No. of Printed Pages : **12**

MS-97

MANAGEMENT PROGRAMME

Term-End Examination

June, 2010

00048

MS-97 : INTERNATIONAL BUSINESS

Time : 3 hours *Maximum Marks : 100*

(Weightage 70%)

Note :

*(i) There are two sections : **A** and **B**.*

*(ii) Attempt **any three** questions from **Section-A**, which carry **20** marks each.*

*(iii) **Section-B** is **compulsory** and carries **40** marks.*

SECTION - A

1. Discuss the stages in the Corporate Life Cycle Theory of international marketing. Critically examine the theory in the light of the present business scenario, with special reference to formation of joint ventures and FDI.

2. Trace the evolution of international business from the perspective of organization structure and point out the dominant characteristics prevalent at each stage of evolution.

3. "The differences between domestic and international business have their implications for the control system in any international enterprise." What are these differences and in what ways have they been affected by developments over the last 20 years or so ?

4. (a) "MNEs transfer managers across national and cultural boundaries." Elaborating the statement, discuss the rationale and merits of such an approach.

   (b) What is meant by "rationalization of production" in the context of international business ? What factors might play a part in such rationalization ?

5. Write notes on ***any four*** of the following :

   (a) Ethnocentric and polycentric approaches to manpower requirements

   (b) Flexible manufacturing systems (FMS)

   (c) ASEAN and India

   (d) Determinants of FDI

   (e) Negotiation skills in international business

SECTION - B

6. Read the following case study carefully and give your analytical responses to the questions given at the end.

Russell Corporation : The Dilemma of Regional Free Trade

Russell Corporation is a leading manufacturer of sports-wear, including sweatshirts, sweatpants, and T-shirts. Owned by Berkshire Hathaway, Russell is based in Atlanta, Georgia, in the United States, and has annual revenues of around $2 billion. Its main competitors include Adidas, Nike, Benetton, and Zara. Russell runs every step of the manufacturing process : from weaving raw yarn into fabric, to dyeing, cutting, and sewing, to selling garments through retailers. Russell's brands include JERZEES, American Athletic, Brooks, Cross Creek, Huffy Sports, Russell Athletic, and Spalding. The firm sells through mass merchandisers, department stores such as Wal-Mart, and golf pro shops. Russell sells its apparel in about 100 countries and recently restructured production. The firm closed plants, moved some manufacturing abroad, and eliminated 1,700 U.S. jobs.

Management at Russell was pleased with the passage of the Dominican Republic-Central American Free Trade Agreement (DR-CAFTA) in 2005. The pact eliminated trade barriers between the United States and six Latin American countries : Guatemala, Honduras, El Salvador, Nicaragua, Costa Rica, and the Dominican Republic. Following DR-CAFTA's passage, Central American countries experienced a significant rise in foreign direct investment (FDI) from abroad. The apparel and clothing sector - consisting of firms like Russell-were among the biggest beneficiaries.

Prior to DR-CAFTA, many North American apparel companies sourced from China and other Asian nations where production costs are low. DR-CAFTA virtually eliminated tariffs on trade between the United States, Central America, and the Dominican Republic. Now Russell can cost-effectively source raw materials in Central America, manufacture fabric in the United States, then send the fabric to its factories in Honduras for assembly. Once the garments are completed they are re-exported to the U.S. for distribution. Without DR - CAFTA it would not have been cost effective to make fabric in the United States, export it to Asia, have the products manufactured there and then re-exported back. Under that scenario, Russell would have shifted *all* its manufacturing to China.

Background on DR-CAFTA

In the past, Central America and the Caribbean were parties to various protectionist trade arrangements, including the worldwide Multi-Fibre Agreement (MFA) of 1974. Among its provisions, the MFA shielded the North and Central American apparel industries from foreign competition by imposing strict import quotas. When the MFA expired in 2005, many countries became exposed to the full force cheap imports from low - cost producers in Asia. China dramatically increased its apparel exports to the United States, to the detriment of U.S. and Central American producers that long had supplied Western markets. For example, Alabama was once the world center of sock manufacturing. When the MFA expired, the sock capital shifted to Datang, China. Alabama sock workers receive an average of $10 an hour, compared to 70 cents an hour in Datang.

Since the expiration of the MFA, China has been flooding the United States with apparel. In recent years, China's share of finished clothing exports to the United States, once less than 20 percent, has leaped past 50 percent in some segments. To protect its home-grown apparel industry, the United States reimposed some trade barriers against Chinese imports. The U.S. government justified this action in part because China's currency, the yuan, is considered undervalued, which makes Chinese exports artificially cheap. However, such protection of the U.S. apparel industry is only temporary. World Trade Organization rules require the U.S. government to remove the trade barriers, at which time Chinese exports to the United States will increase.

Many in the U.S. apparel industry see DR-CAFTA as perhaps the only way to compete with China. DR-CAFTA helps maintain much apparel production in the Western Hemisphere by creating a bigger apparel market in the region and granting favorable trade status to apparel producers who manufacture their products using raw material from the DR-CAFTA region.

The United States is the biggest apparel market, importing more than $9 billion worth of apparel from the DR-CAFTA countries in each of 2004, 2005, and 2006. Honduras was the biggest shipper in dollar value, and exported products such as cotton blouses, shirts, and underwear. Meanwhile, DR-CAFTA gave U.S. producers an equal footing to sell their products to Central America. For example, the region is the second largest market for U.S. textiles and yarn, which Central American manufacturers use to produce finished apparel.

The DR-CAFTA countries are part of a large and growing trade region, and the free trade agreement is helping to improve economic conditions there. Perhaps the most important long-term benefit will be foreign investment in new technologies and a better-educated regional labor force. Some see DR-CAFTA as a further step toward development of the Free Trade Area of the Americas (FTAA), a proposed agreement that would bring free trade to all or most of North, Central, and South America.

The Situation in Honduras

Russell manufactures much of its garments in Honduras, a poor Central American country with 7 million people, one quarter of whom are illiterate. Honduras has an annual per-capita GDP of about $3,000. In 2006, the country's unemployment rate was 28 percent. The Honduras currency, the lempira, has been weakening against the U.S. dollar over time. Growth remains dependent on the U.S. economy, its largest trading partner, and on reduction of the high local crime rate. Honduras sends over 73 percent of its exported goods to the United States and receives about 53 percent of its imports from that country. The Honduran government is counting on the DR-CAFTA agreement to increase trade with the United States and the Central American region.

Few countries rely on their apparel industry more than Honduras. The Honduran government used incentives to create a large cluster of apparel firms. In addition to low-cost labor, Honduras offers a generous tax package: firms pay no income tax, value-added tax, or duties. Honduran apparel manufacturers can truck their merchandise to Puerto Cortes, Central America's biggest port, in just 30 minutes. From there, it takes only 22 hours to ship the goods to Miami by container ship. Honduras' apparel sector employs over 110,000 people, or 30 percent of the country's total industrial employment. The government is investing to improve Puerto Cortes and create a Textiles and Apparel University to train future managers and supervisors. To counter Chinese competition, the apparel industry in Honduras has begun to offer the "total package"–buying fabric, and sometimes even designing the garments, as well as final assembly.

Some Honduran apparel plants employ sophisticated technologies to increase productivity and output. For example, one supplier uses computer-aided design to cut cloth before sending it to be stitched into shirts for brands such as Jockey, Ralph Lauren, and Nautica. In 2003, the stock of U.S. FDI in Honduras was $262 million and rose to $339 million the following year. However, Honduras' legal system remains weak and corruption is a problem.

Honduran apparel producers are taking steps to survive in the evolving free trade environment. Geographic proximity to the United States is a big advantage that gives producers greater flexibility to respond quickly to rapidly evolving tastes. Honduran producers can ship finished merchandise to the United States in less than 24 hours, while similar shipments from China take up to a month.

Russell's Dilemmas

Many consumers shop for athletic clothing based on price, so even slight price increases can affect sales. Unlike Nike and Adidas, Russell does not enjoy much brand loyalty. Russell must decide whether to retain its manufacturing in Honduras or move everything to China. An additional possibility is to establish production in Eastern Europe to gain access to the huge EU market. Meanwhile, Adidas and Nike are pursuing markets in China and other Asian countries.

Labor costs for manufacturing apparel are similar in Central America and China. In both locations, workers earn around a dollar per hour and can produce over a hundred garments per day, from precut cloth. Labor costs are roughly $2 an hour in Eastern Europe, but producers are advantaged by being so close to the nearly 500 million consumers in the EU.

Management at Russell is keeping an eye on the proposed FTAA, which would widen access to the Latin American marketplace with its 500 million consumers. Maintaining a presence in Latin America would give Russell a favorable position for targeting new markets there. But progress on the FTAA has been slowed due to hostile public and governmental opposition from some South American countries. Governments in countries such as Bolivia and Venezuela argue that the FTAA will increase U.S. dominance in the region and harm local workers, subjecting them to sweatshop working conditions.

Meanwhile, regional integration is creating a larger market in the Western Hemisphere and new opportunities to source low-cost inputs from regional suppliers. While increased competition from China poses new challenges, the DR-CAFTA accord is helping to level the playing field. Russell management is concerned about manufacturing costs that are higher than competitors and is poised to consolidate much of its production into suppliers located close to its home market. At the same time, Russell is also contemplating new markets in the Americas and beyond.

Case Questions :

(a) Worldwide, China has the most absolute and comparative advantages in producing apparel. Free trade theory implies that retailers should import clothing from the most efficient country. Nevertheless, DR-CAFTA aims to promote Central American trade with the United States, and the United States has imposed quotas on imports from China. Given this, and the potential drawbacks of regional integration, would it be better to allow free trade to take its natural course ? That is, would it be better to rescind DR-CAFTA and allow apparel retailers to import from the most cost-effective suppliers, wherever they are located worldwide ?

(b) What are the advantages and disadvantages of DR-CAFTA to Honduran firms ? To Honduras as a nation ? Should free trade be extended throughout Latin America through the proposed FTAA ?

(c) Honduras is a poor country that faces the loss of jobs in its apparel sector from growing foreign competition. What can the Honduran government do to help keep jobs in Honduras ? The government can address some problems by attracting more foreign investment into Honduras. In what ways could foreign investment help ? What steps could the government take to attract more FDI ?

(d) Russell Corporation is a smaller player than its formidable rivals. Adidas and Nike. What should Russell do to counter these firms ? What should Russell do to counter the flood of low- cost athletic apparel now entering the United States from China ? What strategic approaches should Russell follow to ensure its future survival and success ?