Chapter 21

MANAGING INTERNATIONAL BUSINESS RISK

21-1 Global Risk Management
21-2 International Insurance
21-3 Reducing Global Risks
Lloyd’s of London

The world’s most famous insurance organization began in Edward Lloyd’s coffeehouse in London. In 1688, ship owners and merchants bought marine insurance from Lloyd’s to cover the risks of sending goods to other countries. In the late 1800s, Lloyd’s of London expanded into nonmarine insurance.

Over the years, this association of insurance underwriters has insured some unusual assets—the legs of Hollywood dancers, the voices of singers (such as Frank Sinatra and Bruce Springsteen), and the athletic ability of sport stars. Other unusual coverage provided by Lloyd’s have included the following.

- Insurance policies providing protection against crocodile attack in northern Australia.
- Employers buying protection against staff members winning the British national lottery and not returning to work.
- Insurance coverage against death or injury caused by a piece of a disintegrating satellite falling from the sky.

Lloyd’s of London is different from other insurance companies. This insurance society consists of investors called Names, who pool their money to cover possible financial risks. The Names profit when insurance claims are less than income. However, when a disaster occurs, the Names have to be prepared to pay for the financial losses from the disaster.

In recent years, Lloyd’s has experienced lower profits due to natural disasters, environmental problems, and changing tax laws in Britain. These events have resulted in changes in the organization. Nonetheless, some traditions continue. In Lloyd’s headquarters is the bell from the Lutine, which shipwrecked in 1857. The bell tolls once for good news, twice for bad news.

Think Critically

1. How does Lloyd’s of London serve the needs of global business organizations?
2. What factors have reduced profits for Lloyd’s?
3. Go to the web site of Lloyd’s of London to obtain information on the history and current operations of the organization. Prepare a one-page summary of your findings.
Whenever a company implements a business decision, risk is involved. The organization faces the risks of consumers not buying its product or a supplier not delivering materials on time. Risk is the uncertainty of an event or outcome. Every company faces potential risks—from employee theft to natural disasters. Companies and individuals must manage risk.

If all business ventures were sure things, life would be a lot simpler. However, in reality, every business activity has some risk. A war may destroy a factory in another country, or a company may go bankrupt and not be able to repay its debts. The three common risks faced by companies involved in international business are political risk, social risk, and economic risk, as shown in Figure 21-1.

**POLITICAL RISK**

Would a company be safer doing business in a democratic country with a newly formed government or in an autocratic nation that has been ruled by the same dictator for ten years? Political risk is difficult to evaluate. Government instability and political uncertainty are risks global companies must monitor constantly. Political control may change hands during civil unrest or a revolution. The new government may not allow certain companies to continue to operate in the country.

Business regulations vary from country to country. Regulations on business might be very tight in one nation, while great freedom is allowed elsewhere. Food packages in one country may require extensive nutritional...
information. However, another market may not have any laws regulating food labeling.

Trade barriers also pose a potential political risk. Tariffs, antidumping laws, import quotas, and currency exchange controls are examples of political actions taken to limit imported goods.

**SOCIAL RISK**

As you know, business is conducted differently in different parts of the world. Social and cultural factors such as religious beliefs, values, and family-business ties affect the risk faced by multinational companies.

Companies doing business in other countries must respect the religious beliefs of people in those nations. Failure to do so is likely to result in an unsuccessful endeavor even if all other business actions are appropriate. In a similar manner, companies that stress individualism would face greater risk when doing business in nations that emphasize collectivism.

The connection between family and business is very important in some cultures and less important in others. In most areas of Central and South America, much of southern Europe, and most of Asia, northern Africa, and the Middle East, family business ties are strong. Companies must work within this cultural environment to minimize business risk.
Economic conditions have ups and downs. The demand for a company’s goods and services varies based on the income of consumers, interest rates, and levels of employment. When fewer people are working, less money is available for consumer spending.

When a company receives one dollar today, it hopes to be able to buy something worth one dollar in the future. However, if inflation erodes the buying power of a currency, the monetary unit will not have as much purchasing power in the future.

Companies that do business in other countries face the risk of receiving payment in a currency that may have less value than expected. With exchange rates changing daily, financial managers must make sure that the payment received is appropriate after the currency conversion.

Monitoring Global Business Risk

Change is the only constant in all aspects of business. Reading current materials, talking with residents, and watching economic data are ways to note changes in a country’s business environment. Awareness of factors such as political stability, religious influences, and fluctuating interest rates can help a manager predict changes in business risk. An ability to anticipate and act early can reduce risk and lessen the chances of poor business decisions.

Think Critically

1. Why do companies conduct disaster drills?
2. Go to the web site of Royal Dutch/Shell to obtain additional information about the risks faced by the company around the world. Write a report of your findings.

Global Business

Practicing for Unexpected Events

Royal Dutch/Shell is one of the world’s largest petroleum and natural gas companies. The company is a joint venture between Royal Dutch Petroleum (60 percent ownership) and Shell Transport and Trading (40 percent ownership). It has business activities in more than 130 countries and operates about 50,000 gas stations.

Shell continually encounters fluctuating oil prices, environmental concerns, and uncertainty in supplier nations. When the Persian Gulf War started in the early 1990s, Shell was no longer able to obtain oil from Kuwait and Iraq. How can a company prepare for these types of risks? Royal Dutch/Shell prepares by simulating disasters.

A couple of times a year, oil shipments are unexpectedly interrupted. Then employees must put backup plans into operation. Therefore, during the Gulf War, the company had already arranged to locate and ship oil from alternative sites.

Global Business Challenges

What are the three main categories of risk faced by multinational companies?
Multinational companies will face many business risks. Figure 21-2 shows four steps commonly taken to manage these international business risks. These are identify potential risks, evaluate risks, select a risk management method, and implement the risk management program.

**STEP 1 IDENTIFY POTENTIAL RISKS**

In the first step of the risk management process, managers list the factors that might affect a company’s operations. Government policies, currency values, and local customs are some examples of risk-causing elements. Managers can use current reports, field interviews, and other data sources to uncover conditions that increase uncertainty.

**STEP 2 EVALUATE RISKS**

In this step, managers analyze the potential effect of risks on a company. Will a change in government mean higher costs to cover new environmental regulations? Or could the change in government result in the company facing new trade barriers when doing business in that nation? Managers must decide how and to what extent the risks will influence sales and profits.
Be aware that a factor in the international business environment can affect different companies in different ways. A weak economy may hurt a company selling entertainment products. However, the same poor economic conditions may benefit a company selling low-cost clothing.

**STEP 3 SELECT A RISK MANAGEMENT METHOD**

Next, managers must decide how to handle the identified risks. The four methods used to manage risk—risk avoidance, risk reduction, risk assumption, and risk sharing—are shown in Figure 21-3.

*Figure 21-3* Companies manage risks in four main ways.

**Risk Avoidance** Certain risks can be avoided. A company avoids the risks related to international business by only selling products in its home country. However, this approach to risk management is not always practical. A business limits its potential for expansion by selling only in its domestic market or in markets in safe geographic regions.

**Risk Reduction** The risk of an event may be reduced by taking precautionary actions. For example, businesses use security systems and sprinklers to reduce the risk of theft and fire. Multinational companies can reduce business risks by selling products that have been successful in other countries.

**Risk Assumption** Sometimes a company takes responsibility for losses from certain risks. For example, a business may set aside funds for fire damage that may occur to its factories. This action, called *self-insurance*,...
Involves setting aside money to cover a potential financial loss. A company with many stores or factories in different locations may save money by using self-insurance.

**Risk Sharing** Sharing risks among many companies that face similar risks is a common practice. Insurance is often purchased for financial protection from property losses, motor vehicle accidents, and other business activities.

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**STEP 4 IMPLEMENT THE RISK MANAGEMENT PROGRAM**

Finally, managers must execute the risk management plan. This phase involves both taking relevant action and measuring the success of the action. Various factors in the business environment and within the company may change an organization’s risk management course in the future.

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### A Question of Ethics

**UNREPORTED BUSINESS ACTIVITIES**

In most countries, an *underground* economy exists. This phrase, sometimes called the *black market*, refers to business activities outside the formal economy. Underground economy transactions are not reported to government agencies.

In some regions of developing countries, over half of the construction work and other business activities are “off the books”—never reported for paying sales and income taxes. These unreported business transactions could benefit the people of a country. Jobs are created, and people earn income for paying living expenses.

However, the underground economy also has a negative impact. Since sales revenue and incomes are not reported, governments do not collect taxes. Money is not available to pay for public services such as education, police protection, road construction, and trash collection.

**Think Critically**

Use the three guidelines for ethical analysis to examine the above situation. How does the underground economy affect businesses, consumers, and society?

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**Checkpoint**

What are the steps of the risk management process?
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REVIEW GLOBAL BUSINESS TERMS
Define each of the following terms.

1. risk
2. self-insurance

REVIEW GLOBAL BUSINESS CONCEPTS
3. What are examples of social risks?
4. How can managers monitor international business risk?
5. What are the four methods used to manage risk?

SOLVE GLOBAL BUSINESS PROBLEMS
For each of the following situations, describe actions that the organization might take to manage its business risk.

7. Stealing by employees and customers.
8. Changes in the value of foreign currencies.
11. Political instability in a foreign country.

THINK CRITICALLY
12. What are some examples of government regulations that create global business risks?
13. Describe a risk-reduction action that a company could use.
14. What are some actions you take each day to avoid and reduce risks in your life?

MAKE CONNECTIONS
15. TECHNOLOGY  Explain how changing technology could increase and decrease risks for a global company.
16. CULTURAL STUDIES  Describe differences in customs, traditions, and language that could create a social risk for a company operating in another country.
17. TECHNOLOGY  Use the Internet to identify online resources for risk management.
18. CURRENT EVENTS  Use the Internet to find a recent event that poses a risk to international business. Identify the type of risk and describe a plan for managing this risk.
INSURANCE is planned protection for sharing economic losses among many people. Insurance is commonly purchased to reduce or eliminate the financial loss due to risks. A company’s place of business is usually covered by property insurance. When driving a car, a traveling salesperson probably has automobile insurance. Most everyone reading this book uses insurance as a method for managing risk.

Insurance is an agreement between one party, called the insured, and an insurance company, the insurer. A stock insurance company is owned by stockholders and is operated for profit. A mutual insurance company is owned by its policyholders. This type of organization returns any surplus to policyholders after claims and operating expenses are paid.

INSURABLE INTEREST

A basic requirement of insurance is the presence of an insurable interest, something of value that may be lost or destroyed. For example, equipment owned by a company represents an insurable interest. In the case of life insurance, the insurable interest is the financial loss caused by someone’s death.

INSURABLE RISK

Another basic requirement of insurance is the presence of an insurable risk. An insurable risk is a risk that has the following elements.

- Common to many people—The risk must be one that is faced by many people or businesses. This allows many people with the same risk to share the cost with the few who actually suffer a financial loss due to the risk.
Definite—The risk must be something that can be documented. The destruction of a building by fire or the death of a person is something that can be documented.

Not excessive in magnitude—An insurance company would not be able to cover the cost of replacing all homes it insures at one time. Recent hurricanes in Florida caused such extensive damage that some insurance companies can no longer afford to do business in that state.

Not trivial—Insurance on small items would not be worth the time, effort, and expense necessary to provide coverage.

Able to be calculated—The insurer must be able to calculate the probability that the risk will occur. This allows the insurer to plan what amount to charge for insurance.

AIG IN CHINA
Small business owners in Shanghai are the newest customers of American International Group (AIG), one of the first insurance companies to sell directly to Chinese citizens. The People's Insurance Company of China, a state-owned monopoly, fought to keep AIG out of the country. However, political leaders ruled in favor of AIG. As this business relationship proves to be satisfactory for both sides, the Chinese market is opening for other service companies. Accountants, airlines, banks, freight forwarders, and stockbrokers are hoping to sell in a country with one-fifth of the world's population.

Doing business in more than 130 countries, AIG is one of the world's largest insurance enterprises. The company is involved in property, casualty, auto, life, and worker's compensation insurance. Other business activities of AIG include financial services, currency hedging, and aircraft leasing.

Think Critically
1. What political factors create difficulties when a company attempts to compete in another country against domestic businesses?
2. Go to the web site of AIG to obtain current information about the company's global business activities. Write a report on your findings.

Check Point
What are the elements of an insurable risk?
INSURANCE POLICY ELEMENTS

An insurance policy is the legal agreement between an insurance company and the insured. This contract states the conditions of protection. Figure 21-4 shows the major elements of an insurance policy.

Figure 21-4  An insurance policy is the contract between an insurance company and the insured.

Declaration  The declaration states what is covered and lists the amount of coverage. For example, the declaration for a multinational company’s insurance would describe the enterprise’s factories in different countries and at what amount they were covered.

Insuring Agreement  The insuring agreement explains the coverages of the insurance policy. A company’s insurance policy may cover fire and theft losses for property up to a set amount, such as $14 million—the amount of the coverage.

Conditions  The conditions of an insurance policy provide information about the cost of insurance, called the premium. Also listed are any deductibles. A deductible is the portion of an insurance claim paid by the insured. A company with a $1,000 deductible, for example, may incur $4,500 of wind damage to a building. In this situation, the insurance company would pay $3,500. The first $1,000 of the claim is paid by the insured. Deductibles reduce the cost of insurance premiums.

Exclusions  Property or risks not covered by an insurance policy are called exclusions. For example, many insurance policies do not cover property losses resulting from war. Why do you think insurance companies exclude financial loss due to war from policies?

Endorsement  An endorsement is a certificate that adds to or changes the coverage of an insurance policy. For example, if a company sells a factory, an endorsement would delete the building from its insurance coverage.
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Exports should be insured against loss or damage that could occur while in transit. An *insurance certificate* provides evidence of insurance to protect goods from loss or damage while in transit. Sales terms determine if the importer or the exporter pays insurance costs.

**REGIONAL PERSPECTIVE**

**HISTORY: THE ORGANIZATION OF PETROLEUM EXPORTING COUNTRIES**

To prevent further price cuts by U.S. and European oil companies, the Organization of Petroleum Exporting Countries (OPEC) was created in 1960. The original members were Iran, Iraq, Kuwait, Saudi Arabia, and Venezuela. Today OPEC has 11 members, including the countries of Algeria, Indonesia, and Nigeria that, like Venezuela, are from outside the Persian Gulf region.

During its first decade, OPEC was concerned mostly with maintaining stable world oil prices. However, by 1970, as the world price for oil dropped (supply exceeded demand), OPEC worked to raise oil prices by reducing production levels. During 1973–74, petroleum prices rose by 400 percent. This was followed by a four-year period of stable prices.

The OPEC countries accounted for 66 percent of the world’s petroleum supply in 1979. Ten years later their share dropped to 34 percent. In 1993, increased production, especially by Kuwait after the Gulf War of 1991, resulted in a higher supply and lower worldwide oil prices.

**Think Critically**
1. What factors influence the world market price of oil?
2. Go to the OPEC web site for additional information about the current activities of the organization. Write a paragraph about your findings.

**CheckPoint**

What are the main elements of an insurance policy?
REVIEW GLOBAL BUSINESS TERMS
Define each of the following terms.

1. insurance
2. stock insurance company
3. mutual insurance company
4. insurance policy
5. premium
6. deductible
7. endorsement

REVIEW GLOBAL BUSINESS CONCEPTS
8. How does a stock insurance company differ from a mutual insurance company?
9. What is an insurable interest?
10. What is the purpose of an endorsement?

SOLVE GLOBAL BUSINESS PROBLEMS
For each of the following items, name the insurance policy element that is involved.

11. “For all claims, the insured party will pay the first $2,000 of damages.”
12. “This policy provides coverage for damage to the factory at 1765 Industrial Drive.”
13. “As of June 3, 2001, this policy no longer covers damages as a result of civil riots in foreign countries.”
14. “This coverage has a cost of $5,600 for the period of August 7, 2001, to August 6, 2002.”
15. “This policy does not cover damage resulting from hurricanes or acts of war.”

THINK CRITICALLY

16. What are the benefits of a mutual insurance company?
17. How does a deductible reduce insurance costs for the insurance company and the policyholder?

MAKE CONNECTIONS

18. MATHEMATICS If a company has insurance coverage with a $5,000 deductible and encounters a claim for $6,200, how much would the insurance company pay?
19. LAW Obtain a sample of an insurance policy to observe the elements of this contract.
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21-3 REDUCING GLOBAL RISKS

GOALS
- Identify the major types of insurance coverages for international business activities.
- Describe strategies that multinational companies use to reduce risk.

GLOBAL INSURANCE COVERAGES

Companies involved in international business can share certain risks by using insurance. Commonly used coverages of multinational companies are marine insurance, property insurance, coverage for political risk through the Overseas Private Investment Corporation, and credit risk insurance.

MARINE INSURANCE
Overseas transporters usually assume no responsibility for the merchandise they carry unless the loss is caused by their carelessness. Marine insurance provides protection from loss during shipment of products. This insurance has two types of coverage.

- **Ocean marine insurance** protects goods during shipment overseas or while temporarily in port. In contrast, **inland marine insurance** covers the risk of shipping goods on inland waterways, railroad lines, truck lines, and airlines.
  - Marine insurance is usually sold in three forms with varied coverages.
    1. **Basic coverage** provides protection from hazards such as sea damage, fires, jettisons, explosions, and hurricanes.
    2. **Broad coverage** includes basic coverage plus theft, pilferage, nondelivery, breakage, and leakage.
    3. **All-risk coverage** consists of any physical loss or damage due to an external cause, excluding risks associated with war.
As expected, an all-risk policy is the most expensive of the three types since the most coverage is provided. Also be aware that some losses are not covered by all-risk policies. Items not covered include improper packing, damage caused by natural properties of a product (such as rusting of steel), and loss caused by delay (such as a labor strike).

The amount charged for marine insurance is affected by a variety of factors. Premium factors include the value of the goods, the destination, the age of the ship, the storage location (on deck or under deck), the packaging, and the size of the shipment (volume discounts are common).

**PROPERTY INSURANCE**

Crimes such as burglary, theft, and arson disturb business activities throughout the world. Companies face three main risks as property owners.

1. Loss of real property
2. Loss of personal property
3. Financial responsibility for injuries or damage

**Loss of Real Property** Real property refers to structures permanently attached to land, such as factories, stores, garages, and office buildings. A company's building and land represent a significant financial investment. Property insurance provides protection for damage or loss of real property. Buildings and structures are insured for loss or damage from fire, lightning, wind, hail, explosion, smoke, vandalism, and crashes of aircraft and motor vehicles.

**Loss of Personal Property** Personal property refers to property not attached to the land. Loss or damage of office furniture, machinery, equipment, and supplies also can be covered by property insurance.

**Financial Responsibility for Injuries or Damage** Liability is legal responsibility for the financial cost of someone else's losses or injuries. Customers, company guests, employees, and others may be injured while on the premises of a business. Or a company representative may accidentally damage the property of others. When any of these occur, the company may be responsible for the financial loss that results from the incident.

Quite often legal responsibility is the result of negligence, or failure to take ordinary or reasonable care. An employer may also be held financially responsible for the actions of an employee. Liability insurance protects a company from financial losses due to the actions of its employees.

**THE OVERSEAS PRIVATE INVESTMENT CORPORATION**

To encourage investment in less developed countries, the U.S. government created the Overseas Private Investment Corporation (OPIC). This agency protects U.S. companies from various hazards. OPIC protects 150 developing nations and emerging markets from financial losses, which may be the result of the three major types of risk.
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NOT ALL LANGUAGES ARE EQUAL FOR BUSINESS PURPOSES

Businesses can increase their international risks by using certain languages. For example, Hebrew is not a particularly good language for international business purposes. It is a holy language that evolved primarily for religious purposes, not for common speech purposes, including the accomplishment of business. As the dominant language of only one small country, Israel, Hebrew is not widely known by businesspersons around the world. Very few opportunities for learning Hebrew exist in most countries. Further, finding knowledgeable establishments that can accurately print documents in Hebrew is very difficult in many locations outside of Israel. Thus, a multinational organization that chooses Hebrew as its only business language will likely expose itself to greater communication risks than one that chooses a more common language of international business.

Think Critically
1. How does a multinational organization increase its risks by choosing Hebrew as its only business language?
2. If Hebrew is determined to be too risky as the official business language for an Israeli multinational organization, what other language(s) should be considered? Why?

Credit Risk Insurance

One hazard of conducting business in other countries is not receiving payment. Credit risk insurance provides coverage for loss from nonpayment of delivered goods. This protection helps reduce the risk of international business activities.

Credit risk insurance is available through the Foreign Credit Insurance Association (FCIA), a private association that insures U.S. exporters. FCIA enables exporters to extend credit to overseas buyers.

Credit insurance covers 100 percent of losses due to political reasons, such as war, asset seizure, and currency inconvertibility. This insurance covers up to 95 percent of commercial losses, such as nonpayment due to insolvency or default.

About 200 banks in the United States have purchased master policies from FCIA and can insure loans made to U.S. exporters. Banks typically charge about 1 percent of the amount insured for the coverage.

CheckPoint

What are the three main risks faced by property owners?
Risk is something every company will face in every business situation. However, management experts recommend the four strategies shown in Figure 21-5 to help reduce international business risk.

**Conduct Business in Many Countries.** When a company depends on a variety of nations for its sales and profits, it will not be greatly affected by turmoil in one of its markets. U.S. companies doing business in Cuba when Castro gained power in 1959 lost some of their business assets. Fortunately, most of these multinational companies also were operating in many other nations.

**Diversify Product Offerings.** Just as a company should operate in several nations, it should not be dependent on only one or a few products.
By having a varied portfolio of goods and services, an organization reduces its risk when consumers no longer desire one product. By seeking new uses for products and by creating new products, a company reduces its international business risk.

**Involve Local Ownership** Local ownership of multinational firms usually is viewed favorably by local governments. A company that is completely owned by citizens of another country faces the greatest risks. A host nation feels threatened when people who may have different political and social beliefs control its economic existence. Joint ventures with local private partners are frequently less risky.

**Employ Local Management** Hiring local managers allows a company to maintain a good working relationship with the host government. Administrators who are native to a country or region understand local customs and cultural norms. A comfortable working relationship will be more likely when local managers are employed.

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**Global Business Example**

**THE RUSSIAN INSURANCE INDUSTRY**

When the former Soviet Union evolved from communism to capitalism, many insurance companies were started. Russia’s first insurance law, effective January, 1993, allowed an applicant to become a licensed insurance seller with only 2 million rubles in capital—about $1,100. This allowed many inexperienced entrepreneurs to enter the market.

Foreign ownership of Russian insurance companies is restricted to 49 percent. One company, Giva, received financial support from RBS Holding, a communications and food service firm from Bloomfield Hills, Michigan. In 1993, Giva earned 80 million rubles (about $65,000) on over one billion rubles ($820,000) in insurance premiums.

Vera (Russian for “trust”) is an insurance company that has the Christian Russian Bank as one of its largest shareholders. Vera specializes in insuring the real estate of the Russian Orthodox Church. The company also provides insurance coverage for the church’s art and other priceless treasures made from gold and diamonds.

More recently, Nakhodka Re offers a variety of coverages, including liability, property, motor vehicle, aircraft, cargo, and fishing vessel crew insurance. The company also works with overseas insurance brokers to assist businesses shipping goods to and within Russia and other eastern European countries.

**Think Critically**

1. How did changes in the Russian political and economic environment affect the insurance business in that country?
2. Conduct an Internet search to obtain current information about insurance activities in Russia and other eastern European countries. Write an outline of your findings.

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**Checkpoint**

How does doing business in several countries reduce risk for a global company?
REVIEW GLOBAL BUSINESS TERMS

Define each of the following terms.

1. ocean marine insurance
2. inland marine insurance
3. credit risk insurance

REVIEW GLOBAL BUSINESS CONCEPTS

4. What are the three forms of marine insurance?
5. How does real property differ from personal property?
6. What is the purpose of the Overseas Private Investment Corporation?
7. What is the purpose of credit risk insurance?
8. How can companies reduce risks associated with international business activities?

SOLVE GLOBAL BUSINESS PROBLEMS

For each of the following business situations, indicate the type of insurance that would cover the financial loss.

9. Goods shipped overseas and stolen while in port in southern Europe.
10. Fire damage to a factory in South America.
11. Nonpayment for a shipment of clothing to eastern Europe.
13. Accidental injury to guests from another company visiting a factory in Africa.

THINK CRITICALLY

14. What risks are associated with shipping goods by railroad, truck, and airplane?
15. What problems might a company encounter when involving local ownership or employing local management?

MAKE CONNECTIONS

16. TECHNOLOGY Go to the web site of the Overseas Private Investment Corporation to obtain information on the current activities of this organization. Write a paragraph summarizing your findings.
17. GEOGRAPHY Create a map showing countries with similar climates in which a company could sell its products.
16. TECHNOLOGY Use the Internet to locate online business insurance resources.
Chapter 21 ASSESSMENT

CHAPTER SUMMARY

21-1 GLOBAL RISK MANAGEMENT

A Companies involved in international business commonly face political, social, and economic risks.

B The risk management process involves (1) identifying potential risks, (2) evaluating risks, (3) selecting a risk management method, and (4) implementing the risk management program.

21-2 INTERNATIONAL INSURANCE

A The basic elements of insurance coverage involve (1) an insurable interest—something of value and (2) an insurable risk—an event common to many people that is definite, not excessive in magnitude, not trivial, and able to be calculated.

B The elements of an insurance policy include the declaration, the insuring agreement, the conditions, the exclusions, and any endorsements.

21-3 REDUCING GLOBAL RISKS

A The major types of insurance for international business are marine insurance, property insurance, the Overseas Private Investment Corporation coverage, and credit risk insurance.

B Strategies that multinational companies use to reduce risk include conducting business in many countries, diversifying product offerings, involving local ownership, and employing local management.

GLOBAL REFOCUS

Read the Global Focus at the beginning of this chapter, and answer the following questions.

1. What are the similarities and differences between Lloyd’s and other insurance companies?

2. What actions might Lloyd’s take to expand its operations around the world?
REVIEW GLOBAL BUSINESS TERMS

Match the terms listed with the definitions.

1. The portion of an insurance claim paid by the insured.
2. Coverage for loss from nonpayment of delivered goods.
3. An insurance company owned by stockholders and operated for profit.
4. Setting aside money to cover a potential financial loss.
5. The uncertainty of an event or outcome.
6. Protection from loss while goods are being shipped overseas or while temporarily in port.
7. Planned protection for sharing economic losses among many people.
8. A certificate that adds to or changes the coverage of an insurance policy.
9. The cost of insurance.
10. An insurance company owned by its policyholders.
11. Protection from a loss while shipping goods on inland waterways, railroad lines, truck lines, and airlines.
12. The legal agreement between an insurance company and the insured.

MAKE GLOBAL BUSINESS DECISIONS

13. Name some risks exporters could face that might not be present when a company sells within its own country.
14. Describe ways you could reduce risks in your home and at your school.
15. Speculative risks include such things as starting a new business or introducing a new product. These cannot be covered by insurance. Why will
insurance companies not cover speculative risks? List other examples of speculative risks.

16. Explain why deductibles reduce the premium paid for insurance.

17. An exporter might not make a marine insurance claim, even if it is valid. Many small claims can increase the cost of insurance in the future. Why might an exporter decide not to make a claim?

18. Most people who own or operate a business consider liability insurance coverage vital. Why?

19. You are the regional manager for a multinational company in Saudi Arabia that manufactures and distributes plastic products. What actions would you take to reduce risk for your company?

GLOBAL CONNECTIONS

20. GEOGRAPHY Prepare a map that indicates some of the countries that have had political unrest or military conflicts in recent years. Explain how companies could reduce risks in these countries.

21. COMMUNICATIONS Talk to someone with homeowner’s or renter’s insurance. Report to the class about the types of risks that are covered by property insurance.

22. HISTORY Conduct library or Internet research about marine insurance. Prepare a report that explains risks and hazards of this international business insurance.

23. CULTURAL STUDIES Interview a person who has lived or worked in another country. Obtain information about differences in customs, traditions, and language that could create business risks.

24. VISUAL ART Prepare a poster illustrating methods that companies could use to reduce business risk.

25. MATHEMATICS Contact several insurance agents to obtain information about the cost of property or liability insurance. Prepare a graph that shows differences in costs and coverages.

26. CAREER PLANNING Interview a person who works in an insurance career. What training and skills are required for jobs in the insurance industry?
GLOBAL RISK MANAGEMENT
Conduct research on global business risks and insurance based on the company and country you have been using in this continuing project, or create a new idea for your business in the same or a different country. Make use of previously collected information, and do additional research. This phase of your business plan should answer the following questions.

1. What are the company’s main international business risks?
2. Is self-insurance practical for the company?
3. For what situations might the company make use of marine insurance?
4. What types of property does the company own that need to be insured?
5. Why might liability coverage be important to the company?
6. What types of insurance might the company provide as an employee benefit for its workers?

Prepare a written summary or present a short oral report (two or three minutes) of your findings.
Finance International Business Operations

Obtaining loans, attracting investors, and evaluating international business risk are some of the financial aspects of global operations. As companies expand into various geographic regions, cross-cultural teams allow financial managers to better understand various influences on their decisions.

GOAL
To identify differences in finance activities in various regions of the world.

ACTIVITIES
Working in teams, select a geographic region you will represent—Africa, Asia, Europe, Latin America, the Middle East, or North America.

1. International finance topics may be researched in current articles, library materials, and Web searches. Also, if possible, have a discussion with people who have lived or visited your region of the world.
2. Research attitudes toward the use of credit in your region. How do tradition, religion, and culture affect borrowing?
3. List common financial institutions that operate in your geographic region. What services do they provide for businesses?
4. Identify common investments people make in the region. To what extent are stocks, bonds, mutual funds, real estate, and other investments used to achieve financial goals?
5. Describe the major political, social, and economic risks faced by companies doing business in this region. What actions might be taken to reduce or eliminate these risks?
6. Global Business Decision An international company has asked your team for advice to finance the expansion of business operations around the world. How might the use of debt be viewed in different regions? What additional financing alternatives might be taken?

TEAM SKILL
Measuring the Success of Cross-Cultural Teams
The completion of a team project includes evaluating the level of achievement. Measures of success vary among geographic regions. Describe possible items that might be used to measure the success of a team in your region. Compare your list with those of other members of your team.

PRESENT
Plan and present a debate among your team members to compare the risks associated with doing business in various geographic areas. Discuss the types of risks and actions that might be taken to reduce or eliminate these risks.
The global economy depends upon international trade. When a business decides to conduct international trade or to locate in another country, important information must be researched. Good international business decisions depend upon understanding the major economic, political, and demographic issues of other countries where international trade will take place. The best research will convince decision makers to conduct trade with other countries. Also a well-planned presentation will convince other countries of the value to accepting a new multinational company. You are challenged to prepare a presentation to convince the audience to conduct business in another country. Your presentation will be evaluated on content and possible results.

Choose a country that conducts international trade with the United States. Prepare a multi-media presentation that covers demographics, political system, currency, education, culture, economic system, and customs for the country.

This presentation will prepare business leaders who have been promoted to positions in companies located in your chosen country. The presentation should give strategies to make seamless adjustments to a new country. The presentation should include a wide array of features, including transitions, sound effects, music, and other enhancements.

PERFORMANCE INDICATORS EVALUATED

- Define the demographics, political system, currency, education, culture, economic system, and customs for the country.
- Explain how transfer employees can make smooth transitions to jobs located in the new country.
- Use solid examples to describe all aspects of the country.
- Incorporate a wide array of multimedia functions to enhance the presentation.

For more detailed information about performance indicators, go to the FBLA web site.

THINK CRITICALLY

1. Outline information about the demographics, political system, currency, education, culture, economic system, and customs for your chosen country.
2. List three tips for an individual who has been promoted to a position in the new country.
3. What customs should the business leader understand about the country? Why?