UNIT 3 EMERGING HORIZONS IN BUSINESS

LESSON 7 PUBLIC AND PRIVATE SECTOR ENTERPRISES

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7. PUBLIC AND PRIVATE SECTOR ENTERPRISES

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7.1 Introduction

1. Public sector enterprises

Public Sector Enterprise often referred to as public sector, state sector, government owned undertakings or state-owned enterprises. These are formed under the legal proceedings, wholly or partly owned and controlled by the government and produce goods and services, have an explicit or extractable budget, and are supposed to finance their operating costs from their own resources.

Public sector enterprises are different from other two sub-sets of public sector, viz, the government and the public sector institutions. In a public sector enterprise, the majority of equity shares are owned by the government directly or indirectly through governmental institutions and the government has decision making control either directly or through its appointed bodies.

In majority of cases, public sector enterprise normally has three forms of organizational structure-

- Departmental undertakings
- Statutory corporations and
- Joint stock companies.

7.1.1 Some Major Forms of Public Sectors in India

a. Departmental undertakings

These PSUs are not formed by or with the consent of the legislative authority rather set up by the executive actions of government with/ without any capital structure and budget, and charged with the duty of carrying out specially defined functions within the purview of the government agencies that set them up.

These undertakings are not independent entities, although they enjoy a fairly high degree of monopoly. They are subject to budgetary, audit (CAGI in case of

India) and other controls of the government and are managed by ministers and civil servants. They are financed by annual appropriation from the Treasury, state or central, which also receives their revenues. A departmental undertaking is best suited where the main purpose of the enterprise is to collect revenue for the state and to provide public utilities and services at fair prices in larger public interest. Some examples of departmental undertakings in India are the Indian Railway, Postal Department, Department of Atomic Energy, Department of Telecom etc.

b. Statutory corporations

These are enterprises normally engaged in economic or manufacturing activities and are set up by the act of legislature or special acts behind their formation. These corporations are legal entities separate from the government and also the persons who conduct their affairs. Reserve bank of India, State Bank of India, Life and General insurance corporations, are examples of statutory corporations in the Indian context.

Shares of such corporations are in the name of the government and these are thus owned and controlled by the government. Statutory corporations enjoy extensive legal autonomy, and their rules, objectives, functions and duties are defined and specified in the act. Financing statutory corporations is not part of the Treasury and therefore, they can retain their revenues, and also spend as per the rules laid down by the statute. A statutory corporation set up by an Act cannot be regarded to fit in with the changed circumstances without legislative amendments.

c. Joint Stock Companies

They are set up under the provision of the companies act. 1956. In India, the term is used to refer to companies in which the government (either the central government or state or governments, or both) owned a majority (51 percent or more) of the company equity.

Establishment of companies is easier and is best suited where the nature of the work is substantially commercial. Most joint stock companies are not public sector enterprises in the strict sense. They are free from day-to-day control and intervention by the ministry or government departments and are not subject to government's budgetary discipline. They are managed by the board of directors, and are subject to audit and other provisions of the Companies Act.

The distinctive feature of a government controlled joint stock company is that the government, except when it sets up a mixed enterprise, puts up the entire capital. Such a company is wholly autonomous and makes its own rules and decisions in respect of investment, finance, personnel and commercial audit. BHEL, VSNL, MTNL. ONGC, NTPC, IOC, BPCL, HPCL are examples of joint stock forms of public sector enterprises in India.

d. Other forms

- **Boards:** Rubber board, Tea board, Coffee Board, Spices Board
- **Commissions:** Khadi & Village Industries Commission.

- **Regulatory & Development Authorities:** Municipal Corporations, Agra/ Delhi Development Authority, Telecom Regulatory Authority of India (TRAI)
- **Trusts:** Port Trusts of India, Press Trust of India.

7.1.2 DISINVESTMENTS

"Disinvestment involves the sale of equity and bond capital invested by the government in PSUs. It also implies the sale of government's loan capital in PSUs through securitization."

However, it is the government and not the PSUs who receive money from disinvestment. The fixation of share/bond price is an important aspect of disinvestment. Now, the Disinvestment Commission determines the share/bond price. Disinvested shares are listed, quoted and traded on the stock market. Indian and foreign financial institutions, banks, mutual funds, companies as well as individuals can buy disinvested shares / bonds.

Background

In India for almost four decades the country was pursuing a path of development in which public sector was expected to be the engine of growth. However, the public sector had overgrown itself and their shortcomings started manifesting in the shape of low capacity utilization, unproductive assets and low efficiency due to over manning , lack of innovative processes, poor work ethics and over capitalization due to substantial time and cost overruns, inability to innovate, take quick and timely decisions, large interference in decision making process etc.

Hence, Government started to deregulate the areas of its operation and subsequently, the disinvestment in Public Sector Enterprises (PSEs) was announced. The process of deregulation was aimed at enlarging competition and allowing new firms to enter the markets. The market was thus opened up to domestic entrepreneurs / industrialists and norms for entry of foreign capital were liberalized.

At present, due to the current revenue expenditure on items such as interest payments, wages and salaries of Government employees and subsidies, the Government is left with hardly any surplus for capital expenditure on social and physical infrastructure. While the Government would like to spend on basic education, primary health and family welfare, large amount of resources are blocked in several non-strategic sectors such as hotels, trading companies, consultancy companies, textile companies, chemical and pharmaceuticals companies, consumer goods companies etc.

Additionally, the continued existence of the PSEs is forcing the Government to commit further resources for the sustenance of many non-viable PSEs. The Government continues to expose the taxpayers' money to risk, which it can readily avoid. To top it all, there is a huge amount of debt overhang, which needs to be serviced and reduced before money is available to invest in infrastructure. All this makes Disinvestment of the Government stake in the PSEs absolutely imperative.

Moreover, the role of the State versus Market has been one of the major issues in development economics and policy. In a mixed economy such as India, historically the public sector had been assigned an important role. However, in the year 1991 the national economic policy underwent a radical transformation. The new policy of liberalization, privatization and globalization de-emphasized the role of the public sector in the nation's economy.

7.2 Privatization

Privatization is the incidence or process of transferring ownership of business from the public sector (government) to the private sector (business). In a broader sense, privatization refers to transfer of any government function to the private sector including governmental functions like revenue collection and law enforcement.

A very broad term--but most simply, privatization is the transfer of assets or service delivery from the government to the private sector institutions or commercial enterprises. Privatization runs a very broad range, sometimes leaving very little government involvement, and other times creating partnerships between government and private service providers (Public-Private Partnership) where government is still the dominant player or party.

The broader definition of privatization also includes a wide range of public-private partnerships, such as voucher systems. Even the creation of federal corporations, quasi government organizations and government-sponsored enterprises is often classified under the general category of privatization. In such organizations, though, it is often difficult to tell where the influence of government ends and that of the private sector begins.

7.2.1 Types and Techniques of Privatization

A variety of alternative service delivery techniques can be employed to maximize efficiency and increase service quality. Some methods will be more appropriate than others depending on the service. In searching for ways of cutting costs and increasing delivery, consider using a combination of these techniques:

- **Contracting Out** (also called "outsourcing"/ Franchising). The government competitively contracts with a private organization, for-profit or non-profit, to provide a service or part of a service.

- **Management Contracts.** The operation of a facility is contracted out to a private company. Facilities where the management is frequently contracted out include airports, wastewater plants, arenas and convention centers. On the other hand, the private sector can also build, finance and operate public infrastructure such as roads and airports, recovering costs through user charges. Several techniques commonly are used for privately building and operating infrastructure.

With Build-Operate-Transfer (BOT) arrangements, the private sector designs, finances, builds, and operates the facility over the life of the contract. At the end of this period, ownership reverts or transfers back to the government.

A variation of this is the Build-Transfer-Operate (BTO) model, under which title transfers to the government at the time construction is completed. For instance Turnkey project like telecommunication, power plants etc.

Finally, with Build-Own-Operate (BOO) arrangements, the private sector retains permanent ownership and operates the facility on contract

- **Public-Private Competition** (also called "managed competition," or "market testing"). When public services are opened up to competition, in-house public organizations are allowed to participate in the bidding process, generally in the case of units operating in manufacturing or processing industries.

- **Internal Markets.** Departments are allowed to purchase support services such as printing, maintenance, computer repair, stationeries, office equipments and training/consultancy from in-house providers or outside suppliers. In-house providers of support services are required to operate as independent business units competing against outside contractors for departments' business. Under such a system, market forces are brought to bear within an organization. Internal customers can reject the offerings of internal service providers if they don't like their quality or if they cost too much.

- **Vouchers.** Government pays for the service (for e.g. promotion of export industries in India); however, individuals are given redeemable certificates or provisions to purchase the service in the open market. These subsidize the consumer of the service, however, services are provided by the private sector. In addition to providing greater freedom of choice, vouchers bring consumer pressure to bear, creating incentives for consumers to shop around for services and for service providers to supply high-quality, low-cost services.

- **Self-Help** (also referred to as "transfer to non-profit organization"). Community groups and neighborhood organizations take over a service or government asset such as a local park. The new providers of the service also are directly benefiting from the service. Governments increasingly are discovering that by turning some non-core services—such as zoos, museums, fairs, remote parks and some recreational programs—over to non-profit organizations, they are able to ensure that these institutions don't drain the budget.

- **Volunteers.** Volunteers are used to provide all or part of a government service. Volunteer activities are conducted through a government volunteer program or through a non-profit organizational effort.

- **Corporatization.** Government organizations are reorganized or restructured along business lines. Typically they are required to pay taxes, raise capital on the market (with no government backing—explicit or implicit), and operate according to commercial principles. Government corporations focus on maximizing profits and achieving a favorable return on investment (ROI). They are freed from government interventions, procurement, personnel and budgetary control or regulations.

- **Asset Sale or Long-Term Lease.** Government sells or enters into long-term leases for assets such as Special Economic Zones (SEZs in India), airports, gas utilities or real estate to private firms, thus turning physical capital into financial capital. In a sale-leaseback arrangement, government sells the asset to a private sector entity and then leases it back.

7.3 References and Suggested Further Reading

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LESSON 8 GLOBALISATION

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8. GLOBALISATION

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- Globalization-History, Measurement and Impact.
- Multinational Organizations

8.1 Globalisation

8.1.1 Concept & History

The **International Monetary Fund** defines globalization as the growing economic interdependence of countries worldwide through increasing volume and variety of cross-border transactions in goods and services, free international capital flows, and more rapid and widespread diffusion of technology.

Meanwhile, the **International Forum on Globalization** defines it as the present worldwide drive toward a globalized economic system dominated by supranational corporate trade and banking institutions that are not accountable to democratic processes or national governments.

Globalization has many facets like Cultural, Economic & Political. Culturally, globalization is defined as a process of growing interdependence between all people of this planet. People are linked together economically and socially by trade, investments and governance. These links are spurred by market liberalization and information, communication and transportation technologies.

Cultural global ties also grow through globalization as news ideas and fashions through trade, travel and media move around the globe at lightning speed. Global brands such as Coca-Cola, Nike & Sony serve as common reference to consumers all over the World. An individual in China enjoys the same soft drink as an individual in Puerto Rico--at opposite ends of the globe. However, these ties may also cause strains: for example Western Ideas of freedom of expression may clash with Islamic views on Religious tolerance. And if not strains, critics contend this is really an imposition of cultural imperialism in order to preserve economic interests.

The economic aspects stressed in globalization are trade, investment and migration. The globalization of trade entails that human beings have greater access to an array of goods and services never seen before in human history.

From German cars, to Colombian coffee, from Chinese clothing, to Egyptian cotton, from American music to Indian software, human beings may be able to purchase a wide range of goods and services. The globalization of investment takes place through Foreign Direct Investment, where multinational companies directly invest assets in a foreign country, or by indirect investment where individuals and institutions purchase and sell financial assets of other countries. Free migration allows individuals to find employment in jurisdictions where there are labor shortages.

In the end, the political aspects of globalization are evidenced when governments create international rules and institutions to deal with issues such as trade, human rights, and the environment. Among the new institutions and rules that have come to fruition as a result of globalization are the World Trade Organization (WTO), the Euro currency (Euro), the North American Free Trade Agreement (NAFTA), to name a few. Whether a government is to consciously open itself to cross-border links, is the central question of this aspect.

- **History**

A global economy is an unprecedented phenomenon, not to be confused with economic internationalization. In fact, a world economy has existed since the 16th century, based on the development of international trade, foreign direct investment and migration.

Globalization can be traced to times when Buddhism spread from India to China in 1st century AD. That was when cultural links between both countries were established. By 1300 AD, the Song Dynasty in China linked Europe and China by land and sea across Eurasia and the Indian Ocean. The year 1300 saw the creation of the Ottoman Empire which spanned Europe, North Africa, and the Middle East, and connected the dynasties in Central Asia and India.

This led to the expansion of trading activities between Europe and Asia. By 1300, networks of trade ran from England to China, France, Italy, across the Mediterranean to Egypt, and then to Central Asia (the Silk Route). The trade in commodities continued well into the 17th century. By 1800, the Atlantic and Indian Ocean systems were connected to one another through the flow of commodities and by the operations of the British, French, and Dutch overseas companies.

The economic conditions that prevailed in the eighteenth century continued well into the nineteenth century. With the introduction of railways and steamships, transportation costs came down significantly, and this created new circuits of capital accumulation. In the twentieth century, technological developments were further reducing natural barriers like geographical distance. The cost of information processing and communication fell significantly in the last few decades, accelerating the pace of globalization.

Firms go abroad for organizational and environmental reasons. Organizational factors are internal to the organization, while environmental reasons are external to the organization. Internal reasons might range from wanting to exploit worldwide market imperfections to opportunities that arise in different stages of the lifecycle of a firm’s product. There are six ways to enter a foreign market. They are: exporting, turnkey projects, licensing, franchising, setting up a joint venture with a host country firm, and setting up a wholly-owned subsidiary in the host country.

An organization goes through five stages of evolution: domestic, international, multinational, global, and transnational stages before becoming a metanational corporation. The classification is based on the firm's orientation at each stage. To be competitive, companies have to constantly innovate and make their own products obsolete. Competition has transformed the marketplace from a seller's market to a buyer's market where the customers' focus is on value. Metanational companies see the world as a place with specialized knowledge pockets: market intelligence, technology and capabilities, scattered around. These companies sense the untapped potential in these knowledge pockets, and try to exploit it to the fullest extent.

8.1.2 Other Globalization Time-Lines (Modern Time)

In general use within the field of economics and political economy, however, it is a history of increasing trade between nations based on stable institutions that allow firms in different nations to exchange goods and services with minimal friction.

The period of the gold standard and liberalization of the 19th century is often called "The First Era of Globalization". This era grew along with industrialization. In essence, it was argued that nations would trade effectively, and that any temporary disruptions in supply or demand would correct themselves automatically. The institution of the gold standard came in steps in major industrialized nations between approximately 1850 and 1880, though exactly when various nations were truly on the gold standard is contentiously debated.

Globalization in the era since World War II has been driven by trade negotiation rounds, originally under the auspices of GATT, which led to a series of agreements to remove restrictions on "free trade". The Uruguay round led to a treaty to create the World Trade Organization or WTO, to mediate trade disputes. Other bi- and trilateral trade agreements, including sections of Europe's Maastricht Treaty and the North American Free Trade Agreement have also been signed in pursuit of the goal of reducing tariffs and barriers to trade.

(Source: http://www.legalserviceindia.com/articles/glob_is.htm)

- **Stages:**
  - **First Wave**: globalization of colonization (3/4th of world colonized by UK, France, Spain, Portugal)
  - **Second wave**: Self-reliance, Independence and decolonization
  - **Third wave**: Religious Globalization (Missionaries from west came to east and vice versa)
  - **Fourth wave (Modern Era)**: Economic Globalization.

8.2 Measuring Globalization

Globalization has had an impact on different cultures around the world. Japanese McDonald's fast food is an evidence of international integration. Looking specifically at economic globalization, demonstrates that it can be measured in different ways. These centers around the four main economic flows that characterize globalization:

- **Goods and services,** e.g. exports plus imports as a proportion of national income or per capita of population

- **Labor/people,** e.g. net migration rates; inward or outward migration flows, weighted by population

- **Capital,** e.g. inward or outward direct investment as a proportion of national income or per head of population

- **Technology,** e.g. international research & development flows; proportion of populations (and rates of change thereof) using particular inventions (especially 'factor-neutral' technological advances such as the telephone, motorcar, broadband)

As globalization is not only an economic phenomenon, a multivariate approach to measuring globalization is the recent index calculated by the Swiss think tank KOF. The index measures the three main dimensions of globalization:

- **Economic**
- **Social, and**
- **Political.**

In addition to three indices measuring these dimensions, an overall index of globalization and sub-indices referring to actual economic flows, economic restrictions, data on personal contact, data on information flows, and data on cultural proximity is calculated. Data is available on a yearly basis for 122 countries, as detailed in Dreher, Gaston and Martens (2008). According to the index, the world's most globalized country is- Belgium, followed by Austria, Sweden, the United Kingdom and the Netherlands. The least globalized countries according to the KOF-index are Haiti, Myanmar the Central African Republic and Burundi.

A.T. Kearney and Foreign Policy Magazine jointly publish another Globalization Index. According to the 2006 index, Singapore, Ireland, Switzerland, the U.S., the Netherlands, Canada and Denmark are the most globalized, while Indonesia, India and Iran are the least globalized among countries listed.

8.3 Effects of globalization

Globalization has various aspects which affect the world in several different ways such as:

- **Industrial** - emergence of worldwide production markets and broader access to a range of foreign products for consumers and companies. Particularly movement of material and goods between and within national boundaries.

- **Financial** - emergence of worldwide financial markets and better access to external financing for borrowers. Simultaneous though not necessarily purely globalist is the emergence of under or un-regulated foreign exchange and speculative markets.

- **Economic** - realization of a global common market, based on the freedom of exchange of goods and capital.

- **Political** - some use "globalization" to mean the creation of a world government, or cartels of governments (e.g. WTO, World Bank, and IMF) which regulate the relationships among governments and guarantees the rights arising from social and economic globalization. [13] Politically, the United States has enjoyed a position of power among the world powers; in part because of its strong and wealthy economy. With the influence of globalization and with the help of The United States' own economy, the People's Republic of China has experienced some tremendous growth within the past decade. If China continues to grow at the rate projected by the trends, then it is very likely that in the next twenty years, there will be a major reallocation of power among the world leaders. China will have enough wealth, industry, and technology to rival the United States for the position of leading world power.

- **Informational** - increase in information flows between geographically remote locations. Arguably this is a technological change with the advent of fibre optic communications, satellites, and increased availability of telephony and Internet.

- **Language** - the most popular language is English

    - About 75% of the world's mail, telexes, and cables are in English.

    - Approximately 60% of the world's radio programs are in English.

    - About 90% of all Internet traffic is using English.

- **Competition** - Survival in the new global business market calls for improved productivity and increased competition. Due to the market became worldwide not specific area, there are many industries around the world. Industries have to upgrade their products and use technology skillfully for facing the competition and increasing their competitive.[16]

- **Cultural** - growth of cross-cultural contacts; advent of new categories of consciousness and identities which embodies cultural diffusion, the desire to increase one's standard of living and enjoy foreign products and ideas, adopt new technology and practices, and participate in a "world culture". Some bemoan the resulting consumerism and loss of languages. Also see Transformation of culture.

- **Ecological**- the advent of global environmental challenges that might be solved with international cooperation, such as climate change, cross-boundary water and air pollution, over-fishing of the ocean, and the spread of invasive species. Since many factories are built in developing countries with less environmental regulation, globalism and free trade may increase pollution. On the other hand, economic development historically required a "dirty" industrial stage, and it is argued that developing countries should not, via regulation, be prohibited from increasing their standard of living.

- **Social** (International cultural exchange) - increased circulation by people of all nations with fewer restrictions.

    - Spreading of multiculturalism, and better individual access to cultural diversity (e.g. through the export of Hollywood and Bollywood movies). Some consider such "imported" culture a danger, since it may supplant the local culture, causing reduction in diversity or even assimilation. Others consider multiculturalism to promote peace and understanding between peoples.

    - Greater international travel and tourism

    - Greater immigration, including illegal immigration

    - Spread of local consumer products (e.g. food) to other countries (often adapted to their culture).

    - Worldwide fads and pop culture such as Pokémon, Sudoku, Numa Numa, Origami, Idol series, YouTube, Orkut, Facebook, and MySpace. Accessible to those who have Internet or Television, leaving out a substantial segment of the Earth's population.

    - Worldwide sporting events such as FIFA World Cup and the Olympic Games.

    - Incorporation of multinational corporations in to new media. As the sponsors of the All-Blacks rugby team, Adidas had created a parallel website with a downloadable interactive rugby game for its fans to play and compete.

- **Technical**

    - Development of a global telecommunications infrastructure and greater transborder data flow, using such technologies as the Internet, communication satellites, submarine fiber optic cable, and wireless telephones

    - Increase in the number of standards applied globally; e.g. copyright laws, patents and world trade agreements.

- **Legal/Ethical**
    - The creation of the international criminal court and international justice movements.
    - Crime importation and raising awareness of global crime-fighting efforts and cooperation.

While it is all too easy to look at the positive aspects of Globalization and the great benefits that are apparent everywhere, there are also several negative occurrences that can only be the result of or major motivating factors that inspire some corporations to globalize.

Globalization – the growing integration of economies and societies around the world – has been one of the most hotly-debated topics in international economics over the past few years. Rapid growth and poverty reduction in China, India, and other countries that were poor 20 years ago, has been a positive aspect of globalization. But globalization has also generated significant international opposition over concerns that it has increased inequality and environmental degradation.

8.4 Multinational Corporations (MNCs)

Though there is no universally acceptable definition of MNCs they may be generally defined as companies that operate in more than one country and invest directly in operations instead of being involved in licensing, franchising, etc. The operations are not just confined to sales but also involve manufacturing and R&D. MNCs tend to be oligopolistic and dynamic in sensing and exploiting local opportunities.

The various subsidiaries of an MNC enjoy substantial autonomy in decision making, except in some critical areas, which are handled by the parent firm. MNCs can be vertically or horizontally integrated. They can also take the form of conglomerates, joint ventures, or strategic alliances. The growth of MNCs in the last few decades may be attributed to the revolution in information technology and the removal of restrictions on capital flows by several countries around the globe. Many theories have been framed to explain the evolution of MNCs.

8.5 Organizational Structure of MNCs

Organizational structure is a representation of the formal reporting relationships within an organization. Span of control refers to the maximum number of subordinates a manager can effectively supervise. A narrow span of control means less number of people reporting to a manager and a wide span means more subordinates reporting to one manager.

While a narrow span of control creates a tall organization with many managers and centralized decision making, wide span creates a flat organization with fewer managers and more delegation of authority. The degree to which authority is delegated determines centralization and decentralization.

Though centralization helps avoid conflict of interest that could arise in a decentralized environment, it generally leads to slower, ineffective and inefficient decision-making. Horizontal differentiation is concerned with how the departments in an organization function together. An organization based on functions is the traditional and the most logical.

But a firm offering many product lines will find this structure less successful. In a product division based organizational structure, product heads are responsible for all functions relating to a product. This enables the managers to gain expertise of various functions relating to the product. Marketing plans can vary among product groups and need not be tied up with the overall organizational marketing plan.

Most MNCs in their initial stages of globalization employed an international division covering certain regions of the world to supervise the functions in those regions. But conflicts could arise between the functional heads and the heads of the international division.

WorldWide Area Structure and Strategic Business Units (SBU) are more popular forms of organizational structure in big corporations. SBUs function as independent organizations with a separate income statement and balance sheet. But the challenge of globalization and the growth in technology have brought about more complex organizational structures like the Matrix structure and the management networks.

Matrix organizations are a hybrid of the functional and divisional structures. Normally, this results in a subordinate having to report to two bosses. But matrix structures can prove very effective without any conflict in the reporting relationships, if they are well chalked out. Network or virtual organizations use technology to collect and disseminate information. They identify customer requirements and deliver products and services through a network of specialists.

8.6 References and Suggested Further Reading

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LESSON 9 REGIONAL TRADING BLOCS

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9. REGIONAL TRADING BLOCS

9.0 Objectives

- 1.Regional Trading Blocs
- 2.Conceptual framework of Free trade area, Custom union, Economic Union etc.

9.1 Modes of Entry/ Internationalisation

- Exporting
- Turnkey Projects
- Licensing
- Franchising
- Wholly owned Subsidiaries
- Joint Ventures
- Strategic Alliance

Export: The advantage of exporting is that it facilitates realization of experience curve economies and prevents cost of setting up manufacturing operations in another country. Disadvantages include high transport costs, trade barriers and problems with local marketing agents.

Turnkey projects: Turnkey projects allow firms to export their process technology where FDI is not permitted. The disadvantage is that the firm may create competitors in the process.

Licensing: The main advantage of licensing is that the licensee bears the cost and risk of opening a foreign market. The disadvantages include the risk of losing technological know-how to the licensee.

Franchising: The advantage of franchising is similar to that of licensing and the disadvantage is that the franchiser has to keep strict control over the franchisee.

Wholly owned Subsidiary: The advantages of wholly owned subsidiary include tight control over operations and technology. However, the firm has to bear all the costs and risks of opening a foreign market.

Joint Ventures: The advantage of joint ventures is the partners share the costs and risk of opening a foreign market and of gaining knowledge and political influence. The disadvantage is the risk of losing control over technology.

Strategic alliance: The advantage of strategic alliance is that it facilitates entry into foreign market and enables partners to share the fixed costs and risks associated with new products and processes. The disadvantage is that firms may sometimes have to give away technological know-how and market access to the alliance partner. To make the alliance work, factors to be taken into consideration are selection of partner, structure of the alliance and management of the alliance. The key issues involved in managing alliances are building trust and learning from each other.

- Continuum of Internationalization:

International –Multinational/Transnational-Global

- Entry strategies:

Export-Licensing-Franchising-Turnkey projects-subsidiary-Joint ventures

- Organizational structure:

International division-Functional-Geographic-Product-Matrix-Network

9.2 Trade block

A trade bloc is a large free trade area formed by one or more tax, tariff and trade agreements. Typically trade pacts that define such a bloc specify formal adjudication bodies, e.g., North American Free Trade Agreement (NAFTA) trade panels. This may include even a more democratic and participative system, as the European Union (EU) and its parliament.

Particularly since the demise of most of the world's empires, a number of international— generally regionally based—economic blocs have been developed to promote trade between member states.

Several blocs also have stated or implicit political goals—notably the EU. Varieties of economic blocs include free trade areas, customs unions, single markets, and economic and monetary unions.

One of the first economic blocs was the German Customs Union (Zollverein) initiated in 1834, formed on the basis of the German Confederation and subsequently German Empire from 1871.

A trade bloc is established through a trade pact (or pacts) covering different issues of the economic integration.

9.3 Most active regional trade blocs

It is possible that a country is member of two (or more) different blocs. To avoid overlapping for this classification such countries are only included in the most active of the blocs in question. The "activity" of each block is measured by the following three criteria:

- To have greater real practical achievements (not only declarations that are not followed by actual actions by its members)
- To have more recent (or regular) activities (meetings, new agreements, other internal procedures)
- To have more ambitious plans for future integration and a tighter timescale for it.

Examples:

9.3.1 Association of Southeast Asian Nations (ASEAN)

- Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam
- candidate: Timor-Leste
- +3: China, Japan, South Korea

9.3.2 European Union (EU)

  - Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, United Kingdom

9.3.3 North American Free Trade Agreement (NAFTA)

- Canada, Mexico, United States of America

9.3.4 South Asian Association for Regional Cooperation (SAARC)

- Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, Sri Lanka

9.3.5 Case-Study (European Union EU)

- The European Union (EU) is a political and economic union of 27 member states, located primarily in Europe. It was established by the Treaty of Maastricht in 1993 upon the foundations of the pre-existing European

Economic Community. With almost 500 million citizens, the EU combined generates an estimated 30% share of the world's nominal gross domestic product (US$16.8 trillion in 2007).

- The EU has developed a single market through a standardised system of laws which apply in all member states, guaranteeing the freedom of movement of people, goods, services and capital.

- It maintains a common trade policy, agricultural and fisheries policies, and a regional development policy. Fifteen member states have adopted a common currency, the euro. It has developed a role in foreign policy, representing its members in the World Trade Organisation, at G8 summits and at the United Nations. Twenty-one EU countries are members of NATO.

- The EU operates through a hybrid system of intergovernmentalism and supranationalism. In certain areas it depends upon agreement between the member states.

- However, it also has supranational bodies, able to make decisions without the agreement of all national governments. Important institutions and bodies of the EU include the European Commission, the European Parliament, the Council of the European Union, the European Council, the European Court of Justice and the European Central Bank. EU citizens elect the Parliament every five years.

9.4 Free Trade Area

- **Free trade area** is a designated group of countries that have agreed to eliminate tariffs, quotas and preferences on most (if not all) goods between them. It can be considered the second stage of economic integration.

- **Free trade area** is a result of a free trade agreement (a form of trade pact) between two or more countries. Free trade areas and agreements (FTAs) are cascadable to some degree — if some countries sign agreement to form free trade area and choose to negotiate together (either as a trade bloc or as a forum of individual members of their FTA) another free trade agreement with some external country (or countries) — then the new FTA will consist of the old FTA plus the new country (or countries).

- Countries choose this kind of economic integration form if their economical structures are complementary. If they are competitive, they will choose customs union. Unlike a customs union, members of a free trade area do not have the same policies with respect to non-members, meaning different quotas and customs.

- To avoid evasion (through re-exportation) the countries use the system of certification of origin most commonly called rules of origin, where there is a requirement for the minimum extent of local material inputs and local transformations adding value to the goods. Goods that don't cover these minimum requirements are not entitled for the special treatment envisioned in the free trade area provisions.

- Cumulation is the relationship between different FTAs regarding the rules of origin — sometimes different FTAs supplement each other, in other cases there is no cross-cumulation between the FTAs.

- Within an industrialized country there are usually few if any significant barriers to the easy exchange of goods and services between parts of that country. For example, there are usually no trade tariffs or import quotas; there are usually no delays as goods pass from one part of the country to another (other than those that distance imposes); there are usually no differences of taxation and regulation. Between countries, on the other hand, many of these barriers to the easy exchange of goods often do occur. It is commonplace for there to be import duties of one kind or another (as goods enter a country) and the levels of sales tax and regulation often vary by country.

- The aim of a free trade area is to so reduce barriers to easy exchange that trade can grow as a result of specialisation, division of labour, and most importantly via (the theory and practice of) comparative advantage. The theory of comparative advantage argues that in an unrestricted marketplace (in equilibrium) each source of production will tend to specialize in that activity where it has comparative (rather than absolute) advantage.

- The theory argues that the net result will be an increase in income and ultimately wealth and well-being for everyone in the free trade area. However the theory refers only to aggregate wealth and says nothing about the distribution of wealth. In fact there may be significant losers, in particular among the recently protected industries with a comparative disadvantage. The proponent of free trade can, however, retort that the gains of the gainers exceed the losses of the losers.

9.5 Custom Union

A customs union is a free trade area with a common external tariff. The participant countries set up common external trade policy, but in some cases they use different import quotas. Common competition policy is also helpful to avoid competition deficiency.

Purposes for establishing a customs union normally include increasing economic efficiency and establishing closer political and cultural ties between the member countries.

9.6 Common Market

A common market is a customs union with common policies on product regulation, and freedom of movement of the factors of production (capital and labour) and of enterprise. The goal is that movement of capital, labour, goods, and services between the members is as easy as within them. This is the fourth stage of economic integration.

Sometimes a single market is differentiated as a more advanced form of common market. In comparison to common a single market envisions more efforts geared towards removing the physical (borders), technical (standards) and fiscal (taxes) barriers among the member states. These barriers obstruct the freedom of movement of the four factors of production. To remove these barriers the member states need political will and they have to formulate common economic policies.

9.7 Economic and Monetary Union

An economic and monetary union is a single market with a common currency. It is to be distinguished from a mere currency union (e.g. the Latin Monetary Union in the 1800s), which does not involve a single market. This is the fifth stage of economic integration. EMU is established through a currency-related trade pact.

9.8 Assignment Questions (Lesson 7, 8 & 9)

1. Discuss the concept and organizational types of PSUs.
2. Explain Disinvestments. Highlight the approaches of Privatization.
3. Discuss Globalization and its potential impacts.
4. Explain trading blocks and enumerate some key examples of trade blocs.
5. What is free trade area? What are the stages of trade integration and evolution? Explain.
6. Describe the modes of entry for International business operations. .

9.9 References

1. www.icmrindia.org
2. en.wikipedia.org

9.10 Suggested Further Reading

1. Bhushan, Y.K. 2000. Business Organization. Sultan Chand & Sons, New Delhi.

2. Basu C.R. 2000. Fundamentals of Higher Secondary Business Organization. Macmillan Publishers India, New Delhi.

3. Entrepreneurship Development- New Venture Creation David Holt

4. Student’s Guide to Business Organisation, Dr. Neeru Vashistha,Taxman