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# UNIT 5 GLOBALIZATION: AN OVERVIEW

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## 5.0 OBJECTIVES

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After studying this unit, you should be able to:

- describe the concept of globalization
- discuss the major forces of globalization
- explain the effects of globalization on the world economy
- describe the Indian perspective of globalization
- analyse the approaches to globalization at the firm/corporate level
- discuss the scenario of cross-border mergers and acquisition
- describe the concept of glocalization.

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## 5.1 INTRODUCTION

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In the 1980s, a new catchword entered international business and nation states' policy objectives. This word, Globalization, refers to a number of changes in the world economy, such as increased international mobility of capital and growing incidence of mergers and acquisition and strategic alliances in firms not only within the country but also across the borders. Further, this is reinforced with expansion of trade and its relationship to the Gross Domestic Product (GDP). Technological revolutions especially in communication have abetted the intensification of globalization. In this Unit, you will learn the major forces of globalization, the effects of globalization on the world economy, the Indian perspectives of globalization and various approaches to globalization. You will also be acquainted with the scenario of cross-border mergers and acquisition and the concept of glocalization.

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## 5.2 WHAT IS GLOBALIZATION?

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Globalization is the process by which an activity or undertaking becomes worldwide in scope. It refers to the absence of borders and barriers to trade between nations. Globaliza-

tion is defined as increased permeability of traditional boundaries of almost every kind, including physical borders such as time and space, nation states and economies, industries and organisations and less tangible borders such as cultural norms. As a consequence of increased global operation, the global economy is becoming more integrated than ever before. This gradual integration leads to the emergence of global village.

UNCTAD defines globalization at the macro level as follows : "The concept of globalization refers to both an increasing flow of goods and services and resources across national borders and to the emergence of complementary set of organisational structure to manage expanding network of international economic activity and transaction. Strictly speaking, a global economy is one where firm and financial institutions operate transnationally, i.e., beyond the confines of national boundaries. In such a world of goods, factors of production and financial assets would be almost perfectly substitutes everywhere and it would no longer be possible to consider nation states as distinct economic identities with autonomous decision making power in the pursuit of national objectives. The public goods that are needed to maintain an open market system, such as secure property rights and stable monetary system would become a global responsibility"

However, The World economy has not reached this level. Although, the nation state is having less control as the forces regulating trade, finance and technology, it has still not given way to a new set of institutions with global responsibility. Hence, the current situation is termed by some as 'global interdependence'.

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## 5.3 MAJOR FORCES OF GLOBALIZATION

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Globalization is not a new phenomenon either at the firm level or at the national/world economy level. Around 1880, the process of globalization of the economy and the firm began. This was the recognition of comparative advantage. Many firms went global. They included Ford, Singer, Gillette, National Cash Register, Otis and Western Electronics. This was because of enjoyment of scale of economies due to the advancement of technology. In the interwar period, the thrust of globalization declined. But the post war period witnessed once again tremendous growth of globalization. Let us learn some of the important forces of globalizations.

### 5.3.1 International Trade and Globalization

International trade has grown substantially over the years. The growth experienced is in the range of 4-10 per cent per annum. In fact, international trade has grown more faster than the world economy in recent years. For developing countries, trade is the primary vehicle for realizing the benefits of globalization. Growing trade has contributed to the ongoing shift of some manufacturing and service activities from industrial to developing countries, which further accelerates the process of globalization. The creation of World Trade Organization in 1995 is another step toward creating an environment conducive to the exchange of goods and services. Another significant and more important indicator of globalization is the rate of growth of Gross Domestic Product (GDP) of the world. The world merchandise trade and the world GDP have been steadily growing since 1990. The rate of growth in merchandise exports is faster than the rate of growth in the world GDP. Look at Table 5.1 which shows that world merchandise exports and world GDP have been steadily growing till the year 1997. The world merchandise trade has been also growing faster than the world merchandise production.. Of course, world merchandise trade, world merchandise production and world GDP have decelerated sharply in the year 1998 due to oil crisis, fall in prices of international trade of goods and services and several other factors.

Trade expansion does not confine to merchandise trade alone. Even international trade in services has grown tremendously. Trade in commercial services continued to be stronger than the merchandise trade throughout the entire 1990-1998 period.

The world merchandise exports, world merchandise production, world GDP and international trade in services have witness substantial growth as a result of the globalization.

**Table 5.1: Growth in the Volume of World Merchandise Exports, Production and GDP**

**Annual Percentage Change**

| Year    | World Merchandise Trade | World Merchandise Production | World GDP |
|---------|-------------------------|------------------------------|-----------|
| 1990-98 | 6.5                     | 2.0                          | 2.0       |
| 1996    | 6.0                     | 3.0                          | 3.0       |
| 1997    | 10.5                    | 4.5                          | 3.0       |
| 1998    | 4.0                     | 1.5                          | 2.0       |

Source: WTO Annual Report, 1999.

### 5.3.2 International Capital Flows

Apart from expansion of international trade, the massive capital flows among countries has further strengthened globalization of capital by a large number of countries. The catalyst for globalization in the late eighties and nineties is not international trade, but cross border international finance flows. World inflow and outflow of FDI have been growing significantly. The inflow of FDI has increased from 359 billion dollar in the year 1996 to 644 billion dollars in the year 1998. Likewise the outflow of FDI has also increased from 380 billion dollar to 649 billion dollar. These levels were reached despite the unfavourable conditions in the world economy. FDI flows grew in 1998 by 39% in case of inflows and 37% in case of outflows. This is the highest growth rate attained in FDI since 1987.

On an average, virtually all of the increase in FDI in the year 1998 was concentrated in developed countries, FDI inflows to and outflows from developed countries reached new heights of 460 billion dollar and 595 billion dollar. In case of developing countries, FDI inflows decreased slightly from 173 billion dollar in 1997 to 166 billion dollar in the year 1998. Most of the FDI is located in the developed world. Although the share of developing countries had been growing steadily until the year 1997, when it reached to 37%. It subsequently declined to 28% in the year 1998 due to the strong performance of the developed countries. The flows to the economies in transition of Central and Eastern Europe remained almost stable. The continuous growth in FDI will further accelerate the process of globalization. Look at Table 5.2 which shows the world FDI inflows and outflows.

**Table 5.2: World FDI Inflows and Outflows**

**Billion dollars**

| Year | Inflows | Outflows |
|------|---------|----------|
| 1996 | 359     | 380      |
| 1997 | 464     | 475      |
| 1998 | 644     | 649      |

Source: World Investment Report, 1999.

### 5.3.3 Globalization and Technology

Technological revolutions in transport and communications over the last three centuries have integrated the world economy. The advances of technology in transport and communication have also brought peoples of the world nearer.

The revolution of technology that has taken place in transport, communication and information is of qualitative difference during the last ten years from that of previous generation of technology. It is not only integrating but also bringing into existence a common culture,

common political system etc. It has also led experts like Ohame think that there is not concept of national consumer. Consumer preference can be global and regional.

Technological revolution has been rapidly transforming all productive systems and facilitating the process of globalizations. Technology has become one of the most important element of the competitiveness. In modern production activities, competitiveness entails new, more rapid product innovation, flexible response, greater networking and closely integrated production systems across firms and regions. The leaders of technological change are evolving new strategies in response. Apart from investing heavily in innovation they are moving their technological assets around the world to match them to immobile factors, entering new alliances and reorganising production relations. This has further facilitated the process of globalization.

At the corporate level also technology is getting globalized. This is at two levels. First, technology is being sold in the world market. Although the market of technology is governed by slightly different rules such as relative importance of information, a few sellers and large number of buyers leading to oligopolistic market structure, the market for technology is vibrant. Consequently many countries derive benefits from this. For instance, the US earns substantially from technology trade. The mechanisms of technology sale are outright purchases and technology collaboration agreements. There has been substantial increase in technology collaboration over the last two decades. Second, the globalization of technology is also taking place in establishment of R & D centres. A large number of TNCs are establishing their R & D in various countries thus globalizing their R & D operations.

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## **5.4 EFFECTS OF GLOBALIZATION ON THE WORLD ECONOMY**

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The impact of this level of globalization has undoubtedly led to economic growth.

In specific terms, the effect of globalization are as follows:

- i) The major effect of globalization is that the global economy is becoming more integrated day by day.
- ii) The volume of world trade has grown at a faster rate than the volume of world output.
- iii) There has been a trend of lowering the barriers to the free flow of goods, services and capital among countries.
- iv) Foreign direct investment has been playing an important role in the global economy. In order to become competitive, company have started investing in overseas operations.
- v) Global operations have led to the emergence of Multilateral Trading Systems.
- vi) Imports are penetrating deeper into the world's largest economies as well.
- vii) The growth of world trade, foreign direct investment and imports leads to more foreign competition in the domestic markets.
- viii) In order to compete with the foreign players, domestic firms are required to enhance the production and distribution capabilities.
- ix) companies have started looking the world as a market for their products.
- x) Companies have started dispersing their manufacturing, marketing and research facilities around the globe where cost and skill conditions are most favourable.
- xi) Opportunities have been increasing for the firms.
- xii) Innovations have started spreading faster.

1) What is globalization?

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2) Enumerate three forces of globalization.

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3) Enumerate three effects of globalization on the world economy

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4) State whether following statements are **True** or **False**.

- i) World GDP has grown at the faster rate than the world merchandise trade.
- ii) Trade in commercial services continued to be stronger than the merchandise trade throughout the year 1990-1998.
- iii) World inflow and outflow of FDI have been growing significantly.
- iv) The leaders of technological change are not moving their technological assets around the world.
- v) There has been a trend of lowering the barriers to the free flow of goods, services and capital.

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## 5.5 GLOBALIZATION AT THE FIRM/CORPORATE LEVEL

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From the point of view of international business globalization of the firm is very important. There have been a number of approaches to globalization of the firm. A few important approaches are discussed below:

1. The term globalization was first used by Professor Theodore Levitt of Harvard Business School. Globalization according to him was referred to as an alleged consequence of markets in the world.

Globalization in Levitt's view is the emergence of global markets for standardized consumer products enabling a firm to benefit from enormous economics of scale in production, distribution, marketing and management. The impact of technology would be toward further standardization. According to Levitt a successful globalized corporation does not abjure customerization or differentiation and for the requirements of markets that differ in product preferences, spending patterns and

shopping preferences. Global Corporations accept these differences only reluctantly. For instance, Ford, the US car maker has at several points in history tried to launch a world car.

2. In the Japanese view as presented by Ohame Kenichi Globalization is understood as a 'business chain'. A business chain comprises a firm's main activities such as Research and Development, engineering, manufacturing, marketing and sales and services. He distinguishes five steps in globalization of a firm. Each of these steps involves the transfer of activities in the business chain to a foreign location. It is in reference to development in the 1980s. Since 1980s had been dominated by unprecedented flows of foreign direct investment as has been seen, mergers and acquisitions and strategic alliances as well as by ever-fiercer competition from Japanese and South East Asian firm.; Ohame argued that these developments would constitute a new era in international business. Companies and customers horizons would stretch, 'beyond national borders', they would become global citizens.
  - a) **Export:** The entire range of activities is performed at home. Exports are often handled by an exclusive local distributor.
  - b) **Direct Sales and Marketing:** If the product is accepted in the overseas market, it will lead to establishment of an overseas sales campaign to provide better marketing, sales and service & functions to the customers.
  - c) **Direct Production :** This step involves the establishment of local production activities.
  - d) **Full Autonomy :** All activities of the business chain as mentioned above are transformed to the key national markets.
  - e) **Global Integration :** In the ultimate stage of globalization, according to Ohame, companies conduct their R & D and finance their cash requirements on a worldwide scale and recruit their personnel from all over the world.
3. Globalization is also presented in management centred concepts especially of Japanese firms (i) Management Centred around the head office; (ii) Management delegated to overseas operating units (iii) Management centering overseas operating units with regional coordination; and (iv) Management with a global perspective and conscious integration of total system and sub-system.
4. The fourth globalization strategy that of a global supplies, is one of export centred global expansion. All systems such as R & D, procurement, sales, marketing, distribution and the organizational structure are designed so as to enhance export of products manufactured in the home country in such an operation.

This process consists of four stages: (i) creation of a global vision, (ii) integration of overseas organization and establishment of multiple corporate headquarters; (iii) promotion of a global hybridization process; and (iv) globalization of personnel administration and the cultivation of entrepreneurial middle management.
5. **Porter's View of Globalization:** An industry can be defined as global if there is some competitive advantage to integrating activities on a worldwide basis. To diagnose the sources of competitive advantage in any context, domestic or global, it is necessary to adopt a disaggregated view of the firm which Porter calls 'Value Chain'. "Every firm is a collection of discrete activities performed to do business in its industry", which he calls 'value activities'. The activities performed by a firm include such things as sales people selling the product, service technicians performing repairs, scientists in the laboratory designing products, processes or accountants keeping books. These functions are technical and physically distinct. The firm's value chain resides in a larger stream of activities termed as value system. Suppliers have value chains that provide the purchased inputs to the firm's chain, buyer's have value chains in which the firm's product or service is employed, channels have value chains through which the firms's product or service passes. The connections among these activities become essential to competitive advantage. Value chain concept needs the notion of competitive scope. Competitive scope is the breadth of

activities the firm performs in competing in an industry. There are four basic dimensions of competitive scope. They include: Segment scope, industry scope, vertical scope and geographic scope. **Segment scope** refers to the range of scope the firm serves, for example product varieties, customers types, etc. **Industry scope** refers to the range of related industries the firm competes in with a coordinated strategy. **Vertical scope** refers to the activities that are performed by the firm versus suppliers and channels. **The geographic scope** refers to the geographic regions in which the firm operates with coordinated strategy. Competitive scope is vital for competitive advantage. It shapes the configuration of the value chain how activities are performed and whether activities are shared among units. International strategy is an issue of geographic scope. A firm that competes internationally must decide how to spread the activities in the value chain among countries. The distinctive issues in international, as contrasted to domestic, strategy can be summarized in two key dimensions of how a firm competes internationally. Porter calls the first the configuration of a firms' activities worldwide, or the location in the world where each activity in the value chain is performed including how many places. The second dimension is called by Porter 'coordination' which refers to how liked activities performed in different countries are coordinated with each other.

Industries globalize when the benefits of configuration and/or coordination globally exceed the costs of doing so. The way in which an industry globalizes reflects the specific benefits and costs of global configuration and/or coordination of each value activity. Further, in global competition, a country must be viewed as a platform and not as the place where all activities of a firm are performed.

6. Michael Taylor and Nigel Thrift considered that the emerging global corporation was the result of the complex process of interlocking between the relatively autonomous development sequences of subsidiaries, branches and affiliates. These firms grow into complex international economic network.
7. Globalization: A Macro-Fordist view: This approach has been developed by Wisse Dekker, former president of Philips who calls it "transnationalization of business". Dekker defines globalization as a relatively early stage in the internationalization of the firm. According to him transnationalization takes place in the following steps.
  - The local enterprise produces and sells in one and the same country.
  - The international enterprise still produces entirely or predominantly in the parent country but establishes sales in foreign markets. International firms are characterized by a strong central organisation.
  - The global enterprise is transferring part of its production process abroad - often limited to assembling - to circumvent input barriers or because of transportation costs;
  - Multinational enterprise has complete production facilities, sometimes even R & D in a host of countries. The MNC often has a federal structure, a network organisation in which synergy plays an important role. Production in many cases is no longer local for local.

W. Rugrook and Rob Van Tulder in his book the Logic of International Restructuring has given the following elaboration of globalization.

#### *Elaboration of Globalization*

Have based Industrial Complex  
United States United Kingdom &  
The Netherlands Examples: Ford,  
General Motors, IBM, BP Exim,  
British Telecom, GEC, Royal Dutch,  
Shell, Unilever, Philips

- Division of labour in world region and between world region between core firms and suppliers.
- Sizable reimportation into home base from other regions.
- Primarily biregional (USA and EU). Some times partly retreat strategy and/or regional configuration
- Shift of some decision making centres

Larger European Economies  
Examples: Siemens, Daimler, Benz, Volkswagen, Fiat, Renault, Vebe, Aciuntaine, IRI, ENI Olivetti, Alacatel, Alsthom

Small European Economies  
Examples: ABB, Volvo, Saab, Svania, Nokia, Electrics, Ciba Geigy, Heineken

South Korea  
Examples: Samsung, Hyundai, Lucky Goldstar, Sunkyong

Japan  
Examples: Toyota, Nissan, NEC, Hitachi, Mitsubishi

(functional and product line) to other triad region is possible.

- Considerable internationalization of stock and capital provision over Triad region.
- Expansion mostly via acquisition and/or greenfield investment.
- Intended internationalization of production and marketing more than 50 per cent in home Triad region (USA, European Union, Japan), 15 per cent second and third Triad regions and 15 per cent in development areas.
- Regional division of labour within Europe Eastern Europe as the low end market.
- reimportation within own region/industrial complex.
- Build up European stronghold, concentrated production for integrated market, export strategy.
- Shift of some decision making centres within the European region.
- Inclined to enter into international strategic alliances (but as the strongest partner)
- Regional concentration of stock and capital provision
- FDI object also via mergers and/or acquisition
- Multi-domestic presence
- Limited international division of labour
- Seeking local player status over the world
- Shift of headquarters is possible
- Less inclined through sometimes forced into alliances
- Sizable internationalization of stock and capital provision
- Expansion also via mergers and acquisitions.
- Triad from screw driving to globalization strategy
- Limited international division of labour, limited reimportation into home country.
- Pax Nipponica succeeds Pax Americana: Pacific Asia under Japanese leadership both market and low end of production.
- No shift of decision making centres to other countries and regions
- Less inclined to strategic alliances and acquisitions; going it alone
- Low internationalization of stock and capital provisions
- FDI object primarily Green Field investment.

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## 5.6 CROSS BORDER MERGERS AND ACQUISITIONS

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The process of globalization of the economy has been strengthened at the global economy and firms level as the phenomenon of cross border mergers and acquisition. These affect the foreign direct investment flows, the World economy and competition.

Merger and acquisitions are a popular mode of investment for firms wishing to project, consolidate and advance their global competition position by selling off divisions that fall outside the scope of their core competence and acquiring strategic assets that enhance their competitions. For these firms, the 'ownership' assets acquired from another firm, such as technical competence, established brand names and existing supplier networks and distribution systems can be put to invertable use towards better serving global customers, enhancing projects, expanding market share and increasing corporate competitiveness by employing international production networks more efficiently.

For the past several years, cross border merger and acquisitions world wide have increased significantly. The absolute value of all cross border M & A sales and purchases amounted to \$544 billion in the year 1998 representing an increase of about 60% over the year 1997. The amount was \$342 billion in the year 1997. Cross-border M & A are primarily concentrated in developed countries, but there is also a trend towards on increase in such deals in some developing countries. In the year 1998, there were 89 mega cross-border M & A deals, each with more than \$1 billion value. These mega deals accounted for nearly three-fifths of the total all cross-border M & A in the year 1998. Recent cross-border M & A have been concentrated in industries that are losing comparative advantages. In the year 1998, the industry that recorded the largest cross-border M & As include: oil industry , automobile industry, banking and telecommunication industry and non-petroleum mining and refining industries.

## 5.7 INDIAN PERSPECTIVES

India was not completely a closed economy although international transactions were not quantitatively important till 1990 for the Indian economy either in trade or finance. But since 1990, India has deliberately pursued a policy which will enhance the role of international transactions in trade, finance and technology. Thus one can say that India has also entered the globalization process in a significant manner.

The reasons for India to take recourse to this policy options have been many. A few major factors can be highlighted. First, India went into serious difficulties in the late eighties with regard to its balance of payments. Second, traditional flows of capital such as aid had declined. Third, to meet the balance of payments crisis India had to borrow from the International Monetary Fund under Standby Credit Arrangement. The conditionality that is part of this arrangement made India liberalize trade and foreign direct investment policies. Finally, the appreciation of the fact that India cannot stand alone in the face of a fierce globalization that is taking place made the policy makers pursue policies which could strengthen its international transaction of the Indian economy. Look at Tables 5.3 and 5.4 on foreign trade and foreign investment flows which give evidence to India's efforts to globalize its economy.

**Table 5.3 Foreign Trade of India**

| Years   | Exports | Imports |
|---------|---------|---------|
| 1990-91 | 6.2     | 9.4     |
| 1993-94 | 8.3     | 9.8     |
| 1994-95 | 8.4     | 11.2    |
| 1995-96 | 9.2     | 12.4    |
| 1996-97 | 8.9     | 12.8    |
| 1997-98 | 8.8     | 12.6    |
| 1998-99 | 8.2     | 11.3    |

Source: Ministry of Finance, Government of India, Economic Survey 1999-2000.

Table 5.4 Foreign Investment Flow into India

(US million dollar)

| Year    | Direct Investment | Portfolio Investment | Total |
|---------|-------------------|----------------------|-------|
| 1992-93 | 315               | 244                  | 559   |
| 1993-94 | 586               | 3567                 | 4153  |
| 1994-95 | 1314              | 3824                 | 5138  |
| 1995-96 | 2144              | 2748                 | 4892  |
| 1996-97 | 2821              | 3312                 | 6133  |
| 1997-98 | 3557              | 1828                 | 5385  |
| 1998-99 | 2462              | -61                  | 2401  |

Source: Ministry of Finance, Government of India, Economic Survey, 1999-2000.

## 5.8 GLOCALIZATION

The alternative to the Globalization strategy is dubbed as 'Glocalization'. The objective of glocalization is to establish a geographically concentrated inter-firm division of labour in the three major bonding blocks. Manufacturers strive to build their competitive advantage in a combination of vertical de-integration of production to local supplies and sub-contractors, and structural control over local suppliers, dealers, workers, and governments. As glocalization aims to establish production within the major markets international trade may decline. Glocalisation pertains to a company's attempt to become accepted as a local citizen in a different trade bloc.

Glocalization also leads to the concept of global firms meaning that large firms cease to be national firms. Therefore, they can be treated as stateless Corporations. It is argued that time has not yet arrived to think of global firms. This is for a number of reasons.

- (a) Even the large multinational corporations are still tied to a parent country
- (b) The ownership and control of the firm is still retained by the parent firm. The subsidiaries profit accrue to the parents
- (c) There are very few non-nationals on the boards of parent company
- (d) The legal nationality of the parent firm is still the nation state where it is registered
- (e) In most cases technological activities are concentrated in the parent company.

### Check Your Progress B

- 1) What is value chain?

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- 2) What do you mean by cross-border mergers and acquisition?

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3) What is glocalization?

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4) State whether following statements are **True** or **False**.

- i) India has not entered in the globalization process in a significant manner.
- ii) According to porter an industry can be defined as global if there is some competitive advantage to integrating activities on a worldwide basis.
- iii) According to Levitt's view, globalization is understood as a business chain.
- iv) For the past several years, cross-border merger and acquisitions worldwide have increased significantly.
- v) The objective of glocalization is to establish a geographically concentrated inter-firm division of labour in the three major bonding blocks.

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## 5.9 LET US SUM UP

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Since the eighties there has been growing trend towards globalization of the economies. However this is only a continuation of historical tendencies. The main indicators of globalization of the world economy is increasing growth of international trade. The rate of growth of international trade is higher than the growth of GDP. Deregulation of finances by countries has led to massive movement of capital among countries further strengthening the globalization process. Technological and communication revolution have provided further impetus to the globalization process. There are compulsions for large firms to globalize. There are a number of approaches to the globalization process of firms/industry. India has also entered the globalization process in the nineties. International trade as proportion of its GDP is steadily increasing. Policy towards foreign direct investment is liberalized. There is increased flow of FDI as well as FII's into India.

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## 5.10 KEYWORDS

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**Triad** — It refers to the three major industrial countries/regions: USA, European Community and Japan

**Greenfield Investment** — Investment in new ventures as opposed to acquisition.

**Global Firm** — Firms having no nationality attachment. Ownership, control and R & D are globally spread.

**Macro Level** — Any activity which cores the economy as a whole is referred to as macro level activity.

**Micro Level** — Aspects affecting the firm/industry is called micro level.

**Cross-border Activities** — Activities that transcend or cross the national frontiers are called cross border transaction.

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## 5.11 ANSWERS TO CHECK YOUR PROGRESS

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- A4    i) False    ii) True    iii) True    iv) False    v) True
- B4    i) False    ii) True    iii) False    iv) True    v) True

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## 5.12 TERMINAL QUESTIONS

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- 1) What do you mean by globalization? Describe various forces of globalization.
- 2) Do you think that the effects of globalization have been favourable on the world economy. Discuss.
- 3) Explain the Indian scenario of globalization. Do you think that India has entered into the globalization process significantly.
- 4) Describe various approaches of globalization with suitable examples.
- 5) Write notes on:
  - i) Cross-border Mergers and Acquisition
  - ii) Glocalization
  - iii) Porter's view of Globalization