

14.5: Reading- The Global Economic and Regulatory Environment

The Economic Environment

If you plan to do business in a foreign country, you need to know its level of economic development. You also should be aware of factors influencing the value of its currency and the impact that changes in that value will have on your profits.

Economic Development

If you don't understand a nation's level of economic development, you'll have trouble answering some basic questions, such as, Will consumers in this country be able to afford the product I want to sell? How many units can I expect to sell? Will it be possible to make a reasonable profit? A country's level of economic development can be evaluated by estimating the annual income earned per citizen. The World Bank, which lends money for improvements in underdeveloped nations, divides countries into the following four income categories:

- *High income*—\$12,276 or higher (United States, Germany, Japan)
- *Upper-middle income*—\$3,976 to \$12,275 (China, South Africa, Mexico)
- *Lower-middle income*—\$1,006 to \$3,975 (Vietnam, Philippines, India)
- *Low income*—\$1,005 or less (Kenya, Bangladesh, Haiti)

Note that even though a country has a low annual income per citizen, it can still be an attractive place for doing business. India, for example, is a lower-middle-income country, yet it has a population of a billion, and a segment of that population is well educated—an appealing feature for many business initiatives.

The long-term goal of many countries is to move up the economic development ladder. Some factors conducive to economic growth include a reliable banking system, a strong stock market, and government policies to encourage investment and competition while discouraging corruption. It's also important that a country have a strong *infrastructure*—its systems of communications (telephone, Internet, television, newspapers), transportation (roads, railways, airports), energy (gas and electricity, power plants), and social facilities (schools, hospitals). These basic systems will help countries attract foreign investors, which can be crucial to economic development.

The Legal and Regulatory Environment

One of the more difficult aspects of doing business globally is dealing with vast differences in legal and regulatory environments. The United States, for example, has an established set of laws and regulations that provide direction to businesses operating within its borders. But because there is no global legal system, key areas of business law—for example, contract provisions and copyright protection—can be treated in different ways in different countries. Companies doing international business often face many inconsistent laws and regulations. To navigate this sea of confusion, American businesspeople must know and follow both U.S. laws and regulations and those of nations in which they operate.

Business history is filled with stories about American companies that have stumbled in trying to comply with foreign laws and regulations. Coca-Cola, for example, ran afoul of Italian law when it printed its ingredients list on the bottle cap rather than on the bottle itself. Italian courts ruled that the labeling was inadequate because most people throw the cap away. In another case, 3M applied to the Japanese government to create a joint venture with the Sumitomo Industrial Group to make and distribute magnetic tape products in Japan. 3M spent four years trying to satisfy Japan's complex regulations, but by the time it got approval, domestic competitors, including Sony, had captured the market. By delaying 3M, Japanese regulators managed, in effect, to stifle foreign competition.

One approach to dealing with local laws and regulations is hiring lawyers from the host country who can provide advice on legal issues. Another is working with local businesspeople who have experience in complying with regulations and overcoming bureaucratic obstacles.

Foreign Corrupt Practices Act

One U.S. law that creates unique challenges for American firms operating overseas is the Foreign Corrupt Practices Act, which prohibits the distribution of bribes and other favors in the conduct of business. Unfortunately, though they're illegal in this country, such tactics as kickbacks and bribes are business-as-usual in many nations. According to some experts, American businesspeople are at a competitive disadvantage if they're prohibited from giving bribes or undercover payments to foreign officials or

businesspeople who expect them; it's like asking for good service in a restaurant when the waiter knows you won't be giving a tip. In theory, because the Foreign Corrupt Practices Act warns foreigners that Americans can't give bribes, they'll eventually stop expecting them.

Where are American businesspeople most likely and least likely to encounter bribe requests and related forms of corruption? Transparency International, an independent German-based organization, annually rates nations according to "perceived corruption," which it defines as "the abuse of public office for private gain." Table 14.5.1, "Corruptibility Around the World, 2010," reports a sampling of the 2010 rankings.

Table 14.5.1. Corruptibility Around the World, 2010

Rank	Country	CPI Score*
1	Denmark	9.3
1	New Zealand	9.3
1	Singapore	9.3
4	Finland	9.2
4	Sweden	9.2
6	Canada	8.9
15	Germany	7.9
17	Japan	7.8
20	United Kingdom	7.6
22	United States	7.1
98	Mexico	3.1
175	Iraq	1.6
176	Afghanistan	1.4
178	Somalia	1.1

*A score of 10 means that a country is squeaky clean. Anything under 3 means that corruption is rampant.

Source: "Corruption Perceptions Index 2010 Results," Transparency International, Corruption Perceptions Index 2010 Results, www.transparency.org/policy_research/surveys_indices/cpi/2010/results (accessed September 20, 2011).

KEY TAKEAWAYS

- Success in international business means understanding an assortment of cultural, economic, and legal differences between countries.
- Cultural challenges stem from differences in language, concepts of time and sociability, and communication styles.
- If you do business in a foreign country, you need to know the country's level of economic development.
- In dealing with countries whose currency is different from yours, you have to be aware of the impact that fluctuations in **exchange rates** will have on your profits.
- Finally, in doing business globally, you must deal with the challenges that come from the vast differences in legal and regulatory environments.

Check Your Understanding

Answer the question(s) below to see how well you understand the topics covered in this section. This short quiz does **not** count toward your grade in the class, and you can retake it an unlimited number of times.

Use this quiz to check your understanding and decide whether to (1) study the previous section further or (2) move on to the next section.

<https://assessments.lumenlearning.com/assessments/164>

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