigeria
- Assets from the home country are now **owned (or partly owned)** by foreign businesses who may not reinvest the money into the local economy but may **move it abroad/offshore**
- MNCs seek to maximise profits and will try to **reduce their tax liabilities**
  - Transfer pricing is a method used by MNCs to shift profits from where they are generated to countries with lower tax rates
  - This is a method of **tax avoidance** and means that the businesses will pay less tax in the host country