

1.5: The Globalization Debate

Learning Objectives

1. Understand the flattening world perspective in the globalization debate.
2. Understand the multidomestic perspective in the globalization debate.
3. Know the dimensions of the CAGE analytical framework.

In today's global economy, everyone is accustomed to buying goods from other countries—electronics from Taiwan, vegetables from Mexico, clothing from China, cars from Korea, and skirts from India. Most modern shoppers take the “Made in [a foreign country]” stickers on their products for granted. Long-distance commerce wasn't always this common, although foreign trade—the movement of goods from one geographic region to another—has been a key factor in human affairs since prehistoric times. Thousands of years ago, merchants transported only the most precious items—silk, gold and other precious metals and jewels, spices, porcelains, and medicines—via ancient, extended land and sea trade routes, including the famed Silk Road through central Asia. Moving goods great distances was simply too hard and costly to waste the effort on ordinary products, although people often carted grain and other foods over shorter distances from farms to market towns. William J. Bernstein, *A Splendid Exchange: How Trade Shaped the World* (New York: Atlantic Monthly Press, 2008).

What is the globalization debate? Well, it's not so much a debate as it is a stark difference of opinion on how the internationalization of businesses is affecting countries' cultural, consumer, and national identities—and whether these changes are desirable. For instance, the ubiquity of such food purveyors as Coca-Cola and McDonald's in practically every country reflects the fact that some consumer tastes are converging, though at the likely expense of local beverages and foods. Remember, globalization refers to the shift toward a more interdependent and integrated global economy. This shift is fueled largely by (1) declining trade and investment barriers and (2) new technologies, such as the Internet. The globalization debate surrounds whether and how fast markets are actually merging together.

We Live in a Flat World

The **flat-world view** is largely credited to Thomas Friedman and his 2005 best seller, *The World Is Flat*. Although the next section provides you with an alternative way of thinking about the world (a **multidomestic view**), it is nonetheless important to understand the flat-world perspective. Friedman covers the world for the *New York Times*, and his access to important local authorities, corporate executives, local *Times* bureaus and researchers, the Internet, and a voice recorder enabled him to compile a huge amount of information. Many people consider globalization a modern phenomenon, but according to Friedman, this is its third stage. The first stage of global development, what Friedman calls “Globalization 1.0,” started with Columbus's discovery of the New World and ran from 1492 to about 1800. Driven by nationalism and religion, this lengthy stage was characterized by how much industrial power countries could produce and apply.

“Globalization 2.0,” from about 1800 to 2000, was disrupted by the Great Depression and both World Wars and was largely shaped by the emerging power of huge, multinational corporations. Globalization 2.0 grew with the European mercantile stock companies as they expanded in search of new markets, cheap labor, and raw materials. It continued with subsequent advances in sea and rail transportation. This period saw the introduction of modern communications and cheaper shipping costs. “Globalization 3.0” began around 2000, with advances in global electronic interconnectivity that allowed individuals to communicate as never before.

In Globalization 1.0, nations dominated global expansion. Globalization 2.0 was driven by the ascension of multinational companies, which pushed global development. In Globalization 3.0, major software advances have allowed an unprecedented number of people worldwide to work together with unlimited potential.

The Mumbai Taxman

What shape will globalization take in the third phase? Friedman asks us to consider the friendly local accountants who do your taxes. They can easily outsource your work via a server to a tax team in Mumbai, India. This increasingly popular outsourcing trend has its benefits. As Friedman notes, in 2003, about 25,000 US tax returns were done in India. Thomas L. Friedman, *The World Is Flat* (New York: Farrar, Straus and Giroux, 2005). By 2004, it was some 100,000 returns, with 400,000 anticipated in 2005. A software program specifically designed to let midsized US tax firms outsource their files enabled this development, giving better job prospects to the 70,000 accounting students who graduate annually in India. At a starting salary of \$100 per month, these accountants are completing US returns and competing with US tax preparers.

Chris C. Got It Wrong?

In 1492, Christopher Columbus set sail for India, going west. He had the Niña, the Pinta, and the Santa María. He never did find India, but he called the people he met “Indians” and came home and reported to his king and queen: “The world is round.” I set off for India 512 years later. I knew just which direction I was going in—I went east. I was in Lufthansa business class, and I came home and reported only to my wife and only in a whisper: “The world is flat.”

And therein lies a tale of technology and geoeconomics that is fundamentally reshaping our lives—much, much more quickly than many people realize. It all happened while we were sleeping, or rather while we were focused on 9/11, the dot-com bust, and Enron—which even prompted some to wonder whether globalization was over. Actually, just the opposite was true, which is why it’s time to wake up and prepare ourselves for this flat world, because others already are, and there is no time to waste. Thomas L. Friedman, “It’s a Flat World, After All,” *New York Times Magazine*, April 3, 2005, accessed June 2, 2010, www.nytimes.com/2005/04/03/magazine/03DOMINANCE.html.

This job competition is not restricted to accountants. Companies can outsource any service or business that can be broken down to its key components and converted to computerized operations. This includes everything from making restaurant reservations to reporting corporate earnings to reading x-rays. And it doesn’t stop at basic services. With the “globalization of innovation,” multinationals in India are filing increasing numbers of US patent applications, ranging from aircraft-engine designs to transportation systems and microprocessor chips. Japanese-speaking Chinese nationals in Dailian, China, now answer call-center questions from Japanese consumers. Due to Dailian’s location near Japan and Korea, as well as its numerous universities, hospitals, and golf courses, some 2,800 Japanese companies outsource operations there. While many companies are outsourcing to other countries, some are using “home sourcing”—allowing people to work at home. JetBlue uses home sourcing for reservation clerks. Today, about 16 percent of the US workforce works from home. In many ways, outsourcing and home sourcing are related; both allow people to work from anywhere.

How the World Got Flat

Friedman identifies ten major events that helped reshape the modern world and make it flat: Thomas L. Friedman, *The World Is Flat* (New York: Farrar, Straus and Giroux, 2005), 48–159.

1. **11/9/89: When the walls came down and the windows went up.** The fall of the Berlin Wall ended old-style communism and planned economies. Capitalism ascended.
2. **8/9/95: When Netscape went public.** Internet browsing and e-mail helped propel the Internet by making it commercially viable and user friendly.
3. **Work-flow software: Let’s do lunch. Have your application talk to my application.** With more powerful, easier-to-use software and improved connectivity, more people can share work. Thus, complex projects with more interdependent parts can be worked on collaboratively from anywhere.
4. **Open-sourcing: Self-organizing, collaborative communities.** Providing basic software online for free gives everyone source code, thus accelerating collaboration and software development.
5. **Outsourcing: Y2K.** The Internet lets firms use employees worldwide and send specific work to the most qualified, cheapest labor, wherever it is. Enter India, with educated and talented people who work at a fraction of US or European wages. Indian technicians and software experts built an international reputation during the Y2K millennium event. The feared computer-system breakdown never happened, but the Indian IT industry began handling e-commerce and related businesses worldwide.
6. **Offshoring: Running with gazelles, eating with lions.** When it comes to jobs leaving and factories being built in cheaper places, people think of China, Malaysia, Thailand, Mexico, Ireland, Brazil, and Vietnam. But going offshore isn’t just moving part of a manufacturing or service process. It means creating a new business model to make more goods for non-US sale, thus increasing US exports.
7. **Supply-chaining: Eating sushi in Arkansas.** Walmart demonstrates that improved acquisition and distribution can lower costs and make suppliers boost quality.
8. **Insourcing: What the guys in funny brown shorts are really doing.** This kind of service collaboration happens when firms devise new service combinations to improve service. Take United Parcel Service (UPS). The “brown” company delivers packages globally, but it also repairs Toshiba computers and organizes delivery routes for Papa John’s pizza. With insourcing, UPS uses its logistics expertise to help clients create new businesses.
9. **Informing: Google, Yahoo!, MSN Web Search.** Google revolutionized information searching. Its users conduct some one billion searches annually. This search methodology and the wide access to knowledge on the Internet transforms information into a commodity people can use to spawn entirely new businesses.

10. **The steroids: Digital, mobile, personal, and virtual.** Technological advances range from wireless communication to processing, resulting in extremely powerful computing capability and transmission. One new Intel chip processes some 11 million instructions per second (MIPS), compared to 60,000 MIPS in 1971.

These ten factors had powerful roles in making the world smaller, but each worked in isolation until, Friedman writes, the convergence of three more powerful forces: (1) new software and increased public familiarity with the Internet, (2) the incorporation of that knowledge into business and personal communication, and (3) the market influx of billions of people from Asia and the former Soviet Union who want to become more prosperous—fast. Converging, these factors generated their own critical mass. The benefits of each event became greater as it merged with another event. Increased global collaboration by talented people without regard to geographic boundaries, language, or time zones created opportunity for billions of people.

Political allegiances are also shifting. While critics say outsourcing costs US jobs, it can also work the other way. When the state of Indiana bid for a new contract to overhaul its employment claims processing system, a computer firm in India won. The company's bid would have saved Indiana \$8 million, but local political forces made the state cancel the contract. In such situations, the line between the exploited and the exploiter becomes blurred.

Corporate nationality is also blurring. Hewlett-Packard (HP) is based in California, but it has employees in 178 countries. HP manufactures parts wherever it's cheapest to do so. Multinationals like HP do what's best for them, not what's best for their home countries. This leads to critical issues about job loss versus the benefits of globalization.

Since the world's flattening can't be stopped, new workers and those facing dislocation should refine their skills and capitalize on new opportunities. One key is to become an expert in a job that can't be delegated offshore. This ranges from local barbers and plumbers to professionals such as surgeons and specialized lawyers.

We Live in a Multidomestic World, Not a Flat One!

International business professor Pankaj Ghemawat takes strong issue with the view that the world is flat and instead espouses a world he characterizes as "semiglobalized" and "multidomestic." If the world were flat, international business and global strategy would be easy. According to Ghemawat, it would be domestic strategy applied to a bigger market. In the semiglobalized world, however, global strategy begins with noticing national differences. Pankaj Ghemawat, "Distance Still Matters," *Harvard Business Review* 79, no. 8 (2001): 137–47.

Ghemawat's research suggests that to study "barriers to cross-border economic activity" you will use a "CAGE" analysis. The **CAGE framework** covers these four factors: Pankaj Ghemawat, "Distance Still Matters," *Harvard Business Review* 79, no. 8 (2001): 137–47.

- **1. Culture.** Generally, cultural differences between two countries reduce their economic exchange. Culture refers to a people's norms, common beliefs, and practices. Cultural distance refers to differences based in language, norms, national or ethnic identity, levels of trust, tolerance, respect for entrepreneurship and social networks, or other country-specific qualities. Some products have a strong national identification, such as the Molson beer company in Canada (see Molson's "I am Canadian" ad campaign). "I Am Canadian," YouTube video, posted by "vinko," May 22, 2006, accessed May 4, 2011, <http://www.youtube.com/watch?v=BRI-A3vakVg>. Conversely, genetically modified foods (GMOs) are commonly accepted in North America but highly disdained in Western Europe. Such cultural distance for GMOs would make it easier to sell GMO corn in the United States but impossible to sell in Germany. Some differences are surprisingly specific (such as the Chinese dislike of dark beverages, which Coca-Cola marketers discovered too late).
- **2. Administration.** Bilateral trade flows show that administratively similar countries trade much more with each other. Administrative distance refers to historical governmental ties, such as those between India and the United Kingdom. This makes sense; they have the same sorts of laws, regulations, institutions, and policies. Membership in the same trading block is also a key similarity. Conversely, the greater the administrative differences between nations, the more difficult the trading relationship—whether at the national or corporate level. It can also refer simply to the level and nature of government involvement in one industry versus another. Farming, for instance, is subsidized in many countries, and this creates similar conditions.
- **3. Geography.** This is perhaps the most obvious difference between countries. You can see that the market for a product in Los Angeles is separated from the market for that same product in Singapore by thousands of miles. Generally, as distance goes up, trade goes down, since distance usually increases the cost of transportation. Geographic differences also include time zones, access to ocean ports, shared borders, topography, and climate. You may recall from the opening case that even Google was affected by geographic distance when it felt the speed of the Internet connection to Google.com was slowed down because the Chinese were accessing server farms in other countries, as none were set up in China (prior to the setup of Google.cn).

- **4. Economics.** Economic distance refers to differences in demographic and socioeconomic conditions. The most obvious economic difference between countries is size (as compared by gross domestic product, or GDP). Another is per capita income. This distance is likely to have the greatest effect when (1) the nature of demand varies with income level, (2) economies of scale are limited, (3) cost differences are significant, (4) the distribution or business systems are different, or (5) organizations have to be highly responsive to their customers' concerns. Disassembling a company's economy reveals other differences, such as labor costs, capital costs, human capital (e.g., education or skills), land value, cheap natural resources, transportation networks, communication infrastructure, and access to capital.

Each of these CAGE dimensions shares the common notion of distance. CAGE differences are likely to matter most when the CAGE distance is great. That is, when CAGE differences are small, there will likely be a greater opportunity to see business being conducted across borders. A CAGE analysis also requires examining an organization's particular industry and products in each of these areas. When looking at culture, consider how culturally sensitive the products are. When looking at administration, consider whether other countries coddle certain industries or support "national champions." When looking at geography, consider whether products will survive in a different climate. When looking at economics, consider such issues as the effect of per capita income on demand.

An Amusing Anecdote

Pankaj Ghemawat provides this anecdote in partial support of his multidomestic (or anti-flat-world) view. "It takes an aroused man to make a chicken affectionate" is probably not the best marketing slogan ever devised. But that's the one Perdue Chicken used to market its fryers in Mexico. Mexicans were nonplussed, to say the least, and probably wondered what was going on in founder Frank Perdue's henhouse. How did the slogan get approved? Simple: it's a literal translation of Perdue's more appetizing North American slogan "It takes a tough man to make a tender chicken." As Perdue discovered, at least through his experience with the literal translation of his company motto into Spanish, cultural and economic globalization have yet to arrive. Consider the market for capital. Some say capital "knows no boundaries." Recent data, however, suggests capital knows its geography quite well and is sticking close to home. For every dollar of capital investment globally, only a dime comes from firms investing "outside their home countries." For every \$100 US investors put in the stock market, they spend \$15 on international stocks. For every one hundred students in Organisation for Economic Co-operation (OECD) universities, perhaps five are foreigners. These and other key measures of internationalization show that the world isn't flat. It's 90 percent round, like a rugby ball. Pankaj Ghemawat, *Redefining Global Strategy: Crossing Borders in a World Where Differences Still Matter* (Boston: Harvard Business School Press, 2007), 42.

While the world may not be flat, it is probably safe to say that it is flattening. We will use the CAGE framework throughout this book to better understand this evolving dynamic.

KEY TAKEAWAYS

- The globalization debate pits the opinions of Thomas Friedman against those of Pankaj Ghemawat. Their differing views help you better understand the context of international business. Through exposure to Friedman's ideas, you gain a better perspective on the forces, or "flatteners," that are making cross-border business more prominent.
- Ghemawat portrays a world that is "semiglobalized" and "multidomestic," where global strategy begins with noticing national differences.
- Ghemawat's CAGE framework covers four factors—culture, administration, geography, and economics.

EXERCISES

(AACSB: Reflective Thinking, Analytical Skills)

1. What are the basic tenets of the flat-world perspective?
2. Why does Ghemawat disagree with the flat-world perspective?
3. What are the four components of the CAGE analytical framework?

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