# Global Economic Environment

Chapter 2



## Economic Integration

- 1900- only 10 percent integration
- 2000- 50 percent integration
  - European Union
  - NAFTA
  - ECOWAS



## New realities

- Capital movements replaced trade levels
- Production "uncoupled" from employment
- World economy dominate- country economies are secondary
- End of the capitalism/socialism struggle
- E-commerce changes all models
  - Business and national



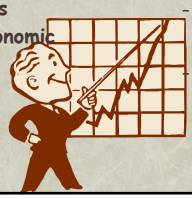
## Economic Indicators

**Gross Domestic Product**

- Total market value of all goods and services produced within a nation's borders
- Measure of economic output

**Gross Domestic Income**

- GDP plus income generated from non-resident sources
  - Example: money sent to families in home countries
  - Profits from selling goods made in another country in the home country





## Economic Systems

- Type of economy
- Type of government
- Trade and capital flows
- The commanding heights
- State provided services funded by taxation
- Institutional transparency
- Free markets/entrepreneurial behavior



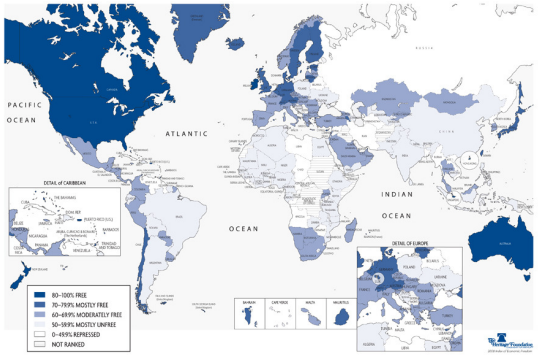
## Economic System Structures

| Resource Ownership | Resource Allocation: *Market* | Resource Allocation: *Command* |
|---|---|---|
| *Private* | Market Capitalism | Centrally Planned Capitalism |
| *State* | Market Socialism | Centrally Planned Socialism |

## Heritage Foundation Economic Freedom

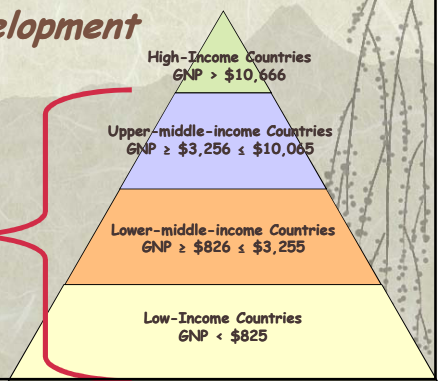
- Free
  - 20 nations (includes US)
- Mostly Free
  - 52 nations
- Mostly Unfree
  - 73 nations
- Repressed
- Unrated

## DISTRIBUTION OF ECONOMIC FREEDOM






## Stages of Market Development






## BOP Myths

- Poor have NO money
- Poor are too concerned with satisfying basic needs to "waste" money on non-essential items
- Goods sold in developing markets are too inexpensive for new entrants to make a profit.
- Individuals in BOP markets cannot use advanced technology
- Global companies targeting BOP countries will be criticized for exploiting the poor.



## Kopeyia, Ghana

FORTUNE AT THE BOTTOM OF THE PYRAMID, Prahalad

## True Nature of BOP market

- There is Money at the BOP
- Ease of access to BOP markets
- BOP Markets are brand-conscious
  - Extremely value conscious
- BOP Market is connected
- BOP Customers accept advanced technology readily

## The Market Development Imperative

- Create the capacity to consume
  - Affordability
    - Single serve packaging
    - Creative purchasing plans
  - Access
    - Intensity of distribution *(walking distance)*
  - Availability
- The Need for New Goods and Services
- Dignity and Choice
- Trust is a Prerequisite





## Philosophy for Developing Products and Services for BOP market

The basic economics of the BOP market are based on small unit packages, low margin per unit, high volume, and high return on capital employed.





## Twelve Principles of Innovation

- Focus on price performance
- Innovation requires hybrid solutions
- Solutions must be transportable across countries, cultures, and languages
- Conserve resources- eliminate, reduce, recycle
- Start with understanding of functionality
- Process innovations are just as critical
- Deskilling work is critical
- Education consumers on product usage
- Products must work in hostile environments
- Research on interfaces given nature of population
- Innovations must reach the consumer
- Feature and Function evolution in BOP markets can be rapid



## Institutions and Groupings

- G8
- OECD
- The Triad

## Balance of Payments (the other BOP)

- Record of economic transaction all over the world
- Current and capital accounts
- Just like a company balance sheet
  - Focus is on trade and cash flow expenditures



## International Finance

- Foreign exchange
  - Devaluation
    - (one's currency looses value in comparison to another)
  - Revaluation
    - Strengthening of currency value in relation to others

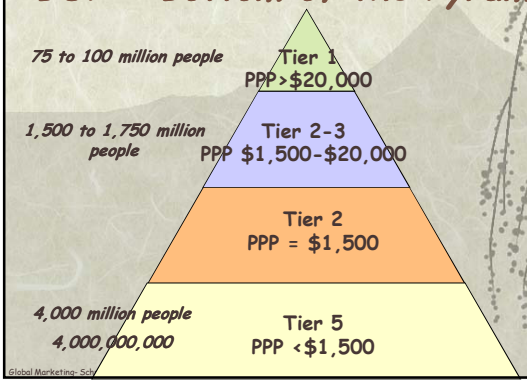
## PPP- Purchasing Power Parity

- http://www.economist.com/markets/bigmac/



FORTUNE AT THE BOTTOM OF THE PYRAMID, Prahalad

## BOP = Bottom of the Pyramid






## Currency Risk

- Economic Exposure
- Reducing Exposure
  - Hedging
  - Forward Market
    - Put option
    - Call option

- Purchases aircraft from Boeing
  - 10% down payment
  - Rest upon delivery (5 years later)
- Revenues of JAL in Yen
- Payments in USD
- In 1985- entered into 10 year forward exchange contract
  - Value of Yen surged against dollar from ¥240 to ¥99 in 1994
  - Misjudgment cost JAL 86 percent more per each aircraft.
  - Admitted loss of USD 45 million or ¥45 billion