

Chapter 2

The Political, Legal, and Technological Environment

Learning Objectives and Chapter Summary

1. Introduce the basic political systems that characterize regions and countries around the world and offer brief examples of each and their implications for international management.

The global political environment can be understood via an appreciation of ideologies and political systems. Ideologies, including individualism and collectivism, reflect underlying tendencies in society. Political systems, including democracy and totalitarianism, incorporate ideologies into political structures. There are fewer and fewer purely collectivist or socialist societies, although totalitarianism still exists in several countries and regions. Many countries are experiencing transitions from more socialist to democratic systems, reflecting related trends discussed in Chapter 1 toward more market-oriented economic systems.

2. Present an overview of the legal and regulatory environment in which MNCs operate worldwide, and highlight differences in approach to legal and regulatory issues in different jurisdictions.

The current legal and regulatory environment is both complex and confusing. There are many different laws and regulations to which MNCs doing business internationally must conform, and each nation is unique. Also, MNCs must abide by the laws of their own country. For example, U.S. MNCs must obey the rules set down by the Foreign Corrupt Practices Act. Privatization and regulation of trade also affect the legal and regulatory environment in specific countries.

3. Review key technological developments, including the growth of e-commerce, and discuss their impact on MNCs now and in the future.

The technological environment is changing quickly and is having a major impact on international business. This will continue in the future with, for example, digitization, higher-speed telecommunication, and advancements in biotechnology as they offer developing countries new opportunities to leapfrog into the 21st century. New markets are

being created for high-tech MNCs that are eager to provide telecommunications service. Technological developments also impact both the nature and the structure of employment, shifting the industrial structure toward a more high-tech, knowledge-based economy. MNCs that understand and take advantage of this high-tech environment should prosper, but they also must keep up, or go ahead, to survive.

The World of *International Management*: Social Media and Political Change

1. Summary

This vignette discusses the ability of social media to influence world events—ongoing conflict in Syria, which arose in the wake of the “Arab Spring” that spread across Egypt, Tunisia, and Libya in the early 2010s. Unlike previous revolutions, which lacked any widespread, immediate communication tools, the Arab spring protestors were equipped with smartphones and social media. Twitter and Facebook morphed from informal, friendly networking sites to powerful weapons. Groups used Facebook to announce events, garner online support, and encourage people to participate. Attempts to block social media backfired and increased the number of protestors. In addition, protestors became journalists to the international community, with no lag time in broadcasting the news. As a result, governments such as the United States were pressured to take a stand and to lend assistance.

During the Syrian civil war, social media, used as a visual medium, led the global community to unite behind the plight of the Syrian refugees in an unprecedented way. The role of social media as an organizing tool, a journalistic tool, and a support-building tool, all in the context of political change, underscores the interesting interactions of technological progress and political conflict and change.

2. Suggested Class Discussion

- a. Students should be able to discuss how social media influences the political and business environments in countries seeking to transition into democracies—without the blessing of the government.
- b. Students should be encouraged to consider strategies to use social media to the advantage of international markets in unstable political environments.

3. Related Internet Sites

- a. Google Arab Spring, Tunisia, Egypt, Yemen, Libya: <http://www.google.cn/>
- b. Facebook—Arab Spring: <http://www.facebook.com>

- c. Wikipedia: http://en.wikipedia.org/wiki/Arab_Spring
- d. Bloomberg Businessweek: www.businessweek.com

Chapter Outline with Lecture Notes and Teaching Tips

I. Political Environment

- The political system or system of government in a country greatly influences how its people manage and conduct business.
- Underlying the actions of a government is the ideology informing the beliefs, values, behavior, and culture of the nation and its political system.
- A political system can be evaluated along two dimensions.
- The first dimension is the ideology of the system, while the second measures the degree of individualism or collectivism.

A. Ideologies

Individualism

- Adopters of **individualism** adhere to the philosophy that people should be free to pursue economic and political endeavors without constraint.
 - This means that government interest should not solely influence individual behavior.

Collectivism

- **Collectivism** views the needs and goals of society at large as more important than individual desires.

Socialism

- **Socialism** is a moderate form of collectivism in which there is government ownership of institutions, and profit is not the ultimate goal.
 - Communism is an extreme form of socialism that was realized through violent revolution and was committed to the idea of a worldwide communist state.
 - *Social democracy* refers to a socialist movement that achieved its goals through nonviolent revolution.

Teaching Tip: The U.S. State Department produces a series of annual “Country Reports” to acquaint American businesses with other countries. Each report contains nine sections: (1) Key

Economic Indicators, (2) General Policy Framework, (3) Exchange Rate Policies, (4) Structural Policies, (5) Debt Management Policies, (6) Significant Barriers to U.S. Exports and Investments, (7) Export Subsidies Policies, (8) Protection of U.S. Intellectual Property, and (9) Worker Rights. The site is available at

http://www.state.gov/www/issues/economic/trade_reports/99_toc.html. Another source of information on other countries is the CIA's "The World Factbook," available at <https://www.cia.gov/library/publications/the-world-factbook/>.

B. Political Systems

Democracy

- **Democracy** is a political system in which the government is controlled by the citizens either directly or through elections.
- A democratic society cannot exist without at least a two-party system.

Totalitarianism

- **Totalitarianism** is a political system in which there is only one representative party which exhibits control over every facet of political and human life. Power is often maintained by suppression of opposition.

II. Legal and Regulatory Environment

- There are four foundations on which laws are based around the world.
 - **Islamic Law:** This law is derived from interpretation of the *Qur'an* and the teachings of the Prophet Muhammad. It is found in most Islamic countries in the Middle East and Central Asia.
 - **Socialist Law:** This law comes from the Marxist socialist system and continues to influence regulations in former communist countries.
 - **Common Law:** This comes from English law, and it is the foundation of the legal system in the United States, Canada, England, Australia, New Zealand, and other nations.
 - **Civil or code law:** This law is derived from Roman law and is found in the non-Islamic and nonsocialist countries such as France, some countries in Latin America, and even Louisiana in the United States.

A. Basic Principles of International Law

Sovereignty and Sovereign Immunity

- The **principle of sovereignty** holds that governments have the right to rule themselves as they see fit.

International Jurisdiction

- International law provides for three types of jurisdictional principles:
 - The first is the **nationality principle**, which holds that every country has jurisdiction (authority or power) over its citizens no matter where they are located.
 - The second is the **territoriality principle**, which holds that every nation has the right of jurisdiction within its legal territory.
 - The third is the **protective principle**, which holds that every country has jurisdiction over behavior that adversely affects its national security, even if that conduct occurred outside the country.

Doctrine of Comity

- The **doctrine of comity** holds that there must be mutual respect for the laws, institutions, and governments of other countries in the matter of jurisdiction over their own citizens.

Act of State Doctrine

- Under the **act of state doctrine**, all acts of other governments are considered to be valid by U.S. courts, even if such acts are illegal or inappropriate in the United States.

Treatment and Rights of Aliens

- Countries have the legal right to refuse admission of foreign citizens and to impose special restrictions on their conduct, their right of travel, where they can stay, and what business they may conduct.

Forum for Hearing and Settling Disputes

- This is a principle of U.S. justice as it applies to international law.

B. Examples of Legal and Regulatory Issues

Financial Services Regulation

- The global financial crisis of 2008–2010 underscored the integrated nature of financial markets around the world and the reality that regulatory failure in one jurisdiction can have severe and immediate impacts on others.

Foreign Corrupt Practices Act

- The **Foreign Corrupt Practices Act (FCPA)** is an act that makes it illegal to influence foreign officials through personal payment or political contributions.

Teaching Tip: The U.S. Department of Justice maintains an updated website on the Foreign Corrupt Practices Act, including a “lay person’s” simplified interpretation of the Act. The website is available at <http://www.usdoj.gov/criminal/fraud/fcpa/>.

Bureaucratization

- Very restrictive foreign bureaucracies are one of the biggest problems facing MNCs.

C. Privatization

- Another example of the changing international regulatory environment is the current move toward privatization by an increasing number of countries.

D. Regulation of Trade and Investment

- The regulation of international trade and investment is another area in which individual countries use their legal and regulatory policies to affect the international management environment.
- The rapid increase in trade and investment has raised concerns among countries that others are not engaging in fair trade, based on the fundamental principles of international trade as specified in the WTO and other trade and investment agreements.

III. Technological Environment and Global Shifts in Production

- Technological advancements not only connect the world at incredible speed but also aid in the increased quality of products, information gathering, and R&D.

A. Trends in Technology, Communication, and Innovation

- The innovation of the microprocessor could be considered the foundation of much of the technological and computing advancements seen today.
- One Laptop Per Child (OLPC) is a U.S. nonprofit organization set up to oversee the creation of an affordable educational device for use in the developing world.
 - o Its mission is “to create educational opportunities for the world’s poorest children by providing each child with a rugged, low-cost, low-power, connected laptop with content and software designed for collaborative, joyful, self-empowered learning.”

B. Biotechnology

- **Biotechnology** is the integration of science and technology to create agricultural or medical products through industrial use and manipulation of living organisms.

C. E-Business

- As the Internet becomes increasingly widespread, it is having a dramatic effect on international commerce.
- Table 2-2 shows Internet penetration rates for major world regions.

Teaching Tip: An interesting website to show students is the real-time web monitor, Akamai (<https://www.akamai.com/us/en/solutions/intelligent-platform/visualizing-akamai/real-time-web-monitor.jsp>). This site monitors the flow of Internet traffic around the world. It then displays a value between 0 and 100 for different regions of the world. Higher values indicate faster and more reliable connections.

D. Telecommunications

- One of the most important dimensions of the technological environment facing international management today is telecommunications.

E. Technological Advancements, Outsourcing, and Offshoring

- As MNCs use advanced technology to help them communicate, produce, and deliver their goods and services internationally, they face a new challenge: how technology will affect the nature and number of their employees.
- In the future technology has the potential to displace employees in all industries, from those doing low-skilled jobs to those holding positions traditionally associated with knowledge work.
- The new technological environment has both positives and negatives for MNCs and

societies as a whole.

The World of International Management—Revisited

Questions and Suggested Answers

1. How will changes in the political and legal environment in the Middle East and North Africa affect U.S. MNCs conducting business there?

Answer: Political uncertainty and instability is a challenge. MNCs need to assess the political risk and strategies to cope with the situations. The Arab Spring highlighted some of the issues: supply chain disruptions, longer shipping times, and spikes in oil prices. MNCs must collaboratively work with new governments as laws, policies, and regulations are introduced and altered.

2. How might evolving political interests and legal systems affect future investment in the region?

Answer: With changing political and legal systems, the environment for investment may result in more caution. Regulations can change quickly, protection may disappear, and unfavorable subsidies may come into being. On the other hand, new markets and new offshoring options may open up.

3. How does technology result in greater integration and dependencies among economies, political systems, and financial markets, but also greater fragility?

Answer: These changes have been manifested in terms of increased e-commerce and telecommunications, as well as their implications in terms of outsourcing, offshoring, transparency, and financial market integration in general. On the positive side, technology allows organizations to capitalize on their core competencies and create sustainable competitive advantage through networking, outsourcing, and other globally flexible arrangements. Moreover, the integration of financial and labor markets and the mobility found in these markets allow for the use of more competitive sources of capital and labor. Increasingly, technology is also facilitating open communication and transparency, eliminating much of the opaqueness that existed in many regions. On the other hand, various challenges are presented by technology. Jobs and investments have been dislocated in many developed countries. Political and economic crises in one region now have further reach and stronger ramifications on the rest of the world.

Key Terms

Act of state doctrine: A jurisdictional principle of international law which holds that all acts of other governments are considered to be valid by U.S. courts, even if such acts are illegal or inappropriate under U.S. law

Civil or code law: Law that is derived from Roman law and is found in the non-Islamic and nonsocialist countries

Collectivism: The political philosophy that views the needs or goals of society as a whole as more important than individual desires

Common law: Law that derives from English law and is the foundation of legislation in the United States, Canada, and England, among other nations

Democracy: A political system in which the government is controlled by the citizens either directly or through elections

Doctrine of comity: A jurisdictional principle of international law which holds that there must be mutual respect for the laws, institutions, and governments of other countries in the matter of jurisdiction over their own citizens

Foreign Corrupt Practices Act (FCPA): An act that makes it illegal to influence foreign officials through personal payment or political contributions; became U.S. law in 1977 because of concerns over bribes in the international business arena

Individualism: The political philosophy that people should be free to pursue economic and political endeavors without constraint

Islamic law: Law that is derived from interpretation of the Qur'an and the teachings of the Prophet Muhammad and is found in most Islamic countries

Nationality principle: A jurisdictional principle of international law which holds that every country has jurisdiction over its citizens no matter where they are located

Principle of sovereignty: An international principle of law which holds that governments have the right to rule themselves as they see fit

Protective principle: A jurisdictional principle of international law which holds that every country has jurisdiction over behavior that adversely affects its national security, even if the conduct occurred outside that country

Socialism: A moderate form of collectivism in which there is government ownership of institutions, and profit is not the ultimate goal

Socialist law: Law that comes from the Marxist socialist system and continues to influence regulations in countries formerly associated with the Soviet Union as well as China

Territoriality principle: A jurisdictional principle of international law which holds that every nation has the right of jurisdiction within its legal territory

Totalitarianism: A political system in which there is only one representative party which exhibits control over every facet of political and human life

Review and Discussion Questions

1. In what ways do different ideologies and political systems influence the environment in which MNCs operate? Would these challenges be less for those operating in the EU than for those in Russia or China? Why, or why not?

Answer: The international political climate on the whole is improving. Former communist nations are seeing the benefits of free market systems. While this presents obvious opportunities in new markets for MNCs, the risks of doing business in many of these countries are still high. Also, in countries like Russia and China, the government still has some control over many industries. Hence, the political risk is much higher for MNCs wishing to do business in these countries than, say, Europe. While China is still communist, free market principles are encouraged. Another consideration for MNCs is the stability of the currency. Wide fluctuations in the value of money are still occurring in emerging nations such as in Eastern Europe or Southeast Asia, as well as in Northern Africa and the Middle East.

2. How do the following legal principles impact MNC operations: the principle of sovereignty, the nationality principle, the territoriality principle, the protective principle, and principle of comity?

Answer: The legal environment in the international marketplace can be quite complex. This is due to laws that have developed from individual countries, treaties, and such items as the Geneva Convention. The situation is further complicated by the fact that many principles of law are unwritten understandings between nations. Fortunately, most of what MNCs need to know can be found in several broad principles that govern the conduct of international law.

The principle of sovereignty holds that governments have the right to rule themselves as they see fit. Therefore, MNCs must understand the laws of other countries when operating there and abide by them. In the United States, for example, there are many safety rules and regulations governing the workplace. A Japanese-owned company opening a production operation in the United States must follow U.S. laws. Should violations occur, the territoriality principle allows the dispute to be handled in the U.S. court system, regardless of where the MNC's headquarters is located.

However, the nationality principle holds that every country has jurisdiction over its own citizens, regardless of where they are located. Therefore, a Japanese citizen doing business in the United States is not exempt from the laws of his or her own country just because he or she is outside the borders.

The protective principle holds that every country has jurisdiction over behavior that adversely affects its national security, regardless of where the conduct took place. Therefore, if an MNC is engaging in conduct that threatens another country, international law allows the violator to be subject to the host country's legal system, regardless of where the violations are taking place.

The doctrine of comity holds that there must be mutual respect for the laws, institutions, and governments of other countries in the matter of jurisdiction over their own citizens. This common sense principle will foster better relations between MNCs doing business in foreign countries.

3. How will advances in technology and telecommunications affect developing countries? Give some specific examples.

Answer: Technological advancements are connecting the world at lightning speed while increasing quality of products, information gathering, and R&D. The world can be seen as becoming increasingly more flat, which will allow developing countries to more easily enter the international market. Developing countries are eager to attract telecommunication firms and offer liberal terms. For example, General Electric has opened a trade office in Vietnam. Increased competition and expansion is expected to continue across the world, even in developing countries.

4. Why are developing countries interested in privatizing their state-owned industries? What opportunities does privatization have for MNCs?

Answer: Many developing countries are recognizing the benefits of advanced communication technology. For example, using cellular phones in many developing

countries is cheaper than landline phones, as phone lines do not have to be installed. To facilitate this quickly and efficiently, many countries are turning to the private sector. In addition to the obvious benefits for international firms that provide these products, this will allow the developing countries to get up to speed with the rest of the world.

Internet Exercise: Hitachi Goes Worldwide

Suggestions for Using the Exercise

1. This exercise provides an excellent opportunity to conduct an “in-depth” analysis of the business activities of an international firm—Hitachi. Ask students to browse the Internet and find at least five additional sites that provide information on Hitachi.
2. As suggested in the exercise, after doing their research, ask students to write a brief assessment of Hitachi’s operations in Asia (specifically Hong Kong and Singapore), North America, or Europe.

In the International Spotlight: Greece

Questions and Suggested Answers

1. If you are a consultant for a business looking to expand in Europe, is Greece even an option?

Answer: Students’ answers will vary. However, they should consider the following points while answering this question. In recent years, the country has struggled economically, leading to the third highest unemployment rate in the world. Greece was significantly impacted by the financial crisis of 2008. The Greek government was required to implement dramatic spending cuts and tax increases to reduce its budget deficits.

2. Do the facts that its population is comprised largely of government workers, that the citizens were largely in favor of defaulting on its national debt, and that the country nearly left the European Union constitute a deal breaker?

Answer: Students’ answers to this question will vary.

3. If the government does, in fact, implement the agreed-upon austerity measures, would that be a sign that the country is on the right track?

Answer: Students’ answers to this question will vary.

4. What other concerns would you have about entering the Greek market?

Students' answers will vary. However, they should address the following points in their answers. Relations between Greece and its creditors remain strained and are contentious. Greece has threatened to default on its loans and has even contemplated exiting the European Union.

A Closer Look: Comparing Recent Global Financial Reform

Summary

1. The G20 wants to end the belief that banks are “too big to fail” by requiring resolution mechanisms and “living wills” for speedy windups that don’t destabilize markets.
 - a. The U.S. Senate set up an “orderly liquidation” process.
 - b. The EU executive, European Commission, published a policy outline on resolution funds so that banks pay for future bailouts.
 - c. *Winners/Losers*: Banks face an extra levy on top of higher capital and liquidity requirements. Taxpayers should be better shielded.
2. Over-the-Counter Derivatives
 - a. U.S. Senate: The Dodd–Frank Act requires banks to spin off their swaps desk.
 - b. In 2016, the EU and the United States reached a deal on the oversight of clearinghouses, paving the way for a more unified global market.
 - c. *Winners/Losers*: Global banks will shift some trading. Corporations face higher costs.
3. Bonuses
 - a. The United States and the EU are applying the G20 principles to curb excessive pay and bonuses.
 - b. *Winners/Losers*: It is harder to justify big bonuses in the future.
4. Credit Ratings Agencies
 - a. The G20 agreed that ratings agencies should be required to register, report to *supervisors*, and show how they manage internal conflicts of interest; the EU adopted even stricter laws, increasing the liability of ratings agencies and improving

transparency.

- b. *Winners/Losers*: Ratings agencies must justify what they do. There will be more competition in the EU for the “Big Three.”

5. Hedge Funds/Private Equity

- a. The United States and the EU are introducing a G20 pledge to require hedge fund managers to register and report a range of data on their positions.
- b. *Winners/Losers*: It will be harder for U.S. hedge fund managers to do business in the EU. European investors may end up with less choice. Regulators will have better data on funds.

6. Banks Trading

- a. The U.S. Senate has adopted the “Volcker rule,” which would ban risky trading unrelated to customers’ needs at deposit-insured banks. In the EU, key states disagree with the rule as they want to preserve their universal banking model.
- b. *Winners/Losers*: Some trading could switch to the EU from the United States inside global banks.

7. Systemic Risk

- a. The U.S. Senate sets up a council of regulators; the House wants a bigger role for the Fed.
- b. The EU is approving a reform that will make the European Central Bank (ECB) the hub of a pan-EU systemic risk board.
- c. *Winners/Losers*: The ECB has an enhanced role. Banks will have yet another pair of eyes staring down at them.

8. Bank Capital Requirements

- a. The U.S. bill directs regulators to increase capital requirements on large financial firms as they grow in size or engage in riskier activities.
- b. The EU is approving new rules on requirements to discourage risky behavior.
- c. *Winners/Losers*: Bank return on equity is set to be squeezed. Regulators will have many more tools to control the sector. Higher costs are likely to be passed on to consumer investors. There could also be timing issues.

9. Fixing Securitization

- a. The U.S. Senate forces securitizers to keep a baseline of 5 percent of credit risk on securitized assets.
- b. The EU already approved a similar bill.
- c. *Winners/Losers*: Banks believe 5 percent is not enough and that the key problem is investor confidence.

Source: “Factbox: Comparing EU and U.S. Financial Reform,” Reuters, May 19, 2010. Additional research by authors.

International Management in Action: Bitcoin and other Decentralized Currencies in the Digital Age

Summary

1. Extra-governmental currencies have sparked the interest of many due to the global nature of online transactions. In the past, these virtual currencies were centrally controlled and often quickly shut down by governmental regulations. In 2008, a paper published online by Satoshi Nakamoto, titled “Bitcoin: A Peer-to-Peer Electronic Cash System,” outlined a new concept for digital currency, in which open peer-to-peer transactions replace the need for centralized currency oversight and regulation. In 2009, Nakamoto released the first peer-to-peer Bitcoin software and issued the first round of currency. Like traditional paper currency, Bitcoin depends on faith of the users for the system to work. Transactions in Bitcoin are, in essence, just the debiting and crediting of those balances.

Bitcoin and other decentralized digital currencies could provide an alternative method of storing value in times of currency uncertainty. Governments appear to be cautiously open to the use of Bitcoin within their borders. Bitcoin’s growth has not been completely smooth. A series of rapid increases and decreases in the value of a Bitcoin, from US\$0.08 in 2010 to over US\$1,200 in 2013, has led to many economists, including former U.S. Federal Reserve Chairman Alan Greenspan, to declare the currency a bubble.

While some economists insist that Bitcoin will ultimately sink to a value of zero, others predict that the currency will rise to a value of over US\$40,000. If consumers continue to cast doubt over government-issued, centralized currencies, Bitcoin could continue to grow in popularity for years to come.

2. Articles on this issue are multiple. Check the following sites for examples:
 - <https://www.bitcoin.com/>
 - <https://www.zebpay.com/what-is-bitcoin/>