

Module 2: International Trade and Investment

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SUMMARY

This module provides an overview of trends and theories regarding international trade and foreign direct investment. International trade and foreign direct investment have grown dramatically over recent decades. Although new trading and investment patterns are emerging, developed nations tend to trade with and invest in other developed nations, not in developing countries. Much trade is conducted based on regional trade partners and bilateral or multilateral trade agreements. Trade theories attempt to explain why nations trade with each other. Mercantilists believed that trade should be a vehicle for accumulating gold and other precious minerals. Adam Smith, displeased with mercantilist ideas, showed that a nation could acquire what it does not produce by means of free, unregulated trade. A nation could gain most by producing only goods that it could produce with less labor than other nations. Ricardo carried Smith's argument a step farther by proving that a country that was less efficient in the production of all goods could still gain from trade by exporting those products in which it was less inefficient. Newer trade theories are also discussed, including differences in resource endowments, overlapping demand, international product life cycle, economies of scale and the experience curve, and national competitive advantage from regional clusters.

The traditional approach to international involvement was to begin with exporting, then setting up foreign sales companies and finally, where the sales volume warranted, establishing foreign production facilities. Increasingly, because countries have liberalized trade restrictions and IT has made communication instantaneous, companies are becoming involved in trade and FDI for many reasons. International investment theory attempts to explain why foreign direct investment occurs. Product and factor market imperfections as well as strategic behavior help explain foreign investment patterns and help explain why firms primarily from oligopolistic industries may develop advantages not open to indigenous companies. The internalization theory states that international firms will seek to invest in a foreign subsidiary rather than license their superior knowledge to receive a better return on investment used to produce the knowledge. Dynamic capabilities theory suggests that successful international investment requires firms to have an ability to dynamically create, sustain, and exploit unique knowledge or resources over time. There is a brief description of the Eclectic Theory of International Production.

LEARNING OBJECTIVES

- LO 2-1** Describe the magnitude of international trade and how it has grown.
- LO 2-2** Identify who participates in trade.
- LO 2-3** Distinguish among the theories that explain why certain goods are traded internationally.
- LO 2-4** Describe the size, growth, and direction of foreign direct investment.
- LO 2-5** Explain several of the theories of foreign direct investment.

KEY TERMS AND DEFINITIONS

Absolute advantage (p. 35)	A nation's ability to produce more of a good or service than another country for the same or lower cost of inputs.
Comparative advantage (p. 37)	When one nation is less efficient than another nation in the production of each of two goods, the less efficient nation has a comparative advantage in the production of that good for which its absolute disadvantage is less.
Cross-border acquisition (p. 51)	The purchase of an existing business in another nation.
Currency devaluation (p. 41)	A reduction in the value of a country's currency relative to other currencies.
Direct investment (p. 45)	The purchase of sufficient stock in a firm to obtain significant management control.
Dynamic capability theory (p. 53)	Theory that for a firm to successfully invest overseas, it must have not only ownership of unique knowledge or resources, but also the ability to dynamically create, sustain, and exploit these capabilities over time.
Eclectic theory of international production (p. 53)	Theory proposing that for a firm to invest in facilities overseas, it must have three kinds of advantages: ownership specific, location specific, and internalization.
Economies of scale (p. 43)	The predictable decline in the average cost of producing each unit of output as a production facility gets larger and output increases.
Exchange rate (p. 38)	The price of one currency stated in terms of another.
Experience curve (p. 43)	The rising scale on which efficiency improves as a result of cumulative experience and learning.
Greenfield investment (p. 51)	The establishment of new facilities from the ground up.
Internalization theory (p. 52)	Theory that to obtain a higher return on investment, a firm will transfer its superior knowledge to a foreign subsidiary

that it controls, rather than sell it in the open market.

International product life cycle (IPLC) (p. 42)

A theory explaining why a product that began as a nation's export eventually becomes its import.

mercantilism (p. 35)

An economic philosophy based on the belief that (1) a nation's wealth depends on accumulated treasure, usually precious metals such as gold and silver; and (2) to increase wealth, government policies should promote exports and discourage imports.

monopolistic advantage theory (p. 52)

Theory that foreign direct investment is made by firms in industries with relatively few competitors, due to their possession of technical and other advantages over indigenous firms.

National competitiveness (p. 44)

A nation's relative ability to design, produce, distribute, or service products within an international trading context while earning increasing returns on its resources.

Oligopolistic industry (p. 52)

An industry with a limited number of competing firms.

Overlapping demand (p. 41)

The existence of similar preferences and demand for products and services among nations with similar levels of per capita income.

Perfect competition (p. 36)

A market situation in which there is a sufficiently large number of well-informed buyers and sellers of a homogeneous product, such that no individual participant has enough power to determine the price of the product, resulting in a marketplace that is efficient in production and allocation of products.

Portfolio investment (p. 45)

The purchase of stocks and bonds to obtain a return on the funds invested.

Product differentiation (p. 42)

Unique differences producers build into their products with the intent of positively influencing demand.

Resource endowment (p. 41)

The land, labor, capital, and related production factors a nation possesses.

Strategic behavior theory (p. 52)

Theory suggesting that strategic rivalry between firms in an oligopolistic industry will result in firms closely following and imitating each other's international investments in order to keep a competitor from gaining an advantage.

Trade deficit (p. 34)

The amount by which the value of imports into a nation exceeds the value of its exports.

Trade surplus (p. 34)

The amount by which the value of a nation's exports exceeds the value of its imports.

CONTENT OUTLINE

The following section provides the flow of information using the **LEARNING OBJECTIVES** as a guide, **KEY TERMS** learners will need to take away from the course and a notation of when to use **POWERPOINT SLIDES** with **LECTURE NOTES** to drive home teaching points.

LO 2-1	Describe the magnitude of international trade and how it has grown <ul style="list-style-type: none"> • Introduction • International Trade <ul style="list-style-type: none"> • Volume of international trade • How evenly has trade grown? • Which nations account for the most exports and imports? 	Key Terms:
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Lecture Outline and Notes:

- I. Introduction: In this module, two topics are examined that relate directly to exporting and production in foreign countries: (1) international trade, which includes exports and imports, and (2) foreign direct investment.
- II. International Trade
 - A. Volume of International Trade:
 1. The volume of international trade in goods and services was \$4 trillion in 2000 and exceeded \$23.4 trillion in 2013.
 2. Trade in physical goods accounted for \$18.8 trillion of the \$23.4 trillion in 2013, while trade in services was \$4.6 trillion.
 3. While smaller in absolute terms, trade in services has grown faster in the past 20 years than has merchandise trade.
 4. Nearly 60% of global output is now destined for international trade.
 - B. How evenly has trade grown?
 1. The proportion of exports from North America, Latin America, Africa and the Middle East has *decreased* since 1980.
 2. The proportion of merchandise exports from Asia has nearly doubled since 1980, with China accounting for nearly two-thirds of the increase.
 3. Rapid expansion of international trade has helped transform nations such as Singapore, Taiwan, and South Korea from poverty in the 1950s to developed country standards of living, and 500 million Chinese have been lifted out of poverty by China’s trade-driven policies.

4. The European Union increased its proportion of world trade, though the increase is largely due to the EU’s expansion to 28 member countries.
5. All regions and essentially all primary-world nations experienced an absolute increase in the dollar volume of their services exports, though the proportion of world exports of commercial services from Latin America, the EU, Africa and the Middle East has declined since 1980.
6. The rapid increase of world exports since 1980 demonstrates that exporting is a viable growth strategy and one that can benefit exporting nations by creating jobs for their citizens.

C. Which nations account for the most exports and imports?

1. **Table 2.1** shows the ranking of the world’s 10 leading exporters and importers of merchandise and services.
2. The top exporters and importers are generally developed countries, though China ranks in the top 5 for each list and India in the top 10 for imports of merchandise and for both imports and exports of services.
3. The 10 largest exporters and importers collectively account for over 50% of the world’s exports and imports.

LO 2-2	Identify who participates in trade. <ul style="list-style-type: none"> • Direction of trade <ul style="list-style-type: none"> ○ The increasing regionalization of trade ○ Major trading partners: Their relevance for managers ○ Major trading partners of the United States 	Key Terms: <ul style="list-style-type: none"> • Trade deficit • Trade surplus
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Lecture Outline and Notes:

- I. Introduction: More than half the exports from developing nations go to developed countries, but this proportion has been declining, from 72% in 1970 to about 50% in 2013; about 2/3 of exports from developed countries go to other developed countries .
- II. The Increasing Regionalization of Trade
 - A. World Trade is dominated by exchanges within, not between, geographic regions.
 1. In 2014, about half of exports from North American nations went to other nations in North America
 2. A little more than half of Asian nations’ exports were to other Asian nations.
 3. Over 70% of exports from European nations went to other European nations.
 4. Regionalization of trade is reinforced by the development of expanded regional trade associations and agreements such as ASEAN, Mercosur, the EU, and NAFTA.

5. There are more than 200 regional trade agreements in operation worldwide and the share of world trade they account for increased from 37% in 1980 to over 70% by 2013.

A. Growth of exports into developing country markets, and corresponding growth from developing countries to developed countries, are due in part to developing nations increased ability to export manufactured goods, but also due to growing intrafirm trade among international companies' affiliates around the world.

III. Major trading partners: Their relevance for managers.

A. Advantages of focusing attention on a nation that is already a sizable purchaser of goods from the would-be exporter's country include:

1. Business climate in the importing nation is relatively favorable.
2. Export and import regulations are not insurmountable.
 1. There should be no strong cultural objections to buying that nation's goods.
 2. Satisfactory transportation facilities have already been established.
 3. Import channel members are experienced in handling import shipments from the exporter's area.
 4. Foreign exchange to pay for the exports is available.

IV. Major Trading Partners of the United States

A. **Figure 2.2** shows the major trading partners of the United States.

1. The top 10 accounted for 62% of U.S. exports and 69% of US imports in 2013.
2. Mexico and Canada are major trading partners, sharing a common border with the U.S. and being partners in the NAFTA.
3. 9 of the top 15 nations the U.S. imports from have remained on the list over the past 45 years.
4. Rankings of America's trading partners are rapidly changing. Asian nations, like China, have become increasingly important, yet challenging, trade partners for both exports and imports.
5. Between 1991 and 2014, China rose from 6th to 1st place in exports to the U.S. and to 3rd place as an importer of U.S. goods, albeit with a substantial trade deficit for the U.S.

B. Many Asian countries are becoming major importers of American goods because:

1. their rising standards of living enable their people to afford more imported products, and export earnings provide foreign exchange to pay for imports, they are purchasing large amounts of capital goods to further their industrial expansion,
2. they are importing raw materials and components to assemble into subassemblies or finished goods to subsequently export, often to the U.S., and their governments,

sometimes under pressure from the U.S. government, have sent buying missions to the U.S. to seek products to import.

- C. New international business opportunities can be identified by examining trade statistics from various governmental sources.

<p>LO 2-3</p>	<p>Distinguish among the theories that explain why certain goods are traded internationally.</p> <ul style="list-style-type: none"> • Explaining Trade: International Trade Theories <ul style="list-style-type: none"> • Mercantilism • Theory of absolute advantage <ul style="list-style-type: none"> ○ Absolute advantage: An example <ul style="list-style-type: none"> • Each country specializes • Terms of trade (ratio of international prices) • Gains from specialization and trade • Theory of comparative advantage <ul style="list-style-type: none"> ○ Comparative advantage: An example <ul style="list-style-type: none"> • Each country specializes • Terms of trade • Gains from specialization and trade • How exchange rates can change the direction of trade • Some newer explanations for the direction of trade <ul style="list-style-type: none"> ○ Differences in resource endowments ○ Overlapping demand ○ International product life cycle ○ Economies of scale and the experience curve ○ National competitive advantage from 	<p>Key Terms:</p> <ul style="list-style-type: none"> • mercantilism • absolute advantage • perfect competition • comparative advantage • exchange rate • currency devaluation • resource endowment • overlapping demand • product differentiation • international product life cycle (IPLC) • economies of scale • experience curve • national competitiveness
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regional clusters

- Summary of international trade theory

Lecture Outline and Notes:**I. Explaining Trade: International Trade Theory**

International trade is large in volume and growing, and is also critical to the economic performance of most nations. International trade theory attempts to answer the question, “Why does this trade occur, both overall and between particular nations?”

A. Mercantilism

1. One of the first economic doctrines.
2. Central idea—precious metals were viewed as the only source of wealth and nations could accumulate these precious metals by exporting more goods than they import.
3. Governments should control foreign trade to ensure a favorable trade balance.

B. Theory of Absolute Advantage

1. Adam Smith (*The Wealth of Nations* – 1776) attacked mercantilism and said that to trade in order to accumulate gold and other precious metals was foolish. By means of free, unregulated trade, a nation could acquire what it did not produce.
2. He stated that a nation should produce only those goods in which it was most efficient (country specialization). The surplus could be traded to obtain the products that could not be produced advantageously.
3. Ask: “What are the limits within which both countries are willing to trade?” Discuss these topics: Terms of Trade (Ratio of International Prices) and Gains from Specialization and Trade to further explain Absolute Advantage Theory.
4. Use the examples in the text to explain Absolute Advantage Theory in depth.

C. Theory of Comparative Advantage

1. David Ricardo (1817) showed that if a nation were less efficient in the production of two products, it could still gain from international trade if it were not equally less efficient in the production of both goods.
2. Smith’s and Ricardo’s theories considered labor as the only important factor in calculating production costs and no thought was given to the possibility of producing the same goods with different combinations of factors.
3. Use the examples in the text to explain Absolute Advantage Theory in depth.

D. How Exchange Rates Can Change the Direction of Trade.

1. Traders must know a price in domestic currency to determine if it is better to produce locally or import.
2. Exchange rate is the price of one currency stated in terms of the other.
3. Countries can regain a competitive position through currency devaluation.

4. Use examples from the text to explain Exchange Rates.
- E. Some Newer Explanations for the Direction of Trade
1. Differences in Resource Endowments
 2. Some countries have more abundant resources than others, which can result in different opportunity cost of producing these resources and bringing them to market.
 3. Difference in resource endowments suggest that developed countries would more likely trade with developing countries rather than other developed countries with similar factor endowments.
 4. Overlapping Demand
 - a. Consumers' tastes, preferences, and their nation's per capita income affect market demand in any country.
 - b. Customers in countries with similar levels of per capita demand will demand similar goods and services.
 - c. Unlike the theory of comparative advantage, overlapping demand theory does not specify the direction a given good will go.
 5. International Product Life Cycle (IPLC)
 - a. Developed by Raymond Vernon, this theory addresses the role of innovation in trade patterns by explaining why a product that begins as a nation's export may eventually become its import.
 - b. Figure 2.3 illustrates the evolution of this life cycle.
 - c. The IPLC may have less relevance for "born global" companies and under conditions of increased international competition and short product life cycles.
 6. Economies of Scale and the Experience Curve
 - a. Economies of scale refer to the predictable decline in the average cost of producing each unit of output as a production facility gets larger and output increases
 - b. Experience curve effects may also decrease production costs due to cumulative experience and learning.
 - c. These concepts can help explain a nation's ability to become a low cost producer even without an abundance of resources like labor or minerals.
 7. National Competitive Advantage from Regional Clusters
 - a. National competitiveness results from a country's ability to complete the functions necessary to drive a product/service to market and while increasing ROI: design, produce, distribute, and service.
 - b. Alfred Marshall explained that many industries or firms cluster together geographically because of three reasons:
 - i. Advantages gained from pooling a common labor force,
 - ii. gains attained from the development and pooling of specialized

- labor which can be coordinated with the needs of buyers, and
- iii. benefits gained from the sharing of technological information and corresponding enhancement of the rate of innovation.
- c. Porter’s Diamond Model of National Advantage (Fig. 2.4) identifies four variables that will have an impact on local firms’ abilities to use a country’s resources to gain competitive advantage:
 - i. Demand conditions, the nature of domestic demand within the country,
 - ii. Factor conditions, the level and makeup of production infrastructure,
 - iii. availability of Related and supporting industries such as suppliers and support services, and,
 - iv. the Firm’s strategy, structure and strategic rivalry, including the organization and management style of the firm, level of domestic competition and barriers to market entry.
 - v. Porter also claimed that competitiveness could be affected by government and chance.

F. Summary of International Trade Theory

International trade theory shows that nations will attain a higher level of living by specializing in goods for which they possess a comparative advantage and importing those for which they have a comparative disadvantage.

LO 2-4	Describe the size, growth, and direction of foreign direct investment. <ul style="list-style-type: none"> • Foreign investment <ul style="list-style-type: none"> ○ Portfolio investment ○ Foreign direct investment (FDI) <ul style="list-style-type: none"> • The outstanding stock of foreign direct investment • Annual inflows of FDI • Level and direction of FDI ○ Does trade lead to FDI? 	Key Terms: <ul style="list-style-type: none"> • Portfolio investment • Direct investment
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Lecture Outline and Notes:

- I. Foreign investment is divided into two components: (1) portfolio investment and (2) direct investment. The distinction between these two has begun to blur, particularly with growing

size and number of international mergers, acquisitions, and alliances.

A. Portfolio Investment

1. Not directly concerned with the control of a firm but to gain ROI
2. Nonresidents owned American stock and bonds with a value of \$8.0 trillion in 2014. Americans owned \$8.7 trillion in foreign securities in 2014.

B. Foreign Direct Investment (FDI)

1. The Outstanding Stock of FDI (**Fig. 2.5**).

- a. The book value of all FDI worldwide was nearly \$26.3 trillion at the beginning of 2014.
- b. The U.S. is one of the largest investor nations, with \$6.3 trillion invested abroad, over 2 times the FDI of the next-largest investor, the United Kingdom.
- c. The proportion of FDI accounted for by the United States declined by over one-third in the past 20 years; the proportion accounted for by the EU increased, though at least partly due to inclusion of additional member countries. Japan' proportion of FDI declined by over half. Developing countries increased their proportion of FDI, from 1% in 1980 to 19% in 2014.

2. Annual Outflows of FDI

- a. Outflows often fluctuate substantially across years, due to factors such as level of economic growth within and across nations and regions of the world.
- b. Outflows hit a historical high in 2000—\$1.24 trillion, more than 2.5 times the level in 1997. Global economic slowdown in late 2000 resulted in subsequent decline in annual FDI flows to \$531 billion in 2002, then increasing to \$2.27 trillion in 2007 before another economic slowdown resulted in a decline to \$1.41 trillion in 2013.
- c. The volume of outward FDI from developing nations in 2013 was 9 times the level in 2003; the proportion of outward FDI worldwide from developing nations increased from under 5% in 1990 to over 32% in 2013.
- d. The vast proportion of outward FDI, about two-thirds, comes from developed nations.
- e. Much of outward FDI is associated with global mergers and acquisitions, because:
 - i. U.S. corporate restructuring put underperforming businesses and assets on the market
 - ii. Foreign companies want rapid access to U.S. advanced technology
 - iii. Foreign firms felt that access to the lucrative U.S. market would be more successful through acquiring known brand names rather than promoting unknown foreign brands
 - iv. Increased international competition, including pursuit of economies of scale, led to restructuring and consolidation of many global industries and acquisition of firms in major markets like the U.S.

3. Annual Inflows of FDI
 - a. Industrialized nations invest and trade with one another, but this proportion has declined in recent years: from an average of 76% for 1998-2002 to 45% for 2010-2013.
 - b. FDI flowing into developing countries was 7 times larger in 2000 than 1990 and tripled again by 2013, although the proportion of FDI funds flowing to these nations fluctuates widely.
 - c. Asia has seen a dramatic increase in FDI inflows in recent years, accounting for nearly half of all investments not directed at the U.S. and the EU during 2010-2013.
 4. Level and Direction of FDI
 - a. Difficult to accurately determine present value of foreign investments, but if a nation continues to receive growing amounts of FDI, its investment climate must be favorable and the political forces of that country are attractive.
 - b. If there is political instability and low levels of FDI inflow, little investment will occur.
- C. Does Trade Lead to FDI?
1. Historically, FDI followed foreign trade because trade costs less and has less risk than FDI and business can be expanded in smaller, controllable increments rather than incurring large investments and larger risk. A firm would start exporting by using agents and then set up an export department with foreign sales personnel as business expanded.
 2. However, FDI can now lead to trade. Significant changes in today’s global business environment make FDI a possible first step into international trade.

LO 2-5	Explain several of the theories of foreign direct investment. <ul style="list-style-type: none"> • Explaining FDI: Theories of international investment <ul style="list-style-type: none"> • Monopolistic advantage theory • Strategic behavior theory • Internalization theory • Dynamic capabilities • Eclectic theory of international production 	Key Terms: <ul style="list-style-type: none"> • Greenfield investment • Cross-border acquisition • Monopolistic advantage theory • Oligopolistic industry • Strategic behavior theory • Internalization
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		<p>theory</p> <ul style="list-style-type: none"> • Dynamic capability theory • Eclectic theory of international production
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Lecture Outline and Notes:

I. Explaining FDI: Theories of International Investment

Accepted theories to explain FDI: FDI can either be greenfield investment, where new facilities are built from the ground up, or cross-border acquisition, the purchase of existing business facilities in another nation. Strategic motives for FDI include finding new markets, accessing raw materials, accessing new technologies or managerial expertise, achieving production efficiencies, enhance political safety of firm’s operations, or respond to competition.

- A. Monopolistic Advantage Theory - based on the premise that FDI is made by firms in oligopolistic industries possessing technical and other advantages over indigenous firms. These advantages could be economies of scale, superior technology, or superior knowledge of marketing, management, or finance, giving the MNE competitive advantage over local firms.
- B. Strategic Behavior Theory – in oligopolistic industries, where there is a limited number of competing firms, the actions of one firm can strongly affect the performance of others in that industry, so firms closely follow and imitate each other’s international investments to keep a competitor from gaining an advantage.
- C. Internationalization Theory - to obtain a higher ROI, a firm will transfer its superior knowledge to a foreign subsidiary and not sell it in the open market. Firms transfer knowledge across borders without it leaving the firm.
- D. Dynamic Capabilities - ownership of specific knowledge or resources is necessary but not sufficient enough for success in FDI, but firm must also develop distinctive competitive advantages to complement their knowledge or resources.
- E. Eclectic Theory of International Production states that for a firm to invest overseas, it must possess 3 types of advantages:
 - 1. Ownership specific – tangible and intangible assets not available to competitors but can be transferred abroad (e.g., a recognizable brand name).
 - 2. Location specific – foreign market offers economic, social or political advantages which will let the firm exploit its ownership specific advantages (market size, tariff or nontariff barriers, or transportation cost advantages)
 - 3. Internalization – firms have choice as to the way to enter foreign markets, ranging from arm’s length market transactions to hierarchy via a wholly owned subsidiary. It is in the firm’s interest to exploit ownership specific advantages through internalization

in those situations where either the market does not exist or it functions inefficiently.

Eclectic Theory (also referred to as OLI Model) explains MNEs' choice of foreign production facilities.

- F. The common factor for all three of these theories is that FDI is typically made by large, research-intensive firms in oligopolistic industries and is the reason why these companies find it profitable to invest overseas.

CONNECT TOOLS FOR CLASS PREPARATION

SmartBook

What is SmartBook?

SmartBook is a digital version of your course textbook. It contains the same content within the textbook, but unlike a typical eBook, SmartBook actively tailors that content to your individual needs as a student. SmartBook can be accessed online through your laptop, tablet or smartphone and is also accessible when you're offline!

How Does SmartBook Help You/Students?

- Assignable – assigning students their reading and studying their textbook content ensures they are coming to class prepared.
- Proven to help students get a better grade. Studies show SmartBook technology can help increase grades by a full letter.
- Save time. Study smarter. SmartBook makes sure students focus on the things you don't know so they can prioritize your study time wisely.
- No more cramming. SmartBook helps learners retain key concepts so you can learn—not memorize.
- Accessible on the go. Use SmartBook on your laptop, tablet or smartphone—online or offline—via your browser or mobile app.
- Results in real time. Track student progress—and prevents them from wait for midterms or finals. Know how well you understand the material now.

How to assign SmartBook to ensure students come to class prepared?

- On the Connect course homepage click “add assignment” > LearnSmart > Select the chapter
- Decide what content you'd like your students to study, and how much time you'd like students to spend on their work. Start by narrowing down the content prior adjusting the slider bar. – Many instructors find it useful to limit the assignment to a maximum of 45 minutes.
- Assign points to the assignment. Instructors have found that if they give the LearnSmart/SmartBook assignment a minimum of 10% of the course grade that students are more likely to complete the assignment.
- The entire LearnSmart/SmartBook module is available to your student at all times, however, assigning it will prompt students to try it. You are required to select a due date for this assignment, however, this will not prevent the student from access to the tool; it is designed to show you that the student has taken the LearnSmart/SmartBook

assignment. LearnSmart/ SmartBook is an adaptive study tool designed for students. It can also show you where students are struggling to understand specific concepts.

- The student's LearnSmart/SmartBook score in the Connect reports is based on their mastery of the material at the time the assignment is due. Mastery is an evaluation of the number of learning objectives they completed via performance on answering questions.
- Students may, and are encouraged, to continue to use LearnSmart/SmartBook throughout the semester. After the assignment due date, they can continue to access this tool. Continued use of LearnSmart will not affect their LearnSmart/SmartBook assignment results in the Connect reports, but has shown to improve test scores by as much as a full letter grade.

ENGAGEMENT & APPLICATION (FACETOFACE & ONLINE & HYBRID)**BOXED TEXT DISCUSSION QUESTIONS WITH SUGGESTED ANSWERS****IB IN PRACTICE: Are Economic and Social Developments Affected by Trade and Investment?**

International trade clearly plays an important role in influencing nations' economic and social performance, especially for developing countries. Yet the mere expansion of trade does not guarantee benefits for a country and its people. Rather, countries need to view trade performance in the context of its effects on their employment levels, economic growth, development, and improvement in their people's living standards. The United Nations Conference on Trade and Development (UNCTAD) compiled the Trade and Development Index (TDI) to capture interactions among a range of institutional, structural, financial, trade, and development factors underlying trade and development, with a goal of measuring a country's trade and development performance and to identify strategies to help trade to produce improved development.

The 20 highest-ranked nations are all developed countries, while 9 of the bottom 10 nations are in sub-Saharan Africa. The best regional performance among developing nations was that of the countries of the East Asia and Pacific region, while South Asia and sub-Saharan Africa lagged behind. A critical factor contributing to high TDI scores is trade liberalization, and FDI was found to have a significant and positive impact on export performance. UNCTAD emphasized that merely improving trade factors, such as by liberalizing the trade environment, will yield only marginal benefits for a nation unless these efforts are made in conjunction with others aimed at social development and poverty reduction. There is a strong need for trade policy and other social, political, and economic undertakings to be integrated and consistent with each other.

Online and Hybrid: Assign questions to be prepared in virtual teams and submitted as a team assignment, or submitted individually and then discussed in a blog or group discussion site.

Face-to-Face: Students develop responses to the questions in class in teams/groups

1. Why might trade and investment affect the social and economic development of a country?

Trade and investment can influence the level of knowledge and other resources that are available to a country, impacting the efficiency of various sectors of an economy, employment, economic growth, the level and distribution of wealth, and opportunities within and across various sectors and groups within a nation.

2. What actions should a developing country take in order to enhance the potential benefits from international trade and development?

Results of UNCTAD's analyses suggest that trade performance strongly impacts the economic and social development of a nation. In that regard, a government can liberalize policies regarding

trade and foreign investment and the reduction or removal of barriers. Evidence suggests that government efforts to liberalize policies and reduce market failures such as government intervention can be effective in promoting development. However, the pace of these efforts must be managed. Too rapid of a liberalization effort may result in short term disruptions and adjustment difficulties, suggesting that governments must carefully assess not only the nature of changes to promote but also the pace of such changes. At the same time, governments must ensure that trade and investment liberalization efforts are integrated with other policy actions aimed at promoting social development and the alleviation of poverty, such as efforts aimed at education, social welfare, infrastructural support, and so on. Having an integrated approach, with consistency across policies and an appropriate pace, is the goal, as well as the challenge for emerging market governments.

GLOBAL DEBATE: Comparative Advantage: Should the United States be Sending Service Jobs to India?

This Global Debate provides an overview of the use of outsourcing as a way for multinational corporations to improve profitability through comparative advantage offered by markets where the cost of labor is significantly less than in the home country of a multinational. However, this simple lesson in economics is quite controversial and serves as a starting point for a stimulating class discussion. This simple lesson in economics is quite controversial and serves as a starting point for a stimulating class discussion on such topics as:

- What are the profit motives for outsourcing? What advantages other than profit can be gained by outsourcing?
- How should a company manage outsourcing?
- How can outsourcing impact (help or hurt) a company's corporate image?
- Is there a potential for an "upward creep" where low level, low skill tasks start to move upward into higher skilled, higher level jobs being outsourced? What impact can this shift have on home country jobs? On host country jobs?
- Is there a risk of a country losing its innovative edge if higher skilled jobs are outsourced?
- Will outsourcing cause a shift in the home country's workforce by creating new job opportunities to replace those being outsourced?

Online and Hybrid: Virtual teams can be assigned questions and submit their work as a group. Alternatively, virtual teams can be assigned to take different roles or perspectives to argue for (or against) and these assignments can be submitted as a group and then opened up to discussion and debate on an online class discussion site or blog, or presented and debated in a face-to-face setting.

Face-to-Face: Students develop responses to the questions in class in teams/groups, or else assign perspectives and conduct an in-class debate and discussion.

1. Can a company gain advantages besides profit by offshoring? If so, what are they? If not, why not?

The answer to this question will vary, and it is intended to help people think through the issue. Certainly, students are likely to focus on the profit motives as a key driver, and many times their responses will relate at least in part to profit-based drivers. However, by probing on this topic it may be possible to extract comments about enhancing the capabilities of a company, through expanding into new and attractive markets or incorporating a more diverse workforce with different ideas (e.g., on how to design or manage a product or process). Offshoring may enable the firm to be more competitive when faced with new or existing competitors who also have operations abroad in lower cost locations. Companies may also offshore activities in order to help disperse risks such as those associated with currency fluctuations, differences in economic growth rates within and across regions, shortages of home country labor, or political risk factors. To the extent that offshoring might also help to promote economic and social development in other nations, a company might feel that offshoring enables them to enhance their reputation and to engage in meaningful, socially responsible investment activity intended to enhance human welfare. Of course, outsourcing can also bring challenges for companies. By moving activities abroad, it may expose the company to loss of capabilities (e.g., going from experienced workers located close to each other to workers located in distant locations), challenges managing different workforces and institutional contexts, challenges with logistics of globally dispersed operations, etc. Offshoring may damage a company's reputation in the home country, due to strikes or other responses to moving jobs away. Many companies find that moving activities to a foreign location where labor costs are lower may expose them to a higher level of overall costs, due to factors such as increased transportation costs, increased uncertainty in logistics and scheduling, exposure to a range of political, economic and other risks, etc.

2. Does a company face ethical considerations in deciding whether to offshore activities? Why or why not?

This question raises an issue that almost always generates strong opinions and a variety of perspectives. Some students may feel that companies have a primary responsibility to maximize their returns to shareholders, so going abroad to a lower cost location may be argued to be the ethical responsibility of managers. Some students may also argue that failure to be cost-competitive on key dimensions of the company's activities, especially when faced with competitors who have lower cost structures, may put the entirety of the company's operations at risk: "it is better to sacrifice a portion of the home country business for the benefit of the overall operations" might be the theme here. Other students will often raise the notion of the harm that a company may cause to workers and their communities when their jobs and associated activities are moved from the home country to another host country. Exploring the variety of perspectives and allowing the debate to blossom can yield a rich and insightful learning experience for the participants.

3. What might be the long-term implications of offshoring, from the perspective of the home country? The host country?

This question also raises issues that almost always generates strong opinions and a variety of perspectives. Some students may feel that the home country is being hollowed out, with jobs, knowledge, and growth opportunities moving abroad to where costs are lower. In some cases, this can be argued to be a “race to the bottom,” as companies seek those places where lax health or environmental standards, weak labor protection, and other factors will enable the weakest and most inexpensive and powerless to be exploited, with corresponding damage to the stakeholders in the home country. This could also be argued to be an initial step toward an “upward creep,” where low level, low skill tasks that are offshored can start a process whereby higher skill jobs will subsequently be outsourced as host country labor builds competencies. Other students will often raise the notion of moving low value added jobs abroad, thereby enhancing the competitiveness of the overall company and creating the opportunity to create new, better jobs in the home country. Students may very well link some of this discussion to the theoretical perspectives of the module, whereby international companies develop and exploit dynamic capabilities in order to gain international advantage. Students might also argue that going abroad may enable the company to access new, better resources, capabilities, growth opportunities, and other advantages that can enhance the company’s long term competitiveness, as well as enhance the benefits flowing back to the home country through the success of companies headquartered within its borders. Exploring the variety of perspectives and allowing the debate to blossom can yield a rich and insightful learning experience for the participants.

When examining this perspective from the host country, some students may suggest that it is essential for economic and social development that the host country encourage foreign investment and/or job creation associated with bringing in offshored jobs. These jobs can help promote economic growth, transfer knowledge and skills, and provide the foundation for a virtuous cycle of enhanced opportunities for more and better job prospects and the benefits that accompany them. Others might argue that the “race to the bottom” syndrome may cause countries to try to undercut each other, through less rigorous health or environmental practices or lax enforcement, or through devaluation of their currency or economic mercantilist behavior, in order to attract the offshored jobs. In so doing, this may stunt rather than promote the economic and social well-being of the host countries, according to these perspectives.

GET THAT JOB! FROM BACKPACK TO BRIEFCASE Katie Lasco: Accept the Challenge of a New Culture!

Katie Lasco discusses her career goal to integrate the study and practice of sustainability with her business career objectives, and how she could use an internship with a sustainability focus in Ecuador to enhance her experience and career opportunities.

Online and Hybrid: Virtual teams evaluate Hotzman’s advice for their own career development and their ability to understand and adapt to life in another culture, particularly one that is quite different from one’s home culture. Share conclusions with class, either online or in face-to-face setting.

Face-to-Face: Students evaluate their own career strategy in light of Holtzman’s advice.

1. How would you evaluate Lasco’s efforts to prepare for her Ecuadorian experience by studying the language and culture of Ecuador? How can such efforts help her to achieve her objective of entering the culture “ready to learn and engage” and “with realistic expectations about my experience”? Were there other actions she could have undertaken to prepare for her experience?

Students will have various answers to this question, depending on their experience with other cultures as well as their own self-awareness and self-confidence. Lasco has chosen to intern in a country that is quite different from her home country, with a different primary language, different level of economic development, different history, and different institutions. In this regard, language and cultural training undertaken prior to departure seems to be a justifiable foundation for enhancing the likelihood of successful cultural adjustment. Although it is unlikely that someone would be able to develop a high level of linguistic and cultural fluency in only a few months of training, at least such efforts can help mitigate the extent of the void between the home and host cultures and make Lasco more effective in recognizing, understanding, and responding to her new environment.

2. Despite Lasco’s efforts to prepare herself prior to departure, she notes that she still experienced culture shock, both within the host country and subsequently upon her return to the United States. Do you think such experiences are typical? Is there anything she could have done to avoid culture shock? How well do you think she responded once she found herself experiencing culture shock, in terms of coming to grips with it and engaging in constructive responses?

Students will have various answers to this question, depending on their experience with other cultures as well as their own self-awareness and self-confidence. Lasco does acknowledge that she still experienced culture shock during her experience in Ecuador, despite her pre-departure preparations and once the “honeymoon phase” wore off. It can be valuable to discuss the likelihood of this happening for the students in the class, and whether culture shock can really be avoided or whether we can merely prepare students to anticipate such an experience and be able to more effectively manage the situation when they find themselves in it. Lasco does outline a series of actions she took to manage the situation once she found herself experiencing culture shock, such as preparing a detailed schedule, finding classes to take to keep her learning and getting out into the community, establishing deeper personal relationships with locals, additional language immersion and training, and trying to take a positive, constructive approach to her experience.

END OF MODULE EXERCISES**CRITICAL THINKING QUESTIONS**

- 1. Discuss and explain how international trade in merchandise and services has changed over the past two decades and what the major trends are. What future trends can you speculate about? How might this information be of value to a manager?**

The answers to this question may vary. The introductory vignette, “Firms invest overseas, but they also export,” shows how exports of both goods and services have grown since 2000. Except for a significant drop in 2009, and a slight decline during the 2000 to 2003 period, both associated with a worldwide economic slowdown and mainly affecting demand for goods, the curve has basically been continuously upward sloping. The text also states that services growth has been greater on a percentage basis in recent decades than has the growth of goods exports. The growth in export demand is attributable to global competition, liberalized trade policies of various national governments, and advances in technology, among other factors, and the two slowdowns shown on Figure 2.1 suggests that the growth in goods and services exports is likely to continue, except during periods of significant worldwide economic slowdown. This trend will also be encouraged by international companies as they not only develop markets in foreign locations but also establish increasingly international supply chains. As the text discusses, most of the trade has been occurring within regional trade agreements, rather than on a global basis per se. Certain areas, particularly Asia, have exhibited an increasing proportion of world trade. Although developed countries have historically dominated international trade, we also see that an increasing portion of world trade involves developing countries, both as sources and as destinations for trade. This information will be of value to managers who want to serve international companies as customers, as well as in identifying which areas within and across regions might be more or less likely to experience an increase in trade.

- 2. Where do merchandise exports come from, and where do they typically go? How and why has this been changing over time, and do you think these trends are likely to continue? Why or why not? Why might this information be valuable to a marketing analyst?**

The answers to this question may vary. More than half the exports from developing nations go to developed nations, but this proportion has been declining, from 72% in 1970 to about 50% by 2013. About two-thirds of exports from developed countries go to other industrialized nations. Trade is dominated by exchanges within, rather than between, geographic regions, reinforced by expanded regional trade associations and agreements. Indeed, about 70% of world trade in 2013 was accounted for by trade involving countries who are partners in regional trade agreements. There may be differences of opinion about whether these trends will continue. Proliferation of regional trade agreements may suggest continued growth in regional trade. Interregional trade agreements such as occur between Europe and some of the former colonies around the world, or the proposed Transpacific Partnership between Australasia and the Americas, may create a basis for increased regional trade. The internationalization of supply chains by international companies may also promote continued growth in trade, as companies ship products among their international affiliates as well as to international customers. Some

may argue that the pendulum may swing back from international trade, due to protectionism, costs of transportation, and so forth, although evidence suggests that growth of trade tends to be associated with economic and social benefits for countries that have liberalized their trade policies. A marketing analyst could find the information about not merely the level of trade but the regionalization of trade and the internationalization of supply chains to be valuable when identifying where to focus efforts for market development or expansion.

3. Describe mercantilism, and explain why some call it a poor approach to promoting economic development and prosperity. Given the criticisms, why do some countries continue to rely on practices based on mercantilism?

Mercantilism is an economic philosophy based on the belief that (1) a nation's wealth depends on accumulated gold and (2) to increase wealth, government policies should promote exports and discourage imports. As a means of promoting economic development and prosperity mercantilism has a poor record. Mercantilism views trade as a zero sum game with one specific winner. It has been proven that the markets, not the government should determine the direction, volume and composition of world trade.

4. Explain Adam Smith's theory of absolute advantage. What are the potential limitations of this theory for helping policy makers when making decisions related to international trade? How does Ricardo's theory of comparative advantage differ from the theory of absolute advantage?

According to Adam Smith's theory of absolute advantage, each nation should specialize in producing the goods it can produce most efficiently. Some of them can be exported to pay for imports of goods that can be produced more efficiently elsewhere. Ricardo showed that even though a nation did not hold an absolute advantage in producing any good, it could still trade with another with advantages for each as long as the less efficient nation was not equally less efficient in producing both goods. Absolute advantage may have some limited value for policy makers, especially when a country does not have a condition of absolute advantage, or where its absolute advantage may erode or disappear over time due to developments elsewhere, such as devaluation of currency, economies of scale that emerge in other nations, competitive declines in one or more areas of advantage within a regional competitive cluster, and so forth.

5. "Sending service jobs to low-cost nations, such as India, is good for America." What are the arguments in support of such an assertion? Under what circumstances might such an assertion be viewed as false?

The answers to this question may vary. For example, there may be situations in which a country does not have, or cannot maintain, competitive advantage in one or more activities. By outsourcing these activities to another country that might have advantage, it may allow the company to avoid this competitive disadvantage and to make the remaining activities more competitive globally, thereby enhancing prospects for the company and its various stakeholders. These outsourcing efforts may promote international trade and even open new or expanded market opportunities abroad for American companies, both in the country where activities are being outsourced to, and perhaps elsewhere as well. On the other hand,

outsourcing may result in job losses that cannot be quickly and fully replenished through the creation of other jobs, due to the different skills required and the time needed to acquire such skills. Job losses may also result in the loss of domestic competencies, and result in a continuing migration of increasingly skilled jobs from America to the foreign locations, especially if the destination nations have the policies and competencies to acquire and enhance their human capital or otherwise enable the development of internationally competitive regional clusters.

6. Name some products that you believe have passed through the four stages of the international product life cycle. Try to identify industries or products for which the international product life cycle still helps explain international trade and investment. Can you identify industries or products for which this concept does not apply?

The answers to this question may vary. Microwave ovens and athletic shoes are two examples of products that have passed through the four stages of the international product life cycle. Other examples include ships, automobiles and computer chips, the latter two being sectors where the life cycle process appears to still be occurring. Students might identify sectors where the IPLC does not apply, such as those where transportation poses a barrier to locating operations abroad (e.g., due to extreme perishability) or where government-driven barriers to trade inhibit the movement of production across borders (e.g., due to national security or other policy priorities).

7. Use Porter's diamond model of national advantage to explain why an emerging market such as Indonesia would be expected to experience great difficulty in achieving global competitiveness in a new industry sector such as "smart" cell phones or hybrid electric-gasoline automobile engines.

An emerging market such as Indonesia would be expected to experience great difficulty in achieving global competitiveness in a new industry sector such as "smart" cell phones or hybrid electric-gasoline automobile engines because: (a) The nature of demand conditions would be unlikely to include the most sophisticated and demanding customers, who would pressure companies to produce high-quality, innovative, competitively viable products. (b) Factor conditions are likely to be deficient, since these new sectors are likely to depend on highly skilled, highly educated workforces, advance communication systems, the most advanced design and production equipment, and so forth. (c) Related and supporting industries are likely to be deficient, since an emerging market is unlikely to have strong computer hardware and software industries, venture capital markets, a pool of highly experienced entrepreneurs and business people in similar or related advanced sectors, etc. (d) The extent of domestic competition is likely to be limited due to the emerging nature of the market, hindering the beneficial competitive rivalry that is key to innovation and success. (e) There could be beneficial government policies oriented toward nurturing new industry sectors, and an emerging market could, by chance, achieve a breakthrough in technology or design. However, in the absence of the above 4 factors, it will be difficult for competitors from the emerging market to sustain this position long term, especially in the face of vigorous competition from competitors in nations with stronger profiles on the above factors.

8. What are the possible explanations for the observed decline in the proportion of FDI accounted for by the United States and Japan? What are the implications of such a decline? Do you expect that this decline will continue in the future? Why or why not?

The answers to this question may vary quite a bit across students. The United States only accounts for about 5% of the world's population, and Japan only about half that much. Therefore, as economic development occurs around the world, it can be expected that more wealth and other resources will be built up within industrially developed and newly industrialized nations. This enhanced wealth and desire for international competitiveness is likely to encourage multinational companies from emerging and newly industrialized nations like the BRICs (Brazil, Russia, Indonesia, China), Mexico and South Korea to expand their investments abroad in order to build globally viable scale and scope. Much of this investment will likely be made via mergers and acquisitions, as companies try to acquire brands, technology, and other capabilities to enhance international competitiveness. While the percentage of FDI accounted for by the United States and Japan may decline, that does not mean that the absolute level of outstanding stock of FDI will decline. Indeed, as global competition continues to escalate, it is likely that the overall level of FDI worldwide will increase over time. On the other hand, some students may suggest that globalization may reverse course over time, due to environmental, political, military, or other factors, and they may also suggest that the emergence of China and other countries as major economic forces will erode the scale and importance of developed countries in global trade and investment. They may even suggest that either the absolute level of global FDI will decline, or that the U.S. and Japanese (and perhaps European, as well) proportions will shrink as the power of developed countries wanes and the power of emerging markets grows. This can be an interesting discussion to have within class.

9. How has the level and direction of FDI changed over the past two to three decades, both overall and in terms of annual outflows and inflows? What might explain why these changes have occurred? Why would this information be of relevance to managers?

The answers to this question may vary. The proportion accounted for by the United States has declined by over 1/3 during the past 20 years, although the U.S. still accounts for more than 3 times the level of the next-largest investor. The European Union's proportion of FDI has increased, but that is at least partially due to the enlargement of the EU through adding new member countries. Developing nations have dramatically increased their proportion of FDI, growing from 1% in 1980 to 19% in 2014, largely reflecting the increasing internationalization that has occurred in emerging markets such as China, Mexico, Brazil, India, and other nations. Overall, as shown in Figure 2.5, the level of FDI worldwide has continued to rise significantly over the past 35 years. Increasing internationalization of competition, economic liberalization (especially in emerging markets), growth in the international financial markets, developments in technology and transportation, and the development of regional trade and investment agreements, among other factors, have favored this growth in FDI, both in absolute level and in the sources and destination of investments. This information is of great potential value to

managers, in terms of identifying potential sources of new or increased competition (or collaboration) as well as new sources of supply or of customers.

10. According to theories presented in this module, why might companies engage in foreign direct investment rather than international trade?

The answers to this question may vary. Each of the trade theories presented in this chapter offer an explanation for why companies engage in foreign direct investment, because each of the theories helps to explain why production costs differ across national borders or how competitive responses are necessary in a globalized economy. However, in some cases there may not be sufficient market mechanisms in place to protect a company's assets (e.g., inability to protect a company's intellectual assets if it tries to license its technology to a foreign company to serve international market opportunities) or to enable the company to adequately capture the value of its competencies. The Eclectic Theory discusses factors that might be relevant to this argument. In addition, it might be argued that corporations, especially those in oligopolistic industries, may engage in foreign direct investment in order to imitate or counterbalance the actions of their international competitors.

The answers to this question may vary. Some techniques and concepts can be applied to operations in other nations. However, the differences among the environmental forces often require that these techniques are altered and in some cases, they cannot be used at all.

MINICASE: Can Brazil Become a Global Competitor in the Information Technology Outsourcing Business?

This minicase explores the issue of outsourcing and how countries may compete to be the destination for outsourced activities. The specific example is of Brazil and how it has emerged as an alternative to countries such as India, China, or various Central or Eastern European nations for the outsourcing of sophisticated IT activities. Brazil has an advanced telecommunications and network services infrastructure, sometimes rated above those of nations such as India or China. Brazil has a large base of jobs in the IT sector and a strong tradition of producing competent graduates from engineering schools. Brazil's banking sector is highly automated and a dynamic marketplace for IT software and support services, helping to encourage domestic demand for advanced IT services. Brazilian wage rates are significantly below those in the USA, and recent devaluations of the real, Brazil's currency, may further enhance the country's competitiveness in this regard. With lower employee turnover rates and attractive levels of total operating costs, as well as less time zone difference than found for European or Asian outsourcing countries, Brazil can be attractive for real-time services. Brazilian culture and business practices also tend to be more similar to those in the U.S. than may be the case for China, for example.

1. Use the theories of international trade and investment in this module to help explain Brazil's intentions and actions regarding the international information technology sector.

Answers are likely to vary quite a bit on this question. Students may refer to absolute or comparative advantage theories to show why Brazil is a superior site to the USA (absolute advantage), and to other potential offshoring sites (e.g., China, India), based on labor cost, labor quality, and other factors. Students may refer to Porter's diamond model to show how Brazil has developed a cluster that has internationally competitive competencies, enabling it to compete effectively with other sites internationally. Some students might refer to Linder's theory of overlapping demand, arguing that the culture and business practices are similar, but this would probably be an incorrect application of the theory as Linder refers to countries with similar income levels and Brazil and the USA are quite different. Students might use resource endowment theory, arguing that Brazil has an ample supply of talented IT specialists and engineers, helping to compensate for shortages in the USA. Some students might even use the IPLC (International Product Life Cycle) to explain the situation, arguing that advanced IT services often begin in a lead market such as the U.S., get exported from the U.S., and then as skills develop abroad there may be replacement of export market supply from the lower cost foreign sites (displacing U.S. exports of these services) and ultimately replacing these services in the U.S. as well. Strategic behavior theory, for example, might help explain why firms from the U.S. or elsewhere might set up operations to exploit the talented, low cost labor available in Brazil, in order to service U.S. demand in a more cost competitive manner. Dynamic capabilities theory might also suggest that firms might invest in Brazil in order to participate in the development and exploitation of cost competitive centers of excellence in emerging markets such as Brazil. The variety of positions and theoretical perspectives that are likely to be presented can provide the basis for a lively discussion or even debate within the classroom and provide a strong link to the concepts of internationalization of businesses, economic globalization, and offshoring.

2. What recommendations would you give to the Brazilian government and its outsourcing industry in order to improve their prospects for success in building a strong international competitive position in the information technology outsourcing business?

This question can prove to be difficult for some students to answer, and there can be a range of alternative responses. Policy actions might be taken to enhance the absolute advantage of Brazil versus the USA, through continued investment in skilled labor, or encouragement of economies of scale and experience curve benefits, for example. Monetary policy may also be managed so that the Brazilian currency, the real, is kept at a lower valuation and therefore Brazilian labor is quite inexpensive versus U.S. labor, and perhaps versus labor costs in China or India or elsewhere as well. Providing evidence of political and economic stability might also make Brazil a more attractive offshoring location versus other emerging markets. Emphasis on the similarities of culture, business practices, and time zone, among other factors, might also help to encourage potential customers to consider Brazil as a more attractive location for offshoring, versus other locations that may be more geographically or culturally distant.

BONUS ACTIVITIES (additional resources not in the text)

This section provides you with support of your course above and beyond what's found in the text. We have developed these resources to support your course, to support your traditional, hybrid, online, flipped class.

VIDEO SUGGESTIONS

McGraw Hill's collection of international business videos is available on pinterest at <https://pinterest.com/mheibvideos>. The International Trade Theory board is rich and varied, updated monthly, as is the Foreign Direct Investment board. Both represent a great resource.

See <https://www.pinterest.com/pin/387591111656465664/> for a discussion of "will falling euro end up boosting Europe's economy" to discuss how currency fluctuations affect international competitiveness of nations.

The video on "World Bank: Let Africa Trade with Africa" helps to highlight regional trade opportunities as well as potential growth of trade between developing countries (rather than between developing and developed countries); this video can be found at: <https://www.pinterest.com/pin/387591111650417128/>.

The video "How Currency Choices 'Made in China' have Big Impact on U.S. Economy," at <https://www.pinterest.com/pin/387591111650417123/>, helps to highlight currency fluctuations and economic mercantilism.

The video "India Economy to Overtake China but Many Still in Poverty," at <http://www.bbc.com/news/world-asia-india-31668217>, discusses issues of economic growth and social welfare.

MapsofWorld.com has an interesting series of facts and discussion about the history of international business and trade, which you can find at <http://finance.mapsofworld.com/trade/history-international.html>.

GlobalEdge and the Academy of International Business provide links to a number of organizations that offer videos about international business. You can find these links at <https://aib.msu.edu/resources/videodepositories.asp>.

YouTube has many international business-related videos in its collection. For example, you can find a 31:03 minute video on How Beneficial is World Trade at <https://youtu.be/xRJZWfqWcs0?list=PL9E6D9764746EA546>.

TEAM EXERCISES

These may be done individually or in groups or teams, either in or out of class, for later class presentation. Some are also appropriate for hybrid and online courses.

1. Ask the students to check advertisements in *The Wall Street Journal*, the *Financial Times* and *New York Times*, for ads in which investment inducements are offered by foreign governments. Similar ads also appear in *The Economist*, *Business Week*, and *Fortune*. Students can also search the web to find such inducements for various countries. What kinds of inducements are offered? Does your city and state offer foreign firms inducements to invest in your area? How successful have they been in attracting foreign FDI into your state, region, or local area?

2. Students typically understand that products are exported and imported because of their tangible nature and the benefits derived through their consumption are apparent. The import and export of services are more difficult for students to grasp. Have students research this and explain their findings. Have them rank the volume of U.S. services' imports and exports, the countries, and the top 10 types of services involved. Have them do the same for an EU and an Asian country and compare their findings. Then, have them answer the question, "Why export services?"

3. You can check the students' comprehension of trade theory through the following activity:

This is the output of cigars and calculators for countries A and B.

Output/Man/Day

<u>Country:</u>	<u>A</u>	<u>B</u>
Calculators:	6	2
Cigars:	20	10

Country A:

Calculators: $\frac{\$30}{6 \text{ calculators}} = \$5/\text{calculator}$

Cigars: $\frac{\$30}{20 \text{ cigars}} = \$1.50/\text{cigar}$

Country B:

Calculators: $\frac{120 \text{ pesos}}{2} = 60 \text{ pesos/calculator}$

Cigars: $\frac{120 \text{ pesos}}{10} = 12 \text{ pesos/cigar}$

- Would it be advantageous for B and A to trade?
- What would be the range of values within which trading of cigars for calculators would make economic sense? (Answer: 3-1/3 cigars/calculator to 5 cigars/calculator).

c. Total production costs per day are \$30 in A and 120 pesos in B. If the exchange rate is 10 pesos in B = \$1 in A, will trade still place in the same direction as for part a?

Converting to dollars:

<u>Country:</u>	<u>A</u>	<u>B</u>
Calculators:	\$5/Calculator	\$6/calculator
Cigars:	\$1.50/cigar	\$1.20/cigar

d. What change must be made in the exchange rate to change the flow of trade?

Answer:

(1) If rate goes to 12 pesos = \$1, calculator will cost \$5 in B, which is the same price as in A, so based on price alone, B will not import from A. B can still sell cigars to A because their price has improved and gives them a greater price advantage.

(2) If the rate goes to 8 pesos = \$1, then B’s cigars will cost A \$1.50 and B will lose its price advantage. Calculators in B will cost \$7.50 to produce.

e. If rate goes to 8 pesos or even 7 pesos = \$1, will B sell any cigars to A?

Answer:

(1) They probably will if their cigars taste better or are handmade, if A’s are machine made. Cigars, like most products, are not bought purely on the basis of price.

SUPPLEMENTAL ACTIVITIES

Case Studies

Case studies that focus on the internationalization of business and on issues related to the globalization debate are available through Ivey Publishing and Harvard Business School. Ivey’s catalog is available for browsing (www.iveycases.com); the cases are downloadable and pricing is in the U.S. \$3.50 range. Harvard Business Publishing (<https://cb.hbsp.harvard.edu/cbmp/pages/home>) requires an account and offers free review copies for educators. The case prices begin in the \$3.95 to \$6 range.

“Free Trade vs. Protectionism: The Great Corn-Laws Debate” examines the conflict that arose between those advocating free trade and those advocating protectionism in 19th century Britain. The Corn Laws were a series of acts that protected British agricultural interests for nearly 200 years, and the decision on whether to repeal the acts had significant implications for industrialists and landowners. This is a Harvard case. There is also an abridged version available.

“Yue Yuen Industrial (Holdings) Limited: (A) Making 200 Million Pair of Shoes a Year and Growing” describes the industry for outsourcing shoes by companies such as Nike and Adidas.

Yue Yuen has become the largest contract footwear maker in the world, five times larger than its next largest competitor. The case allows students to understand the decisions for offshoring parts of a company's value chain, such as manufacturing, and the challenges that a company faces in not only achieving competitiveness as an offshore supplier but being able to remain competitive as the environment changes over time. This is a University of Hong Kong case distributed by Harvard.

"Background and Agreements on Foreign Direct Investment" provides a brief history of foreign direct investment, including various conflicts, issues associated with FDI-related legal frameworks, and international agreements and principles for resolving FDI-related disputes. It can provide a useful basis for discussing the "whys" and "hows" of FDI. This is a Harvard case.

"Foreign Direct Investment in China" examines the role that FDI has played in China in helping that nation to achieve rapid economic growth since 1978. This is a University of Hong Kong case distributed by Harvard.

CONTROVERSIAL ISSUES

1. Global Debate: The *GLOBAL DEBATE: Comparative Advantage: Should the United States be Sending Service Jobs to India?* Boxed element described earlier in this module's Instructor Guide provides an excellent foundation for debating some of the issues raised in the text.

Online and Hybrid: Virtual teams can be assigned questions and submit their work as a group. Alternatively, virtual teams can be assigned to take different roles or perspectives to argue for (or against) and these assignments can be submitted as a group and then opened up to discussion and debate on an online class discussion site or blog, or presented and debated in a face-to-face setting.

Face-to-Face: Students develop responses to the questions in class in teams/groups, or else assign perspectives and conduct an in-class debate and discussion.

2. Debate on whether trade and investment are beneficial for a country's development

Drawing from the content in the IB in Practice box, "Are Economic and Social Development Affected by Trade and Investment," you can ask students to take opposing perspectives to argue that trade and investment are desirable for the social, cultural and economic development of a country, as well as arguments for why trade and investment may produce undesirable social, cultural and economic outcomes.

Online and Hybrid: Virtual teams can be assigned to take different perspectives to argue for or against international trade and foreign direct investment and these assignments can be submitted as a group and then opened up to discussion and debate on an online class discussion site or blog, or presented and debated in a face-to-face setting.

Face-to-Face: Students can be assigned to take different perspectives to argue for or against international trade and foreign direct investment and then they can be asked to argue their positions within an in-class debate and discussion.

3. Current events for sources of culture controversy

A focus on current events that are relevant to the module's topics is a good way to bring home the concepts, review their application and build news-review habits. Five minutes at the beginning of class is devoted to discussion of current events. Recent relevant current events include the on-going controversy in the U.S. about whether free trade agreements such as NAFTA or the Trans-Pacific Partnership will promote domestic job creation and improved economic prosperity, or whether they send jobs abroad and harm American workers and the overall economy. Depending on the online interface, this activity may be done in chat forums (Blackboard) or discussion boards, before class begins. This activity also works well in large lecture classes. Ask everyone to come prepared with an article for every meeting. If a meaningful percentage of the final grade is allocated to discussion (15-25), motivation is there. All of these opportunities to share applications of course concepts found in current events count towards the participation grade. Call on two people at the beginning of class, with a penalty allocated to non-performers. If there is time at the close of class, open up new discussion for volunteers.

TEACHING SUGGESTIONS

1. Students often are unaware of the rapid growth of international trade, so we discuss Figure 2.1 in class. We point out that there have been numerous changes in trade relationships as Table 2.1 illustrates. Most students believe that the major trade direction is between developed and developing nations (exchanging raw materials for finished goods). Figure 2.2 shows the major trading partners of the United States, which shows that there are several Asian trading partners in addition to the traditional European and NAFTA trade partners among the key export markets for U.S. goods, as well as for imports into the U.S.

2. The material on Theories of International Trade is somewhat difficult for many students and it is easy to lose their interest when discussing theories from the 17th century. We emphasize in class that there are good, practical reasons for knowing the essentials as we have also emphasized in the text. We recommend that you go slowly in discussing comparative advantage. If you whip through it, you will probably lose most of the class. We commonly ask a student to come to the board and create a table to explain the theory and we give him or her all of the help required. We came across a short haiku-like summary of comparative advantage that might help students get the general idea: Do what you do best and trade the rest.

3. We find it advantageous to follow the discussion of comparative advantage with the example in which we introduce money because the students learn quickly about the importance of exchange rates and they are better prepared when we examine the financial markets.

4. Generally students are surprised to learn that the United States' share in total foreign investment is still as large as it is (see Figure 2.5). They often believe that China's share is largest, due to all of the press that China's growth has received and the number of Chinese firms that have entered foreign markets through acquisitions. Do you want to see how many read the assignment? Ask them which country has the largest share of foreign direct investment (answer: the U.S.).

5. The Global Debate box on, "Comparative Advantage: Should the United States be Sending Service Jobs to India?," is generally a good way to generate many different perspectives on globalization, offshoring, and the movement of jobs to foreign locations.

6. We often find it useful to use the International Product Life Cycle, illustrated in Figure 2.3, to stimulate discussion. We ask questions such as, "Can you identify any products or services that have completed the IPLC?" "Can you identify any products or services which are still in the early stages of the IPLC but that you would expect to continue evolving along the lines of this model? Can you explain why you expect this evolution to occur and the implications for business managers?"

7. You may be interested in discussing the IB in Practice box, "Are Economic and Social Development Affected by Trade and Investment?" This illustrates how closely trade and FDI are interlinked with the economic and social development of nations and their people. It helps students to understand how international business practices can have important, and positive, implications for the achievement of social and economic development goals.

8. Guest Lecturer possibilities: Some businesspeople who could contribute to the material in this module would be:

- a. Someone in the technical department of a multinational to talk about licensing and contract manufacturing arrangements that firm has with overseas licensees.
- b. Product manager of the international division of a multinational who should be knowledgeable about licensing and all the means for entering a market. Such a person can also explain why the firm went overseas.
- c. Financial person in the international division who can discuss the points mentioned in questions 1 and 2 plus the ROI obtained from these arrangements.
- d. Representatives from a foreign-owned subsidiary in your area. Ask them to tell the class what motivated their company to come to the United States and your area.
- e. If you have an economic development department in your state that is active in attracting foreign investors, you may be able to get a representative to explain to the class what it does to attract foreign investors and what foreign investors are looking for.

Your chamber of commerce director of economic development may have had visits from foreign company representatives that he or she is willing to share.

f. If you are in an area with foreign consuls, you might invite a member of the consulate to discuss his or her government's policy with respect to trade restrictions and economic development, especially as it affects foreign investment in that country. The representative could also be asked about that government's efforts to promote foreign trade.

CONNECT TOOLS FOR ASSESSEMENT OF LEARNING

Interactive Applications

Assigning Interactives

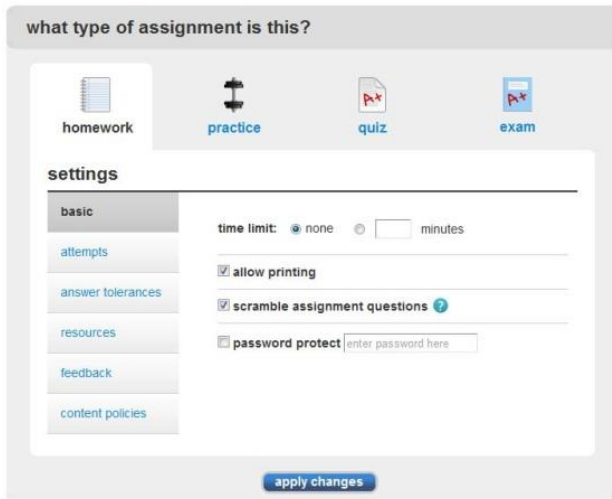
Consider assigning only 2 interactives per chapter. Interactive applications allow students to see concepts in practice and assess higher order thinking skills. There are numerous exercises of different types available. Click'n'drag, video cases, and case analysis are the types you will see most frequently in this program.

Time-Saving Hints:

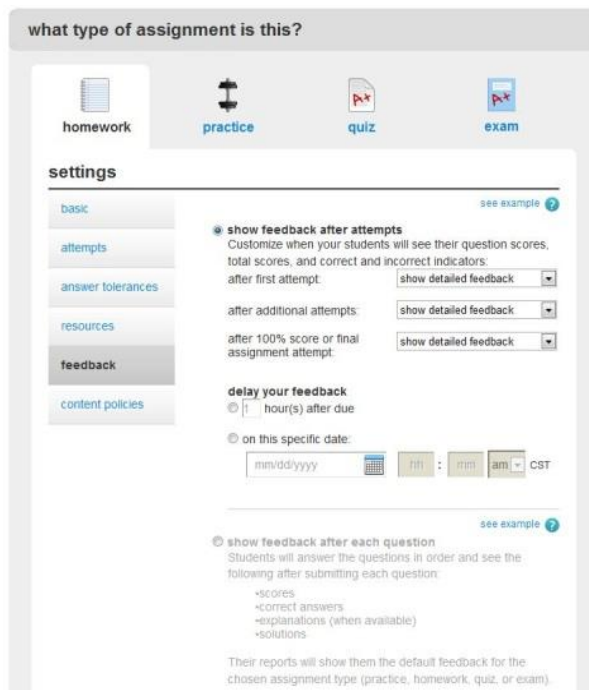
- Instructors may want to give students unlimited or multiple attempts on the first few assignments so the students have a chance to learn and navigate the system before selecting the option for one attempt only.

The screenshot shows a form titled "when is this assignment available and due?". It has two sections. The first section is "available:" with two radio buttons: "now" (selected) and "later". The second section is "due:" with a date input field (mm/dd/yyyy), a calendar icon, a time input field (hh : mm), a dropdown menu for "am", and a dropdown menu for "CST". Below the "due:" section are two radio buttons: "automatically submit *as is* on due date" and "allow for late submittal if the student begins the assignment before it's due". At the bottom, there is a "reduce credit by" field with a value of "0" and a dropdown menu for "hour".

- The value of each question should probably be relatively low, since multiple questions are usually assigned for each chapter. A good rule of thumb would be to make "Quiz Questions" worth 1 point each and "Interactives" worth 5-10 points each since these require more time and thought.



- Feedback given to students is time flexible. Selecting feedback to be displayed after the assignment due date helps to limit students from giving the correct answers to other students while the interactive is still available.



Connect Content Matrix

Instructor Guide to Module 2	<i>International Business</i> Geringer, McNett, Minor, Ball
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For every chapter, please refer to the Connect Content Matrix to see what application exercises are available, what Learning Objectives they help reinforce/assess.

Module	Assignment Type	Title	Topic(s)	Learning Objective(s)	AACSB Accreditation Tagging	Bloom's Taxonomy
2	Comprehension Case	Volume and Direction of International Trade	International Trade	02-01; 02-02; 02-04	Analytical	Remember
2	Drag and Drop	International Trade	Direction of Trade	02-01; 02-02	Reflective thinking	Understand
2	Drag and Drop	International Trade Theories	Explaining Trade: International Trade Theories	02-03	Reflective thinking	Understand
2	Video Case	Trade, Investment, and Economic and Social Development in Ethiopia	Foreign Investment	02-04; 02-05	Analytical	Understand/ Analyze
2	Decision Generator	Exporting, Licensing or FDI	Explaining FDI: Theories of International Investment	02-04; 02-05	Analytical	Apply