DP IB Business Management: SL

Your notes

1.6 Multinational Companies (MNCs)

Contents

Multinational Companies (MNCs)

Your notes

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

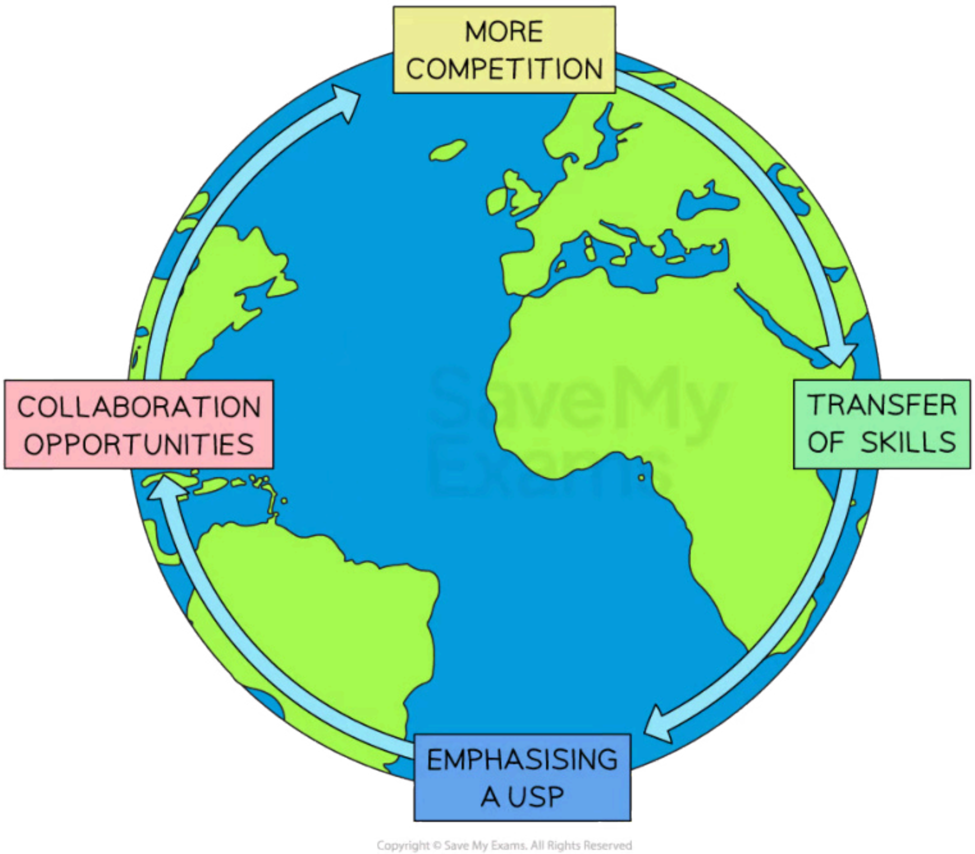
The Four Main Characteristics of Globalisation

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

Diagram: the impacts of globalisation

Your notes



- 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

Your notes

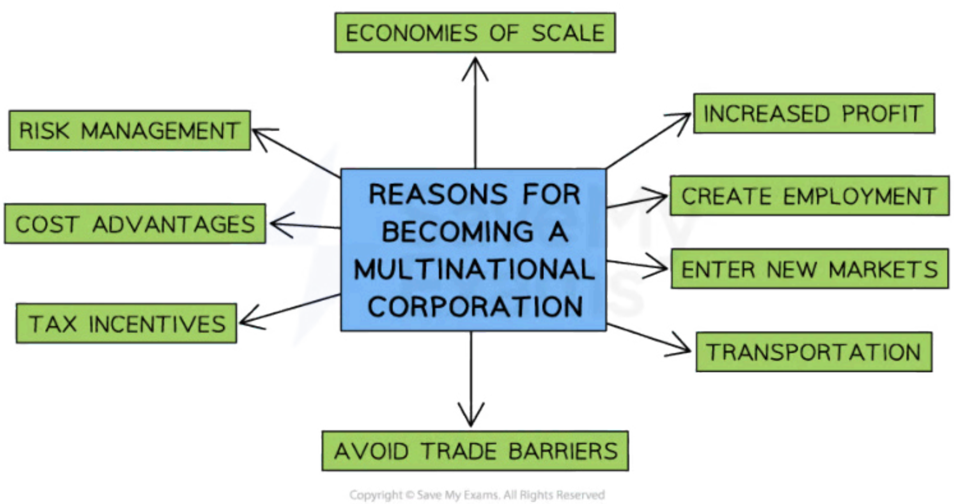
Reasons for the Growth of Multinational Corporations (MNCs)

- **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

Diagram: reasons to become a multinational



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** rates, 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

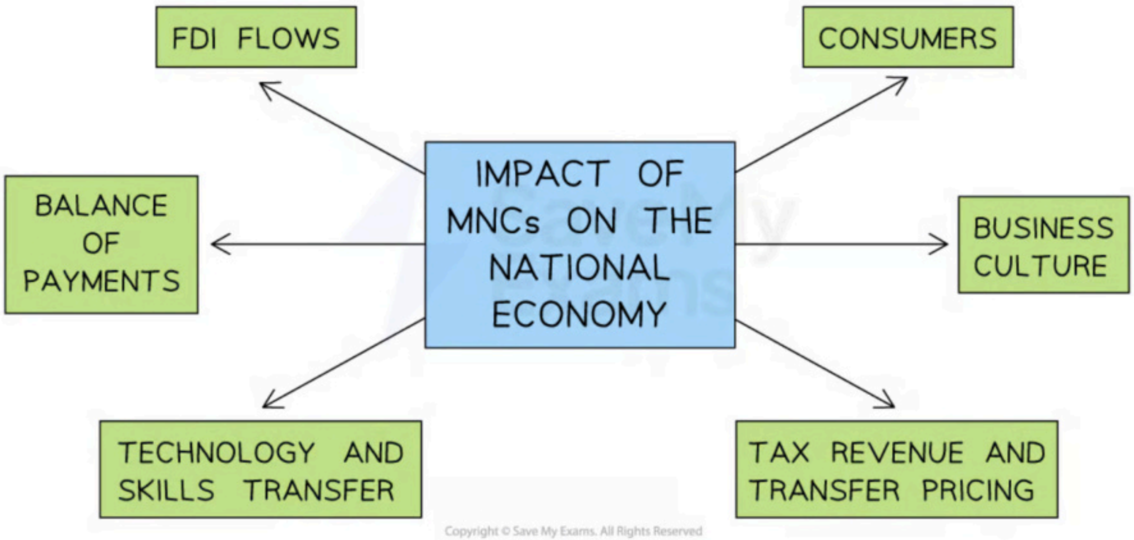
The Impact of MNCs on the Host Countries

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

Diagram: the impacts of an MNC on the host country

Your notes

Your notes



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

Evaluation of the Impacts of MNCs on the Host Country

Advantages	Disadvantages
▪ MNCs can help **boost the local economy** creating **jobs** and opportunities for local businesses ▪ MNCs often offer **competitive wages** and **better working conditions** than local businesses ▪ If the population is benefiting from higher wages, they may **spend more** on local business products	▪ MNCs may exploit local workers if employment regulation is **weak or not enforced** and may **reduce the supply of workers** available to local businesses if they offer better pay and working conditions ▪ **MNCs tend to establish production facilities in regions where labour costs are lower and pay relatively low wages**

- 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 become **more competitive** in the national and international market
- Customers in countries which host MNCs benefit from
  - 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**, they 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, which 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 businesses will pay less tax in the host country

Your notes

- 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	

Your notes