**Chapter 2: National Differences in Political, Economic, and Legal Systems**

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# Learning Objectives

2-1 Understand how the political systems of countries differ.

2-2 Understand how the economic systems of countries differ.

2-3 Understand how the legal systems of countries differ.

2-4 Explain the implications for management practice of national difference in political economy.

# Chapter Summary

This chapter focuses on the different political, economic, and legal systems that are influential in the world. It is made clear to the reader that these differences are significant and must be clearly understood by the managers of international firms. The section focusing on legal systems includes a discussion of intellectual property including patents, copyrights, and trademarks. Protecting intellectual property is particularly challenging in international trade. Finally, the chapter ends with a discussion of the managerial implications of differing political, economic, and legal systems of a country.

# Chapter Opening Activity

In this activity, students will research and reflect on legal and political systems in several countries. Use [globaledge.msu.edu](https://globaledge.msu.edu/) to research the legal and representative political systems in the United States, Canada, Britain, and other advanced economies. The basic tenet of the U.S. system is preservation of individual rights, and this may be grounded in America’s passion with individualism. Explain that the U.S. scores very high on Hofstede’s individualism versus collectivism dimension of cultural differences (more on this in Chapter 4). Suggest that individualistic cultures value:

* Individual responsibility for decisions
* Individual freedoms and achievement
* Decisions can be rapid
* Importance of nuclear family
* Rewards given to those who venture into business alone—the entrepreneur

Cultures including Russian, Chinese, and Indian may be more collectivist and may employ more authoritarian political systems and planned economic systems. Suggest that collectivist cultures value:

* Group and shared responsibility for decisions
* Decisions may be slow, consensual, and consultative
* Group nurtures individual.
* Importance of extended families and in-group priorities
* Recognition of collective business ventures, with family and friends

As students work through this chapter, ask them to research the evolution of political and legal systems in a country they are familiar with (not the U.S.) by using [globaledge.msu.edu](https://globaledge.msu.edu/). Some traditionally authoritarian countries are transitioning towards representative governments: suggest that this may be in response to changes driven by globalization and technology.

# Chapter Outline

China’s Mixed Economy

opening case

**Summary**

The opening case explores the political economy of China. Over the past four decades, China has transformed from a one-party state where private enterprise was banned, and all economic activity was centrally planned to a thriving economy blending state-owned enterprises with privately held corporations. The transformation began when it became apparent that the Marxist model that had been in place was not working. Following a series of reforms, China embarked on its path as one of the world’s fastest growing economies. Today, the country boasts the world’s second largest economy as measured by nominal GDP, and the largest when measured by GDP on a purchasing power basis.

**Discussion Questions**

1. How can China’s political economy be characterized? How do its policies facilitate economic growth? What does the country’s blend of state-owned and privately held companies mean for the current business environment and for the future business environment?

As a one-party state ruled by the Communist Party, China clearly does not enjoy the freedoms of other large economies like the United States. Instead, China, with its mix of private sector companies and state-owned enterprises, operates as a mixed economy. Indeed, in China, the economy is described as a “socialist market economy” dominated by large multinational tech companies such as Alibaba, Tencent, Baidu, and Huawei. Certain sectors of China’s economy remain the domain of state-owned enterprises. In banking for example, nearly 90 percent of value added is attributed to state-owned corporations. However, regardless of ownership, the influence of the state is felt across all sectors of the economy and is central to economic growth in the country. For companies considering doing business in China, understanding this dynamic is essential. Huawei, for example, may have received as much as $75 billion in state-support, making the playing field for tech companies anything but level.

2. Discuss China’s reliance on the state as a driver of economic growth. What does it mean for the efficiency and productivity of companies receiving assistance? What are the implications of a large state-owned sector for trade relations with other countries?

The presence of the visible hand in driving economic growth in China is evident across numerous sectors, and especially in industries related to the development of infrastructure. While government assistance typically leads to greater inefficiency and productivity, for China, the biggest issue may be its impact on trade relations with other countries. The United States and other nations have made it clear that China’s assistance to its companies gives them an unfair advantage in global trade. Donald Trump attempted to force China’s hand on the issue when he levied hefty tariffs on steel imports from China. So far, however, China seems to be unwilling to back down. Going forward, it is expected that Joe Biden’s administration could work together with European counterparts and present a united front to China on trade, something that could prompt China to reassess its policies.

**Teaching Tip:** Students can explore China’s political economy in greater detail at https://www.worldbank.org/en/country/china/overview.

**Lecture Note:** To extend this discussion, consider <https://www.nytimes.com/2020/10/18/business/china-economy-covid.html> and <https://www.economist.com/finance-and-economics/2020/10/31/if-chinas-economy-is-so-strong-why-isnt-its-currency-stronger>.

**Video Note:** To extend this discussion, consider *Tech Decoupling: China’s Race to End Its Influence on the U.S.*  in the International Business Library at [http://bit.ly/MHEIBVideo](https://na01.safelinks.protection.outlook.com/?url=http%3A%2F%2Fbit.ly%2FMHEIBVideo&data=01%7C01%7Canke.weekes%40mheducation.com%7Ca25dc9eb643246ce47ad08d41a1dec6d%7Cf919b1efc0c347358fca0928ec39d8d5%7C1&sdata=PGTbnKJeqo4tban6vepacEyP5nezpxGm42CaB%2B3aOG8%3D&reserved=0). Click “Ctrl+F” on your keyboard to search for the video title.

CONNECT

Case Analysis

*China’s Mixed Economy*

Summary

This activity focuses on differences in political and economic systems between countries, and specifically on China’s mixed economy. Described by China as a “socialist market economy”, China blends a vibrant private sector with a significant state-owned sector.

Activity

Students are asked to read a short case exploring China’s mixed economy and then respond to a series of questions related to the case.

Class Discussion

A country’s political and economic systems can have important implications for international businesses and how they do business in that country. Discuss the situation in China. What does it mean for companies looking to do business in the country? How does China’s blend of public and private enterprise create opportunities and challenges for foreign companies?

**Introduction**

A) Different countries have different political, economic, and legal systems. Cultural practices can vary dramatically from country to country, as can the education and skill level of the population. All of these differences have major implications for the practice of international business.

B) This chapter explores how the political, economic, and legal systems of countries differ. Together these systems are known as the **political economy** of a country.

**Political Systems**

A) By **political system,** we mean the system of government in a nation. Political systems can be assessed according to two related dimensions. The first is the degree to which they emphasize collectivism as opposed to individualism. The second dimension is the degree to which they are democratic or totalitarian.

**COLLECTIVISM AND INDIVIDUALISM**

B) **Collectivism** refers to a system that stresses the primacy of collective goals over individual goals. When collectivism is emphasized, the needs of the society as whole are generally viewed as being more important than individual freedoms. Advocacy of collectivism can be traced to Plato, in modern times the collectivist mantle has been picked up by **socialists**, and their champion, Karl Marx.

**Socialism**

C) **Communists** generally believed that this could only be achieved through violent revolution and totalitarian dictatorship, while s**ocial democrats** worked to achieve the same goals by democratic means.

D) While state-owned firms might have been intended to promote the public interest, experience suggests that this is not always the case. In many countries, the performance of state-owned companies has been poor. Consequently, a number of Western democracies voted social democratic parties out of office and moved toward free market economies by selling state-owned enterprises to private investors, a process known as **privatization**.

**Individualism**

E) **Individualism** refers toa political philosophy that an individual should have freedom over his or her economic and political pursuits. In contrast to collectivism, individualism stresses that the interests of the individual should take precedence over the interests of the state.

F) While collectivism asserts the primacy of the collective over the individual, individualism asserts the opposite. This ideological difference shapes much of recent history and the Cold War. Individualism is usually associated with democratic political systems and free markets.

country FOCUS: Putin’s Russia

**Summary**

This feature explores the state of the Russian economy since the collapse of the USSR, and in particular under the leadership of Vladimir Putin. While Russia’s economy has grown rapidly in the so-called pseudo-democracy that now exists, the country is heavily dependent on oil and gas exports—both industries that are still largely state controlled. Indeed, the presence of the government remains an issue for the economy as a whole. Currently, roughly half of the total economy is still controlled by the state, a situation that could hamper future growth. Even private enterprises are dealing with considerable red tape and corrupt government officials. Freedom House ranks Russia low for civil and political liberties, a ranking that was confirmed by Putin’s 2014 decision to annex the Crimea region of neighboring Ukraine.

**Discussion Questions**

1. Discuss the implications of corruption on the development and growth of a country. How can Russia’s current political system best be described? What conclusions can you draw regarding Russia’s economic prospects?

Since the collapse of the USSR, Russia has struggled to get its economy on track. Today, there is considerable concern that the government’s involvement in the business sector combined with high level of corruption could hamper future economic growth. High levels of corruption and Putin’s authoritarian approach to governing create an uncertain environment for foreign investors. In addition, the sanctions brought about by the annexing of the Crimea region of Ukraine have further disrupted economic growth

2. Discuss the pros and cons of investing in Russia. As a CEO of a company in the oil industry would you invest in Russia? How does a stable government affect a country’s ability to attract investment?

In general, companies exploring the opportunity to expand into foreign markets will be more attracted to countries where it is easy to conduct business as compared to locations where it is not. That being said, many students will probably suggest that the situation in Russia today is a tricky one. Corruption in the country is high, and many students will probably advise caution given that the oil industry is still largely under the control of the government. Some students may also wonder whether sanctions by the United States and/or the European Union could further complicate matters if Putin’s aggressive stance towards Ukraine continues to persist. Students may also wonder how the relationship between Donald Trump and Vladimir Putin will evolve.

**Lecture Note:** To extend the discussion of Russia’s economy under Vladimir Putin, consider <https://www.bloomberg.com/view/articles/2018-08-29/russia-s-economy-is-stuck-in-a-putin-trap>.

**Teaching Tip:**Information on doing business in Russia is available at <http://www.doingbusiness.org/data/exploreeconomies/russia>.

**Video Note:** The relationship between the United States and Russia has been under significant scrutiny as a result of Russia’s meddling in the 2016 Presidential election. To learn more, consider *Tech Companies Set to Tell Congress About Russian Election Meddling* in the International Business Library at [http://bit.ly/MHEIBVideo](https://na01.safelinks.protection.outlook.com/?url=http%3A%2F%2Fbit.ly%2FMHEIBVideo&data=01%7C01%7Canke.weekes%40mheducation.com%7Ca25dc9eb643246ce47ad08d41a1dec6d%7Cf919b1efc0c347358fca0928ec39d8d5%7C1&sdata=PGTbnKJeqo4tban6vepacEyP5nezpxGm42CaB%2B3aOG8%3D&reserved=0). Click “Ctrl+F” on your keyboard to search for the video title.

Additionally, our McGraw-Hill Education International Business Video Library at [http://bit.ly/MHEIBVideo](https://na01.safelinks.protection.outlook.com/?url=http%3A%2F%2Fbit.ly%2FMHEIBVideo&data=01%7C01%7Canke.weekes%40mheducation.com%7Ca25dc9eb643246ce47ad08d41a1dec6d%7Cf919b1efc0c347358fca0928ec39d8d5%7C1&sdata=PGTbnKJeqo4tban6vepacEyP5nezpxGm42CaB%2B3aOG8%3D&reserved=0) provides an ongoing stream of updated video suggestions correlated by key concept and major topic. Every new clip posted is supported by teaching notes and discussion questions. Please feel free to leave comments in the library that you feel might be helpful to your colleagues.

**DEMOCRACY AND TOTALITARIANISM**

G)Democracyand totalitarianism are at different ends of a political dimension. **Democracy** refers to a political system in which government is by the people, exercised either directly or through elected representatives. **Totalitarianism** is a form of government in which one person or political party exercises absolute control over all spheres of human life, and opposing political parties are prohibited.

**Democracy**

H) Democracy in its pure state, with each individual voting on every issue, has generally been replaced by **representative democracy**, where elected representatives vote on behalf of constituents.

**Totalitarianism**

I) Under totalitarianism, a single political party, individual, or group of individuals monopolize the political power and do not permit opposition. There are four major forms of totalitarianism: **communist totalitarianism**, (a form of totalitarianism that advocates achieving socialism through totalitarian dictatorship), **theocratic totalitarianism**, (a form of totalitarianism in which political power is monopolized by a party, group, or individual that governs according to religious principles), **tribal totalitarianism** (a form of totalitarianism found mainly in Africa in which a political party that represents the interests of a particular tribe monopolizes power), **right-wing** **totalitarianism** (a form of totalitarianism in which individual economic freedom is allowed but individual political freedom is restricted in the belief that it could lead to communism). There has been a general trend away from communist and right-wing totalitarianism and towards democracy.

Video Note: Hong Kong’s two system, one country model is under threat as moves by Beijing effectively destroy the freedoms enjoyed by citizens of the city since its independence from Great Britain. To learn more, consider *From Tokyo to Sydney, Cities Vie to Replace Hong Kong as Asia Hub* in the International Business Library at [http://bit.ly/MHEIBVideo](https://na01.safelinks.protection.outlook.com/?url=http%3A%2F%2Fbit.ly%2FMHEIBVideo&data=01%7C01%7Canke.weekes%40mheducation.com%7Ca25dc9eb643246ce47ad08d41a1dec6d%7Cf919b1efc0c347358fca0928ec39d8d5%7C1&sdata=PGTbnKJeqo4tban6vepacEyP5nezpxGm42CaB%2B3aOG8%3D&reserved=0). Click “Ctrl+F” on your keyboard to search for the video title.

**Pseudo-Democracies**

J) The political system in many nations of the world can best be described as imperfect or pseudo-democracies—lying somewhere between a pure democracy and complete totalitarianism.

CONNECT

Click and Drag

*Differences in Political Systems*

Summary

This activity focuses on differences in political systems. Political systems can be assessed according to two dimensions: the degree to which they emphasize collectivism as opposed to individualism and the degree to which they are democratic or totalitarian. International businesses need to be aware of the differences in political systems and appreciate the significance of these national differences.

Activity

Students are asked to match various political systems to the country where they are in place.

Class Discussion

A country’s political system shapes its economic and legal systems. Discuss the different types of political systems, how they are reflected in a country’s economic and legal systems, and what they mean for companies doing business in those countries.

**Economic Systems**

A) In countries where individual goals are given primacy over collective goals, a free market system is more likely to exist. In contrast, in countries where collective goals are dominant, enterprises may be state-owned, and markets may be restricted. Three broad types of economic systems can be identified—a market economy, a command economy, and a mixed economy.

**MARKET ECONOMY**

B) In a pure **market economy**, the goods and services that a country produces, and the quantity in which they are produced, is not planned by anyone. Rather price and quantity are determined by supply and demand.

**COMMAND ECONOMY**

C) In a pure **command economy**, the goods and services that a country produces, the quantity in which they are produced, and the price at which they are sold are all planned by the government. Resources are allocated "for the good of society." The government owns most, if not all, businesses.

**MIXED ECONOMY**

D) A **mixed economy** includes some elements of each.

**Legal Systems**

A) The **legal** **system** of a country refers to the rules, or laws, that regulate behavior, along with the processes by which the laws of a country are enforced and through which redress for grievances is obtained.

**Teaching Tip:** To learn more about international law and the legal systems of the countries of the world, consider <http://www.doingbusiness.org/law-library>.

**DIFFERENT LEGAL SYSTEMS**

B) There are three main types of legal systems in use around the world: common law, civil law, and theocratic law.

**Common Law**

C) The **common law** system (based on tradition, precedent, and custom) evolved in England over hundreds of years. It is now found in most of Great Britain’s former colonies, including the United States.

**Civil** **Law**

D) A **civil law** system is based on a very detailed set of laws organized into codes. Over 80 countries, including Germany, France, Japan, and Russia, operate with a civil law system.

**Theocratic** **Law**

E) Islamic law is the most widely practiced **theocratic law** system (based on religious teachings) in the modern world.

**DIFFERENCES IN CONTRACT LAW**

F) **Contract law** is the body of law that governs contract enforcement. A **contract** is a document that specifies the conditions under which an exchange is to occur and details the rights and obligations of the parties involved. The **United Nations Convention on Contracts for the International Sales of Goods (CIGS)** establishes a uniform set of rules governing certain aspects of the making and performance of everyday commercial contracts between sellers and buyers who have their places of business in different nations.

**PROPERTY** **RIGHTS** **AND** **CORRUPTION**

G) Control over **property rights** (the bundle of legal rights over the use to which a resource is put and over the use made of any income that may be derived from that source) are very important for the functioning of business. Property rights can be violated by either **private action** (theft, piracy, blackmail, Russian Mafia) or **public action** (governmental bribery and corruption, nationalization).

**Private** **Action**

H) Private action refers to theft, piracy, blackmail, and the like by private individuals or groups.

**Public** **Action** **and** **Corruption**

I) Public action to violate property rights occurs when public officials extort income or resources from property holders using various legal mechanisms including excessive taxation, requiring expensive licenses or permits from property holders, or taking assets into state ownership without compensating the owners.

CONNECT

Click and Drag

*Property Rights and Corruption*

Summary

This activity focuses on differences in legal systems. Firms need to understand the differences between private actions such as blackmail and public actions such as corruption. While both pose a threat to international businesses, how that threat is addressed depends on the action in question.

Activity

Students are asked to match various scenarios to the type of legal action they represent.

Class Discussion

A country’s legal system regulates the business environment, defines how business transactions take place, and details the rights and obligations of parties to a contract. Discuss the different types of legal systems and what they mean for companies doing business in those countries. Discuss how companies can protect themselves from risk associated with property rights violations and corruption.

countryFOCUS**:** Corruption in Brazil

**Summary**

This country focus segment examines the extent of corruption in the country of Brazil. Even though the country is the seventh-largest economy in the world and considered to be a moderately free market economy, the corruption that exists in Brazil typically involves political connections. This is reflected in the relatively high perception of corruption in international surveys on the subject by Transparency International and the World Economic Forum. Known to exist for decades, the *mensalao* ("monthly payoff") and Petrobras scandals underscore the pervasiveness of the problem in Brazil.

**Discussion** **Questions**

1. What is the nature of the *mensalao* scandal? How extensive was it? What was the reaction in Brazil to its occurrence?

Even though a midlevel postal worker was caught taking a bribe for government contract favors, the awarding of such contracts and the backing of specific government programs in the Brazil’s National Congress involved about 25 politicians and business executives. Bribery, money laundering, and corruption were the charges on which they were found guilty. Even though the *mensalao* case became known in 2005, the public outcry was significant through the time this case was resolved in the courts in 2012.

2. What was the extent of the Petrobras scandal? Who did it impact? What made this case such a problem for Brazil? Discuss why the scandal might help prevent further corrupt behavior by government officials.

The Petrobras scandal became known in 2014, although it had been taking place since 1997. Construction firms would pay bribes to the state-owned company’s executives who were typically politically appointed. A three percent fee was assessed to contracts and subsequently shared by Petrobras executives, construction industry executives, and politicians. As the Brazilian president, Dilma Rousseff was chair of Petrobras at the time, her presidency was suspended and, in 2016, Rousseff was impeached and removed from the presidency. Students should recognize that the highly public nature of the scandal as well as its resolution should act as a warning sign to others who may be flirting with corrupt behavior.

**Teaching Tip:** Students can explore past and present information concerning Transparency International’s Corruption Perceptions Index at <http://www.transparency.org/research/cpi/overview>.

**Lecture Note:** To extend the discussion to include the economic impact of corruption in Brazil, consider <https://www.reuters.com/article/us-brazil-politics-poll/bolsonaros-popularity-jumps-as-brazil-economy-improves-crime-drops-idUSKBN1ZL1ZQ>.

**Foreign** **Corrupt** **Practices** **Act**

J) The **Foreign Corrupt Practices Act** makes it a violation of the United States law to bribe a foreign government official in order to obtain or maintain business over which the foreign official has authority and requires all publicly traded countries to keep detailed records so that it is clear whether a violation of the act has occurred or not.

management FOCUS: Did Walmart Violate the Foreign Corrupt Practices Act?

**Summary**

This feature explores corruption at Walmart’s Mexico division where managers allegedly bribed Mexican government officials to obtain permission to build the San Juan Teotihuacan store in the early 2000s. After leaders at Walmart’s headquarters were alerted of the situation, Walmart launched an internal investigation. However, the investigation was turned over to Walmart Mexico to complete and only after a 2012 *New York Times* article again raised questions about the situation did Walmart reopen the investigation. Today, the company has spent more than $612 million on legal fees and paid a $283 million settlement to the U.S. Department of Justice.

**Discussion** **Questions**

Please see Critical Thinking Question #5 for discussion of this feature.

**Did You Know? Video Clip**

The video clip asks: Did you know that Venezuela has dropped to one of the worst performing economies in the world?”

**Discussion Questions**

1. How would you describe Venezuela’s political system, and how has that system contributed to the country’s economic distress?

*Venezuela’s economic distress can be directly attributed to the country’s non-democratic, authoritarian regime. Venezuela, once a prosperous nation, is now a country in which 90 percent of its citizens are in poverty, the inflation rate is at an astounding 1 million percent, and unemployment stands at a staggering 33 percent. Students should recognize that repressive policies focusing on short-term gains have destroyed the longer-term potential of Venezuela’s economy.*

2. Discuss corruption as it relates to Venezuela. What does it mean for the business environment in the country? How might foreign companies view Venezuela as a location for investment?

*Most students will probably suggest that rampant corruption in Venezuela has put the country near the top of Transparency International’s ranking of corrupt nations, making it a highly unattractive destination for foreign investment. Many students will also point out that the economic situation in Venezuela is so poor, that most foreign companies would likely not entertain the thought of investing in the country and those that had previously made investments have probably already pulled out.*

3. What can Venezuela do to turn its economy around?

*Responses to this question will vary by student. Most will agree that Venezuela’s best hope may be a new government, one that promotes democratic ideals and reduces the corruption that has plagued the country in recent years. Students will likely note however, that even in the unlikely event that a new government takes over, change will be slow, and the chance for social unrest could threaten any sort of economic turnaround. Indeed, following the most recent election, which existing president Nicolas Maduro claims to have won, opposition leader Juan Guaido, recognized by many countries including the United States, as the real winner, has been unable to assume governing power.*

**Teaching Tip:** Learn more about the battle over the presidency in Venezuela, consider <https://www.bbc.com/news/world-latin-america-36319877>.

**Video Note:** To extend this discussion, consider *Oil Rich Venezuela Suffers as Global Prices Plummet* in the International Business Library at [http://bit.ly/MHEIBVideo](https://na01.safelinks.protection.outlook.com/?url=http%3A%2F%2Fbit.ly%2FMHEIBVideo&data=01%7C01%7Canke.weekes%40mheducation.com%7Ca25dc9eb643246ce47ad08d41a1dec6d%7Cf919b1efc0c347358fca0928ec39d8d5%7C1&sdata=PGTbnKJeqo4tban6vepacEyP5nezpxGm42CaB%2B3aOG8%3D&reserved=0). Click “Ctrl+F” on your keyboard to search for the video title.

**THE** **PROTECTION** **OF** **INTELLECTUAL** **PROPERTY**

K) **Intellectual property** refers to property, such as computer software, a screenplay, or the chemical formula for a new drug that is the product of intellectual activity. Intellectual property rights include **patents** (documents giving the inventor of a new product or process exclusive rights to the manufacture, use, or sale of that invention); **copyrights** (exclusive legal rights of authors, composers, playwrights, artists, and publishers to publish and dispose of their work as they see fit); and **trademarks** (designs and names, often officially registered, by which merchants or manufacturers designate and differentiate their products).

**Teaching Tip:** For information on intellectual property rights and policies, go to the World Trade Organization at <http://www.wto.org/english/tratop_e/trips_e/trips_e.htm> and the United States Patent and Trade Office at [http://www.uspto.gov/ip](http://www.uspto.gov/ip/).

**Lecture Note:** The U.S. Department of Commerce has made intellectual property protection a priority. To learn more about what the Department is doing go to <http://www.stopfakes.gov/about>.

**Teaching Tip:** For more information on U.S. Trademark law go to <https://cyber.harvard.edu/metaschool/fisher/domain/tm.htm>.

L) Over 185 nations are part of the **World Intellectual Property Organization**. These countries have all signed an international agreement to protect intellectual property rights known as the **Paris Convention for the Protection of Industrial Property**. In addition, an agreement known as the Trade-Related Aspects of Intellectual Property Rights (TRIPS) requires WTO members to grant and enforce patents lasting at least 20 years and copyrights lasting 50 years.

**Teaching Tip:** The World Intellectual Property Organization provides extensive information on various treaties and agreements between countries regarding the protection of intellectual property. Go to <http://www.wipo.int/portal/index.html.en> and click on About WIPO.

**PRODUCT** **SAFETY** **AND** **PRODUCT** **LIABILITY**

M) Different countries have different **product safety laws** (safety standards to which a product must adhere). In some cases, businesses must customize products to adhere to local standards if they are to do business in a country, whether these standards are higher or just different. **Product liability** involves holding a firm and its officers responsible when a product causes death, injury, or damage.Some executives believe that the high cost of liability insurance in U.S. hampers the competitiveness of the U.S. companies in the global marketplace.

CONNECT

Video Case

*Turmoil in Venezuela*

Summary

This activity focuses on the political and legal situation in Venezuela where an unpopular president is failing to adequately address the needs of the country. Many foreign companies have left the troubled country as doing business there has become increasingly challenging.

Activity

Students are asked to watch a video on the political and legal situation in Venezuela and then respond to a series of questions related to the video.

Class Discussion

A country’s political, legal, and economic systems have important implications for international businesses. Discuss the situation in Venezuela and how the policies being pursued by the current government have changed the business environment. How should companies respond? Can a company be successful in Venezuela today?

360° View: MANAGERIAL IMPLICATIONS

A) The material discussed in this chapter has two broad implications for international business. First, political, economic, and legal systems of a country raise important ethical issues that have implications for the practice of international business. Second, the political, economic, and legal environments of a country clearly influence the attractiveness of that country as a market and/or investment site.

B) The overall attractiveness of a country as a potential market and/or investment site for an international business depends on balancing the benefits, costs, and risks associated with doing business in that country.

C) In general, a country with democratic political institutions, a market-based economic system, and strong legal system that protects property rights and limits corruption will be more attractive to companies than a country that lacks democratic institutions, where there is strong government regulation of economic activity, and where the level of corruption is high and the rule of law is not respected.

CONNECT

Case Analysis

*Kenya: An African Lion*

Summary

This activity focuses on Kenya’s economic, political, and legal systems. Kenya has made significant economic gains since its independence from Britain in 1963, however continued growth is being hampered by numerous challenges including corruption, barriers to entrepreneurship, and limited property rights.

Activity

Students are asked to read a case on Kenya describing changes in the country since 1963 and then respond to a series of questions related to the case.

Class Discussion

A country’s economic, political, and legal systems can have important implications for international businesses and how they view the attractiveness of a country as a place in which to do business. Discuss how U.S. companies might view the benefits, costs, and risks of doing business in Kenya.

**CONNECT**

**Video Case**

***Did You Know? Venezuela Has Dropped to One of The Worst Performing Economies in The World***

**Summary**

This activity focuses on Venezuela’s remarkable shift from being an emerging economic powerhouse to its current economic chaos. The transformation, occurring over just a few short years, has left the majority of the population in poverty. Given the refusal of Nicolas Maduro to cede power to recently elected Juan Guaidó, the future of the country remains unclear.

**Activity**

Students are asked to watch a video on Venezuela’s transformation and then respond to a series of questions related to the video.

**Class Discussion**

Venezuela’s stunning transformation from being a prosperous country with a promising future to its current impoverished and corrupt state is remarkable by many measures. Ask students to discuss what prompted Venezuela’s fall and what other countries can learn from Venezuela’s experience. Then, ask students to reflect on the battle for power in the country and its implications for the future of democracy in Venezuela.

# End-of-Chapter Resources

**Critical Thinking and Discussion Questions**

1. Free market economies stimulate greater economic growth, whereas state-directed economies stifle growth. Discuss.

Answer: In a market economy, private individuals and corporations are allowed to own property and other assets. This right of ownership provides a powerful incentive for people to work hard, introduce new products, develop better advertising campaigns, invent new products, etc., all in the hopes of accumulating additional personal capital and wealth. In turn, the constant search on the part of individuals and corporations to accumulate wealth enriches the entire economy and creates economic growth. In contrast, in a command economy, private individuals and corporations are not allowed to own substantial quantities of property and other assets. The objective of a command economy is for everyone to work for “the good of the society.” Although this sounds like a noble ideal, a system that asks individuals to work for the good of society rather than allowing individuals to build personal wealth does not provide a great incentive for people to invent new products, develop better advertising campaigns, find ways to be more efficient, etc. As a result, command economies typically generate less innovation and are less efficient than market economies.

2. A democratic political system is an essential condition for sustained economic progress. Discuss.

Answer: This question has no clear-cut answer. In the West, we tend to argue that democracy is good for economic progress. This argument is largely predicated upon the idea that innovation is the engine of economic growth, and a democratic political system encourages rather than stifles innovation. However, there are examples of totalitarian regimes that have fostered a market economy and strong property rights protection and experienced rapid economic growth. The examples include four of the fastest growing economies of the past 35 years—South Korea, Taiwan, Singapore, and Hong Kong—all of which have grown faster than Western economies. However, while it is possible to argue that democracy is not a necessary precondition for the establishment of a free market economy, it seems evident that subsequent economic growth leads to the establishment of democratic regimes. Several of the fastest-growing Asian economies have recently adopted more democratic governments.

3. What is the relationship between corruption in a country (i.e., government officials taking bribes) and economic growth? Is corruption always bad?

Answer: Economic evidence suggests that high levels of corruption significantly reduce the economic growth rate in a country. By siphoning off profits, corrupt politicians and bureaucrats reduce the returns to business investment, and hence, reduce the incentive that both domestic and foreign businesses have to invest in that country. The lower level of investment that results has a negative impact on economic growth. However, while most students will probably agree that corruption is bad, some may point out that the United States, despite its Foreign Corrupt Practices Act, does allow “grease payments” to expedite or secure the performance of a routine governmental action. According to Congress, “grease payments,” while technically bribes, are not being used to obtain or maintain business, but rather are simply made to facilitate performance of duties that the recipients are already obligated to perform.

4. You are the CEO of a company that has to choose between making a $100 million investment in either Russia or Poland. Both investments promise the same long-run return, so your choice of which investment to make is driven by risk considerations. Assess the various risks of doing business in each of these nations. Which investment would you favor and why?

Answer: When assessing the risks of investment, one should consider the political, economic, and legal risks of doing business in either Russia or Poland. Today, the risk in Russia would probably be considered higher than the risk in Poland. Poland has recently been accepted as a member of the EU, and as such gains the benefits and stability offered by the EU. Russia, by contrast, is still many years away from even being in a position to be considered by the EU for membership, and the recent actions of President Vladimir Putin, particularly in Ukraine, have been alarming to many.

5. Reread the Management Focus "Did Walmart Violate the Foreign Corrupt Practices Act?" What is your opinion? If you think it did, what do you think the consequences will be for Walmart?

Answer: The Foreign Corrupt Practices Act prohibits companies from bribing foreign government officials to obtain or maintain business over which that foreign official has authority. Most students will probably agree that Walmart clearly violated the Act when it bribed Mexican officials to redraw the zoning area so that Walmart’s San Juan Teotihuacan store could be built outside the commercial-free zone rather than inside it.

**globalEDGE™ Research Task**

Use the globalEDGE™ site ([globaledge.msu.edu](https://globaledge.msu.edu/)) to complete the exercises in the text.

**Exercise 1**

The definition of words and political ideas can have different meanings in different contexts worldwide. In fact, the Freedom in the World survey published by Freedom House evaluates the state of political rights and civil liberties around the world. Provide a description of this survey and a ranking (in terms of “freedom”) of the world’s country leaders and laggards. What factors are taken into consideration in this survey?

**Exercise 2**

As the chapter discusses, differences in political, economic, and legal systems have considerable impact on the benefits, costs, and risks of doing business in various countries. The World Bank’s “Doing Business Indicators” measure the extent of business regulations in countries around the world. Compare Brazil, Ghana, India, New Zealand, the United States, Sweden, and Turkey in terms of how easily contracts are enforced, how property can be registered, and how investors can be protected. Identify in which area you see the greatest variation from one country to the next.

Kenya: An African Lion

closing case

**Summary**

This closing case explores the emergence of Kenya as a regional power in Africa. Kenya can be viewed as an economic and political success in sub-Saharan Africa. Acting as the economic, financial, and transportation hub in East Africa, Kenya boasts a range of industries including agriculture, mining, manufacturing, tourism, communications, and financial services. Kenya’s assent to its position as a top economy in the region has been decades in the making. Following its independence from Great Britain in 1963, Kenya adopted African Socialism and a policy of large public investment in infrastructure by state-owned companies and the promotion of smallholder agricultural production. During this time Kenya also adopted an import substitution policy to promote domestic production. In 1993, faced with a stagnating economy, Kenya implemented a series of economic reforms eventually leading to today’s market economy, strong private sector, and relatively low barriers to cross-border trade and investment. Kenya also implemented political reforms shifting from what was essentially a one-party state to a decentralized system where political power is held by 47 semiautonomous regions and a free and fair election process is emphasized. Today, while corruption remains a problem and ethnic conflict continues, Kenya’s well-educated young population and growing urban middle class are contributing to the country’s thriving economy and stable democracy.

**Case Discussion Questions**

1. What is “African Socialism” and how might it differ from “socialism” in general?

Socialism involves public ownership of the means of production for the common good of society. Those who believe in socialism feel that the state, rather than the individual, is better suited to ensuring that workers are adequately compensated for their labor. Like socialism, African Socialism promotes social development encouraged through a large public sector. In addition, African socialism supports the notion of what it means to be African and the avoidance of social classes within society.

2. Why do you think that Kenya’s post-independence policy of African Socialism failed to deliver consistent economic growth?

Some students may suggest that while at the time of its independence in 1963, when ethnic divisions were creating conflict in Kenya, and one large group held a disproportionate share of power, African Socialism was likely appealing, yet as time went on, the policy fell out of favor. For Kenya, African Socialism involved a policy of import substitution, the promotion of smallholder agricultural production, and large public investment in infrastructure by state-owned companies. While the approach was positive in the short term, especially in agricultural gains, it soon became clear that Kenya’s economy was not growing and that changes needed to be made.

3. Kenya was a creation of Britain, a colonial power that once occupied the area. What problems were created when colonial powers drew national borders? Have these problems hampered the country’s economic development? How is Kenya dealing with these problems?

Students will probably suggest that Kenya’s problems derive from the challenges involved in fully recognizing and appreciating the deep differences among the various ethnic groups that claimed allegiance to the land. In 1993, Kenya implemented a series of economic and political reforms, working to remove price controls, lower barriers to trade and investment, and be more fiscally responsible. In addition, political power was decentralized to 47 semiautonomous regions and holding free and fair elections was made a key focus for the country. Today, the success of Kenya’s political and economic reforms is evident. The country’s market-based economy is growing at a steady clip and is spread across a range of industries including agriculture, mining, manufacturing, tourism, communications, and financial services. A new constitution was introduced in 2010 limiting the power of the central government and increasing the power of regional governments. In addition, the focus on ensuring free and fair elections has contributed to increased business confidence supported by a young well-educated population and a thriving middle class.

4. What significant economic problems does Kenya face today? How might it overcome these problems? What advantages does the country have?

Despite the economic and political reforms that have helped Kenya become a strong player in sub-Saharan Africa, Kenya continues to face several challenges. One challenge is the country’s complicated bureaucratic process that makes it difficult for companies to establish new businesses. This, combined with ongoing corruption, could slow future business development. Furthermore, property rights are weak making the situation even more precarious. Some students may note that foreign companies could see the situation in Kenya as too risky and complicated and take their investment dollars elsewhere. Students may also note that ethnic conflicts and terrorism are likely to impact business decisions especially for foreign investors. However, despite challenges like these, many students will be optimistic about the future of Kenya, noting that its growing middle class, well-educated young workforce, diversified industrial base, and position as regional leader will all be important to the future of Kenya.

**Teaching Tip:**Information on Kenya is available at <https://www.bbc.com/news/world-africa-13681341>.

**Video Note:** To learn more about Kenya, consider *Kenya Races Toward Goal of Electrifying Every Household* in the International Business Library at [http://bit.ly/MHEIBVideo](https://na01.safelinks.protection.outlook.com/?url=http%3A%2F%2Fbit.ly%2FMHEIBVideo&data=01%7C01%7Canke.weekes%40mheducation.com%7Ca25dc9eb643246ce47ad08d41a1dec6d%7Cf919b1efc0c347358fca0928ec39d8d5%7C1&sdata=PGTbnKJeqo4tban6vepacEyP5nezpxGm42CaB%2B3aOG8%3D&reserved=0)*.* Click “Ctrl+F” on your keyboard to search for the video title.

CONNECT

Geography Mapping Activity

Summary

This activity is designed to test the student’s knowledge of geography. Questions related to chapter material are asked, requiring students to understand the topics and the locations of the countries involved.

Activity

Students are asked to respond to a series of question related to the geographic location of several countries.

Class Discussion

Understanding the geographic location of countries is essential to the understanding of international business. Ask students to discuss the implications of the geographic locations of the countries in this exercise on the subject matter.

# Continuous Case Concept

The growing realization that aggressive changes will be needed to stop climate change has prompted many countries to develop stiff CO2 emissions requirements for automakers. Within the European Union (EU), ambitious goals have been established requiring automakers to significantly reduce average emissions in their fleets. For automakers, the new regulations represent a considerable challenge. Demand for relatively low CO2 emission diesel powered vehicles is down. Typically, automakers depend on these vehicles to offset higher emission vehicles like SUVs allowing the car makers to meet overall standards. Furthermore, despite considerable progress, most automakers still have only a few electric vehicles in their fleets, making it difficult to attract buyers. Indeed, in Europe, buyers are currently flocking to SUVs, some of the more profitable vehicles auto companies produce, but also among the vehicles that emit the highest levels of CO2. As a result, auto companies, in their effort to meet the EU standards, are left with the difficult task of trying to capitalize on demand for SUVs while convincing buyers of the merits of lower emission vehicles too.

* Ask students to consider the impact of the new regulations for the auto industry in Europe. How do the regulations change the cost of doing business in Europe?
* Then, ask students to consider the strategic alternatives that are open to automakers. Should they abandon the market in Europe in favor of countries with less ambitious environmental goals?
* Finally, ask students to consider how differing regulations between countries can impede or facilitate strategic decisions for multinational companies. Will the European Union regulations make it more, or less, difficult for automakers to compete in North America?

This exercise could be used at the beginning of the discussion of this chapter’s material, and/or again at the end. To take the discussion into greater depth, ask students to read the pertinent selections in the Additional Readings section below. The exercise also works well at the beginning of the Managerial Implications section.

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# Additional Readings and Sources of Information

Vladimir Putin: Russia’s action man president

<http://www.bbc.com/news/world-europe-15047823>

The End of One Country, Two Systems in Hong Kong

<https://www.ft.com/content/5d3d7d2e-bba8-11ea-a05d-efc604854c3f>

IMF Sees Surprise Upward Revision of Kenya’s Economic Growth

<https://www.bloomberg.com/news/articles/2020-09-09/imf-sees-surprise-upward-revision-of-kenya-s-economic-growth>

The Worst May Be Over for the Saudi Economy

<https://www.bloomberg.com/news/articles/2018-07-02/worst-may-be-over-for-saudi-economy-as-oil-brightens-outlook>

Bolsonaro Declares Brazil Corruption Free and Ends Carwash Probe

<https://www.bloomberg.com/news/articles/2020-10-07/bolsonaro-declares-brazil-corruption-free-and-ends-carwash-probe>

25l Corruption Scandals That Shook the World

<https://www.transparency.org/en/news/25-corruption-scandals#>

Walmart Inc. and Brazil-Based Subsidiary Agree to Pay $137 Million to Resolve Foreign Corrupt Practices Act Case

<https://www.justice.gov/opa/pr/walmart-inc-and-brazil-based-subsidiary-agree-pay-137-million-resolve-foreign-corrupt>

How Companies Can Take a Stand Against Bribery

<https://hbr.org/2018/09/how-companies-can-take-a-stand-against-bribery>

China’s Economy Continues to Bounce Back from Virus Slump

<https://www.bbc.com/news/business-54594877>

Communist China Turns 70. Who Shares It Economic Growth?

<https://www.npr.org/2019/10/01/765676993/communist-china-turns-70-who-shares-its-economic-growth>

Putin’s Biggest Fear is to Be Held Accountable for His Regime’s Crimes

<https://www.washingtonpost.com/opinions/2020/11/13/putins-biggest-fear-is-be-held-accountable-his-regimes-crimes/>