International Business
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Lecture – 21
Economic Factors, Economic Environment

Hi, everyone. Welcome to the course of International Business. So, in the last few classes, we have been talking about the factors affecting international business and we discussed about factors like you know culture, politics and legal, right. So, today we will be talking about the Economic Factors and how they affect international business right.

So, basically we all understand that economy from which this word is derived is economy is basically the optimum utilization of resources and resources are always limited. So, in any country for that right so, there is a the factors of production are always limited. So, how one would utilize it if you are looking at the conditions of its people and it is you know stakeholders. So, that becomes very important.

So, when a new firm enters into an international market they need to understand the economy behind this you know and the different economic factors that impact that can impact its business, right. And, I am very proud to say when I am talking about economy I am proud to say that one of the Indians has been awarded you know the Nobel prize for economics this year. so, congratulations to him.

And, let us see what are economic factors and how do they affect.

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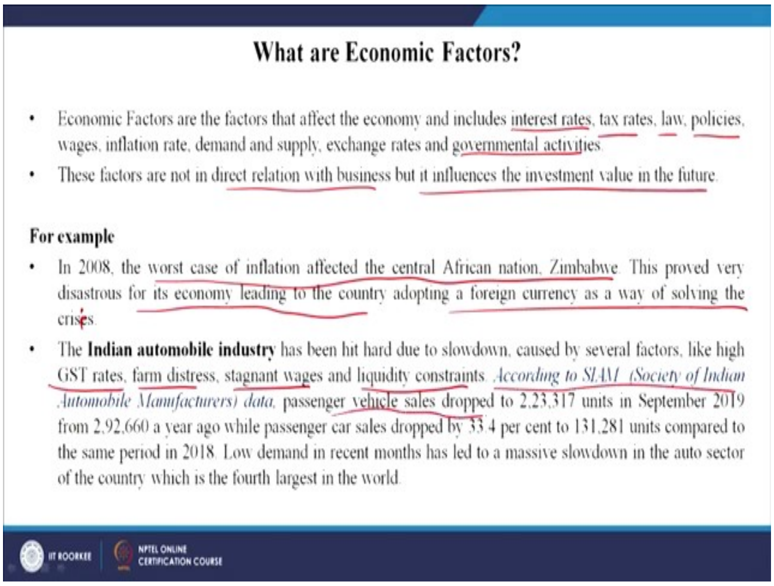

So, economic factors are the factors that affect the economy and includes things like interest rates, tax rates, law, policies, wages, inflation rate, demand and supply, exchange rates and governmental activities. So, all these things are you know made to run the economy in a better way, right. So, these are the factors which are connected to the economy. These factors are not in direct relation with business maybe, but it influences the investment value in the future, right.

So, if the tax rates changes suppose for example, for certain products luxury products the tax rates are increased or for essential commodities for example, the government wants to reduce the tax rate. So, what kind of an influence it will have and what kind of influence it will have then on the you know connected in connecting industries right, the industries who are make those products. So, these are some of the things that are very very important right and as an student of management or international business or economics one needs to be very clear with it.

The example who would forget the crisis that has happened in the past; for example, the great recession that had happened in the early 1900 right 1930s and 20 – 30s, then we came about the you know 2008 crisis which we happen the subprime crisis. So, these were issues that shake the nation right then we had 1999 the Southeast Asian crisis, right.

So, in 2008, for example, the worst case of inflation affected the central African nation, Zimbabwe one of the examples taken. So, although it shook the world, but we are talking about Zimbabwe how Zimbabwe was affected and I still remember that Zimbabwe's economy had crashed and they had they were you know producing very large valued currencies for example, of very high value right so, which is not a very good sign. This proved very disastrous for its economy leading to country adopting a foreign currency as a way of solving the crisis. So, to solve this crisis they had to depend on some foreign currency.

Recently the Indian it automobile industry in fact, the Indian industry has been hit hard last year and this year, but especially the automobile industry it has been hit hard due to the slowdown caused by several factors like high GST rates. It was first of all we can say high GST rates and again the GST was not very clear to many of the players the farm distress that has happened stagnant wages and liquidity constraints right.

So, liquidity constraints stagnant wages all these things taken together has affected the demand side. So, the demand has been affected largely and you know I would take this point to explain that presently the Indian government has used strategy to you know uplift the economy for example, to buy they have slashed the corporate rate. But, to me it is not a very wise decision because you see what happens is when you reduce the corporate rate the money stays with the corporate and it is expected they would pass it on the customers, but that it is not necessarily true right.

So, what happens is you have helped the supply side, but the problem lies in the demand. So, when demand is not growing and demand is has not grown who would buy these products right. So, giving a slash in the corporate rate it is good enough maybe, but then the demand does not change. So, until unless the demand changes, the economy would not get a facelift. So, these are very important things which the government also has to take into account.

So, according to the society of Indian automobile manufacturers passenger vehicle sales dropped to 223,317 units in September 2019 from 292,660 right a year while passenger car sales dropped by 33 percent 33.4 percent. And you know the low demand in the recent months has led to a massive slowdown in the auto sector of the country which is a fourth largest in the world.

Now, this is not all this is not only the automobile sector. There has been a slowdown in the even the fast moving consumer goods sectors, many companies have cut down their workers. So, there has been lot of worker been fired and all. So, on totality in fact, to correct this, the government has changed its policies, tried to support, but things have not seen much of a change at the moment right.

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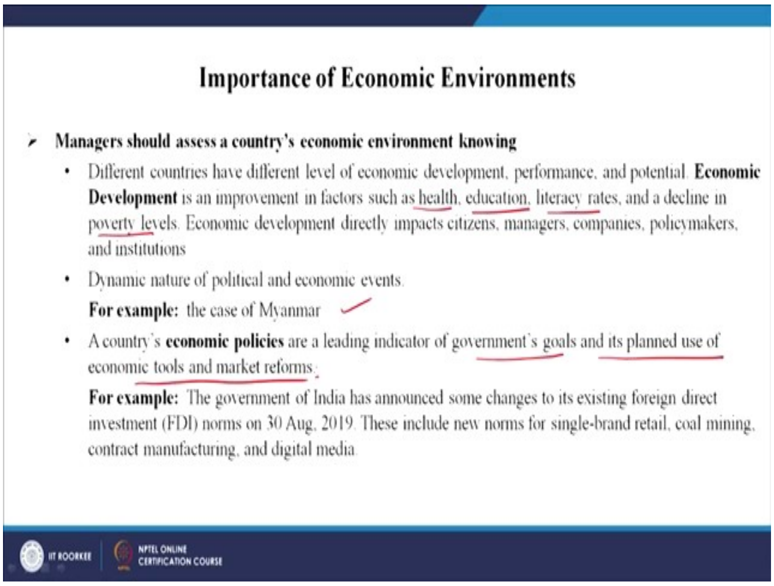

What is the importance? So, from and looking at the examples that we have talk taken we can understand that economic environment is very very vital right. So, managers should assess a country's economic environment knowing the different countries have different level of economic, development, performance and potential. Economic development is an improvement in factors such as health, education, literacy rates and a decline in poverty levels. Economic development directly impacts the citizens, managers, companies, policymakers and institutions right.

The dynamic nature of political and economic events. So, there is a strong correlation between political and economy politics and economy right. If I draw you know correlation I would see it would be very very high because the change in policies the political situation changes, the economic situation can also change right because with the political you know ideologies the ideas the economy also gets affected right.

For example, we have seen in the past that we are taken the case of Myanmar; how Myanmar changed its governance and in 2011 and then, from there they started doing better and in the past they were having a very very bad time.

A country's economic policies are a leading indicator of the government's goals and its planned use of its economic tools and the market reforms. Now, when it comes to economic policies there are lots of policies right, for example, the bank purchase rate the repo rate for example, the bank constantly been working on it to reduce the interest rates right. They have been the Indian government has been trying to infuse more of you know liquidity, but then still things will not work till we do not attack on the or we do not foster the demand side right. We have been trying working hard on the supply but demand is the one where it is to be worked out.

The government of India announced some changes to it is existing foreign direct investment on 30th August, 2019 which is very recent. These include new norms for single-brand retail, coal mining, contract manufacturing, and digital media. These are some of the good things that the government of India has done.

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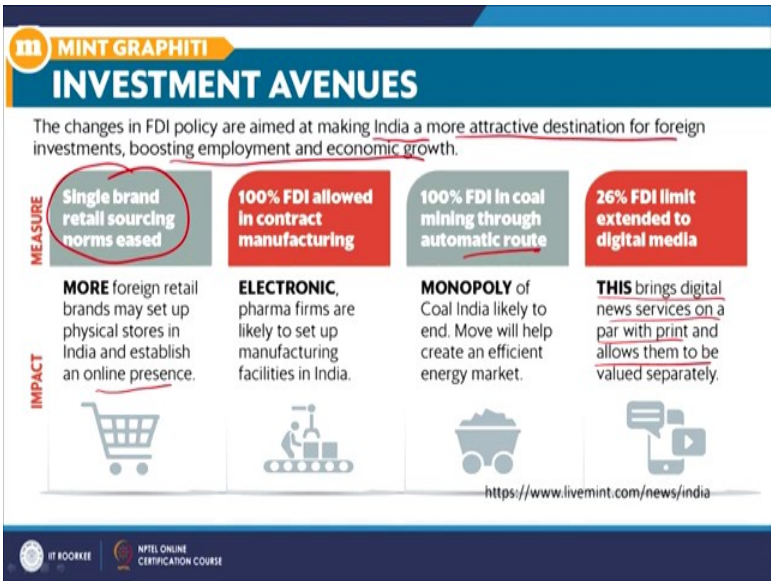

So, let us see what it has done. So, to make it make India a very attractive destination for foreign investments and boosting employment and economic growth, you see as we will understand the till employment does not grow. The economic growth cannot happen right; a product that is made by any company is just an inventory. So, the inventory till does not get a value if people do not consume it, if they do not use it. So, till that time it is of no use. So, how do you boost the employment, how do you pay them right, that is very important?

Anyway, so, in terms of the single brand retail sourcing norms were eased right. So, now, what is the expectation the more foreign retail brands may set up physical stores in India and established their online presence too right. 100 percent FDI allowed in contract manufacturing. So, electronic, pharma firms are likely to set up manufacturing facilities in India this is the hope right.

100 percent FDI in coal mining through automatic route, right. So, automatic is the government route right. So, monopoly of Coal India likely to end. Move will help create an efficient energy market. This then the 26 percent FDI limit extended to the digital media. This again brings in a hope that new services on par with print would be and allows would grow up and it would be valued separately.

So, these are some of the changes the government has tried to do thinking hoping that it would help in boosting the you know domestic market, helping more the you know investors to come in and start their business and finally, boost up the employment and do good for the economy as a whole right.

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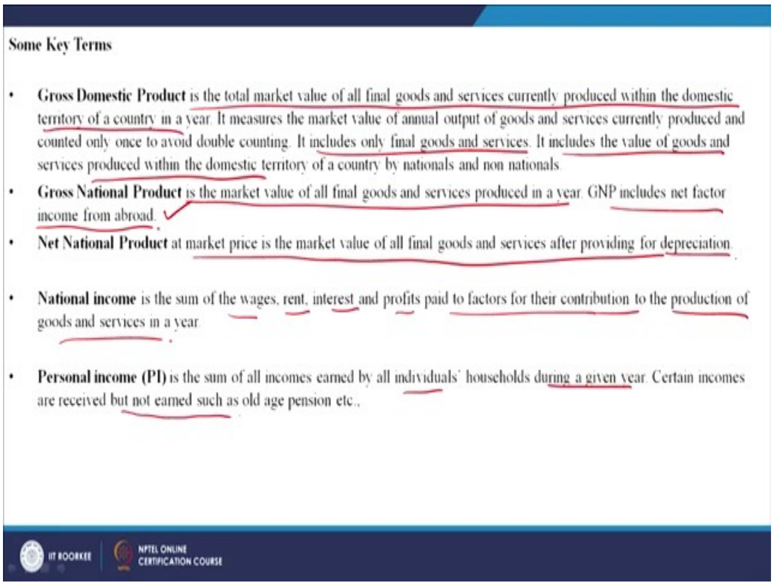

Some key terms that we need to understand when we talk about economy for example, GDP. What is GDP? Is a total market value of all final goods and services currently produced within the domestic territory of a country in a particular year; so, all goods and services right currently produced are comes under the GDP right.

Now, what is GNP? Is the market value of all final goods and services produced in a year right; it includes net worth income from abroad. Now, this if you see what it was saying here in GDP case if you go back, so, it says it includes only final goods and services. It includes the value of goods and service produced within the domestic territory. So, anything you know done outside was not there, but here we are including the income from abroad.

Net National Product at market price is the market value of all final goods and services after allowing for or factoring for the depreciation, the wear and tear right. National income is another term which is important which will be using frequently is the sum of the wages, rent, interest and profits paid to the factors for their contribution; factors are like land, labor and capital to the production of the goods and services right.

Finally, personal income is the sum of all incomes earned by an individual or individuals' households during a given year. Certain incomes are received, but not earned as old age pension etcetera right. So, these are some of the terms that we will be using frequently and maybe we will look at it more in detail.

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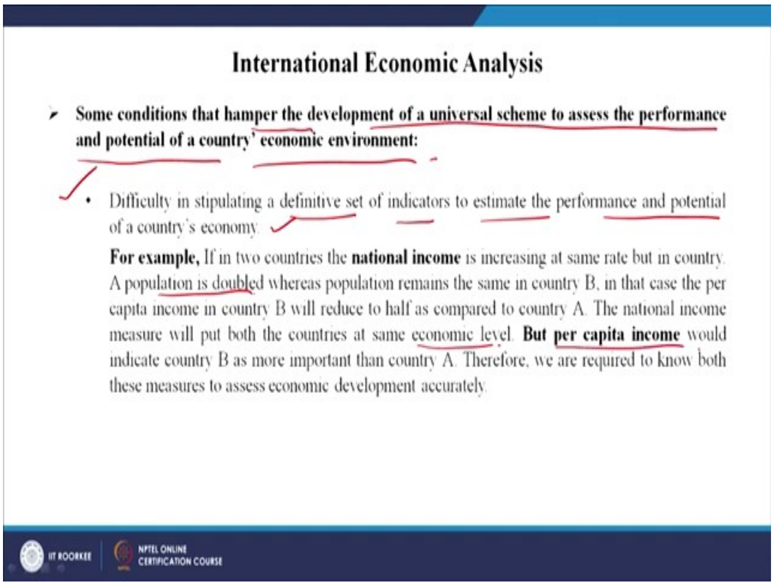

So, international economic analysis, so, what are the factors? What conditions impact let us see? Some conditions that hamper the development of a universal scheme to assess the performance and potential of a country's economic environment: the first one says difficulty in stipulating a definitive set of indicators to estimate the performance and potential of a country's economy. Now, let us see with an example.

Suppose there are two countries and these two countries the national income is increasing at the same rate, but in country A population has doubled whereas, population remains the same in the country B. So, what has happened, national income has been increasing in the same rate but, here the population has doubled and it is same here.

In that case the per capita in the income in the country B will reduce to half as compared to country A. The national income measure will put both the countries the same economic level, but per capita income would indicate country B as more important than country A right. Therefore, we are required to know both these measures to assess the economic development effectively or accurately right.

So, what is the right indicator? So, that is very important to do an economic analysis.

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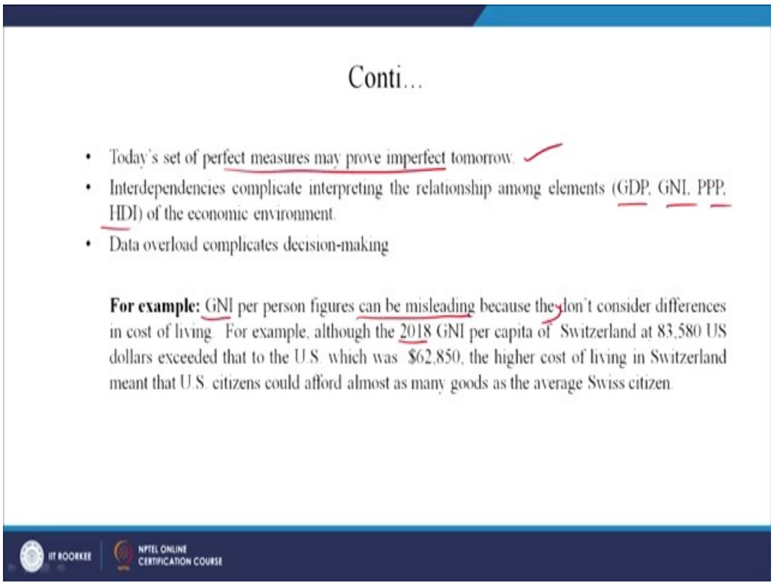

Another thing is that set of perfect measures may prove imperfect tomorrow. So, what is today a perfect measure in a particular condition, might not be a perfect measure tomorrow, right. So, a new measure has to be checked in a different condition. Then interdependencies complicate the interpreting the relationship among elements.

So, a relationship interrelationship between GDP, GNI, PPP and HDI right, human development index also creates a confusion and finally, the data overload complicates the decision making for the managers right. Now, look at this case again gross national income per person figures can be misleading, why? Because, they do not they do not consider differences in the cost of living right.

So, for example, although the 2018 GNI per capita of Switzerland at this much dollars acceded to that of the US which was this much, the higher cost of living in Switzerland meant that US citizens could afford almost as many goods as the average Swiss citizen. So, although you had a higher GNI in Switzerland, but because of the higher cost of living in Switzerland, the Americans were at the same parity right as Swiss people.

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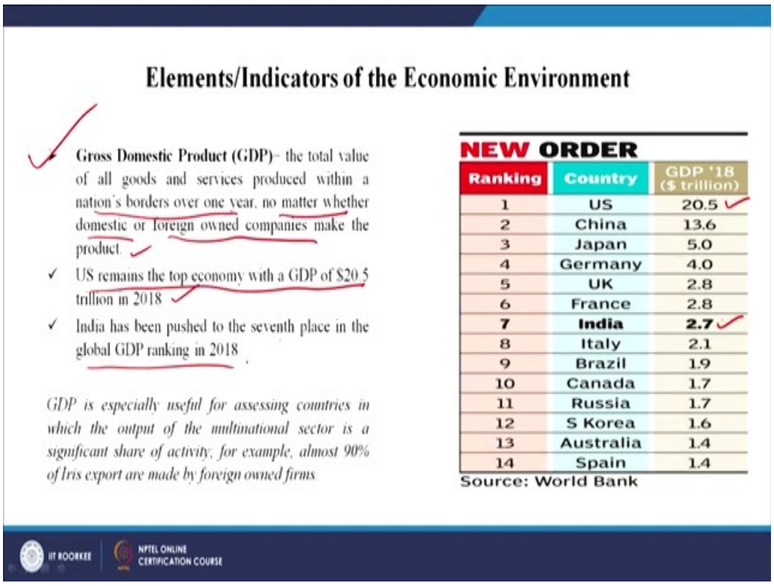

So, the elements or indicators as I said we will be explaining. So, the gross domestic product what it says the total value of all goods and services produced within a nations borders over one year, no matter whether the domestic or foreign owned companies make the product, who makes it is immaterial. Anything that is made within the boundary of the country comes under the GDP right.

But, interestingly I will tell you so, let us see for example, U.S remains the top economy with a GDP of 20.5 trillion in 2018 right. India has been pushed to the seventh place in the global GDP ranking in 2018. So, you can see here India is here, US is 2 point 20.5. So, India is only a 2.7 trillion right, but we have grown with time, but then it is not sufficient.

But, interestingly there are some controversies with GDP also. Some economists think that GDP and I too agree to that the GDP may not be a very strong indicator. GDP does not account it to things like the value, for example. Let us say we cut a tree right and we sell the wood right.

Now, when we sell the wood if the price of the wood maybe becomes a part of the GDP, but what happens to the loss that happens because of the kind of oxygen that was being provided by the tree to us, the shade that was being provided by the tree to us and other kind of you know benefits that was being provided right.

So, all these benefits where have they gone? Right. So, that has been not valued that has been not monetarily valued, but then had they been monetarily valued maybe the GDP score would look different for any country right. GDP is especially useful for assessing countries in which the output of the multinational sector is a significant share of activity. For example, almost 90 percent of the Iris export are made by foreign owned firms and not the local ones right ok.

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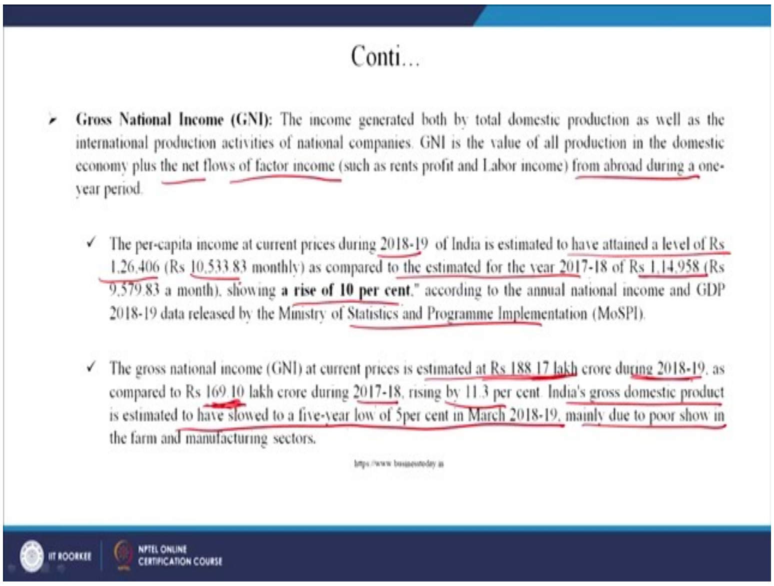

Next is GNI: The income generated both by total domestic production as well as the international production activities right. So, GNI is the value of all production in the domestic economy, plus the net flows of factor income from abroad during a one-year period.

So, look at it the per capita income at current prices during 18 – 19 of India is estimated to have attained a level of rupees 126,406 crores right or this much monthly as compared to the estimated for the year 2017 – 18 of rupees 114,958 right. Showing a rise of 10 percent right according to the annual national income and GDP data released by the Ministry of Statistics and Programme Implementation.

The gross national income at current prices is estimated at rupees this much during 18 – 19 right, as compared to 169.1 lakh crore during 18. So, this is again a rise of 11.3, 13 percent. India's gross domestic product is estimated to have slowed to a 5 year low of 5 percent in march 2018 – 19 mainly due to poor show in the farm and the manufacturing sectors.

So, what has happened although if you see the national income is this much here at 18 – 19 as compared to 17 – 18 it was 169 which has reason right, but now at this moment right India's GDP has slowed down to a 5 year low. Now, this is something that needs one needs to understand that what is the relationship and how this interrelationship matters to anybody right to basically and you know business firm and it is for all the in fact, the you know the critics the business firms and everybody.

So, now this slowdown is something that is very bothering for India right.

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Top 20 countries

http://data.worldbank.org/data-catalog/world-development-indicators

Gross national income per capita 2018, Atlas method and PPP

Ranking	Economy	Atlas methodology (US dollars)	Ranking	Economy	Purchasing power parity (international dollars)
1	Switzerland	83,580	1	Qatar	124,130
2	Norway	80,790	2	Macao SAR, China	112,480
3	Isle of Man	80,340 *	3	Singapore	94,500
4	Macao SAR, China	78,320	4	Brunei Darussalam	85,790
5	Luxembourg	69,420	5	Kuwait	83,390
6	Iceland	67,950 *	6	United Arab Emirates	75,300
7	United States	62,850	7	Luxembourg	71,420
8	Qatar	61,190	8	Switzerland	68,370
9	Denmark	60,190	9	Norway	68,310
10	Ireland	59,770	10	Hong Kong SAR, China	67,700
11	Singapore	58,770	11	Ireland	65,290
12	Sweden	55,040	12	United States	63,390
13	Australia	53,190	13	Netherlands	56,890
14	Netherlands	51,260	14	Denmark	56,410
15	Hong Kong SAR, China	50,310	15	Saudi Arabia	55,650
16	Austria	49,260	16	Austria	55,230
17	Finland	47,750	17	Iceland	55,190
18	Germany	47,180	18	Germany	54,890
19	Belgium	45,340	19	Sweden	53,560
20	Canada	44,860	20	Belgium	50,940

India ranking (atlas methodology) : 144, GNI per capita: 2020 US Dollars

India ranking (PPP methodology) : 126, GNI per capita: 7680 International Dollars

PPP is purchasing power parity; an international dollar has the same purchasing power over GNI as a U.S. dollar has in the United States.

Now, let us look at the gross national income per capita shown for different countries. So, in terms of ranking if you can see right Switzerland stands at the top right and this is for the you know gross national income and this is for the purchasing power parity. India’s ranking is 144 in terms of the gross national income and India’s ranking in terms of the purchasing power parity it is 126.

So, there are two ways you can understand one is the GNI per capita right which is measured through the one method called the atlas methodology and the purchasing power methodology. So, if you look at these two methods and see that India stands at a very low place. It is at a very bottom right and look at if you look at the purchasing power parity what it says is basically Qatar is at the number 1 position. So, these are some of the things that impacts.

So, what it says purchasing power parities; an international dollar has a same purchasing power over GNI as a US dollar has in the United States. So, basically purchasing power parity helps you to tell in this with the same amount of dollars in a different place how much you could have purchased right.

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Gross national income per capita 2018, Atlas method and PPP: (Lowest ranking)

171	Guinea	830	171	Solomon Islands	2,280
171	Mali	830	172	Mali	2,230
173	Haiti	800	173	Rwanda	2,210
174	Ethiopia	790	174	Ethiopia	2,010
175	Rwanda	780	175	Uganda	1,970
176	Guinea-Bissau	750	176	Afghanistan	1,960
177	Gambia, The	700	177	Burkina Faso	1,920
178	Chad	670	177	Chad	1,920
179	Burkina Faso	660	179	Haiti	1,870
180	Togo	650	180	Guinea-Bissau	1,790
181	Uganda	620	181	Togo	1,760
182	Liberia	600	182	Gambia, The	1,680
183	Afghanistan	550	183	Madagascar	1,580
184	Sierra Leone	500	184	South Sudan	1,550 *
185	Congo, Dem. Rep.	490	185	Sierra Leone	1,520
186	Central African Republic	480	186	Malawi	1,310
187	South Sudan	460 *	187	Mozambique	1,300
188	Madagascar	440	188	Liberia	1,130
188	Mozambique	440	189	Niger	1,030
190	Niger	380	190	Congo, Dem. Rep.	900
191	Malawi	360	191	Central African Republic	870
192	Burundi	280	192	Burundi	740

So, this is some of the and the if you look at the lowest rankings as somewhere for example, Burundi is at the lowest rank right and Guinea; these are some of the countries which have a very low rank in terms of the gross GNI right.

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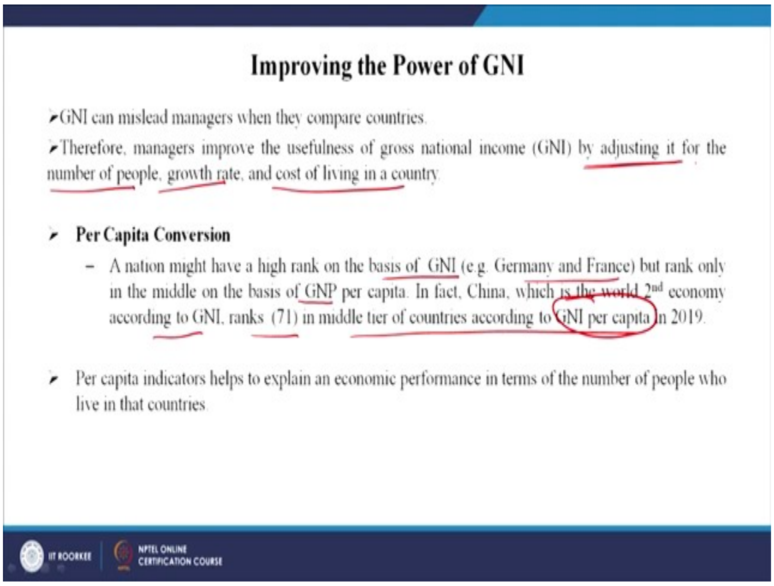

Now, how do you improve the power of GNI? GNI can mislead managers when they compare countries right it can be misleading because you are adding several factors into it. Therefore, managers improve the usefulness of gross national income by adjusting it this is very important for the number of people, the growth rate and cost of living. If you do not adjusted with these three parameters or these the three factors then it becomes a misleading data right.

Now, what is per capita conversion? A nation might have a high rank on the basis of GNI example Germany and France for example, but rank only in the middle on the basis of GNP right per capita. So, in fact, China which is the world's second economy second largest economy according to GNI rank 71 in middle tier of countries according to GNI per capita.

So, if you take absolute GNI and if you take GNI per capita this figures would be very very different right. So, so the business firms needs to understand [FL] whether they are interested for the GDP, the GNI, the GNI per capita, what are they interested in because that is what matters to them right.

So, the per capita indicators help to explain an economic performance in terms of the number of people who live in that countries. So, if your per capita income is high; that means, the people can purchase your products right. So, there is a chance of doing better in that country.

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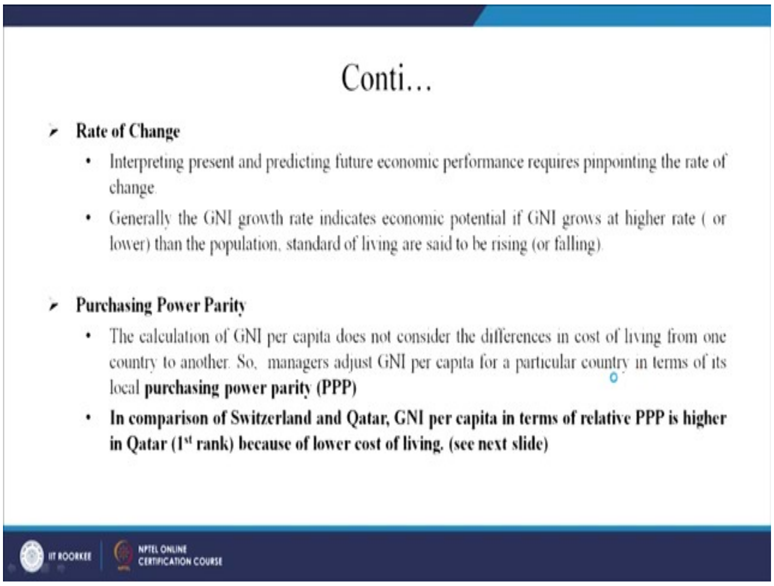

Rate of change – interpreting present and predicting future economic performance requires pinpointing the rate of change right. Generally the GNI growth rate indicates economic potential if GNI grows at higher rate than the population, standard of living and are said to be rising or falling right. So, what it says is, it should grow at a higher rate right. So, if the GNI is growing at a higher rate so, the gross national income right we will say that the economy is doing better right.

Purchasing Power Parity – the calculation of GNI per capita does not consider the differences in cost of living from one country to the other. So, managers adjust GNI per capita for particular country in terms of it is PPP right. So, in comparison of Switzerland and Qatar, you can see as in the table we had shown, GNI per capita in terms of relative PPP is higher in Qatar because of the lower cost of living.

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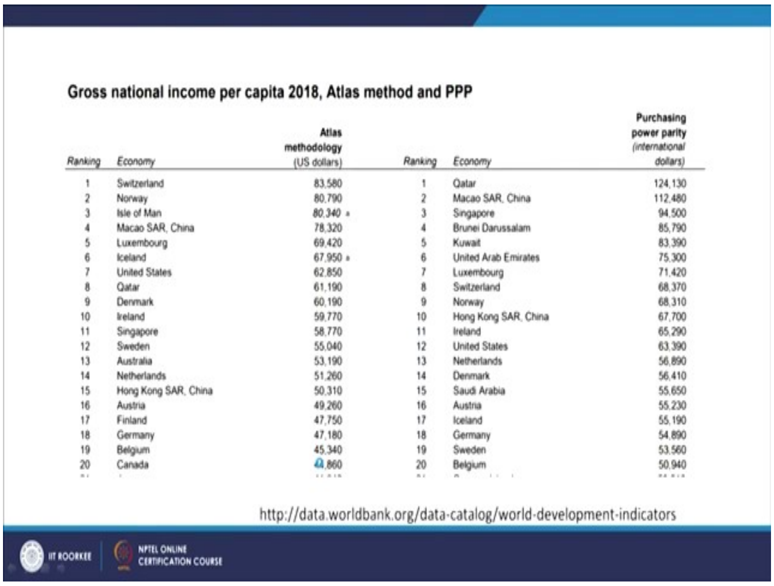

Ranking	Economy	Atlas methodology (US dollars)	Ranking	Economy	Purchasing power parity (international dollars)
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5	Luxembourg	69,420	5	Kuwait	83,390
6	Iceland	67,950 a	6	United Arab Emirates	75,300
7	United States	62,850	7	Luxembourg	71,420
8	Qatar	61,190	8	Switzerland	68,370
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18	Germany	47,180	18	Germany	54,890
19	Belgium	45,340	19	Sweden	53,560
20	Canada	[illegible],860	20	Belgium	50,940

So, again you can see here. So, Qatar has 124,130 and this is purchasing power parity and this is only 83,580 right. So, these are the things that business managers must understand deeply and they should also understand how the currencies are fluctuating, how the local governance the tax rates are changing, how for example, the RBI is trying to do it in India for example, or the Federal does it in US, right.

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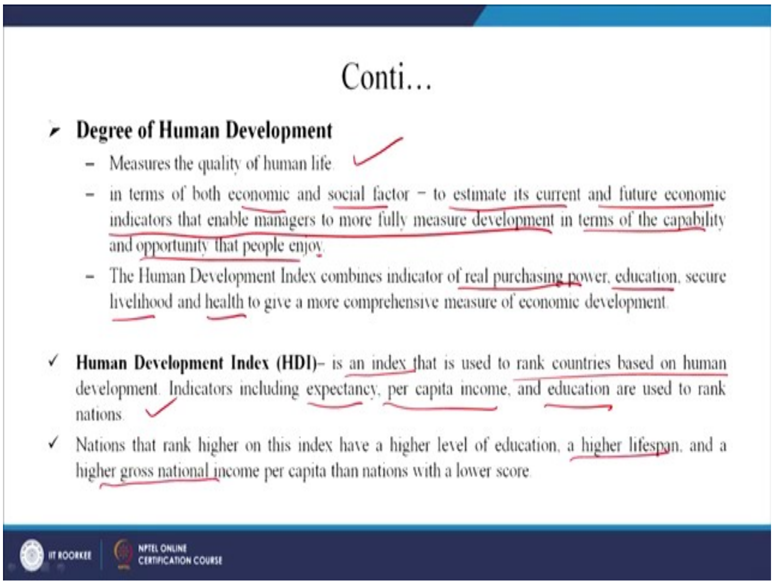

This is the last thing we will talk about today, the degree of human development. Now, degree of human development also has a great relationship with the economy condition right. So, what it measures is basically the quality of human life right in terms of both economic and social. To estimate its current and future economic indicators that enable managers to more fully measure development in terms of the capability and opportunity that people enjoy. The HDI combines indicator of real purchasing power, education, secure livelihood and health right to measure the economic development.

So, what it says HDI is an index that is used to rank countries based on human development. So, indicators including expectancy, life expectancy how much one would live. So, the life expectancy has been growing in India with time because of better medical facilities, better you know opportunities right. The per capita income and education are used to rank the nations ok.

Nations that rank higher on this index have a higher level of education is generally higher life span and a higher gross national income per capita right than the nations with a obviously, lower score.

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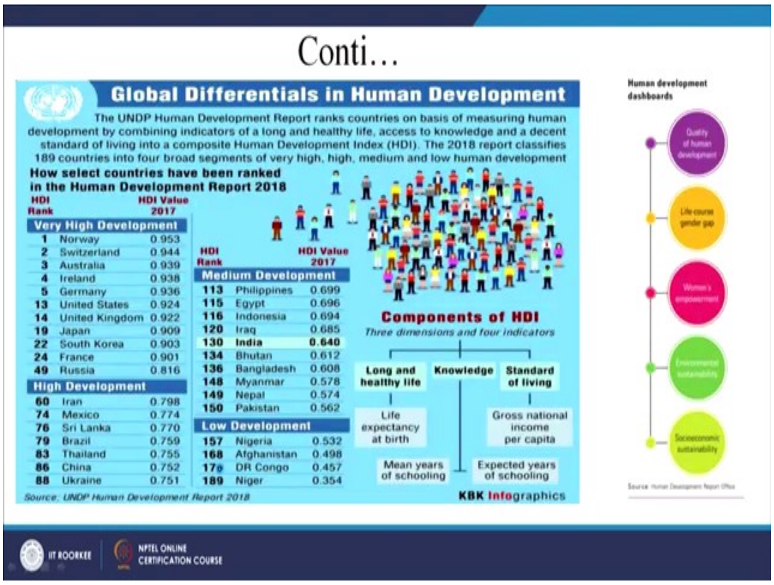

So, this is how this is how it looks like.

So, the UNDP right human development report ranks countries on basis of measuring human development by combining indicators of a long and healthy, life access to knowledge and a decent standard of living into a composite score right of HDI. The 2018 report classifies 189 countries into four broad segments very high, high, medium and low right.

So, let us see these ones which are very high development right. So, it starts with like Norway, so, it ranks between 0 and 1. So, Norway is 0.953, Switzerland 0.94 and Russia is 0.816. So, these are some of the very high development ones and this is a very recent data right and in terms of high development it is Iran, Mexico and till Ukraine right.

Medium development comes where you know the score is like 0.6 around 0.6 to 0.5; so, 0.55 and 0.7 in between that. So, Philippines, Egypt, Indonesia, India, Pakistan also lies at the middle medium development and in low development you have some of the African countries and you know which have a very poor score right.

So, these are some of the things the components as it says right. So, which I have said mean years of schooling, expected years of schooling, gross national income per capita, expected life expectancy at birth all these are the different indicators components.

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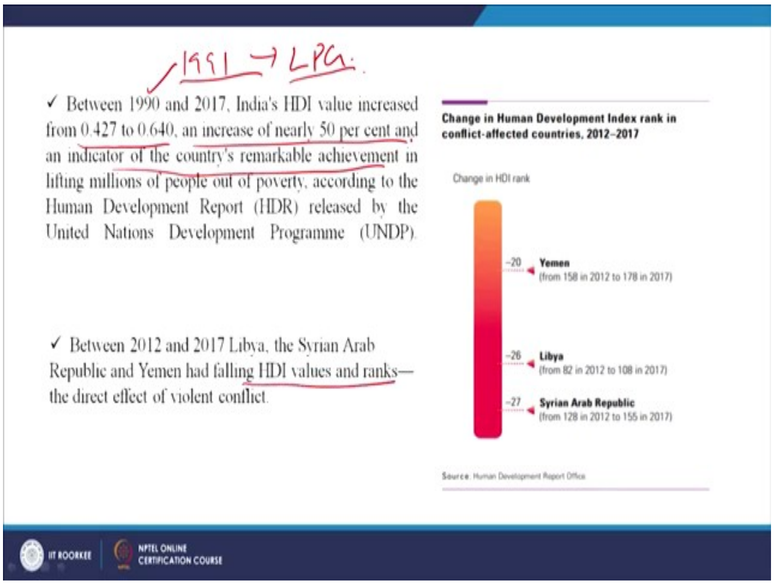

So, between 1990 and 2017, India's HDI value increased from 0.427 to 6, 0.640; this was a very good sign, an increase of nearly 50 percent and indicator of the country's remarkable achievement. So, this is the time if you can remember 1991 when India had gone for the LPG scheme right – Liberalization Privatization Globalization.

Although there are several criticisms against state or for it, but I am a stand supporter because at that point of time which India was going through so, at that point of time that was a great savior for the Indian economy right. Lifting millions of people out of poverty according to the HDI report released by the UNDP right. Between 2012 and 17 Libya, the Syrian Arab Republic and Yemen had falling HDI values; because the direct effect of violent conflict right. So, this is something you can see it from here right.

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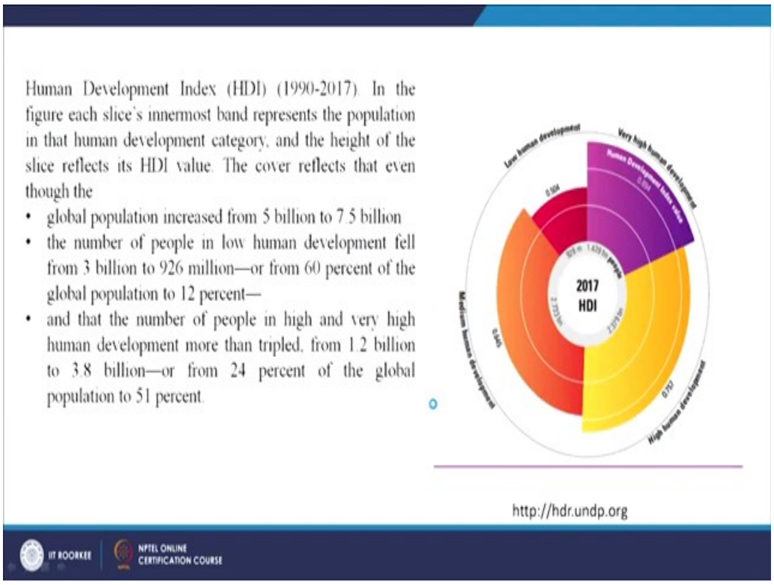

So, now this is the one which we are talking about. So, the human development index how it has been shown – now, 2017 HDI so, this is the number of people. So, very high human development, high human development, medium and low human development and the this is the scores right, the height is the score basically. So, as you can see the height of the slice reflects its HDI value and this is the population right. So, how much people are there.

So, you can see from here the global population increased from 5 billion to 7.5 billion in this time period right. The number of people in low human development fell from 3 billion to 926 million or from 60 percent of the global population to 12 percent. So, that is a very good sign right the number of people in high and very high more, than tripled from 1.2 billion to 3.8 billion or from 24 percent to 51 percent.

So, you can see that because of the trade because of the international business the more economic you know achievements are there, the policies are favorable, the countries open up there is no doubt that the and with education and all. The you know economic condition the social condition in the countries are growing right.

So, we can say for an instance that international trade, international business has a vital role to play in the growth of a nation right and countries were still doubting it and trying to stay in isolation would suffer from it maximum and they would not be able to join the momentum and gain the advantage take the advantages. Yes, criticisms are always there, but it has been seen empirically that this has had a tremendous positive achievement and success on every country.

And, yes the poor have been poor, but they have not become more poorer which is the criticism that generally done right. They have been poor, yes, they have been not to exploit the situation in a way as maybe the developed economies have done, but it does not mean they have become still poorer right. And, so, we can see that these are the factors that affected and every country should try to take as much as advantage as possible which India has done.

And, we can see and even when I am again finishing my today's lecture Abhijit Banerjee who has been given the Nobel Prize for economics with his wife Duflo has talked about his study has been on an experimental you know analysis of poverty elevation right. So, here again they have studied how poverty elevation can be done right with some good economic policies and rules and regulations right. So, this is all we have for the day.

Thank you very much.