Ministry of Education and Science of Ukraine
Sumy State University
Academic and Research Institute
of Business Technologies “UAB”

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INTERNATIONAL CORPORATIONS

Lecture notes

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INTERNATIONAL CORPORATIONS

Lecture notes

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Introduction

The purpose of the course “International Corporations” is to give students the relevant knowledge about the global expansion of the international corporations.

The main tasks of the course are:

- to provide essential knowledge in the field of the key differences among firms, companies, enterprises and corporations;
- to provide basic knowledge on economic performance of the international corporations;
- to address introductory remarks dealing with the international mergers and acquisitions;
- to make students apply relevant knowledge in the global economic environment.

After successful completion of the course the students **will be able to gain knowledge in**:

- elementary understanding of international corporations’ structure;
- understanding of the challenges for international big business;
- deep understanding of multinational investment activity;
- understanding of “too big to fail” corporations;
- positive and negative sides of exporting and importing;
- international corporate rankings;
- why corporations prefer to go global;

- how to distinguish between multinational and transnational corporations;
- how to dissect mergers and acquisitions;
- how to compare corporations and countries.

After successful completion of the course the students **will be able**:

- to classify international corporations;
- to define multinational, transnational and global corporations;
- to discuss the glocalization approach to the international business;
- to identify the stages of going global;
- to recognize key stages of successful global expansion;
- to relate advantages and disadvantages of FDI for host country;
- to explain how multinationals contribute to home country economy;
- to rank corporations by revenue approach;
- to detect the reasons for business combinations;
- to classify international cartels;
- to give examples of holding companies;
- to indicate hostile takeover methods;
- to describe M&A waves;
- to review M&A deals in the global economy.

CHAPTER 1. CLASSIFICATION OF INTERNATIONAL CORPORATIONS

1.1. Export- and Import-Oriented Corporations.
1.2. Multinational Corporations.
1.3. Transnational Corporations.
1.4. Global Corporations.

Key words: importing, exporting, multinationals, transnational corporation, global corporation, glocalization.

1.1. Export- and Import-Oriented Corporations

Corporations are one of the business forms a legal entity can take. International business can go under the name of different legal entities due to the various forms of legal organizations (Fig.1.1).

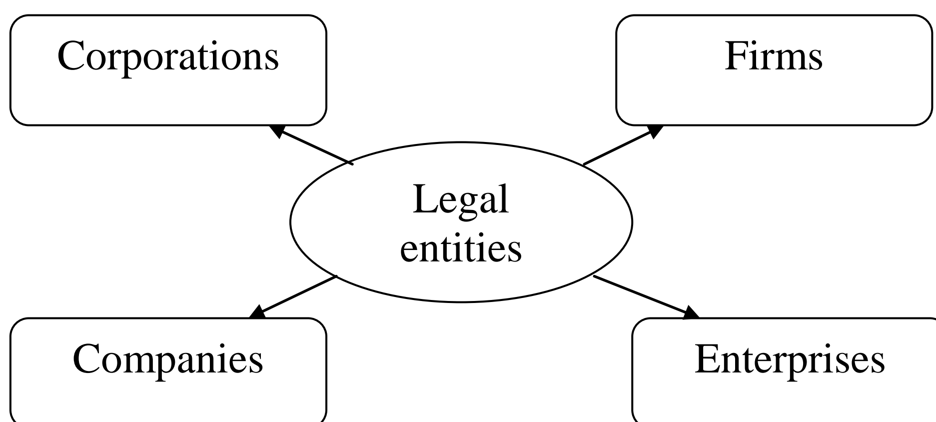

Figure 1.1 – Various forms of legal organizations

A **firm** is usually said of professional businesses such as law firms, consulting firms, architectural firms, investment

firms, etc [9]. Firm is a business concern, especially one involving a partnership of two or more people. When to use the term: in North America, business professionals – such as lawyers, accountants and investment executives – often identify their organizations as firms.

An enterprise is any endeavor including a group of people and resources to achieve a specific goal [9]. When to use the term: it could be a business enterprise, a non-profit enterprise, a government enterprise, etc.

A company is a legally incorporated entity with the purpose of conducting business [9]. When to use the term: it should be used in the context of normal, registered "limited liability" companies. A limited company is one whose owners are legally responsible for only a part of any money that it may owe if it goes bankrupt. Many retail organizations are described as companies. It is still, however, used interchangeably with corporation.

A corporation is a large company or group of companies authorized to act as a single entity and recognized as such in law [14]. When to use the term: in American English the word corporation is most often used to describe large business corporations.

The corporation is an organization engaged in mobilizing resources for productive uses in order to create wealth and other benefits for its multiple constituents, or **stakeholders** [30]. Corporate sector of economy is represented by stakeholders, or shareholders. A company's shares are the many parts into which

its ownership is divided. Shares are bought by shareholders and kept as investments. The stakeholders in a corporation are the individuals that contribute to its wealth creating capacity and activities, and that are therefore its potential beneficiaries and/or risk bearers. The fundamental idea is that stakeholders have a stake in the operation of the firm. Stakeholders share a common risk, a possibility of gaining benefits or experiencing losses or harms as a result of corporate operations. Their common desire is that the corporation should be run in such a way as to make them better off [43]. The stakeholders care about international business in the first place.

All international corporations can be divided into four groups:

- export-oriented (exporters) and import-oriented corporations (importers);
- multinational corporations;
- transnational corporations;
- global corporations.

A major part of international business is, of course, importing and exporting. **Exporters** and **importers** are engaged into international trade only and have no investments outside of their home country. An importer sells products and services that are sourced from other countries; an exporter, in contrast, sells products and services in foreign countries that are sourced from its home country. Example: XEROX.

International business is the core theme in conducting business in current era of globalization. In the competitive

environment, businesses are competing at global level. In international business a company can engage in either of the two ways such as import or export. Import and export are the two basic and primary ways of conducting the business. Whenever a company engages into the international business, there are lot many factors which impact the business. Hence there are advantages and disadvantages of both import and export.

The **advantages** of the **export-oriented business** are as follows [1]:

1. Through export, corporations can establish their business worldwide.

2. Export increases sales, income, market share, and profit.

3. Export business generates employment opportunities.

4. Export enriches domestic competitiveness.

5. It develops communication between two or more countries.

6. It enhances economic status of the country.

7. Corporations must produce high qualitative goods in order to be competitive on the global arena.

There are also risks in relying on the export option. The **challenges** of the **export-oriented business** are as follows [1]:

1. Corporations need basic investment to start export business.

2. Finding the importer from abroad is difficult and takes much time.

3. Obtaining license and documents for export is difficult.

4. Sometimes corporations need to wait for payments.

5. Transportation costs may be high in some cases.

6. When corporations export through the agent, they have to give some money to him.

7. Exporting depletes resources like crude oil, minerals, ores, etc. Countries will lose valuable resources which can never be replenished.

The exporting of goods is specifically difficult and disadvantageous for the small and medium size corporations having employees less than 250. The sale of services and goods into the foreign market is difficult for them rather serving the domestic market. A lack of knowledge of different languages, difference in culture, exchange regulations and trade regulations having the major impact on exporting the goods for these corporations [2].

The **advantages** of the **import-oriented business** are as follows [1]:

1. Corporations can import the goods at very low cost from other countries and sell them with more profit.

2. Corporations can get some materials which can’t be produced domestically in any parts of the world.

3. Corporations can deliver the best quality products.

4. Tax concession is available for some specified goods.

5. Import is the best way to adopt the culture of other countries.

6. Corporations can bring the best technologies to the home country through import.

There are also challenges when relying on the import option only. The **challenges** of the **import-oriented business** are as follows [1]:

1. Unemployment will increase.
2. Local manufacturers will lose their business orders.
3. Corporations can't return the damaged and poor quality goods easily.
4. Reducing the income of the home country.
5. If corporations import the goods through a middleman (an agent), they need to pay for him.
6. Obtaining license and documents for import is difficult.
7. Importing from abroad will destroy domestic industry.
8. Importing reduces the economic growth of the country.
9. Corporations may import the products without quality.

Depending on the purpose and potential of the business, it is essential to decide whether the corporation should indulge into the export or import activity.

1.2. Multinational Corporations

Multinational corporations (MNCs) have investments in other countries, more focused on adapting their products and services to each individual local market via unique selling strategies. They are represented as mostly consumer goods manufacturers and quick-service restaurants. Example: Toyota, Unilever, Seven-Eleven, Microsoft. The International Labor Organization defines MNC as one, which has its operational

headquarters based in one country with several other operating branches in different other countries [42]. In other words, this corporation has its facilities and other assets in at least one country other than its own country. Such companies have offices and/or factories in different countries and usually have a centralized head office where they coordinate global management.

All multinational corporations can be classified as:

1. Ethnocentric MNCs.
2. Polycentric MNCs.
3. Geocentric MNCs.

Ethnocentric, or **home country oriented corporations**, are the type of MNCs which have strong orientation towards home country. They treat international business in the same way as national. This means that home country people are considered as preferable consumers. They manage overseas operations directly to protect the company’s competitiveness at the home market. Communication and information is top down and all strategic decisions are steered from corporate headquarters. Subsidiaries sell products designed and manufactured by parent companies with little or no local control [11].

Advantages of ethnocentric MNCs:

- simple structure;
- more tightly controlled;
- flexible management;
- social and political backlash;
- more ineffective.

Example: Coca-Cola.

Polycentric, or **host country oriented corporations**, are the type of MNCs which have strong orientation towards host country. They take into consideration cultural differences in business. Foreign operations are run from hubs in different countries. Polycentric MNCs come through five stages [11]:

1. The MNC's R&D operations are mostly concentrated in the West. While the MNCs operate in emerging markets, their local units are responsible for sales and marketing.

2. The MNCs start shifting some of their R&D work to low-cost countries (e.g. India) that offer plenty of high qualitative scientists and engineers.

3. The MNC recognizes the massive potential of the emerging markets and delegates more responsibilities to local units in emerging markets which initiate and manage their own R&D projects to cater local needs.

4. The MNC starts networking R&D activities in emerging markets with the rest of their global network in order to develop ideas for new products and business models for multiple regions.

5. The R&D hubs in emerging markets are given a great amount of money as they now own the R&D responsibilities for the global design and produce new products.

Advantages of polycentric MNCs:

- extensive knowledge of foreign markets and workplace;
- more support from host government.

Disadvantages of polycentric MNCs:

- duplication of work;
- difficult to maintain global objectives because of intense focus on local traditions.

Example: McDonalds.

Geocentric MNCs have concentration in the whole world and they make selection for the best employees whether they are from host country or home country it doesn't matter. When they desire an integration of all of their foreign subsidiaries and melding of a worldwide corporate culture, they adopt a geocentric management strategy. They have the most complex organizational structure requiring the greatest amount of communication and integration across national boundaries [11].

Advantages of geocentric MNCs:

- balanced local and global issues;
- best people and work approaches are used regardless the region.

Disadvantages of geocentric MNCs:

- forces needed to understand global issues;
- difficult to achieve;
- managers must have both local and global knowledges.

Example: Microsoft.

Multinational corporations have the following structure in a broad sense [48]:

1. Parent enterprise.
2. Affiliate enterprise.
3. Subsidiary enterprise.

4. Associate enterprise.

5. Branch.

6. Joint venture.

7. Holding company.

A **parent enterprise** is defined as an enterprise that controls assets of other entities in countries other than its home country, usually by owning a certain equity capital stake.

An **affiliate enterprise** is an incorporated or unincorporated enterprise in which a foreign investor has an effective voice in management. Such an enterprise may be a subsidiary, associate or branch.

A subsidiary is an incorporated enterprise in the host country in which another entity directly owns more than half of the shareholders' voting power, or is a shareholder in the enterprise, and has the right to appoint or remove a majority of the members of the administrative, management or supervisory body.

An associate is an incorporated enterprise in the host country in which an investor, together with its subsidiaries and associates, owns a total of at least 10 per cent, but not more than half, of the shareholders´ voting power (the figure may be less than 10 per cent if there is evidence of an effective voice in management).

A branch is an unincorporated enterprise in the host country which is one of the following:

- a permanent establishment or office of the foreign investor;

- an unincorporated partnership or joint venture between the foreign direct investor and one or more third parties;
- land, structures (except structures owned by government entities), and/or immovable equipment and objects directly owned by a foreign resident;
- mobile equipment (such as ships, aircraft, gas or oil-drilling rigs) operating within a country other than that of the foreign investor for at least one year.

A **joint venture** involves share-holding in a business entity having the following characteristics:

- the entity was established by a contractual arrangement (usually in writing) whereby two or more parties have contributed resources towards the business undertaking;
- the parties have joint control over one or more activities carried out according to the terms of the arrangements and none of the individual investors is in a position to control the venture unilaterally.

A joint venture may take one of the following three forms:

1. Jointly controlled entity.

2. Jointly controlled assets: the coordinated use of parts of the investors' enterprises in order to work on a common project which does not form separate entity, and which operates with a loose organizational structure. The assets and expertise of each partner remain under the direct control of that partner.

3. Jointly controlled operation: the contribution of resources by investors to a joint venture project which is managed by either one of the investors or by a joint management

team. In such a venture, a joint venture agreement defines the terms of the project, and each investor possesses an undivided interest in the assets of the project.

A **holding company** is a corporation that owns voting stock (ordinary share) in another corporation and is able to influence its board of directors and therefore control its policies and management. A holding company need not own a majority of the shares of the corporation or be involved in activities similar to those of the company it holds.

1.3. Transnational Corporations

Transnational corporations (TNCs) are more complex organizations. They have invested in overseas operations, but do not have to coordinate product offerings for each country; they give decision-making, R&D and marketing powers to each individual foreign market. Most of them come from petroleum, I.T. consulting, and pharmaceutical industries.

Example: Shell, Deloitte (consulting), Glaxo-Smith Klein (healthcare), Roche (pharmaceuticals), Nestle (foods).

Similarities between TNCs and MNCs [15]:

1. Both MNCs and TNCs are enterprises that manage production or delivers services in more than one country.
2. They are characterized as business entities that have their management headquarter in one country, known as the home country, and operate in several other countries, known as host countries.

3. Industries like manufacturing, oil mining, agriculture, consulting, accounting, construction, legal, advertising, entertainment, banking, telecommunications and lodging are often run through TNCs and MNCs.

4. Many of TNCs and MNCs are owned by a mixture of domestic and foreign stock holders.

5. Most TNCs and MNCs are massive with budgets that outweigh smaller nations' GDPs. Thus, both TNC and MNC have a large impact on globalization, economic and environmental lobbying in most countries.

6. Because of their influence, countries and regional political districts at times tender incentives to MNCs and TNCs in the form of tax breaks, pledges of governmental assistance or improved infrastructure, political favors and soft compliance with environmental and labor standards in order to be at an advantage over their competitors.

7. Due to their size, they can have a significant impact on government policy, primarily through the threat of market withdrawal. They are powerful enough to initiate lobbying that is directed at a variety of business concerns such as tariff structures, aiming to restrict competition of foreign industries.

Nevertheless, multinational and transnational corporations are different by their nature (Table 1.1).

Table 1.1 – Multinational versus transnational corporations [34]

Multinational corporations	Transnational corporations
Multinationals own a home country and its subsidiaries	Transnational corporations do not have subsidiaries but just many companies
Multinationals have a centralized management system	Transnational corporations do not have a centralized management system
Multinationals face a barrier in decision making due to its centralized management system	Transnational corporations are able to gain more interest in the local markets since they maintain their own systems

Differences between TNCs and MNCs [31]**:**

1. TNC has been technically defined by United Nations Commission on Transnational Corporations and Investment as enterprises which own or control production or service facilities outside the country in which they are based. The committee has also placed its preference on the term TNC.

2. The International Labor Organization defines MNC as one which has its operational headquarters based in one country with several other operating branches in different other countries.

3. Transnational corporations are a type of multinational corporations.

4. MNCs have an international identity as belonging to a particular home country where they are headquartered.

5. Transnational corporations are more or less borderless in this regard as they do not consider a particular country as their base.

1.4. Global corporations

Global corporation is an international business that operates in at least 15-20 countries. Key differences between global and international corporations are analyzed in Table 1.2.

Table 1.2 – Global vs international corporations [22]

Global corporations	International corporations
"Global" is a word that is used to refer to issues and concerns of the entire world	"International" is a term that is used to refer to issues and concerns of two or more countries
Global corporations have a much larger scope which includes the whole world	International corporations have a smaller scope encompassing two or more countries
Global means "all encompassing and worldwide"	International means "foreign or multinational"
Global corporations have offices and branches as well as investments in other countries	International corporations are involved into international trade only

Global corporations often offer the same product in different countries, but translate or modify a product's logo and packaging to meet local tastes. A company becomes a global corporation when it integrates all of its units and focuses its

marketing strategy on worldwide scale. For instance, a global software company will sell the same operating system in different countries, but will make some changes to the program, taking into account native speakers. Example: Coca-Cola, McDonalds, Procter&Gamble.

Global corporations are represented in the world by large-scale organizations. The Australian Bureau of Statistics defines a large-scale organization (LSO) as one that employs 200 or more people or has assets worth more than $ 200 million [37]. An LSO may also earn revenue in the millions. Thus, large-scale organizations are characterized be a large number of employees, a large amount of assets and large revenue.

The factors that make large-scale corporations unique for the international business are as follows [37]:

1. Operate in many countries (more than 15).
2. Produce goods and services “en masse”.
3. Have a huge range and large numbers of stakeholders.
4. Make large contributions to the economy.
5. Have access to huge amounts of finance.
6. Produce goods and services efficiently.
7. Produce goods and services cheaply.
8. Undertake long-term planning.
9. Have great political influence.
10. Group staff together into departments.
11. Have management structures.
12. Have owners or shareholders, who have little to do with day-to-day operations.

Global corporations perform in multicultural environment that requires undertaking an adequate mechanism to adapt to local cultures. Such mechanism is considered to be a “think globally, act locally” principle, or so-called “glocalization”. Glocalization is a combination of two words – globalization and localization. Glocalization refers to the practice of conducting business according to both local and global considerations. In order to succeed globally, even the biggest multinationals must think locally.

Glocalization pertained to the idea of adapting a global product to fit a local market. By 2000, the term had become a buzzword in big business, with countless companies looking for ways to glocalize everything from hamburgers to Web sites [32]. Global corporations need to serve a worldwide customer base by looking at value from the customer’s perspective. If they don’t, they run the risk of having no customer, no brand and no market. Customers have local and specific tastes and preferences. The supply chain needs to act locally to understand and meet those needs. Glocalization uses an 80-20 rule, which means that 80 % of behavior is globally the same but 20 % is locally driven, and that’s what counts.

McDonalds corporation is one of the best users of glocalization. Each of its restaurants, in more than 100 countries, offers McDonalds branding, but the actual menus vary to meet the local culinary tastes and dietary requirements. McDonalds restaurants in India offer mostly chicken, lamb and vegetarian dishes since many Hindus don’t eat beef. If we walk

into an Israeli McDonalds, we can order a kosher Big Mac (minus the cheese) [32]. So, glocalization is a dialogue between the global corporations and local sectors of consumers. With glocalization, a global corporation's goal isn't to say, "Here's a sandwich". Rather, the corporation asks, "How can we make a sandwich you'd like?" When glocalization and culture are connected, local communities play crucial roles in developing and sustaining global policies [33].

Conclusions

1. Corporations are one of the business forms a legal entity can take. International business can go under the name of different legal entities due to the various forms of legal organizations.

2. All international corporations can be divided into four groups: export- and import-oriented corporations (e.g. XEROX), multinational corporations (e.g. Toyota), transnational corporations (e.g. Shell), and global corporations (e.g. McDonalds).

3. International corporations operate in multicultural environment that requires undertaking an adequate mechanism to adapt to local cultures. Such mechanism is considered to be a "think globally, act locally" principle, or so-called "glocalization".

End-of-chapter tasks:

1. Distinguish between a firm, an enterprise, a company, and a corporation.
2. Define a multinational corporation.
3. Give an example of a global corporation.
4. Distinguish between MNC and TNC.
5. Discuss the glocalization approach to the business.

CHAPTER 2. INTERNATIONAL CORPORATIONS AS A STRONG FORCE FOR ECONOMIC GLOBALIZATION

2.1. Why Corporations Prefer to go Global.
2.2. Stages of Going Global.
2.3. How Corporations Contribute to Economic Development.

Key words: economic globalization, market entry, global expansion, multinationals, economic impact.

2.1. Why Corporations Prefer to Go Global

Economic globalization refers to increasing economic interdependence of national economies across the world through a rapid increase in cross-border movement of goods, services, technology and capital. International corporations play a key role in this process.

The global economy has become more competitive as companies of all sizes seek to expand beyond domestic borders. The Internet and information technology are among factors that have made it possible for corporations to venture into foreign markets. Before making an international move, though, it is helpful to understand common reasons why corporations enter the international business arena [19; 3].

1. New markets. A saturated domestic industry leaves few opportunities for companies to snap up clients. This drives them to look abroad for new customers and markets. Finding another country where demand for corporate product is higher is a far

superior option to simply waiting out the slump in sales. For example, developing countries can provide an ample opportunity for new revenue sources. Discovering resources or creating partnership opportunities may also contribute to corporation's ability to tap into overseas consumer markets. The corporation can quickly establish a strong foreign presence if it has a first-mover advantage.

2. Geographic advantage. Some companies expand internationally to develop synergies in resources and strengths that multiply the value of expansion. Access to new talent pools is a common motive. For instance, some U.S. companies have expanded into Asian markets to leverage the technological expertise of local populations, boosting their own capabilities while expanding their client bases. Distribution efficiency can also be enhanced by establishing effective global systems. This is especially true for companies that source supplies on a global basis.

3. Risk diversification. Operating in multiple countries offers greater insulation from economic downturns in one or two locations. A company doing business in the U.S., Asia and Africa may not suffer as much from a U.S. economic slump if it's offset by better conditions in its other locations. In this example, the company can use revenue gained in other markets to sustain and develop its U.S. business.

4. Competitive parity. "Everyone is doing it" is a simple but real motive for many companies that go global. If the corporation's competitors enter foreign markets, it seems logical

that this business should do so as well, conditions permitting. If the corporation has a competitive rivalry in the U.S., its competitor could gain increased brand exposure and recognition by entering markets where this corporation doesn't have the presence. By following along or entering before competitors, the corporation maintains parity in activities and exposure.

5. Creating an economy of scale. To put it simply, expanding will enable corporation to produce more units. The more units a corporation produces the lower its' per unit costs. This can increase its profit margins, but the corporation can only get the best of this through selling to more customers, which can only come through expanding to more countries. Such approach helps corporations to maximize on production and sales while effectively minimizing on the average costs.

6. The gig economy. The gig economy is one of the reasons why corporations go global. The Internet has opened the door for companies to trade all over the world. Previously, it was too expensive to do this. Now, you don't even need to have a physical presence in the country in order to do business. You can be an international company from the comfort of your own home. Many companies are now hiring teams they will never meet in person. The freelance economy can help a corporation to get projects done without the need to have employees in the same room as corporation's CEO. It's also cheaper than employing a full-time employer to do the same job. You can easily manage a global empire without visiting the places you are actually doing business in. Solid Wi-Fi connections and

software options like Skype allow you to stay connected at all times. Expensive business travel is a thing of the past.

7. Cultures are homogenizing. Again, this is the work of the Internet. Cultures are becoming more and more similar as Western influences are allowed to permeate. Think back to the state of the former Soviet Union. Thirty years ago it would be impossible for a Western company to appeal to this audience because they had little exposure to the West. Today they dress the same as the West and they love the same stuff as the West. The corporation's audience has increased without it having to do a thing.

8. Become a trusted brand. The fact of moving internationally will increase corporate prestige as a brand. It will increase corporate overall reach because customers are going to look at an international brand and assume they can be trusted. Expanding globally significantly increases the status quo of a given company and grows its prestige among competitors and further to its consumers as a worldwide trusted brand.

9. Cost-saving reasons. Sometimes it's just a matter of cost. It's cheaper to do business abroad because a corporation can reduce production costs and pay employees in more affordable countries less. There's a reason why Apple outsources the bulk of its iPhone production to Asia. Very often corporations are searching for tax preferences allowing to reduce costs. Tax preferences are a gold mine for major global companies. It's a chance to save most of corporate profits for

stakeholders, but this can only happen by expanding internationally.

Let's dwell on domestic market explanation of global corporate expansion. In this case five situations are possible [10]:

1. Domestic markets are saturated and there is pressure to raise sales and profits. When a given product exists in too much surplus in a country, companies opt to find new markets where the product demand is higher. This helps the firms grow favorably the market base as opposed to sticking at the home country where the surplus is too high. Most corporations have very ambitious sales and profit targets. If such figures have to be realized, companies have to move out of their domestic markets.

2. Domestic markets are small. Companies which have ambitions to become big will have to look for bigger markets outside their boundaries.

3. Domestic markets are growing slowly. Most companies are no longer content to grow incrementally. If such companies have to achieve high growth rates, they have to obtain some of their sales from international markets.

4. Domestic market competition. Even if a company decides to concentrate on its domestic market, it will not be allowed to pursue its goals unhindered. Multinational companies will enter its market and make a dent in its market share and profit. The company has no choice but to enter foreign markets to maintain its market share and growth. Only a company which is internationally competitive can protect its domestic market.

No market is or will be protected from incursion by multinational companies. A company's only choice is to go global, even if its prime interest is to protect its domestic turf.

5. High-cost domestic markets. The cost of doing business in certain markets is more favorable compared to other given markets, as such companies opt to expand globally and operate in the given tax heavens or regions with more friendly tax rates, or where the cost of doing business is favorably lower.

2.2. Stages of Going Global and Successful Global Expansion

If the management of a corporation is thinking about going global, it should follow the step-to-step procedure which is as follows [12]:

1. At the first stage (**market entry**), companies tend to enter new countries using business models that are very similar to the ones they deploy in their home markets. To gain access to local customers, however, they often need to establish a production presence, either because of the nature of their businesses (as in service industries like food retail or banking) or because of local countries' regulatory restrictions (as in the auto industry).

2. At the second stage (**product specialization**), companies transfer the full production process of a particular product to a single low-cost location and export the goods to various consumer markets. Under this scenario, different locations begin

to specialize in different products or components and trade in finished goods.

3. The third stage (**value chain disaggregation**) represents the next step in the company's globalization of the supply-chain infrastructure. At this stage, companies start to disaggregate the production process and focus each activity in the most advantageous location. Individual components of a single product might be manufactured in several different locations and assembled into final products elsewhere. Examples include the PC industry market and the decision by companies to offshore some of their business processes and information technology services.

4. At the fourth stage (**value chain reengineering**), companies seek further increase of their cost savings by reengineering their processes to suit local market conditions, notably by substituting capital for lower-cost labor. General Electric's (GE) medical equipment division, for example, has tailored its manufacturing processes abroad to take advantage of low labor costs. The company only uses a more labor-intensive production processes, but also designs and manufactures the capital equipment for its plants locally.

5. Finally, at the fifth stage (**the creation of new markets**), the focus is on market expansion. The McKinsey Global Institute estimates that the third and fourth stages together have the potential to reduce costs by more than 50 % in many industries, which gives companies the opportunity to substantially lower their sticker prices in both old and new

markets and to expand demand. The value of new revenues generated at this last stage is often greater than the value of cost savings at the other stages.

It should be noted that the five stages described above do not define a rigid sequence that all industries follow. As the McKinsey study notes, companies can skip or combine steps. For example, in consumer electronics, product specialization and value chain disaggregation (the second and third stages) occurred together as different locations started to specialize in producing different components (Taiwanese manufacturers focused on semiconductors, while Chinese companies focused on computer keyboards and other components).

Another approach for successful global expansion includes the following stages:

1. Aspirational stage. This stage is marked by the aim, ambition and desire to expand globally**.** The corporation is ready to respond to the global challenges. This stage is characterized mainly by the following successful factors as efficient investing and well-educated human resources. This is the stage where rational approach is used to see the risk worth taking as the global market is competitive.

2. Procedural stage. The management has to apply the knowledge acquired at the initial stage. The international research has to be conducted to reveal market conditions and customer preferences. The management has to learn "the rules of the game", develop technical knowledge and legislation knowledge, and to have adaptive learning to operate

successfully. It is important to understand different legislative practices and different market characteristics. The first successful factor to be taken into account is conducting a research. The first step in the research is choosing an initial (target) market. Then, it is necessary to decide on such essential criterion as tax breaks. This helps to identify cost manufacturing opportunity and eliminate poor market opportunities. The research can be conducted by attending expert seminars and workshops as a mean to gain expertise in comprehensive information about target country, its market and consumers. The second step is choosing distribution channel. This can be done by hiring a sales representative who, preferably, has to be a native, well-educated, with good interpersonal skills, able to support business organizationally and technically, be personally acquainted with the prospective distributor and be able to evaluate cultural differences. The third step is a selection of financial arrangements. The best way to do business with an overseas buyer is a letter of credit as it keeps all transactions and eliminates worries about payment.

3. Behavioral stage. This stage is marked by awareness of new conditions in which the corporation operates. The sensitivity to environmental demands, cultural appreciation and the empathy are required when exploring a new market. At this stage, the corporation has to have better understanding the people and culture in order to create better business relationships. Companies tend to operate mainly in countries which language is similar to the owners of organization, because

language similarity leads to a more thorough understanding and helps to avoid misunderstanding.

4. Conceptual stage. The management has to do a valuation of international business from its experience and observations. An attitude, believes, judgments, opinions, views and ways of thinking have to be included into such an assessment. Therefore, multiple logics have to be applied in order to become a top large company.

2.3. How International Corporations Contribute to Economic Development

International corporations, MNCs in particular, can contribute to economic development in different ways. When a multinational invests in a host country, the scale of the investment (given the size of the firms) is likely to be significant. Indeed governments often offer incentives to firms in the form of grants, subsidies and tax breaks to attract investment into their countries. These foreign direct investments (FDI) have advantages and disadvantages for the host country.

The possible **benefits** of a multinational investing in a **host country** may include [24]:

1. **Improving the balance of payments** – inward investments will usually help a country's balance of payments situation. The investment itself will be a direct flow of capital into the country and the investment is also likely to result in import substitution and export promotion. Export promotion

comes due to the multinational using their production facility as a basis for exporting, while import substitution means that products previously imported may now be bought domestically.

2. **Providing employment** – FDI will usually result in employment benefits for the host country as most employees will be locally recruited. These benefits may be relatively greater given that governments will usually try to attract firms to areas where there is relatively high unemployment or a good labor supply.

3. **Source of tax revenue** – profits of multinationals will be subject to local taxes in most cases, which will provide a valuable source of revenue for the domestic government.

4. **Technology transfer** – multinationals will bring with them technology and production methods that are probably new to the host country and a lot can therefore be learnt from these techniques. Workers will be trained to use the new technology and production techniques and domestic firms will see the benefits of the new technology. This process is known as technology transfer.

5. **Increasing choice** – if the multinational manufactures for domestic markets as well as for export, then the local population will gain form a wider choice of goods and services and at a price possibly lower than imported substitutes.

6. **National reputation** – the presence of one multinational may improve the reputation of the host country and other large corporations may follow suite and locate as well.

7. **Source of management experience** – the host country's business also gets management expertise from MNCs.

8. **Economic liberalization** – MNCs break protectionalism, curb local monopolies, create competition among domestic companies and thus enhance their competitiveness.

The possible **disadvantages** of a multinational investing in a **host country** may include [24]:

1. **Environmental impact** – multinationals will want to produce in ways that are as efficient and as cheap as possible, and this may not always be the best environmental practice. They will often lobby governments hard to try to ensure that they can benefit from regulations being as lax as possible and given their economic importance to the host country, this lobbying will often be quite effective.

2. **Uncertainty** – multinational firms are increasingly "footloose". This means that they can move and change at very short notice and often will. This creates uncertainty for the host country.

3. **Increased competition** – the impact of the local industries can be severe, because the presence of newly arrived multinationals increases the competition in the economy and because multinationals should be able to produce at a lower cost.

4. **Influence and political pressure** – multinational investment can be very important to a country and this will often give them a disproportionate influence over government and other organizations in the host country. Given their economic

importance, governments will often agree to changes that may not be beneficial for the long-term welfare of their people.

5. **Transfer pricing** – multinationals will always aim to reduce their tax liability to a minimum. One way of doing this is through transfer pricing. The aim of this is to reduce their tax liability in countries with high tax rates and increase them in the countries with low tax rates. They can do this by transferring components and part-finished goods between their operations in different countries at differing prices. Where the tax liability is high, they transfer the goods at a relatively high price to make the costs appear higher. This is then recouped in the lower tax country by transferring the goods at a relatively lower price. This will reduce their overall tax bill.

6. **Low-skilled employment** – the jobs created in the local environment may be low-skilled with the multinational employing expatriate workers for the more senior and skilled roles.

7. **Health and safety** – multinationals have been accused of cutting corners on health and safety in countries where regulation and laws are not as rigorous.

8. **Export of profits** – large multinationals are likely to repatriate profits back to their "home country", leaving little financial benefits for the host country.

9. **Cultural and social impact** – large numbers of foreign businesses can dilute local customs and traditional cultures. For example, the sociologist George Ritzer coined the term McDonaldization to describe the process by which more

and more sectors of American society as well as of the rest of the world take on the characteristics of a fast-food restaurant, such as increasing standardization and the movement away from traditional business approaches.

10. **Threat to the economic and political sovereignty** – as MNCs do not operate within the national autonomy, they may pose a threat to the economic and political sovereignty of host countries. Large sums of money flow to foreign countries in terms of payments towards profits, dividends and royalty. Profits earned by MNCs may be remitted back to the MNC's home country rather than reinvested in the host economy.

As well as host economy impacts, multinationals can be analyzed from home country perspective.

Advantages of MNCs for the home country [53]:

1. MNCs create opportunities for marketing the products produced in the home country throughout the world.

2. They create employment opportunities to the people of home country both at home and abroad.

3. It gives a boost to the industrial activities of home country.

4. MNCs help to maintain favourable balance of payment of the home country in the long run.

5. Home country can also get the benefit of foreign culture brought by MNCs.

Disadvantages of MNCs for the home country [53]:

1. MNCs transfer the capital from the home country to various host countries causing unfavourable balance of payment.

2. MNCs may not create employment opportunities to the people of home country if it adopts a geocentric approach.

3. Since investments in foreign countries are more profitable, MNCs may neglect industrial and economic development of the home countries.

In general, global corporations contribute to the economic development in the following way [60]:

1. **Pay higher wages.** Average annual wage paid to U.S. employees of foreign-owned firms grew by almost 6 %; average wages for private sector grew by only 2.7 %.

2. **Increase productivity of the domestic market.** Foreign companies bring new techniques and practices. When employees leave, they take with them new practices that can be shared with other companies in the region. Additionally, if these foreign-owned firms sell products locally, they can demand higher quality or share production technology with suppliers.

3. **Are less likely to go out of business.** U.S. companies that export not only grow faster, but also go out of business by 8.5 % less than non-exporting companies.

4. **Spur more efficient development of technology and R&D.** Companies can get their innovations to market faster.

Conclusions

1. Economic globalization refers to increasing economic interdependence of national economies across the world through a rapid increase in cross-border movement of goods, services,

technology and capital. International corporations play a key role in this process.

2. There are at least five stages of global expansion and at least four stages of developing international business successfully. The former stages include: market entry, product specialization, value chain disaggregation, value chain reengineering, and creation of new markets. The latter stages comprise: the aspirational stage, procedural stage, behavioral stage, and the conceptual stage.

3. International corporations contribute to the economic development of both home and host countries in different ways (positive or negative). In general, global corporations pay higher wages, increase productivity, are less likely to go out of business, and spur more efficient technological development.

End-of-chapter tasks:

1. Give the reasons why corporations prefer to go global.
2. List the stages of going global.
3. Identify key stages of successful global expansion.
4. Relate advantages and disadvantages of FDI to host country.
5. Explain how multinationals contribute to home economy.

CHAPTER 3. INTERNATIONAL CORPORATIONS IN THE GLOBAL BUSINESS ENVIRONMENT

3.1. Challenges for International Big Business.
3.2. Best Countries to Headquarter a Corporation.
3.3. Multinational Investment Activity.

Key words: challenges, headquarter, doing business rank, greenfield strategy, brownfield strategy, FDI.

3.1. Challenges for International Big Business

Expanding business overseas means reaching new clients or customers and potentially boosting profits. At that time, corporations may encounter different challenges when going global. There are some guidelines for conducting business on a global scale that a management should always consider before leaping into new international operations [45].

1. **International company structure.** If the aim of the management is to be competitive globally, it must have a team in place that's up for the challenge. One fundamental consideration is the structure of the corporation and the location of its teams. The challenging questions to be asked are as follows:

1. Will the company be run from one central headquarter?

2. Will the company have offices and representatives "on the ground" in key markets abroad?

3. If so, how will these teams be organized, what autonomy will they have, and how will they coordinate working across time zones?

4. If not, will the management consider hiring local market experts who understand the culture of the target markets, but will work centrally?

Coca-Cola offers one example of effective multinational business structure. The company is organized into continental groups, each overseen by a President. The central Presidents manage Presidents of smaller, country-based or regional subdivisions. Despite its diverse global presence, the Coca-Cola brand and product is controlled centrally and consistent around the world.

2. **Foreign laws and regulations.** Gaining a comprehensive understanding of the local laws and regulations governing target markets is a key. From tax implications through to trading laws, navigating legal requirements is a central function for any successful international business. Eligibility to trade is a significant consideration, as are potential tariffs and the legal costs associated with entering new markets. For example, Airbnb company ran into trouble in 2014 with a crackdown on advertised rental properties falling outside local housing and tourism regulations. The company was forced to pay a €30,000 fine for a breach of local tourism laws in Barcelona. It’s important to note that employment and labor requirements also differ by country. For instance, European countries stipulate that a minimum of 14-weeks maternity leave

be offered to employees, while on the other hand, there is no such requirement for U.S. employers. With the complexity involved in foreign trade and employment laws, investing in knowledgeable and experienced corporate counsel can prove invaluable. Beyond abiding by official laws, engaging in international business often requires following other unwritten cultural guidelines.

3. **International accounting.** Of the main legal areas to consider when it comes to doing international business, tax compliance is perhaps the most crucial. Accounting can present a challenge to multinational businesses that may be liable for corporation tax abroad. Different tax systems, rates, and compliance requirements can make the accounting function of a multinational organization significantly challenging. Accounting strategy is key to maximizing revenue, and the location where the business is registered can impact company's tax liability. A focus on tax efficiency is often the aim of international accounting efforts. In the European Union, companies may benefit from the Common Consolidated Corporate Tax Base proposal, whereby companies with operations around the EU can limit tax liability to one corporate center. Tax consolidation is a feature of several multinationals' decision to be headquartered in Dublin, as Ireland is known for its "business-friendly" corporate tax policy. Well-known companies with operational headquarters in the Republic of Ireland include Google, Facebook, and Intel.

4. **Cost calculation and global pricing strategy.** Setting the price for products and services can present challenges when doing business overseas and should be another major consideration of expansion strategy. You must consider costs to remain competitive, while still ensuring profit. Researching the prices of direct, local-market competitors can give managers a benchmark. For instance, the cost of production and shipping, labor, marketing, and distribution, as well as margin, must be a taken into account for the business to be viable. Pricing can also come down to how the managers choose to position their brand – should the cost of product reflect luxury status? Or will low prices help company to penetrate a new market? Swedish furniture giant Ikea, known in Europe for its low-cost value, struggled initially in China due to local competitor costs of labor and production being much cheaper. By relocating production for the Chinese market and using more locally sourced materials, the company was able to successfully cut prices to better reflect its brand and boost sales among target consumers.

5. **Universal payment methods.** The proliferation of international e-commerce websites has made selling goods overseas easier and more affordable for businesses and consumers. However, payment methods that are commonly accepted in the home market might be unavailable abroad. Determining acceptable payment methods and ensuring secure processing must be a central consideration for businesses who seek to trade internationally. Accepting well-known global payment methods through companies like Worldpay, as well as

accepting local payment methods, such as JCB in Asia can be a good option for large international businesses. Accepting wire transfers, PayPal payments and Bitcoin are other possibilities, with Bitcoin users benefiting from no bank or credit card transaction fees. Despite the risk of fluctuating value, the lack of fees is one of the reasons a number of online companies, including WordPress, the Apple App Store, Expedia, and a number of Etsy sellers accept Bitcoin.

6. **Currency rates.** While price setting and payment methods are major considerations, currency rate fluctuation is one of the most challenging international business problems to navigate. Monitoring exchange rates must, therefore, be a central part of the strategy for all international businesses. However, global economic volatility can make forecasting profit especially difficult, particularly when rates fluctuate at unpredictable levels. Major fluctuations can seriously impact the balance of business expenses and profit. For instance, if the company is paying suppliers and production costs in US dollars, but selling in markets with a weaker or more unpredictable currency, this company could end up with a much smaller margin – or even a loss. One way to protect business against large fluctuations in currency is to pay suppliers and production costs in the same currency as the one company is selling in. This may mean switching to more local production where possible in order to better balance company's outgoings and sales revenue. Another option for mitigating the risk of unpredictable currency

rates can be setting up a forward contract and agreeing a price in advance for future sales.

7. **Choosing the right global shipment methods**. The potential of online sales presents a huge international business opportunity for retailers in the 21st century, but finding reliable, fast, and cost-effective shipment and distribution methods can be a difficult balance in some markets. Depending on the volume and destination of the shipments, it is necessary to decide whether a company sends by land, sea, air, or a combination. The right choice of shipping method can be a major influence on the revenue and may be a limiting factor to the products you can viably sell overseas. There are country-specific regulations and shipping requirements to take into account. For a quick check of costs and compliance, UPS International has created an online tool called TradeAbility to help businesses and individuals manage the movement of goods overseas.

8. **Communication difficulties and cultural differences.** Good communication is at the heart of effective international business strategy. However, communicating across cultures can be a very real challenge. Effective communication with colleagues, clients, and customers abroad is essential for success in international business. And it’s often more than just a language barrier the company needs to think about – nonverbal communication can make or break business deals too. Being aware of acceptable business etiquette abroad, and how things like religious and cultural traditions can influence this, will help

a manager to better navigate potential communication problems in international business. A number of well-known companies have had to consider adapting the names of their brand or product when launching in a foreign market. The Chevrolet Nova is perhaps the most commonly cited example, where “no va” literally translates to “no go” in Spanish – not the best product name for a car. Although slumping sales figures in Latin America have proven to be an urban legend, the story of the “no go” car serves as a useful reminder of the importance of preparing well before launching the business in a new market.

9. **Political risks.** An obvious risk for international business is political uncertainty and instability. Countries and emerging markets that may offer considerable opportunities for expanding global businesses may also pose challenges, which more established markets do not. Before considering expansion into a new or unknown market, a risk assessment of the economic and political landscape is critical. Issues such as ill-defined or unstable policies and corrupt practices can be hugely problematic in emerging markets. Changes in governments can bring changes in policy, regulations, and interest rates that can prove damaging to foreign business and investment. A growing trend towards economic nationalism also makes the current global political landscape potentially hostile towards international businesses. For instance, companies like Facebook are banned in China, partially in preference for national social networks and also due to government regulation over internet content. Monitoring political developments and planning

accordingly can mitigate political risks of doing business abroad.

10. **Supply chain complexity and risks of labor exploitation.** When it comes to sourcing products and services from overseas, managing suppliers and supply chains can also be a tricky process. Unfortunately, the length and complexity of supply chains increases the chance of working with suppliers who have unethical – and even illegal – business practices. Of growing concern is the risk in international business of forced labor and worker exploitation. In October 2015, the UK passed the Modern Slavery Act in response to this often-hidden human rights violation. Recent research led by a partnership between Hult International Business School and the Ethical Trading Initiative revealed that an astonishing 77 % of businesses believe that modern slavery exists at some point in their supply chains.

11. **Worldwide environmental issues.** As the environmental risks and effects of climate change are becoming better understood, sustainability is high on the agenda of many major global corporations. Recent international legislations and proposals, such as the UN's Sustainable Development Goals, have put environmental issues at the forefront of international business development. If the company is considering expanding business overseas, it's important to be aware of the country-specific environmental regulations and issues. Some key considerations include how production methods might impact the local environment through waste and pollution. Beyond a

legal or ethical incentive to be more eco-friendly, establishing environmentally conscious business practices can attract new, forward-thinking consumers to the company. With a number of brands such as Dell, Renault, and MUD Jeans leading a shift towards the circular economy, there is an opportunity and demand for changing production methods and consumer behavior to establish a more sustainable future for the environment and society as a whole.

3.2. Best countries to Headquarter a Corporation

Headquarter is the main office of a business company. Choosing a country to headquarter a corporation in 2017 is determined by favorable business environment. The ranks that estimate decisions on where to headquarter a corporation can be grouped as follows:

1. “Best Countries rankings”.
2. “Ease of doing business” by the World Bank Group.
3. “Best countries for business” by Forbes.

1. **The Best Countries rankings** conducted an annual survey and asked more than 6,000 business decision-makers from four regions to associate 80 countries with 9 specific attributes: connectedness to the rest of the world; corruption; economic stability; educated population; favorable tax environment; a place “I would live”; safety; well-developed infrastructure; well-developed legal framework.

According to this rank, the first five places are distributed in the following way:

1. Switzerland.
2. Canada.
3. Australia.
4. Denmark.
5. Sweden.

Switzerland. Corporations in Switzerland paid in 2017 an income tax rate of 17.77 % [13]. Nestle, Credit Suisse and UBS are among a number of Fortune 500 companies based out of the country. Switzerland is one of the wealthiest countries, and has been well-known for centuries for its neutrality. Switzerland's neutrality has long been honored by its European neighbors – the country didn't take a side in either of the world wars and is not a member of the European Union. As a result, Switzerland, particularly Geneva, is a popular headquarter location for international organizations such as the International Committee of the Red Cross and the United Nations, though Switzerland did not join the latter until 2002. The country is also a member of the IMF, WTO and World Bank. Switzerland has low unemployment, a skilled labor force and one of the highest gross domestic products per capita in the world. The country's strong economy is powered by low corporate tax rates, a highly-developed service sector led by financial services and a high-tech manufacturing industry. Switzerland is also notable for its secretive banking sector. Reporting rules and legislation have led to more transparency, but secrecy rules persist and

nonresidents are allowed to conduct business through offshore entities and various intermediaries.

Canada. Corporations in Canada paid in 2017 an income tax rate of 26.5 % [13]. When the US-based Burger King bought the Canadian chain Tim Hortons in 2014, a headquarters move from Miami to neighborhood of Toronto was estimated to save the new fast food giant hundreds of millions of dollars in taxes (because income tax rate in the United States is 40 %). Canada is a high-tech industrial society with a high standard of living. Trade agreements in the 1980s and 1990s dramatically bolstered trade with the US, and now the two counties are each other’s largest trading partner. While the service sector is Canada’s biggest economic driver, the country is a significant exporter of energy, food and minerals. Canada ranks third in the world in proven oil reserves and is the world’s fifth largest oil producer.

Australia. Corporations in Australia paid in 2017 an income tax rate of 30 % [13]. Those in the mining industry like Rio Tinto and supermarket retailing like Woolworths are some of the largest corporations of this resource-rich nation. Survey participants ranked Australia as the No.1 place they would choose to live and as the least corrupt. Australia is considered a wealthy nation with a market-based economy that has a comparatively high gross domestic product and per capita income. Its economy is driven by the service sector and the export of commodities. The nation has a high rate of participation in sporting activities and boasts a comparatively high life expectancy for both females and males. Its major cities

routinely score well in global livability surveys. Australians remain particularly concerned about environmental issues. Australia is a member of major international and regional organizations, including the United Nations, the Group of 20, the World Trade Organization, the Organization for Economic Cooperation and Development, the Commonwealth of Nations and Asia-Pacific Economic Cooperation.

Denmark. Corporations in Denmark paid in 2017 an income tax rate of 22 % [13]. Survey participants consider the home of Lego and Bang&Olufsen to be the nation with the most transparent business practices. The Danish government is perceived as highly stable and very transparent. By offering reimbursement of losses due to research and development, the tax policy in Denmark promotes innovations, and a central location offers easy access to and expansion opportunities in Europe and Eurasia. Through redistributionist and progressive taxation, Denmark employs a universal health care system in which citizens receive mostly free medical care. Higher education is also free. Denmark has several leading industries including food processing, tourism and the production of iron, steel and machinery. Its main exports are processed foods, agricultural and industrial machinery, pharmaceuticals and furniture. Denmark's economy is based on the flexicurity model, which combines a flexible labor market with a policy for the unemployed. This flexicurity model allows for businesses to establish inexpensively and quickly.

Sweden. Corporations in Sweden paid an income tax rate – which includes federal, state and local taxes – of 22 % in 2017 [13]. A wide range of industries based in Sweden have gained international success and recognition, including companies from Astra Zeneca in pharmaceuticals and Skype in communications to H&M and Ikea in clothing and furniture retail. The large majority of Swedish workers belong to labor unions, fostering accountability and transparency in the workplace. Sweden operates under a model similar to those of other Nordic nations: heavily capitalistic with a large percent of spending going toward public service. Once well above the global average, tax rates have decreased, and an advanced infrastructure and transportation network assist with equal wealth distribution. Health care as well as a college education are free, and its people boast one of the longest life expectancies in the world. Almost all of Sweden's trash is recycled.

2. **Ease of doing business rank by World Bank Group**. According to this rank, countries are ranked on their ease of doing business from 1–190. A high ease of doing business ranking means the regulatory environment is more conducive to the starting and operation of a local firm. The rankings are determined by sorting the aggregate distance to frontier scores on 10 topics, each consisting of several indicators, giving equal weight to each topic. Doing Business measures regulations affecting 10 areas of the life of a business: starting a business; dealing with construction permits; getting electricity; registering property; getting credit; protecting minority investors; paying

taxes; trading across borders; enforcing contracts; resolving insolvency.

Starting a business includes the following sub-components: number of procedures, time (in days), cost (% of income per capita), and minimum capital (% of income per capita).

Dealing with construction permits consists of the following subcomponents: number of procedures, time (in days), cost (% of warehouse value), and building quality control index.

Getting electricity comprises the following indicators: number of procedures, time (in days), cost (% of income per capita), and reliability of supply and transparency of tariff index.

Registering property includes the following sub-components: number of procedures, time (in days), cost (% of property value), and quality of land administration index.

Getting credit consists of the following subcomponents: strength of legal rights index, and depth of credit information index.

Protecting minority investors comprises the following indicators: extent of disclosure index, extent of director liability index, ease of shareholder suits index, extent of shareholder rights index, extent of ownership and control index, and extent of corporate transparency index.

Paying taxes includes the following subcomponents: payments (number per year), time (hours per year), total tax and contribution rate (% of profit), postfiling index, time to comply with VAT refund (hours), and time to obtain VAT refund

(weeks), time to comply with corporate income tax audit (hours), time to complete a corporate income tax audit (weeks).

Trading across borders consists of the following subcomponents: time and cost to export (documentary and border compliance) and time and cost to import (documentary and border compliance).

Enforcing contracts comprises time (days), cost (% of claim), and quality of judicial processes index.

Resolving insolvency includes the following subcomponents: recovery rate (cents on the dollar) and strength of insolvency framework index.

The results of this rank are represented in Table 3.1.

Table 3.1 – The best countries for doing business in 2017 [16]

Country	Total rank
New Zealand	1
Singapore	2
Denmark	3
Hong Kong SAR, China	4
Korea, Rep.	5
Norway	6
United Kingdom	7
United States	8
Sweden	9
Macedonia	10
Taiwan, China	11
Estonia	12
Finland	13
Latvia	14

More detailed information you can find in Table 3.2.

Table 3.2 – Rankings of the top-15 countries for doing business in 2017 [16]

Country	Starting a business	Dealing with construction permits	Getting electricity	Registering property	Getting credit	Protecting minority investors	Paying taxes	Trading across borders	Enforcing contracts	Resolving insolvency
New Zealand	1	1	34	1	1	1	11	55	13	34
Singapore	6	10	10	19	20	1	8	41	2	29
Denmark	24	6	14	12	32	19	7	1	24	8
Hong Kong SAR, China	3	5	3	61	20	3	3	42	21	28
Korea, Rep.	11	31	1	39	44	13	23	32	1	4
Norway	21	43	12	14	75	9	26	22	4	6
United Kingdom	16	17	17	47	20	6	10	28	31	13
United States	51	39	36	36	2	41	36	35	20	5
Sweden	15	25	6	10	75	19	28	18	22	19
Macedonia, FYR	4	11	29	48	16	13	9	27	36	32
Taiwan, China	19	3	2	17	62	22	30	68	14	22
Estonia	14	9	38	6	32	53	21	17	11	42
Finland	28	40	18	20	44	70	13	33	30	1
Latvia	22	23	42	23	7	42	15	25	23	44
Australia	7	2	41	45	5	63	25	91	3	21

3. **Best countries for business by Forbes**. On December 21, Forbes magazine published its annual "Best Countries for Business" list for 2017 [41], ranking the "business friendliness" of 139 countries based on 11 factors covering the legal and economic aspects impacting business. The first 10 leaders of this rank are the following.

1. **Sweden** – new in 2017 at the top spot, up from № 5 the previous year. A booming economy and recent trend toward less government regulation makes Sweden hard to beat for multinational companies. Employment authorization for foreign nationals is still comparatively quick and easy, despite Europe's ongoing refugee crisis.

2. **New Zealand** – claims the № 2 spot again in 2017. Traditionally an easy place to start and run a new business, New Zealand has been corporate immigration-friendly, but large immigration numbers in recent years brought some minor tightening to regulations.

3. **Hong Kong** – still remains perennially strong for business with its huge financial sector and entrepreneurial environment. As with any high-demand destination, there is periodic immigration rule tightening, but it's still open for business.

4. **Ireland** – still holding steady at № 4 from 2016, with a low corporate tax rate and affluent workforce. Ireland will only look more attractive for multinational businesses as Brexit plays out next door in the UK. There have been some significant improvements to the corporate immigration system lately.

5. **United Kingdom** – still a great country for business, but the elephant in the room remains Brexit. The shocking 2016 development admittedly opens a whole host of questions for the future and especially for corporate mobility between the UK and the EU.

6. **Denmark** – down from 2016 № 1 spot, but there's stiff competition in the Nordic region with neighbors: Sweden, Finland, and Norway also highly ranked on the list. Still a great business climate, but the current administration is somewhat less immigration-friendly, mainly because of Europe's current refugee crisis.

7. **Netherland**s – up two spots from 2016 list. The forward-thinking government adopted the EU Intra-Company Transfer Directive in November 2017, which has the potential for major benefits for business in Europe.

8. **Finland** – a stable and predictable regulatory environment and a low corporate tax rate (20 percent) make Finland attractive for international business. A recent survey by the Information Technology and Innovation Foundation ranked Finland as the world's biggest contributor to global innovation. Interestingly, the capital Helsinki has the world's second-highest concentration of commercially successful app developers, behind only the US's Silicon Valley.

9. **Norway** – like its Nordic neighbor Finland, Norway stays competitive by boasting a stable and predictable regulatory environment, a relatively low (but not as low as Finland) corporate tax rate, and a highly-skilled workforce. Also like

Finland, the corporate immigration process is relatively smooth, and both countries benefit from their membership in the Schengen area.

10. **Canada** – The consistent bright spot for international business in North America, due in part to the progressive attitude toward international trade and business, particularly in regards to corporate immigration.

There are many factors describing business environment in a certain economy. Business environment in a country plays a crucial role in choosing a place for headquartering a corporation. Bright leaders among the best countries for doing business are Switzerland, Canada, Australia, Denmark, Sweden, New Zealand, Singapore, Hong Kong, Korea, Ireland, and United Kingdom.

3.3. Multinational Investment Activity

A multinational corporation is an enterprise that engages in foreign direct investment (FDI) and that owns or controls value-added activities in more than one country [39]. FDI is a transfer of funds from the country of the parent firm to the country of the host firm in a form of affiliate, subsidiary, or joint venture.

A country's FDI can be both inward and outward. Inward FDI refers to investments coming into the country and outward FDI are investments made by companies from that country into foreign companies in other countries. The difference between inward and outward is called the net FDI inflow, which can be

either positive or negative. There are different kinds of FDI, two of which – greenfield and brownfield – are increasingly applicable to global firms. Greenfield FDI occur when multinational corporations enter into developing countries to build new factories or stores. These new facilities are built from scratch – usually in an area where no previous facilities existed. The name originates from the idea of building a facility on a green field, such as farmland or a forested area. In addition to building new facilities that best meet their needs, the firms also create new long-term jobs in the foreign country by hiring new employees. Countries often offer prospective companies tax breaks, subsidies, and other incentives to set up greenfield investments. A brownfield FDI is when a company purchases or leases existing production facilities to launch a new production activity. One application of this strategy is where a commercial site used for an "unclean" business purpose, such as a steel mill or oil refinery, is cleaned up and used for a less polluting purpose, such as commercial office space or a residential area. Brownfield investment is usually less expensive and can be implemented faster; however, a company may have to deal with many challenges, including existing employees, outdated equipment, entrenched processes, and cultural differences [46].

After a strong rise in 2015, global FDI flows lost growth momentum in 2016, showing that the road to recovery remains bumpy. FDI inflows decreased by 2 % to $1.75 trillion, amid weak economic growth and significant policy risks, as perceived by multinational corporations (Table 3.3).

Table 3.3 – Global distribution of FDI [61]

FDI inflows, billions of dollars		
Economies	Years	
	2015	2016
World	**1774**	**1746**
Developed economies	**984**	**1032**
Europe	566	533
North America	390	425
Developing economies	**752**	**646**
Africa	61	59
Asia	524	443
Latin America and the Caribbean	165	142
Transition economies	**38**	**68**
FDI share, %		
World	100	100
Developed economies	**55**	**59**
Europe	32	31
North America	22	24
Developing economies	**42**	**37**
Africa	3	3
Asia	30	25
Latin America and the Caribbean	9	8
Transition economies	**2**	**4**

Flows to developing economies were especially hard hit, with a decline of 14 % to $ 646 billion [61]. FDI remains the largest and most constant external source of finance for developing economies – compared with portfolio investments, remittances and official development assistance. But inflows were down across all developing regions [61]:

1. FDI flows to developing Asia contracted by 15 % to $443 billion in 2016. This first decline in five years was relatively widespread, with double-digit drops in most subregions except South Asia.

2. FDI flows to Africa continued to slide, reaching $59 billion, down 3 % from 2015, mostly reflecting low commodity prices.

3. The downward trend in FDI flows to Latin America and the Caribbean accelerated, with inflows falling 14 % to $142 billion, owing to continued economic recession, weak commodity prices and pressures on exports.

4. FDI in structurally weak and vulnerable economies remained fragile. Flows to the least developed countries fell by 13 % , to $38 billion. Similarly, those to small island developing States declined by 6 %, to $3.5 billion. Landlocked developing countries saw stable FDI, at $24 billion.

Flows to developed economies increased further, after significant growth in 2015. Inflows rose by 5 per cent to $1 trillion. A fall in FDI in Europe was more than compensated by modest growth in North America and a sizeable increase in other developed economies. Developed economies' share in global FDI inflows grew to 59 % [61]. FDI flows to transition economies almost doubled, to $68 billion, following two years of steep decline – reflecting large privatization deals and increased investment in mining exploration activities. Major economic groups, such as the G20 and APEC, strongly influenced global FDI trends. Inflows to the G20 reached a

record of more than $1 trillion for the first time. Intragroup FDI is a growing feature in some groups [61].

FDI outflows from developed countries remained weak. They declined by 11 % to $1 trillion, mainly owing to a slump in investments from European MNCs. Outflows from North America remained flat, but those from developed countries in Asia-Pacific reached their highest level since 2008. The flow of outward investment from developing economies registered a 1 % decline to $383 billion, despite a surge of outflows from China, now the second largest investing country in the world. Slower growth in international production contributed to lacklustre global trade expansion. International production by foreign affiliates of MNCs is still expanding, but the rate has slowed in recent years. The average annual growth rates over the last five years of foreign affiliate sales (7.3 %), value added (4.9 %) and employment (4.9 %) were all lower than in the equivalent period before 2010 (at 9.7 %, 10.7 %and 7.6 %, respectively) [61].

UNCTAD's new database on state-owned MNCs shows their growing role in the global economy. About 1,500 state-owned MNCs own more than 86,000 foreign affiliates. They announced greenfield investments accounting for 11 % of the global total in 2016, up from 8 % in 2010. Their headquarters are widely dispersed, with more than half in developing economies and almost a third in the European Union. China is the largest home economy [61]. Despite the movement toward privatizing industry and free trade, government interests in their

most valuable commodity, oil, remains constant. State-owned companies control more than 75% of all crude oil production, in contrast with only 10 percent for private multinational oil firms [61]. The list of the major global state-owned oil companies is represented in the Table 3.4.

Table 3.4 – The major global state-owned oil companies

Company	Country
Aramco	Saudi Arabia
Gazprom	Russia
China National Petroleum Corp.	China
National Iranian Oil Co.	Iran
Petroleos de Venezuela	Venezuela
Petrobras	Brazil
Petronas	Malaysia

In 2016, there were 100 000 multinational corporations with approximately 860 000 foreign affiliates dispersed around the globe [61]. 132 out of 500 largest corporations (26,4 %) are headquartered in USA. 109 out of 500 largest corporations (21,8 %) are headquartered in China [17].

Conclusions

1. Expanding business overseas means reaching new clients or customers and potentially boosting profits. At that time, corporations may encounter different challenges when going global such as company structure, law, cultural differences, etc.

2. There are many factors describing business environment in a certain economy. Business environment in a country plays a crucial role in choosing a place for headquartering a corporation. Bright leaders among the best countries for doing business are Switzerland, Canada, Australia, Denmark, Sweden, New Zealand, Singapore, Hong Kong, Korea, Ireland, and United Kingdom.

3. In 2016, there were 100 000 multinational corporations with approximately 860 000 foreign affiliates. 26,4 % of the largest corporations are headquartered in USA while in China this number accounts for 21,8 %. Totally, USA and China are the home countries for roughly a half of the world largest corporations.

End-of chapter tasks:

1. Reveal major challenges for international big corporations.
2. Define a headquarter, FDI, greenfield and brownfield investment strategies.
3. Describe approaches to indicating the best countries to headquarter a corporation.
4. Classify the countries according to the Doing business rank.
5. Relate FDI to the international corporations.
6. Comment on the situation with the global distribution tendencies of FDI.

CHAPTER 4. INTERNATIONAL CORPORATIONS AS GLOBAL ACTORS

4.1. Corporations vs Countries.
4.2. Fortune Global 500 and Forbes Ranks.
4.3. "Too Big to Fail" Corporations.
4.4. Global Corporate Networks.

Key words: revenue, profit, assets, employees, brands, giants.

4.1. Corporations vs Countries

Large corporations are an economic, political, environmental, and cultural force that is unavoidable in today's globalized world. Large corporations have an impact on the lives of billions of people every day. The growth of these corporations is typically measured in economic terms – profits, assets, number of employees and stock prices. However, the impact of global corporations extends well beyond the economic realm.

The production decisions of large firms have significant environmental implications at the national and global level. Corporations exert political influence to obtain subsidies, reduce their tax burdens and shape public policy. Corporate policies on working conditions, benefits and wages affect the quality of life of millions of people.

Big business is now the most powerful force in the world. In the words of Mark Powell, "Countries don't matter any more.

Corporations do. There is no need to worry who wins the next general election. Worry about who's running General Electric. Company presidents, not White House presidents, are finally in charge. Nearly as many people work for General Motors as live in Wales. Fewer than four hundred billionaires control as much capital as half the global population. Bill Gates alone is worth more than a hundred and thirty-five countries. Just three hundred corporations control 25 % of all the productive assets in the world. As cross-border trade increases, national frontiers become increasingly unimportant and global business begins to take over from government. Goodbye, United Nations! Hello, United Corporations!" [44].

Modern corporations are so large and influential that sometimes experts compare the economic magnitude of the world's largest corporations (expressed in revenue) to various mid-sized national economies (expressed in GDP). But is GDP really compatible to corporate revenue? There are serious conceptual problems with such comparisons because corporate revenue is not equivalent to GDP, which is measured in terms of value added. To make the comparison valid, the economic power of countries should also be measured in terms of revenue, tax revenue in particular. Revenue of the country is a sum of money that it has in its budget from taxation.

Following such logic, the NGO Global Justice Now revealed that in 2015 the world's top 100 economies comprised 31 countries only and 69 corporations already (Table 4.1).

Table 4.1 – Corporations vs countries [50]

№	Country/Corp.	Revenue, bns	Count. / Corp.		Revenue, bns
1	United States	$ 3251	35	Austria	$ 189
2	China	$ 2426	36	**Samsung Electronics**	$ 177
3	Germany	$ 1515	37	Turkey	$175
4	Japan	$ 1439	38	**Glencore**	$ 170
5	France	$1253	39	**Industr. &Comm. Bank of China**	$ 167
6	United Kingdom	$ 1101	40	**Daimler**	$ 166
7	Italy	$ 876	41	Denmark	$162
8	Brazil	$ 631	42	**UnitedHealth Group**	$ 157
9	Canada	$ 585	43	**CVS Health**	$ 153
10	**Walmart**	$ 482	44	**EXOR Group**	$ 153
11	Spain	$ 474	45	**General Motors**	$ 152
12	Australia	$ 426	46	**Ford Motor**	$ 150
13	Netherlands	$ 337	47	**China Construction Bank**	$ 148
14	**State Grid**	$330	48	**AT&T**	$ 147
15	**China National Petr.**	$299	49	**Total**	$ 143
16	**Sinopec Group**	$ 294	50	Argentina	$ 143
17	Korea, South	$ 291	51	**Hon Hai Precision Industry**	$ 141
18	**Royal Dutch Shell**	$ 272	52	**General Electric**	$ 140
19	Mexico	$ 260	53	**China State Construction Eng.**	$ 140
20	Sweden	$ 251	54	**AmerisourceBergen**	$ 136
21	**Exxon Mobil**	$ 246	55	**Agricultural Bank of China**	$ 133
22	**Volkswagen**	$ 237	56	**Verizon**	$ 132
23	**Toyota Motor**	$ 237	57	Finland	$ 131
24	India	$ 236	58	**Chevron**	$ 131
25	**Apple**	$ 234	59	**E.ON**	$ 129
26	Belgium	$ 227	60	**AXA**	$ 129
27	**BP**	$ 226	61	Indonesia	$ 123
28	Switzerland	$ 222	62	**Allianz**	$ 123
29	Norway	$ 220	63	**Bank of China**	$ 122
30	Russia	$ 216	64	**Honda Motor**	$ 122
31	**Berkshire Hathaway**	$ 211	65	**Japan Post Holdings**	$ 119
32	Venezuela	$ 203	66	**Costco**	$ 116
33	Saudi Arabia	$ 193	67	**BNP Paribas**	$ 112
34	**McKesson**	$ 192	68	**Fannie Mae**	$ 110

The outcomes of this investigation allow us to make such conclusions:

1. Walmart is now bigger than Australia.
2. Royal Dutch Shell is richer than India.
3. Volkswagen is richer than Turkey.
4. Honda is richer than United Arab Emirates.
5. Apple is richer than Russia.
6. BP is richer than Turkey.
7. Ford Motor is bigger than Argentina.
8. General Electric is richer than Finland.
9. Chevron is bigger than Indonesia.
10. BMW is richer than Portugal.

Size alone may not guarantee competitiveness, but to go from innovation to mass production quickly and efficiently takes a big company with substantial resources and aggressive marketing strategy. In the words of Andrew Grove, former head of Intel: "We don't beat the competition, we crush it" [44]. Nowadays, more than ever, big is beautiful.

4.2 Fortune Global 500 and Forbes Ranks

Fortune Global 500 rank. The Fortune Global 500 is the annual ranking of the largest 500 corporations worldwide. According to the Fortune Global 500 rank, the revenues of the world's 500 largest corporations are equivalent to 37% of world gross domestic product. In 2017, the world's 500 largest companies generated $28 trillion in revenues and $1.5 trillion in

profits. Together, they employ 67 million people worldwide and are represented by 34 countries. Several approaches are used to rank the world's largest corporations:

1. By revenue (sales).
2. By profit (most profitable corporations).
3. By employees (biggest employers).
4. By assets.

Ranking by revenue approach. Revenue figures include consolidated subsidiaries and reported revenues from discontinued operations, but exclude excise taxes. For banks, revenue is the sum of gross interest income and gross noninterest income. For insurance companies, revenue includes premium and annuity income, investment income, realized capital gains or losses, and other income, but excludes deposits.

Table 4.2 – Top-20 largest corporations in 2017 ranked by revenue [17]

№	Corporation (industry)	Revenue	Country
1	Wal-Mart (retail)	486 $ bil.	USA
2	State Grid (energy)	315 $ bil.	China
3	Sinopec Group (energy)	268 $ bil.	China
4	China National Petroleum (energy)	263 $ bil.	China
5	Toyota Motor (motor vehicles)	255 $ bil.	Japan
6	Volkswagen (motor vehicles)	240 $ bil.	Germany
7	Royal Dutch Shell (energy)	240 $ bil.	Netherlands
8	Berkshire Hathaway (investment)	223 $ bil.	USA
9	Apple (technologies)	216 $ bil.	USA
10	Exxon Mobil (energy)	205 $ bil.	USA
11	McKesson (pharmaceuticals)	199 $ bil.	USA

Continuation of Table 4.2

№	Corporation	Revenue	Country
12	BP (energy)	187 $ bil.	United Kingdom
13	United Health Group (healthcare)	185 $ bil.	USA
14	CVS Health (pharmaceuticals)	178 $ bil.	USA
15	Samsung Electronics (electronics)	173 $ bil.	South Korea
16	Glencore (mining)	173 $ bil.	Switzerland
17	Daimler (motor vehicles)	169 $ bil.	Germany
18	General Motors (motor vehicles)	166 $ bil.	USA
19	AT&T (telecommunication)	164 $ bil.	USA
20	EXOR Group (financials)	156 $ bil.	USA

Ranking by profit approach. Profits are shown after taxes, extraordinary credits or charges, cumulative effects of accounting changes, and non-controlling (minority) interests, but before preferred dividends.

Table 4.3 – Top-20 largest corporations in 2017 ranked by profit [17]

№	Corporation (industry)	Profit	Country
1	Apple (technologies)	46 $ bil.	USA
2	Industrial & Commercial Bank of China	42 $ bil.	China
3	China Construction Bank	35 $ bil.	China
4	Agricultural Bank of China	28 $ bil.	China
5	Bank of China	24 $ bil.	China
6	J.P. Morgan Chase (banking)	24 $ bil.	USA
7	Berkshire Hathaway (investment)	24 $ bil.	USA
8	Wells Fargo (banking)	22 $ bil.	USA
9	Alphabet (internet services)	19 $ bil.	USA
10	Samsung Electronics (electronics)	19 $ bil.	South Korea
11	Bank of America Corp.	18 $ bil.	USA
12	Toyota Motor (motor vehicles)	16 $ bil.	Japan

Continuation of Table 4.3

№	Corporation	Profit	Country
13	Microsoft (computer software)	16 $ bil.	USA
14	Johnson & Johnson (pharmaceut.)	16 $ bil.	USA
15	Citigroup (banking)	14 $ bil.	USA
16	Gazprom (energy)	14 $ bil.	Russia
17	Wal-Mart (retail)	13 $ bil.	USA
18	Gilead Sciences (healthcare)	13 $ bil.	USA
19	SoftBank Group	13 $ bil.	Japan
20	Verizon (telecommunications)	13 $ bil.	USA

Ranking by employees approach. The figure shown is either a fiscal year-end or yearly average number, as published by the company. Where the breakdown between full- and part-time employees is supplied, a part-time employee is counted as one half of a full-time employee.

Table 4.4 – Top-20 largest corporations in 2017 ranked by the number of employees [17]

№	Corporation (industry)	Employees	Country
1	Wal-Mart (retail)	2,3 mln	USA
2	China National Petroleum (energy)	1,5 mln	China
3	China Post Group (delivery)	941,211	China
4	State Grid (energy)	926,067	China
5	Hon Hai Precision Industry (electronics)	726,772	Taiwan
6	Sinopec Group (energy)	713,288	China
7	Volkswagen (motor vehicles)	626,715	Germany
8	U.S. Postal Service (transportation)	574,349	USA
9	Compass Group (HoReCa)	527,180	Britain
10	Agricultural Bank of China	501,368	China
11	Gazprom (energy)	467,400	Russia
12	China Mobile Communications	463,712	China

Continuation of Table 4.4

№	Corporation (industry)	Employees	Country
13	Industrial & Commercial Bank of China	461,749	China
14	Deutsche Post DHL Group (transport.)	459,262	Germany
15	Aviation Industry Corp. of China	457,097	China
16	Kroger (food)	443,000	USA
17	Jardine Matheson (vehicles)	430,000	China
18	Sodexo (HoReCa)	425,594	France
19	China Resources National (pharmaceut.)	420,572	China
20	IBM (information technology)	414,400	USA

Ranking by assets approach. Assets shown are those at the company's fiscal year-end. Stockholders' equity is the sum of capital stock, paid-in capital, and retained earnings on the same date. Noncontrolling (minority) interest is not included.

Table 4.5 – Top-20 largest corporations in 2017 ranked by the value of assets [17]

№	Corporation (industry)	Assets	Country
1	Industrial & Commercial Bank of China	3,4 $ mln	China
2	Fannie Mae (financials)	3,3 $ mln	USA
3	China Construction Bank	3,0 $ mln	China
4	Agricultural Bank of China	2,8 $ mln	China
5	Mitsubishi UFJ Financial Group (banking)	2,7 $ mln	Japan
6	Japan Post Holdings (insurance)	2,63 $mln	Japan
7	Bank of China	2,61 $mln	China
8	J.P. Morgan Chase (banking)	2,5 $ mln	USA
9	HSBC Holdings (banking)	2,3 $ mln	Britain
10	BNP Paribas (banking)	2,2 $ mln	France
11	Bank of America Corp.	2,1 $ mln	USA
12	Freddie Mac (financials)	2,0 $ mln	USA
13	Wells Fargo (banking)	1,9 $ mln	USA

Continuation of Table 4.5

№	Corporation (industry)	Assets	Country
14	Mizuho Financial Group (banking)	1,8$ mln	Japan
15	Citigroup (banking)	1,79$ mln	USA
16	Sumitomo Mitsui Financial Group	1,77$ mln	Japan
17	Deutsche Bank	1,7$ mln	Germany
18	Credit Agricole (financials)	1,6$ mln	France
19	Barclays (banking)	1,5$ mln	Britain
20	Societe Generale (banking)	1,4$ mln	France

Forbes rank. In 2017, the Forbes estimated and revealed the world's most valuable corporate brands. According to the Forbes rank, cumulative value for top 100 brands is worth $ 1,95 trillion [41]. Top-30 brands are shown in Table 4.6.

Table 4.6 – Most valuable corporate brands in 2017 according to the Forbes [41]

Rank	Brand	Brand value	Industry
1	Apple	$ 170,0 B	Technology
2	Google	$ 101,8 B	Technology
3	Microsoft	$ 87,0 B	Technology
4	Facebook	$ 73,5 B	Technology
5	Coca-Cola	$ 56,4 B	Beverages
6	Amazon	$ 54,1 B	Technology
7	Disney	$ 43,9 B	Leisure
8	Toyota	$ 41,1 B	Automotive
9	McDonald's	$ 40,3 B	Restaurants
10	Samsung	$ 38,2 B	Technology
11	General Electric	$ 37,9 B	Diversified
12	AT&T	$ 36,7 B	Telecom
13	IBM	$ 33,3 B	Technology

Continuation of Table 4.6

Rank	Brand	Brand value	Industry
14	Intel	$ 31,4 B	Technology
15	Cisco	$ 30,7 B	Technology
16	Nike	$ 29,6 B	Apparel
17	Mercedes-Benz	$ 29,2 B	Automotive
18	Oracle	$ 29,2 B	Technology
19	Verizon	$ 28,9 B	Telecom
20	Louis Vuitton	$ 28,8 B	Luxury
21	BMV	$ 28,7 B	Automotive
22	Budweiser	$ 24,6 B	Alcohol
23	American Express	$ 24,5 B	Financial services
24	Wal-Mart	$ 24,1 B	Retail
25	Marlboro	$ 24,1 B	Tobacco
26	Honda	$ 24,0 B	Automotive
27	SAP	$ 23,8 B	Technology
28	Visa	$ 21,4 B	Financial services
29	Gillette	$ 19,2 B	Consumer goods
30	Pepsi	$ 18,2 B	Beverages

Cross-country analysis [41] shows that 56 out of 100 the most valuable brands are represented by USA, 11 brands – by Germany, 7 brands – by France, 6 brands – by Japan, 4 brands – by Switzerland, 3 brands – by Spain. Belgium, Korea, Netherlands and Sweden have 2 valuable brands each, while Austria, China, Denmark, Ireland and United Kingdom have 1 brand respectively. Top brands are distributed by industries in the following way: technology – 18 brands; financial services – 13 brands; consumer packaged goods – 12 brands; automotive – 11 brands; retail – 10 brands; luxury – 7 brands; beverages and diversified – 4 brands; alcohol, restaurants and telecom – 3

brands; apparel, leisure, media and transportation – 2 brands; aerospace, business services, heavy equipment and tobacco – 1 brand.

4.3. "Too Big to Fail" Corporations

Too big to fail is a company that's so essential to the global economy that its failure would be catastrophic. Big doesn't refer to the size of the company. Instead, it means it's so interconnected with the global economy that its failure would be a big event.

The Bush administration popularized this phrase during the 2008 financial crisis. It describes why it must bail out some companies to avoid economic collapse. These included financial firms that had relied on derivatives to gain a competitive advantage when the economy was booming. When the housing market collapsed, their investments threatened to bankrupt them. That's when they became too big to fail [29].

The first bank that was too big to fail was *Bear Stearns*. On March 2008 the Federal Reserve lent $30 billion to JPMorgan Chase to buy the failing investment bank. Bear was a small bank but very well-known. The Fed worried that Bear's failure would destroy confidence in other banks.

Lehman Brothers was an investment bank. It wasn't a big company, but the impact of its bankruptcy was alarming. In 2008, Treasury Secretary Hank Paulson said no to its bailout. It filed for bankruptcy. On the following Monday, the

Dow dropped 350 points. By Wednesday, financial markets panicked. That threatened the overnight lending needed to keep businesses running. The problem was beyond what monetary policy could do. That meant a $700 billion bailout was necessary to recapitalize the major banks.

Citigroup received a $20 billion cash infusion from Treasury. In return, the government received $27 billion of preferred shares yielding 8 percent annual return. It also received warrants to buy no more than 5 percent of Citi's common shares at $10 per share.

The investment banks *Goldman Sachs* and Morgan *Stanley* were also too big to fail. The Fed bailed them out by allowing them to become commercial banks. That meant they could borrow from the Fed's discount window. They could take advantage of the Fed's other guarantee programs intended for retail banks. That ended the era of investment banking made famous by the movie, "Wall Street".

The mortgage giants, *Fannie Mae* and *Freddie Mac*, were really too big to fail. That's because they guaranteed 90 percent of all home mortgages by the end of 2008. Treasury underwrote $100 million in their mortgages, in effect returning them to government ownership. If Fannie and Freddie had gone bankrupt, the housing market would have collapsed. That's because banks would not lend without government guarantees.

The *American International Group* was one of the world's largest insurers. Most of its business was traditional insurance

products. When it got into credit default swaps, it got into trouble. These swaps insured the assets that supported corporate debt and mortgages. If AIG went bankrupt, it would trigger the failure of the financial institutions that bought these swaps. AIG's swaps against subprime mortgages pushed it to the brink of bankruptcy. As the mortgages tied to the swaps defaulted, AIG was forced to raise millions in capital. As stockholders got wind of the situation, they sold their shares, making it even harder for AIG to cover the swaps. Even though AIG had more than enough assets to cover the swaps, it couldn't sell them before the swaps came due. That left it without the cash to pay the swap insurance. The Federal Reserve provided an $85 billion, two-year loan to AIG to further stress on the global economy. In return, the government received 79,9 percent of AIG's equity and the right to replace management. It also received veto power over all important decisions, including asset sales and payment of dividends. In October 2008, the Fed hired Edward Liddy as CEO and Chairman to manage the company.

The plan was for the Fed to break up AIG and sell off the pieces to repay the loan. But the stock market plunge in October made that impossible. Potential buyers needed any excess cash for their balance sheets. The Treasury Department purchased $40 billion in AIG preferred shares from its Capital Repurchase Plan. The Fed bought $52,5 billion in mortgage-backed securities. The funds allowed AIG to retire its credit default swaps rationally, saving it and much of the financial industry

from collapse. The AIG Bailout became one of the largest financial rescues in U.S. history.

4.4. Global Corporate Networks

A surprisingly small number of corporations control massive global market shares. There are several huge corporations in the world that spin global networks acquiring more and more companies [58]. The examples of such corporations are shown below.

Media giants. A huge company *Comcast Corporation* owns: MSNBC, NBC Universal, MLB Network, E!Entertainment, Golf Channel, Xfinity, AT&T Broadband.

A large company *Walt Disney* owns: ABC, ESPN, Pixar, Marvel Comics, Touchstone Pictures, Lucasfilm, Walt Disney Records, Hollywood Records, Disney Music Publishing, The Baby Einstein Company, 50% of A&E Networks.

The *Time Warner Company* owns: HBO, Time (Southern Living, Sports Illustrated, Time, Golf Magazine, Health, Entertainment Weekly), IPC Media, Grupo Editorial Expansion, Turner Broadcasting (TNT, TruTV, TBS, TCM, NBC, Cartoon Network, March Madness, CNN), Warner Bros. Picture Group.

Corporation *Viacom* owns: Paramount Pictures, MTV, VH1, BET, Nickelodeon, Spike, Comedy Central.

News Corp owns: News Corp Australia, News UK, Dow Jones, New York Post, Harper Collins Publishers, Storyful, Move.

Food and beverage companies. A corporation *PepsiCo* Inc makes Gatorade, Propel, Pepsi, Aquafina, Sobe, Mountain Dew, Sierra Mist, Cheetos, Doritos, Frito Lay, Funyun's, Lay's, Ruffles, Tostitos, Quaker, Amp Energy, Lipton, Rockstar Energy, Seattle's Best Coffee, Starbucks: Doubleshot, Frappucino, Iced Coffee.

The world's largest chicken processor *Tyson Foods Inc* supplies: KFC, Taco Bell, McDonalds, Burger King, Wendy's, Wal-Mart, Kroger, IGA, Beef O'Grady's.

Nestle (in USA and Canada) owns 74 brands of water and 38 brands of ice cream including Haagen-Dazs, Dreyer's and Nestle Drumstick; frozen food: Stouffers, Lean Cuisine, Hot Pockets, Tombstone Pizza, DiGiorno Pizza, California Pizza Kitchen; candy: Wonka brands, Baby Ruth, Chips Ahoy!, Goobers, Icebreakers; pet food: Alpo, Beneful, Fancy Feast, Friskies, Gourmet, Mighty Dog, ONE, Pro Plan, Purina, Tidy Cats; cosmetics: 30% share in L'Oreal, Garnier, Maybelline, and Lancome, and The Body Shop Stores.

JBS USA, a subsidiary of the world's largest beef processor, has beef brands: Swift, G.F. Swift 1855 Brand Premium Beef, Aspen Ridge Natural Beef, Swift Black Angus, Cedar River Farms, 5 Star Beef, Chef's Exclusive, Showcase Premium Ground Beef; chicken brands: Pilgrim's, Pierce Chicken, Wing Dings, Wing Zings, Speed Grill, Country Pride, To-Ricos; pork brands: 1855 Premium Pork, Swift Premium Dry Rubbed Pork, Swift Premium Natural Guaranteed Tender Pork, Swift Premium Natural Pork, Swift La Herencia Natural Pork.

A beer corporation *Anheuser-Busch InBev* produces over 200 brands made in 30 countries and sold in 130 countries including: St. Pauli Girl, Stella Artois, Spaten, Rolling Rock, Michelob, Hoegaarden, Busch, Budweiser, Bud Light, Beck's, Bass.

Oil giants. The top five oil producing companies produce almost twice what the US's refined petroleum product consumption per day is. *Saudi Aramco* (Saudi Arabia) produces 12,5 million barrels a day. *Gazprom* (Russia) produces 9,7 million barrels per day. *National Iranian Oil Co*. (Iran) produces 6,4 million barrels per day. *ExxonMobil* (America) produces 5,3 million barrels per day. *PetroChina* produces 4,4 million barrels per day [51].

Most experts admit that corporations rule just about everything around us. Big companies supply our cars, gas, food and even our politicians. Recent studies show [21] that somewhere on the order of 147 companies have a hand in just about everything on the Earth. And among these select few, there are a small handful of companies that have roughly enough money and influence to apply for membership to the UN, which would be kind of superfluous since they can buy their way to the top of just about any country they want. Among such giant corporations there are General Electric, Barclays, Moody's, News Corp, and Monsanto.

General Electric is a global digital industrial company. The Company's products and services range from aircraft engines, power generation, and oil and gas production equipment to

medical imaging, financing and industrial products. The Company's segments include Power, Renewable Energy, Oil & Gas, Aviation, Healthcare, Transportation, Energy Connections & Lighting, and Capital. As of December 31, 2016, the Company served customers in approximately 180 countries [18].

Barclays is a British multinational investment bank and financial services company headquartered in London. Apart from investment banking, Barclays is organized into four core businesses: personal banking, corporate banking, wealth management, and investment management [5].

Moody's is an American business and financial services company. It is the holding company for Moody's Investors Service (MIS), an American credit rating agency, and Moody's Analytics (MA), an American provider of financial analysis software and services [38].

Monsanto is a multinational agricultural biotechnology corporation based in the United States. Monsanto is also the largest producer of genetically engineered (GE) seeds on the planet, accounting for over 90% of the GE seeds planted globally [59].

Conclusions

1. Large corporations are an economic, political, environmental, and cultural force that is unavoidable in today's globalized world. Large corporations have an impact on the lives of billions of people every day. The growth of these corporations is typically measured in economic terms – revenues, profits, assets, and number of employees.

2. Corporate performance is tracked by two authoritative ranking agencies – Forbes and Fortune 500. According to the Fortune Global 500 rank, the revenues of the world's 500 largest corporations are equivalent to 37% of world gross domestic product.

3. Too big to fail is a company that's so essential to the global economy that its failure would be catastrophic. Big doesn't refer to the size of the company. Instead, it means it's so interconnected with the global economy that its failure would be a big event.

4. A surprisingly small number of corporations control massive global market shares. There are several huge corporations in the world that spin global networks acquiring more and more companies.

End-of-chapter tasks:

1. Compare countries with corporations.
2. Rank corporations by revenue approach.

3. Classify corporations by size of profit.
4. Evaluate corporations by the value of assets.
5. Apply Forbes approach to classify corporations.
6. Explain “too big to fail” principle.
7. Detect corporations that control massive market shares.

CHAPTER 5. INTERNATIONAL BUSINESS COMBINATIONS

5.1. Types of Business Combinations.
5.2. International Pools and Cartels.
5.3. International Holding Companies.

Key words: trade associations, chambers of commerce, pools, cartels, trusts, holding companies, community of interests, mergers, amalgamations.

5.1. Types of Business Combinations

There are many reasons for business combinations. Most of them are as follows [8]:

1. **Elimination of competition.** Due to growth of competition among firms, the rate of margin decreases. Under such circumstances, small enterprises cannot survive. Therefore, the only solution available to the competing firms – to eliminate competition through business combination.

2. **Expansion of business.** Small units of business face the problem of capital shortage which prevents business expansion. A business combination can easily attract capital to expand business business, buy new machinery, switch to large-scale production, use new and improved technologies and create research departments.

3. **Effective management.** Usually, small units of business cannot afford the services of experienced and qualified

employees. So, business combination is formed to hire services of those employees who are experts in the management of the company.

4. **Market domination.** Business units also combine to dominate the entire market and create monopoly. By dominating the market, the combined firms can sell their products at higher rates and earn maximum profit.

5. **Economic instability.** Frequent changes in government policies increase uncertainty among businessmen. They may, therefore, join together in a more formalized manner to protect themselves against the impact of uncertain policies of the government.

6. **Trade cycle.** During the period of depression, new firms are not willing to enter into industry and even the small existing firms cannot survive. Therefore, the small existing firms are willing to go for the technique of business combination to ensure their survival.

7. Influence of tariffs. The Governments throughout the world offer protection to home industries by imposing high custom duties on imported goods. Imposition of tariffs restricts foreign competition which increases competition among home industries. Consequently, the increase of competition among home industries leads to business combination.

There are top three forms of business combinations which are depicted in Fig. 5.1.

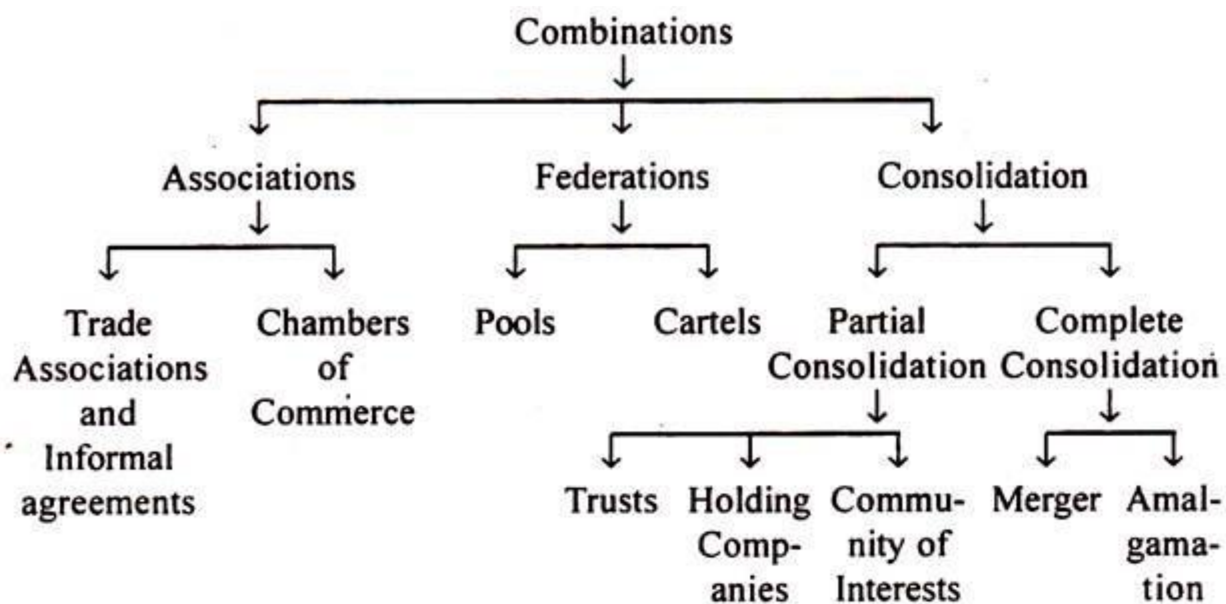

Figure 5.1 – Forms of business combinations [54]

Associations. These are voluntary organizations of traders and businessmen formed to protect and promote their common interests through collective efforts. They act as self-regulators of trading policies and practices. They also act as spokesmen of commercial interests in representation to the Government on all vital matters affecting trade.

Associations are of two categories:

1. Trade associations.

2. Chambers of commerce.

Trade associations and chambers of commerce are necessarily the outcome of developments in the field of trade, commerce and industry after the Industrial Revolution.

Trade associations. Trade association may be defined as voluntary organization for mutual protection or advantage of independent enterprises producing or distributing similar goods

or services [54]. It is an organization formed to promote the mutual interests of individuals or companies engaged in the same kind of business. Members of a trade association are usually competitors. It is a non-profit organization which attempts to promote the interests of its members. It does not enter into any business transactions on its own account. The name of the association is usually after the nature to business conducted by its members. It tries to enroll as members all those engaged in the same line of business in a particular region. It does not involve loss of independence of its members who are free to conduct their business as they please.

Functions of the trade associations [54]:

1. Provision of market information to its members.

2. Supply of legal advice to its members in matters like customs regulations and factory legislation.

3. Safeguarding of credit and strengthening the hands of their members in collective bargaining.

4. Maintaining technical staff who are constantly engaged in research, testing and standardizing the various processes of production.

5. Maintaining trade missions. These trade missions explore the possibilities of new markets and study the causes of the loss or relative decline of old markets in different parts of the world.

6. Most of these associations form special committees to study the employment situation. These committees scrutinize

demands put forth by the trade unions, enforce the agreements reached between employers and employees.

7. They collect, compile, analyze and disseminate business and technical information.

8. They engage themselves in legislative lobbying and try to influence legislation by educating public opinion in various ways.

9. Some of the large associations maintain their research sections.

10. They supply legal, economic and technical information to their members.

11. They send their representatives to serve on various statutory boards and committees.

12. They try to bring uniformity into the system of cost accounting.

13. It is always advantageous to exchange information about the creditworthiness of customers served by various undertakings. A large number of associations undertake this work.

14. It is necessary for the manufacturers, wholesalers and retailers to know the changes in the tastes, fashions or buying habits of the consumers.

15. Many trade associations set up central selling agencies and debt collection departments for the benefit of their members.

Chambers of commerce. A chamber of commerce is an association of merchants, financiers, manufacturers and others

engaged in business in a particular locality or region for promoting the general commercial interests of all the members [54]. Chambers of commerce work to protect the interests of their members and foster the growth and development of commerce and industry of the respective regions in which they operate. They are formed to promote and protect general trade interests of all the members irrespective of the kind or class of trade they are engaged in. In regard to the formation of a chamber of commerce, there is some difference between some of the European countries on the one hand and countries like India, England, the USA etc. on the other. For example, in France, a chamber of commerce is established by the law and is subject to government control. It is financed by government subsidy or special tax payable by all traders of the district of the region covered by it. Contrary to this, in India, England, the USA, etc. it is the creation of private initiative and is "purely a private and voluntary institution". It has no financial resources other than collections through membership dues and small incidental earnings.

Voluntary chambers of commerce are formed in the same way as trade associations. They elect a board of directors in the annual general body meeting of the members. The board elects from among its members a president and a vice-president. The board also forms various subcommittees in charge of different functions or to look after the interests of different traders.

Functions of chambers of commerce may be broadly divided into two groups [54]:

1. Technical and administrative services for the members and the commercial class.

2. Representation of the business community before the government.

Technical and administrative services. It has been said above that in some of the European countries, like France, chambers of commerce are semi-official organizations, whereas in our country, in England, the USA, etc. they are voluntary associations. This difference gives rise to some variation in the functions of the two kinds of chambers as well.

In France, for example, chambers of commerce perform the following technical and administrative functions [54]:

1. They manage and own stock exchanges, employment exchanges, docks, warehouses, commercial schools, museums and libraries.
2. They prepare reports on the development of trade.
3. They issue export certificates and certificates of origin.
4. They appoint experts, inspectors, accountants and commercial arbitrators.

Functions of chambers in England, the USA, India etc. are limited in nature, their functions may be summarized as given below [54]:

1. They provide information on traffic routes and methods of packing for foreign shipping.

2. They collect and disseminate information on general trade conditions and the existing and potential markets.

3. They help the members in exchanging notes on the creditworthiness of their customers.

4. They try to secure for the trade improved transportation at lower freight rates.

5. They act as centers for collecting claims.

6. Many of them maintain research establishments.

7. They make arrangements for labor supply.

8. They try to introduce standardized methods of trade.

9. They undertake general publicity work like advertising etc.

10. They provide for commercial arbitration.

Representation of business community before the government. In France, they have “formal contacts” with the government. They send their representatives on the legislative council and other official committees. Government receives from the chambers reports, advice and proposals for enacting any law [54].

In England, the USA, India, etc. chambers approach the government unofficially. They engage in lobbying, try to bring political pressure, send representations and give general publicity to their views on matters pertaining to the commercial interests. All these activities are directed to get a favourable budget, laws, etc. passed, or to see that unfavourable legislation does not get the support of the legislature. Thus, they function outside the ordinary legislature to influence legislation [54].

Apart from lobbying and bringing political pressure on the government, they perform the following functions [54]:

1. They act as spokesmen of the business community and express their views on such policies of the government as are likely to affect their interests.

2. They make representation to the government against an existing piece of legislation or a proposed legislation and make suggestions for legislation necessary for the promotion and development of commerce and industry.

3. They support candidates for elections to the legislatures.

Federations. Federation means association of firms engaged in the same business with a formalized agreement to follow certain policies in common so as to reduce the intensity of wasteful competition in the respective business line. It is, in other words, an alliance of competing firms into a federal framework [54].

The principle of federation means the federating units, while retaining their identity and autonomy, are bound by a common agreement on one or some aspects of their business policies. In their internal structure, each of the units has full autonomy, independence of decision and action. But in some of their external transactions, they agree to abide by commonly carved out policies or decisions in the collective interest of all of them [54].

A central organization is constituted on which certain agreed rights of decisive action are conferred. They may agree to charge uniform price or stick to some price range, or allocate the markets among the members or to regulate production of output by assignment of quotas to the firms so that there will not

be overproduction. Avoidance of competition, monopolistic control over the market, realization of economies of scale and adjustment of output to demand are also the prime objectives of federal combinations. The rights and obligations of members and powers of the central body of the federation are governed by a definite agreement [54].

Federations are of two types:

1. Pools.
2. Cartels.

Pools. A pool is a horizontal type of combination intended to regulate the market price by collective agreement on factors that influence the price. It is a federal union of competing units handling the same business created and operated in accordance with a specific agreement for mutual benefit. Each firm retains its separate entity. Its autonomy is recognized. But the pool agreement envisages certain working arrangements for the set purposes such as to share the markets, to restrict the output, control the prices, etc. The objectives are therefore mainly to exert control over price, regulate production, equitably apportion the market and maximize the profit [54].

Cartels. A cartel is an association of independent firms agreeing amongst themselves to regulate their output, divide the market, centralize the sales and determine common pricing policies that would be of maximum benefit to all the members. Its members are engaged in the same type of business, and hence it is formed primarily to root out or limit the interfirm competition in the particular line of business. It can be described

as a syndicate for centralized marketing with the pooling of output contributed by members as per the (cartel) agreement [54].

Consolidation. Consolidation is of two types:

1. Partial consolidation.
2. Complete consolidation.

Partial Consolidation. Partial consolidation means coming together of firms under formalized common ownership and control while retaining their separate entity [54]. Obviously, their objective is to avoid competition by integrated management of the firms as one unit. We study briefly three types of partial consolidation: trusts, holding companies and community of interests.

Trusts. A trust is the partial consolidation of firms either horizontally or vertically or both in order to obtain the benefits of integrated management and centralized control. Trust is usually registered as a general association under Trust Act. Under the trust arrangement, the shareholders of different companies agree to transfer their shares to a Board of Trustees in exchange for trust certificates issued by the Board. These trust certificates represent the equitable interests of the holders in the property, assets and profits of the business entrusted to the charge of the Board of Trustees [54].

Features of trusts [54]:

1. Separate identity of companies is formally maintained.

2. Controlling interest of central companies is transferred to a Board of Trustees. This Board actually acts as the top management of the constituent companies.

3. Trusts are registered bodies and they issue trust certificates to the shareholders of the companies who agree to part with their shares.

4. Dividends, declared by the companies, are pooled together, and the net proceeds are distributed among the trust certificate holders in proportion to their holdings.

5. Trusts may be organized horizontally to avoid competition or vertically to be self-sufficient in all the requirements for keeping up the continuity in production.

Benefit of trusts [54]:

1. Trusts are more stable form of business combinations to combat competition of wasteful character.

2. Unified management of constituent companies by the trust leads to scientific planning of production, sales, finance, etc. and more effective control of business operations.

3. Efficient managerial coordination and control are facilitated with all the commercial advantages without affecting the separate legal entity of the component concerns and the dividend rights of the shareholders turned trust certificate holders.

4. Union of several companies under the trust gives wider scope for realizing economies of large-scale operations in respect of centralized purchase, bulk-selling, integrated management, etc.

5. The trust can scrap the inefficient plants owned by any component unit thus reducing the burden of overhead costs and superfluous installed capacity.

6. Trusts can select and assign standard plants to superior production. Thus quality of product is improved while supply is adjusted to the expected level of demand.

7. Benefits of economies in production and management can be passed on to the consumers in the form of reduced prices and improved quality of goods.

Limitations of trusts [54]:

1. There may arise friction and tussle within the trust, i.e., among the constituent firms. Unresolved continuous infight may lead to collapse of the entire trust.

2. Trusts lead to concentration of economic power and wealth in few hands.

3. Trusts tend to exploit the consumers by restricting the output and raising the prices without rhyme or reason.

4. It may become hard to effectively manage the business of several component companies.

5. The government is very often compelled to interfere in the business for controlling the trust to protect the interests of consumers. Shermon Anti-Trust Laws in the USA, Monopoly Control in the UK, Monopolies and Restrictive Trade Practices Act in India, etc. are some of the examples.

Holding companies. Holding company is a more integrated form of business combination whereby control of several companies is vested in one company through transfer of

ownership rights. Holding company is a company which acquires controlling interest through transfer or direct purchase of shares in other companies. Such other companies are called subsidiary companies [54].

Community of interests. Community of interests is an arrangement under which control over different companies is exercised by the same group of directors, managers, shareholders without any formal central organization [54]. Different companies appear to be under separate control but in effect their business policies are all shaped and executed by common directors, managers, etc.

Features of the community of interests [54]:

1. Separate identity of the companies is retained.
2. The management of the different companies is formally vested in respective Boards of Directors.
3. Uniform decisions, policies or plans are all made and acted upon for the companies by common managers, directors.
4. There is no central organization to control the functioning of the companies, unlike pool or cartel.

Community of interests is brought about mainly by three devices [54]:

1. Managerial integration.
2. Administrative integration.
3. Financial integration.

Managerial integration. It occurs when a large number of companies are under the same group of managing agents, managers, secretaries and treasurers. Managing Agency System

which prevailed in India for several decades was a peculiar form of vertical arid horizontal combination [54].

Administrative integration. It means the existence of common directors on the Boards of Directors of several companies. Administrative Policies thus have a common touch to the overall benefit of all the companies comprising the group. This integration is brought about by multiple directorships and interlocutory directorship. Multiple directorship, obviously, means that a group of persons holds directorships in many companies. Interlocutory Directorship means interlinking of two or more firms by virtue of common directorships. Due to influence exerted by common directors, concerned companies tend to blend into one another in respect of policies of common interests [54].

Financial integration. It is common that leading industrial houses hold controlling interests in financial institutions like banks, insurance companies, investment trusts, etc. These financial institutions are eventually persuaded or led to lend or invest in allied concerns. Financial integration is also brought about by intercorporate investments. Integration of this type in Indian industry is found between different firms engaged in the same business, or firms belonging to different groups or between manufacturing, marketing and financing companies [54].

Complete consolidation. It occurs when two or more concerns combine to transfer their assets and liabilities to a new company or when one company absorbs another concern by

outright purchase of its business. Complete consolidation thus means the end of separate identity of constituent units and their amalgamation into a single unit [54].

Complete consolidation is brought about in two forms:

1. Mergers.
2. Amalgamations, or acquisitions.

Mergers and acquisitions are subject to analysis in the Chapter 6.

5.2. International Pools and Cartels

A pool is a written agreement made by members dealing in similar products. It is a form to avert competition among firms. Under this system the firm's entities remain the same [8].

Characteristics of pools [54]:

1. Union of firms operating in the similar field of business.
2. A written agreement binding on all the federating firms.
3. Retention of distinct identity of the combining firms, and autonomy in their internal management.
4. Collective regulation of output or market, or centralized disbursement of income or profits.
5. Administrative arrangement through a central organization to pursue or manage the objectives underlined in the pool agreement.

Types of pools:

1. **Output pool** – it is an agreement whereby each member firm is expected to limit its output to a predetermined quota. The

pool organization estimates the aggregate demand and calculates the necessary output to be produced. Then quotas are allotted to each firm in the pool. No firm is permitted to produce more than the output quota fixed for it. Quota is fixed according to the capacity of the firm, past sales, probable future trends in the market, etc. The basic objective of output pool is to avert overproduction and consequent depressing effect on market price. If any firm produces more than the percentage permitted under its quota, it has to pay an agreed sum for the excess output into the common pool [54].

2. **Market pool** is concerned with equitable allocation of market territories to the member firms with a view to maximize benefit for each of them. No firm will be allowed to encroach on the markets of other firms. Thus competitive scramble for markets trying to undercut the other is sought to be avoided by clear-cut assignment of sales jurisdiction to each firm. Market may be divided into product-wise, area-wise or customer-wise. Pool organization has to carefully and objectively fix the market areas to different firms, depending on their past performance, goodwill, nature and quality of their output, proximity of customers, etc. [54].

3. **Income or profits pool** is an agreement whereby the members undertake to contribute to the common pool the profits earned by them. The minimum price is specified as to cover the normal costs of production. The difference between the selling price and minimum price is paid into the central pool. The profits or earnings so pooled are distributed among members

after deducting expenses of the pool in agreed proportion usually based on capital or output [54].

4. Traffic pool is an agreement among transport companies under which certain fare and freight concessions are granted to those who use the transport services of the pool members. Traffic pools are common mostly among shipping companies. The objective is to avoid undesirable competition [54].

Advantages of pools [54]:

1. Full internal autonomy is assured to members of the pool while eliminating wastes of competition.

2. They are simple to be formed and flexible in operation.

3. Pools ensure stability in industry and trade by avoiding the tension of competition and uncertainties of markets.

4. Pools enable the members to concentrate on improving the quality of their products or service because they need not be unduly worried about markets, price, profits, etc. as they are governed by common agreement.

Disadvantages of pools [54]:

1. Output pools may often result in artificial restriction on output to the detriment of customers.

2. Pools have the scope for exploiting the consumers by charging excessive prices and arbitrary curtailment of output flowing into the market.

3. The pool agreements often provide shelter to inefficient firms in the name of avoiding the competition.

4. Pools block the growth or adoption of inventions in order to keep up their strong hold on the market.

5. Management of pool agreement may not be effective as members may clandestinely violate the critical provisions of the agreement.

6. Vigorous competition by the firms which are not the members of the pool may defeat the objectives of the pool agreement.

Cartel is the European name for the American pools. It is the association of independent firms dealing in the same type of business to fix the amount of production, divide the market, determine the price for their products to create monopoly and maximize profit [8].

Features of cartels [54]:

1. It is a horizontal business combination, i.e., union of firms engaged in the same business.

2. Its members retain their identity and autonomy in their day-to-day operations.

3. It has a federal character whereby its members agree to abide by common decisions on specified matters taken by the central organization.

4. Cartel agreement may provide for regulation of output to be produced by the members as per estimated demand potential.

5. Systematic allocation of market on agreed basis among the members.

6. Formation of central agency, that is, syndicate to assemble the output of the member firms and sell them at remunerative prices.

Cartels are associations of firms bound by agreement as to collective regulation of output, pricing, trading terms, marketing methods, etc. They have taken different forms ranging from simple price agreement to elaborate centralized selling syndicate.

Types of cartels:

1. Term cartel.
2. Price cartel.
3. Output cartel.
4. Territorial cartel.
5. Super cartel.
6. Syndicate.

Term cartels refers to agreement between the members for selling the products on uniform terms to be adopted in common. Very often competition between firms becomes keener on the basis of attractive terms quoted for executing the bulk orders from the customers. The terms of sale refer to discount, credit, dispatching, transportation expenses, etc. Under the simple form of cartel, firms agree to follow commonly arrived at terms of sales so that unnecessary competition between the firms in the same industry is avoided. Avoidance of unfair competition, prevention of undercutting of prices and possibility of securing remunerative prices for all are the motives behind this type of cartel [54].

Price cartel provides for fixation of uniform or common prices of goods dealt in by the members. All the member firms agree to follow common price policies so that competition based

on price differential is averted. The entire cartel is likely to get prominent position in the market and may gain monopoly profits [54].

Output cartel aims at limiting the aggregate output to the level of expected market demand. Firms agree to desist from producing more than the specified output so that there will be least possibility of overproduction. Balance is sought to be established between demand and supply. Undue price fluctuations are ironed out and firms may concentrate on improvement of quality of the products. There is, however, the danger that such cartels may deliberately restrict the output and create a scare of scarcity pushing up the market prices arbitrarily to the disadvantage of the consumer [54] .

Under **territorial cartel** agreement, firms may be assigned specific territories for selling their products, or particular categories of consumers may be assigned to certain firms. Thus firms are assured of adequate sales without the fear of competition from other member firms in the line [54].

Super cartels are formed on an international basis. These refer to agreements between cartels of one country with the cartels of the other countries [55].

Syndicate implies the formation of central agency, or syndicate, for marketing the produce turned out by the members. Each firm has to contribute its output to the syndicate attached to the cartel for a fixed price. The syndicate pools the output and sells the merchandise in the market on remunerative terms. The syndicate being the bulk-seller with least competition may fix

higher prices, discriminate in its price between different markets for the products and thus ensure maximum possible revenue from the sale proceeds. Each member firm is assigned a trade share up to which it can contribute its output to the syndicate. If a firm has exceeded its trade share, it has to pay a fine, and if a firm has fallen short of its share, it is given due compensation. But if the firm is totally unable to produce or deliberately refuses to contribute, then compensation is not payable. The syndicate operates in as a wider market as possible. The profits earned by the syndicate are distributed among the members as per their trade share or the proportion of output contributed by them respectively [54].

Advantages of cartels [54]:

1. Economies in large-scale marketing such as reduced costs of handling and transporting.

2. In syndicate type of cartelling, bargaining influence in the market is higher. Therefore, higher prices and profits may be secured by centralized selling. The desire to reap the advantages of facing buyers with a single seller lies at the root of cartelization.

3. Since market is guaranteed, the member firm need not bother about sales promotion which is the lookout of the syndicate. It can, however, focus its efforts on quality improvement.

4. Minimum margin for profit is assured for all the member firms.

5. Adjustment of supply to demand avoids over production and consequent price effects.

6. There is comparatively greater resistance power among the cartel members to withstand the risks of trade cycles.

Disadvantages of cartels [54]:

1. Cartels tend to purposely restrict the output and starve the market. This creates difficulties for the consumers.

2. The cartels abuse their position and rig up the prices to exploit the consumers.

3. Cartels, under the pretext of eliminating competition, give shelter to inefficient firms.

4. Cartels are reluctant to incorporate new inventions and pass on the consequent benefits to consumers.

5. Cartel being a loose form of federation, its members may violate the terms of agreement and sabotage the agreement.

6. Cartels have also to face competition from firms which are not the members of the cartel.

International cartels are cartels which include business enterprises domiciled under more than one government and doing bushes across national frontiers. A cartel of this type may include the major enterprises operating in a given industrial field throughout the world and may determine trade policies in that field in most of the world's principal markets. Unless there is an international cartel, the power of a business group within a single country is limited by foreign competition, subject to whatever protection tariff policies and international shipping costs may provide [25, 4].

Principal types of international cartel [25, 4–6]:

1. The association – the international cartel association resembles a national trade association which is engaged in restrictive activities. The members of such a body are producing companies in various nations. The cartel arrangement is expressed in a more or less formal agreement to which all are parties or in the rules and regulations of the association itself. Such cartels may formally agree to fix prices; to limit and apportion output, sales, or exports; to allocate market territories; to redistribute profits in accordance with an agreed formula; or even to sell through a jointly maintained sales agency.

2. The patent licensing agreement – among large manufacturing enterprises, especially in industries in which technological progress has been rapid, the most common type of international cartel is the agreement as to patents and processes. Such an agreement rests upon the fact that the participants in the cartel hold patents and/or operate under patent licenses. In most countries the control of a patent gives the owner certain monopolistic rights.

3. The combine – it controls international markets not by contract but by uniting competitors under a common ownership or management. Corporate structure thus becomes the basis for market control. In the simplest and most frequent case, a small corporate combination in a particular field of industrial activity is part of a larger cartel pattern maintained by intercorporate contracts of broader scope. In a few instances, the ramifications

of one or two concerns are so extensive as to constitute the major portion of an international cartel arrangement.

There are three basic industries run by international cartels: oil industry, diamond industry, and olive oil industry [47].

5.3. International Holding Companies

A holding company is a parent corporation, limited liability company, or limited partnership that owns enough voting stock in another company to control its policies and management. The company does not have any operations or active business itself; instead, it owns assets in one or more companies. As per Indian Companies Act, 1956, holding company is one which has its subsidiary [23]. A company is subsidiary of another company (holding company) if that another company controls the composition of its board of directors and holds more than half of nominal value of its equity capital. Thus holding company is that which controls the composition of the Boards of Directors of other companies or which holds more than 50 % of share capital of other companies [54].

A holding company exists for the sole purpose of controlling another company, which might also be a corporation, limited partnership or limited liability company, rather than for the purpose of producing its own goods or services. Holding companies also exist for the purpose of owning property such as real estate, patents, trademarks, stocks

and other assets. If a business is 100 % owned by a holding company, it is called a wholly owned subsidiary [23].

The holding company supports the subsidiaries by lowering the cost of capital due to its overall strength. Using a downstream guarantee, the parent company makes a pledge on a loan on behalf of the subsidiary. A downstream guarantee can be undertaken to help a subsidiary company obtain debt financing that it otherwise couldn't, or to obtain funds at lower interest rates than it could obtain without the holding company's guarantee. In many instances, a lender may be willing to provide financing to a corporate borrower only if an affiliate agrees to guarantee the loan. Once backed by the financial strength of the holding company, the subsidiary company's risk of defaulting on its debt is considerably less [23].

A good example of a holding company is Berkshire Hathaway. One of the world's largest multinational companies by revenue, Berkshire owns assets in over one hundred public and private companies. Its major holdings include Berkshire Hathaway Energy, Business Wire, Dairy Queen, Clayton Homes, Duracell, GEICO, Fruit of the Loom, RC Wiley Home Furnishings and Marmon Group. The company also has minor holdings in companies such as The Coca-Cola Company, Goldman Sachs, IBM, American Express, Apple, Delta Airlines and Kinder Morgan [23].

Types of holding companies [54]:

1. **Primary holding company** – it is at the apex of a complex of different subsidiary companies. It is not however a

subsidiary of any other company. In other words, it is not controlled by any other company.

2. **Parent holding company** – it is an existing undertaking which seeks to consolidate other competing units by organising subsidiaries.

3. Consolidated, or **offspring holding company** – it is a new company to which a group of existing companies has proposed to transfer bulk of their shares carrying controlling right in exchange of shares allotted by the new company.

4. Intermediate holding company – it is a holding company of another but at the same time it is a subsidiary of some other holding company, i.e., it holds controlling interest in the capital of some companies and its own shares are held by some other holding company.

5. Pure holding company – its main purpose is to invest in and control the affairs of the other companies. Associated Cement Co. in India is an example.

6. Mixed holding company – it is engaged in some business operations and at the same time holding majority of voting power in the share capital of other companies.

7. Proprietary holding company – it is one which acquires whole of the share capital of the subsidiary company or companies.

Advantages of the holding company [54]:

1. It offers potential tax consolidation benefits. In the United States, holding companies are required to own 80 % of outstanding stock, either in voting or total value, before any tax

consolidation benefits are permitted. Once that threshold is reached, then tax-free dividends can be claimed, since that process is treated as one company transferring cash assets to the other company. To be eligible for other benefits, more than 50 % of the value of its outstanding stock must be owned directly or indirectly by five or fewer individuals during the last portion of the tax year.

2. It reduces the legal risks of those involved. Holding companies are basically just a major shareholder for the companies where they own outstanding stock. That means there is a reduced risk of legal action taken against them for the goods and services being produced by the company they own. The primary risk that most holding companies face is a loss of stock value because of performance issues that are directly related to the companies they own.

3. It permits companies to perform traditional functions if they choose. If 60 % of the adjusted gross income of an organization comes from dividends, interest, royalties, or rent, then it qualifies as a holding company in the United States. Even with this qualification, it is still permissible for the company to create its own products or services. The only stipulation is that the adjusted gross income from these other activities must stay below the 40 % threshold.

4. It offers diversity within the business world. Holding companies make it possible for a diverse array of businesses to exist, providing products and services for their customers. They invest into companies that provide a strong possibility of

profitability, which then creates profits for the holding company. Many of today's top performing companies are owned by holding companies. Berkshire Hathaway, for example, owns $49.6 billion in Apple, holding over 239 million shares. They own 679 million shares of Bank of America, worth $21.2 billion. They even own 400 million shares of Coca-Cola, valued at $18.4 billion.

5. It creates more opportunities for low-cost loans. Shares are usually classified as a tangible asset. That means they can be used as collateral when lending products are required for some reason. These secured loans are often made available at a very low interest rate because there is virtually no risk for the lender in the transaction. If a default occurs, then the shares are used to pay off the debt. That makes it easier and cheaper to finance new expansion opportunities, support businesses, and even keep prices lower for consumers.

6. It is very easy to form a holding company. To form a holding company, you must first incorporate your business. Then you purchase shares of the companies you wish to hold from the open market. You don't require the consent of the shareholders within the targeted companies under this structure because you're not completing a full takeover.

7. It becomes possible to gain a competitive edge. Holding companies present an opportunity that is similar to a strategic partnership. The resources of the holding company can be combined with the resources of the acquired organization to create unique market opportunities. When both companies are

involved within the same industry, this benefit is magnified even further. It becomes possible to work on large-scale operations instead of trying to funnel strong market shares from small demographics.

8. It can be implemented on a personal scale. Holding companies aren't just for Warren Buffet. They are for individuals too. If you set up a personal holding company, then you gain an opportunity to avoid potential estate taxes. It gives your heirs the ability to avoid probate while still investing and growing your wealth. Investors who hold the possession of a person's assets at death are able to transfer those assets to heirs. Although these companies can be very complex, and sometimes cost more than the benefits they provide, it is a way to protect personal wealth that you may wish to pass along one day.

Disadvantages of the holding company [54]:

1. It creates disadvantages for individual investors. Holding companies hold an influential number of shares in most of the companies they own. If the holding company decides to liquidate their holdings, then the effects on the individual investor can be very traumatic. Imagine what would happen if Berkshire Hathaway sold their 4.9 % stake in Apple tomorrow? People with only 100 shares might see a strong, unanticipated dip in their holdings because of those actions. Holding companies can dramatically change the landscape of a trading day by initiating a handful of transactions.

2. It reduces the level of transparency available to the consumer. Most holding companies are not required to report

on how their company is being internally managed. Their responsibility is to their own shareholders, which means reporting on the status of the dividends they receive. Consumers are often doing business with companies that are owned, in part or in whole, by holding companies without realizing it. Without transparency, it makes things more difficult for the average consumer to make informed investment or purchasing decisions.

3. It is not always easy for holding companies to sell their shares. Holding companies can sometimes find themselves unable to sell their shares in a company, even if they wanted to do so. Dumping a large number of shares on the open market does not guarantee that they will all be sold. Forcing a holding company to hold onto some of their shares is the one option individual investors have to limit their own potential losses. Although strong holding companies should have a diversified portfolio of companies that provide them with stable income, one big loss could destabilize the company and make life difficult.

4. It forces a heavy reliance on a single income resource. Because 60 % of income must come from dividends, interest, or other revenues that are not related to products or services, it forces a holding company to be reliant on the performance of the market. They are only as strong as the strategies they use to procure shares in consistent companies. If there is a bad run on dividends for the company, it could be enough to put it out of business. Even with products or services available to supplement

income, there just isn't enough time to develop new revenue streams during a strategy collapse.

5. It may create competing interests. One of the biggest criticisms of Warren Buffet is that he invests into dividend shares with his holding company, then fails to provide a dividend to his own investors. Although Berkshire Hathaway does use an aggressive buy-back policy, Buffet feels like funneling resources into expanding the reach of his holding company or improving existing products or services is a better investment for his shareholders. There are times when a holding company may find itself competing with itself for market share within its holdings.

6. It creates management challenges for the parent company. Many holding companies prefer to hold shares of a subsidiary rather than a true parent company if a controlling interest is preferred. That is because there are management challenges in play when diversity in holdings is present. Imagine requiring a manager to be knowledgeable about the banking industry, real estate, sugary beverages, and smartphone manufacturing simultaneously. When there is decisional control, the structure makes the process ineffective because there may not be enough experience present to make the correct decision.

7. It can create issues of control. Holding companies are sometimes forced to implement a change of control when they turn a newly acquired business into one of their own subsidiaries. The former managers in the new subsidiary still represent a large percentage of shareholders. These competing

interests in management are similar to the competing interests of shareholders. The end result in this type of situation is an increase in turnover, poor decision-making processes, and quite possibly a reduction in share valuation.

8. It may require a large amount of capital to get started. You must have financing resources in place to have a holding company be able to remain operational. Without sufficient personal capital, equity partners are required to provide enough funding to make the initial investments. This capital must be in place before making acquisitions. At the same time, the owners of any companies you intend to acquire, even if it is only a minority stake, will want assurances that you are able to complete the financial transactions as promised.

9. It can centralize an industry. Although a holding company does not technically form a monopoly, the process of acquiring company shares does begin to consolidate certain industries if enough capital is used. When that occurs, consumers are presented with fewer choices instead of more. There is less competition in the market instead of more. That means the prices for items tends to be higher, not lower, unless specific safeguards are implemented to prevent this from happening. That is why the first holding companies were ordered to be disbanded in the early 20th century.

10. It can result in decisions for personal, not professional, gains. The information that is received from subsidiaries or minority stakes in businesses allows the management of a holding company to create the potential for

personal financial gains. It might be used to create speculative activities in the market, which could negatively impact individual investors. It may even lead to the exploitation of certain companies, forcing them to purchase goods at high prices from companies under the control of holding company management.

These advantages and disadvantages of a holding company do create some investing challenges that everyone must face. There may be issues in volatile markets for such a structure, which could reduce, if not eliminate, the chances at profitability. At the same time, however, holding companies are able to provide supplementary resources to numerous industries, allowing for more variety and competition in the marketplace.

Conclusions

1. There are various types of business combinations. Among them are trade associations, chambers of commerce, pools, cartels, trusts, holding companies, community of interests, mergers, and amalgamations.

2. Business enterprises in the same trade collaborate with one another in numerous ways and for varied purposes. The term “cartel” characterizes those institutions or mechanisms of collaboration that serve to limit or suppress competition. Trade associations are organizations of enterprises in a particular line of business. They may function as cartels.

3. Holding companies are those that own the outstanding stock of another company. A holding company will not usually produce any goods or services on its own. The purpose of the company is to form corporate groups instead through their stock ownership. This reduces the risk for the owners, while still allowing for the control or ownership of several different companies at once.

End-of-chapter tasks:

1. Detect the reasons for business combinations.
2. Define functions of trade associations.
3. Classify international cartels.
4. Suggest factors contributing to cartels' limitation.
5. Give examples of holding companies.
6. Relate different types of business combinations to the global economic challenges.

CHAPTER 6. INTERNATIONAL MERGERS AND ACQUISITIONS

6.1. International Mergers.
6.2. International Acquisitions.
6.3. M&A Deals in a Global Economy.

Key words: mergers, acquisitions, M&A deals, strategy.

6.1. International Mergers

Merger is a financial tool being used for enhancing long-term probability [27]. Mergers can be classified into the following groups based on the nature of merging companies:

1. Horizontal mergers.
2. Vertical mergers.
3. Conglomerate mergers.
4. Product-extension mergers.
5. Market-extension mergers.

Horizontal mergers refer to the merger of two companies who are direct competitors of one another and they serve the same market and sell the same product. It is a merger occurring between companies in the same industry. Horizontal merger is a business consolidation that occurs between firms who operate in the same space, often as competitors offering the same good or service. Horizontal mergers are common in industries with fewer firms, as competition tends to be higher and the synergies

and potential gains in market share are much greater for merging firms in such an industry.

Figure 6.1 – Horizontal mergers [56]

Example. A merger between Coca-Cola and the Pepsi beverage division, for example, would be horizontal in nature. The goal of a horizontal merger is to create a new, larger organization with more market share. Because the merging companies' business operations may be very similar, there may be opportunities to join certain operations, such as manufacturing, and reduce costs.

Vertical mergers occur either between a company and a customer or between a company and a supplier. It is a merger between two companies producing different goods or services for one specific finished product. A vertical merger occurs when two or more firms, operating at different levels within an industry's supply chain, merge operations. Most often the logic behind the merger is to increase synergies created by merging firms that would be more efficient operating as one.

Figure 6.2 – Vertical mergers [56]

Example. A vertical merger joins two companies that may not compete with each other, but exist in the same supply chain. An automobile company joining with a parts supplier would be an example of a vertical merger. Such a deal would allow the automobile division to obtain better pricing on parts and have better control over the manufacturing process. The parts division, in turn, would be guaranteed a steady stream of business. Synergy, the idea that the value and performance of two companies combined will be greater than the sum of the separate individual parts, is one of the reasons companies merger.

Conglomerations refer to the merger of companies which don't sell any related products to any related markets. There are two types of conglomerate mergers: pure and mixed. Pure conglomerate mergers involve firms with nothing in common, while mixed conglomerate mergers involve firms that are looking for product extensions or market extensions. The biggest risk in a conglomerate merger is the immediate shift in business operations resulting from the merger, as the two

companies operate in completely different markets and offer unrelated products/services [56].

Figure 6.3 – Conglomerate mergers [56]

Example. A leading manufacturer of athletic shoes, merges with a soft drink firm. The resulting company is faced with the same competition in each of its two markets after the merger as the individual firms were before the merger. One example of a conglomerate merger was the merger between the Walt Disney Company and the American Broadcasting Company.

Product-extension mergers are executed among companies that sell different products of related category. They also seek to serve a common market. A product-extension merger takes place between two business organizations that deal in products that are related to each other and operate in the same market. The product extension merger allows the merging companies to group together their products and get access to a bigger set of consumers. This ensures that they earn higher profits.

Figure 6.4 – Product-extension mergers [56]

Example. The acquisition of Mobilink Telecom Inc. by Broadcom is a proper example of product-extension merger. Broadcom deals in the manufacturing Bluetooth personal area network hardware systems and chips for IEEE 802.11b wireless LAN. Mobilink Telecom Inc. deals in the manufacturing of product designs meant for handsets that are equipped with the Global System for Mobile Communications technology. It is also in the process of being certified to produce wireless networking chips that have high speed and General Packet Radio Service technology. It is expected that the products of Mobilink Telecom Inc. would be complementing the wireless products of Broadcom.

Market-extension mergers occur between two companies that sell identical products in different markets. The main purpose of the market extension merger is to make sure that the merging companies can get access to a bigger market and that ensures a bigger client base.

Figure 6.5 – Market-extension mergers [56]

Example. A very good example of market extension merger is the acquisition of Eagle Bancshares Inc by the RBC Centura. Eagle Bancshares is headquartered at Atlanta, Georgia and has 283 workers. It has almost 90,000 accounts and looks after assets worth US $1.1 billion. Eagle Bancshares also holds the Tucker Federal Bank, which is one of the ten biggest banks in the metropolitan Atlanta region as far as deposit market share is concerned. One of the major benefits of this merger is that this merger enables the RBC to go ahead with its growth operations in the North American market. With the help of this merger RBC has got a chance to deal in the financial market of Atlanta, which is among the leading upcoming financial markets in the USA. This move would allow RBC to diversify its base of operations.

Legally speaking, a merger requires two companies to consolidate into a new entity with a new ownership and management structure (ostensibly with members of each firm). The more common distinction to differentiating a deal is

whether the purchase is friendly (merger) or hostile (acquisition). Mergers require no cash to complete but dilute each company's individual power. In practice, friendly mergers of equals do not take place very frequently. It's uncommon that two companies would benefit from combining forces with two different CEOs agreeing to give up some authority to realize those benefits. When this does happen, the stocks of both companies are surrendered, and new stocks are issued under the name of the new business identity [35].

According to the EU legislation, there are three types of cross-border mergers which may be pursued by the parties [7]:

- **Merger by absorption** – whereby the target company is "absorbed" by transferring all of its assets and liabilities to the transferee company. The target is then dissolved without going into liquidation.
- **Merger by absorption of a wholly-owned subsidiary** – where the target is a wholly-owned subsidiary of the transferee, the target is dissolved and upon dissolution the target's assets and liabilities transfer upwards to the transferee. There are fewer formal requirements to be completed in this type of merger.
- **Merger by formation of a new company** – whereby two or more companies (the transferors) each transfer all of their assets and liabilities to a newly-formed 3rd company (the transferee). Once the transfer is complete, the two transferor companies are dissolved without going into liquidation.

6.2. International Acquisitions

Many successful corporations often become targets for larger companies. These larger entities may propose a merger with the smaller company, or seek to acquire it through purchasing its stock shares. When one company attempts to buy a controlling interest in another through stock purchases, the purchasing entity is engaging in a takeover, or acquisition.

In an acquisition, a new company does not emerge. Instead, the smaller company is often consumed and ceases to exist with its assets becoming part of the larger company. Acquisitions, sometimes called takeovers, generally carry a more negative connotation than mergers. Due to this reason, many acquiring companies refer to an acquisition as a merger even when it is clearly not. An acquisition takes place when one company takes over all of the operational management decisions of another company. Acquisitions require large amounts of cash, but the buyer's power is absolute. One well-known acquisition in 2019 occurred when Xerox acquired 3D printing company Vader Systems, a company which manufactured liquid metal jet 3D printers. The startup was run by Zachary Vader and Scott Vader, in the Buffalo, New York, area. After the acquisition, Vader Systems was relocated outside of Rochester, New York, at the Xerox Webster campus. Xerox intends on tapping into a market worth $8 billion USD [35].

An international acquisition of a business is similar to other international projects: it requires an initial outlay and is expected

to generate cashflows whose present value will exceed the initial cash outlay. Global consolidation and market share are two possible motivations for international acquisition.

As against establishing a new subsidiary, international acquisitions have some distinct advantages: they take less time, and can benefit from customer relations that have already been established. These incremental benefits have to be traded off against the incremental costs of such acquisitions. International acquisitions usually generate quicker and larger cash flows but also require a larger initial outlay. International acquisitions also require aligning the parent's management style with that of the acquired firm [26]. The international acquisitions may take the form of hostile or friendly takeovers.

A **hostile takeover** occurs when one corporation, the acquiring corporation, attempts to take over another corporation, the target corporation, without the agreement of the target corporation's board of directors [4]. Agents of the acquiring company then attempt to purchase the target company's stock from other sources, gain a controlling interest and force out the board members who voted against the acquisition. When this happens, the acquiring company will aggressively go after shares of the target firm, while the target's board of directors prepares to fight for survival. A hostile takeover is usually accomplished by a tender offer or a proxy fight.

In a **tender offer**, the corporation seeks to purchase shares from outstanding shareholders of the target corporation at a premium to the current market price. This offer usually has a

limited time frame for shareholders to accept. The premium over the market price is an incentive for shareholders to sell to the acquiring corporation. The acquiring company must file a Schedule TO with the SEC if it controls more than 5% of a class of the target corporation's securities. Often, target corporations acquiesce to the demands of the acquiring corporation if the acquiring corporation has the financial ability to pull off a tender offer [4].

In a **proxy fight**, the acquiring corporation tries to persuade shareholders to use their proxy votes to install new management or take other types of corporate action. The acquiring corporation may highlight alleged shortcomings of the target corporation's management. The acquiring corporation seeks to have its own candidates installed on the board of directors. By installing friendly candidates on the board of directors, the acquiring corporation can easily make the desired changes at the target corporation. Proxy fights have become a popular method with activist hedge funds in order to institute change [4].

A corporation may choose to buy back its shares to protect itself from a hostile takeover. With this method, the shares needed to stage the takeover will be in the target company's holdings, not in the open market. Another method is a shareholder's rights plan, also called a "**poison pill**", which enables shareholders to buy new target company stock at a discount if one entity owns a large percentage of outstanding shares. This plan forces the acquirer to negotiate directly with

the target company's board, rather than seeking to acquire stock through the shareholders [20].

There are several methods for implementing a poison pill. One poison pill strategy involves allowing the existing shareholders to buy more stock at a discount. This increases the number of shares the acquirer will have to buy. A variant of this is to offer a highly advantageous preferred stock that is convertible to common shares should the company be acquired. Another related poison pill involves creating an employee stock option plan that vests only if the company is acquired in a takeover. This makes it more difficult to retain key employees after the takeover. One non-stock related method is to create key management incentive plans (called **golden parachutes**) that provide for expensive compensation payments should the acquirer buy the company and fire all the key executives. Another non-stock poison pill is to amend the corporate by-laws to stagger board of director elections. Doing this creates the likelihood the acquirer will face a number of unfriendly board members after the hostile takeover. Poison pills are often controversial because they increase costs for the company should they actually be implemented. Critics also state that poison pills interfere with market efficiencies that encourage takeovers when there are favorable economic conditions.

A **friendly takeover** occurs when one corporation acquires another with both boards of directors approving the transaction [4]. The board of directors then votes on the proposed buyout. If the board believes the stock purchase would benefit the current

stockholders, they vote in favor of the sale. The acquiring company then takes control of the target company's operations and may or may not choose to keep the target company's board of directors in place [20]. Friendly takeover is a type of takeover that is very friendly in nature as the management of the acquired company as well as management of the target company agrees to the terms and conditions of the takeover and takeover is done without any difficulty, arguments, and fights. An acquirer doesn't have to do any plotting or make any strategies against the target company in order to acquire the same [57]. Let's assume there is a company called XYZ who is interested in buying a majority in company ABC. Company XYZ makes a plan to approach company ABC's board of directors with a potential bid. Company ABC's board of directors would then discuss on the bid or votes on the bid. If the company ABC management evaluate that the deal is beneficial to the company, they will accept the offer and recommend the deal to shareholders as well. After all the approvals from a board of directors, shareholders and other regulatory authorities involved, the deal will be finalized. Facebook takeover to WhatsApp is another big example of a friendly takeover where Facebook bought WhatsApp in $19 billion [57].

The friendly takeover has many benefits that it offers to the target company. When a target company sees that the benefit they will have after this takeover is enough to trade of with their current business, they go for or agrees to the deal that an acquirer offer. The biggest benefit that is being offered to the

target company by this takeover is the price per share which is often better than the current market price.

There are 3 global reasons for friendly takeover [57]:

1. The target company might receive other benefits as well in addition to the better per share price that includes better opportunities to expand the business, to explore the different market, expansion in different product line etc.

2. It is very important to note that there is always a country's regulatory body involved in takeover whose approval is mandatory for the takeover to happen.

3. In case the regulatory body doesn't approve the takeover terms or feel that the takeover would be harmful in any circumstances, it would not happen even after both the acquirer and the target company is in agreement to the takeover.

Most takeovers are friendly, but hostile takeovers and activist campaigns have become more popular lately with the risk of activist hedge funds [4].

6.3. M&A Deals in a Global Economy

Mergers and acquisitions are two of the most misunderstood words in the business world. Both terms often refer to the joining of two companies, but there are key differences involved in when to use them.

A merger occurs when two separate entities combine forces to create a new, joint organization [35]. Merger refers to the mutual consolidation of two or more entities to form a new

enterprise with a new name. In a merger, multiple companies of similar size agree to integrate their operations into a single entity, in which there is shared ownership, control, and profit. It is a type of amalgamation. For example, M Ltd. and N Ltd. joined together to form a new company P Ltd [36].

The reasons for adopting the merger by many companies is that to unite the resources, strength and weakness of the merging companies along with removing trade barriers, lessening competition and to gain synergy. The shareholders of the old companies become shareholders of the new company. Meanwhile, an acquisition refers to the takeover of one entity by another. The purchase of the business of an enterprise by another enterprise is known as acquisition. This can be done either by the purchase of the assets of the company or by the acquiring ownership over 51% of its paid-up share capital. In acquisition, the firm which acquires another firm is known as acquiring company while the company which is being acquired is known as target company. The acquiring company is more powerful in terms of size, structure, and operations, which overpowers or takes over the weaker company, i.e. the target company. Most of the firm uses the acquisition strategy for gaining instant growth, competitiveness in a short notice and expanding their area of operation, market share, profitability, etc [36].

Mergers and acquisitions may be completed to expand a company's reach or gain market share in an attempt to create shareholder value [35]. Nowadays, only a few numbers of

mergers can be seen; however, acquisition is getting popularity due to extreme competition.

The following table represents the differences between mergers and acquisitions.

Table 6.1 – Mergers vs acquisitions [36]

Criterion	Mergers	Acquisitions
Definition	The fusion of two or more entities taking place voluntarily to form a new entity	One company purchasing the business of another company
Title	The new entity formed owing to the merger, holds a new title	The acquired company functions under the title of the acquiring company
Terms	Merger is always conducted under a mutual agreement by all the involved companies	An acquisition may be implemented voluntarily or involuntarily by the entities
Size of operations	Two or more companies having the same scale of operations opt for a merger	The larger company takes over the smaller company
Legalities	The process of merger involves a time consuming procedure owing to the high number of legal formalities	It can be done faster as the legal formalities are minimal
Purpose	The purpose of merging entities is to decrease the prevailing competition in the market and to increase operational efficiency	The sole purpose of an acquisition is an expansion of the entity

The history of mergers and acquisitions is probably as long as commerce itself. However, there was made an attempt to identify a few “waves” of mergers and acquisitions (Table 6.2).

Table 6.2 – M&A waves [40]

	Wave 1	Wave 2	Wave 3	Wave 4	Wave 5
Period	1893-1904	1910s-1929	1955-1975	1984-1989	1993-2000
Predominant means of payment	Cash	Equity	Equity	Cash/Debt	Equity
M&A outcome	Creation of monopolies	Creation of oligopolies	Diversification/ conglomerate building	“Bust-up” takeovers	Globalization
Predominant nature of M&A	Friendly	Friendly	Friendly	Hostile	Friendly
Predominant types of M&A	Horizontal mergers	Vertical mergers	Diversified conglomerate mergers	Congeneric mergers, hostile takeovers, corporate raiding	Cross-border mergers
Beginning of wave	Economic expansion; new laws on incorporations; technological innovation	Economic recovery; better enforcement of antitrust laws	Strengthening laws on anti-competitive M&A’s; economic recovery after WW2	Deregulation of financial sector; economic recovery	Strong economic growth; deregulation and privatization
End of wave	Stock market crash; First World War	The Great Depression	Market crash due to an oil crisis	Stock market crash	Burst of the internet bubble; 9/11 terrorist attack

Understanding history can help us identify the proximity to a new wave of M&A. Mergers and acquisitions have become the most frequently used methods of growth for companies in the twenty first century. 2018 year was on pace to be a record-breaking year for corporate consolidation. In the first three quarters of the year, companies around the world announced merger and acquisition deals worth a total of $ 3.3 trillion, the most record keeping began nearly four decades ago [52]. Much of that value was coming out of the United States.

Deals announced involving American companies in the first nine months of the 2018 year were worth over $ 1.3 trillion – more than 40 percent of all global M&A activity and more than the total value of deals in Europe, Australia, Africa, Southeast Asia, and the Middle East combined [52].

In the United States, the energy and power industry accounted for the largest share of M&A deal volume, followed by technology, and healthcare.

M&A deals can result in [52]:

- two companies consolidating to form an entirely new company;
- the dissolution of one company after it is bought by another;
- a company simply operating under the umbrella of a new parent company.

The biggest mergers and acquisitions of 2018 are represented in Table 6.3.

Table 6.3 – The biggest M&A deals in 2018 [52]

Indicators	Facet
Altaba	
Target company	Altaba (stock buyback)
Deal value	$ 15.6 billion
Industry	Finance
Financial & Risk US Holdings Inc	
Target company	Refinitiv
Deal value	$ 17.0 billion
Industry	E-commerce
Broadcom Inc	
Target company	Ca Inc
Deal value	$ 18.3 billion
Industry	Software
Dell Technologies	
Target company	VMware Class V Tracking Stock
Deal value	$ 21.7 billion
Industry	Computers
Keurig Green Mountain Inc	
Target company	Dr Pepper Snapple Group Inc
Deal value	$ 26.6 billion
Industry	Food and beverage
Marathon Petroleum Group	
Target company	Andeavor Corp
Deal value	$ 31.3 billion
Industry	Oil & gas
Shareholders	
Target company	Altice USA Inc
Deal value	$ 32.1 billion
Industry	Cable TV
T-Mobile US Inc	
Target company	Sprint Corp
Deal value	$ 58.7 billion
Industry	Wireless communication
Energy Transfer Equity LP	
Target company	Energy Transfer Partners LP
Deal value	$ 61.8 billion
Industry	Pipelines
Cigna Group	
Target company	Express Scripts Holding Co
Deal value	$ 68.5 billion
Industry	Healthcare

Deal value in the first half of 2018 was higher than the first-half average for 2009 through 2017 and only slightly below the first-half figure in the record-setting year of 2015. Total deal value was $1.7 trillion, with more than 16,000 deals globally [28] (Fig. 6.6).

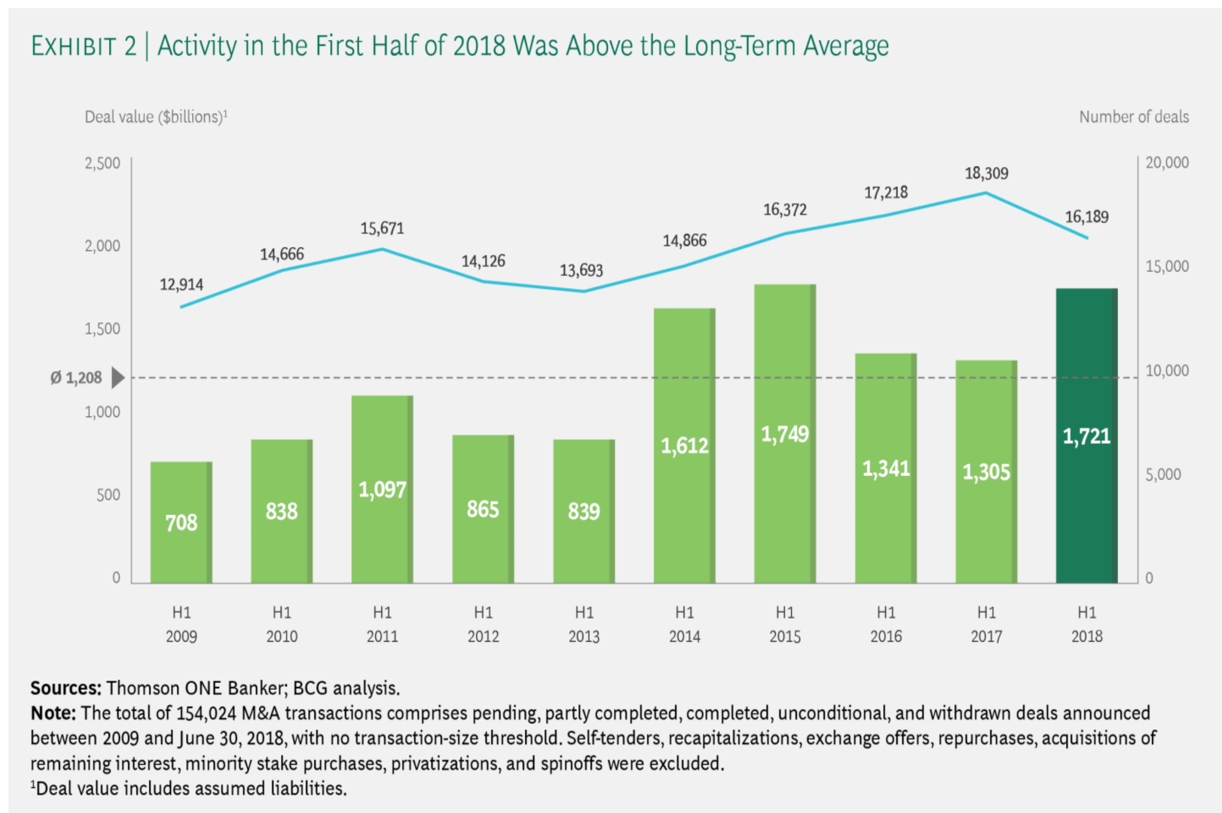

Figure 6.6 – M&A deal value [28]

Advantages of the M&A decisions include [6]:

1. Obtaining quality staff or additional skills, knowledge of your industry or sector and other business intelligence. For instance, a business with good management and process systems will be useful to a buyer who wants to improve their own. Ideally, the business you choose should have systems that complement your own and that will adapt to running a larger business.

2. Accessing funds or valuable assets for new development. Better production or distribution facilities are often less expensive to buy than to build. Look for target businesses that are only marginally profitable and have large unused capacity which can be bought at a small premium to net asset value.

3. Your business underperforming. For example, if you are struggling with regional or national growth it may well be less expensive to buy an existing business than to expand internally.

4. Accessing a wider customer base and increasing your market share. Your target business may have distribution channels and systems you can use for your own offers.

5. Diversification of the products, services and long-term prospects of your business. A target business may be able to offer you products or services which you can sell through your own distribution channels.

6. Reducing your costs and overheads through shared marketing budgets, increased purchasing power and lower costs.

7. Reducing competition. Buying up new intellectual property, products or services may be cheaper than developing these yourself.

8. Organic growth, i.e. the existing business plan for growth, needs to be accelerated. Businesses in the same sector or location can combine resources to reduce costs, eliminate duplicated facilities or departments and increase revenue.

Disadvantages of the M&A decisions include:

1. The bigger the business the harder control is.

2. More decision making and more risks.

3. More expensive.

Mergers and acquisitions gain the advantage of taxation, synergy, financial benefit, increase in competitiveness and much more which can be beneficial, however sometimes adverse effect can also be seen like an increase in employee turnover, clashing in the culture of organizations and others but these are rare to happen.

Conclusions

1. Merger refers to consolidation of two or more companies to form an all-new entity with a new name. Merger assists the companies in uniting their strengths, resources and weaknesses. Merger leads to a reduction in trade barriers and competition.

2. An acquisition is the purchase of an entity by another entity. This can be done either by acquiring ownership over 51% of its share capital or by taking over the assets of the company. The acquiring company is more influential in terms of structure, operations and size as compared to the target company.

3. Merger and acquisition are the two most commonly applied corporate restructuring strategies. These are the form of external expansion. It helps the business in maximizing the profit and growth by increasing the level of production and marketing operation. While merger means "to combine", acquisition means "to acquire."

End-of-chapter tasks:

1. Distinguish between mergers and acquisitions.
2. Indicate hostile takeover methods.
3. Interpret friendly takeovers principle.
4. Describe M&A waves.
5. Review M&A deals in the global economy.

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