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GLOBALISATION AND GLOBAL TRADING SYSTEM: IMPACTS ON BUSINESSES

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ABSTRACT

Globalisation is the phenomenon of the integration of markets worldwide into a single global economy known as free market system that offers equal access to opportunity as entry barriers for trade and investment decline. The world free trading system started off with GATT under U.S. leadership that later led to the formation of WTO and regional trading blocks such as NAFTA, EAEC and AFTA to name a few. AFTA is important as a medium-term vehicle allowing ASEAN countries to participate in the negotiation process towards liberalised global trading. To benefit fullest from globalisation and global trading system, the entrepreneurs have to develop appropriate strategies to maintain an edge over their competitors. In addition business operations may require adjustments and adaptation in order to survive in the new volatile business environment. This paper attempts to look at the definition of globalisation, development of liberalised global trading system and at later part reviews some of the impacts on businesses particularly in Malaysia.

INTRODUCTION

Globalisation is the phenomenon of the integration of markets worldwide into a single global economy and ascendancy of private business. Global independence between nations and regions are growing in terms of trade, investment, production, marketing, distribution and consumption. As a result, nation's competitive advantage depends mostly on the ability of the nation and its people to adapt to this changing environment.

A single global market is known as a **free market economy**. Free market ways are increasingly adopted by many nations of the world including China, the republics of the former Soviet Union, the Indo-China states and the ex-Communist countries of Eastern Europe which have liberalised their economies. The free market system means equal access to opportunity as entry barriers for trade and investment decline, which businesses will face intense competition. In order to survive and succeed in global economy, businesses must focus and concentrate on moving up the value chain, creating innovative goods and providing quality services that the world wants and marketing them well. Thus, the new global economy postulates new rules and new challenges for all economies, including Malaysia.

DEFINITION OF GLOBALISATION

International Monetary Fund (IMF) publication defines globalisation as **'the growing economic interdependence of countries world wide through the increasing volume and variety of cross-border transactions in goods and services and international capital flows, and also through the rapid and widespread diffusion of technology'** (IMF, 1997). Therefore, global economy will involve three fundamental pillars: international trade, outward investment and worldwide transfer of technology. However, globalisation is due to the interconnected manner in which the three pillars grow and reinforce each other in an inextricably complex way without regard for national boundaries (Sieh, 2000).

Globalisation can also be defined as the decline in cost of doing business internationally (Anderson, 2001). The costs of interacting internationally are contributed by two factors, i.e. technological and governmental barriers.

The cost of transporting goods was enormously lowered in the nineteenth century by invention of steam engine, steel hull for ships and refrigerator and telegraph (O'Rourke & Williamson, 1999). Over time, in the middle of twentieth century the cost of moving people has lowered too. And recently the deregulation of telecom markets in many countries, has lowered long-distance communications costs especially the cost of accessing and processing knowledge, information and ideas from anywhere in the world.

Furthermore, methods of industrial production are altering dramatically. Specialized, single-purpose equipment for mass production is being supplemented or replaced by flexible machine tools and programmable multi-task production equipment that permits the firm to produce a variety of products efficiently in small batches (Milgrom & Roberts, 1990).

According to World Bank (1998), wealth creation in the twenty first century will depend on the ability to access and make productive use of the expanding stocks of knowledge and information, and to build on them through creative research and development to design highly flexible production methods. Furthermore, market liberalization with lowering import tariffs, outward-oriented trade and investment policies and deregulation of domestic markets by government decisions of many countries enhance global businesses that demand of good economic governance to ensure stable trading environment.

Globalisation is also a process that entails continuous adjustments and re-adjustments (Sieh, 2000). Thus business entities have to adhere to universal business principles and practices, which are recognised, respected and understood by the regional and global corporate communities (Lee, 2001). The rules of business are changing rapidly which, require management to be sensitive to the changes in order to survive in the market place. There is a need to place more emphasis on product and service differentiation and premium quality performance because of greater competition in international market due to the crumble of trade barriers and protection as a result of globalisation and trade liberalisation – free market without government intervention.

DEVELOPMENT OF THE GLOBAL TRADING SYSTEM

The international trading system began its reformation after the Second World War where the world's economies required re-building after being devastated. The co-operation among countries increased to make the movement of goods and services as well flow of capital easier. The trade-facilitating trend was complimented by the shift of policies of developing countries from export substitution to more market-oriented reforms and the fall of the communist block in Europe (Martin, 2001). Initially the co-operation evolved slowly, but later gain momentum and move forward into more open international trading system with less protectionism known as world free trade system.

The world free trade system started off with the General Agreement on Tariff and Trade (GATT) under US leadership. GATT was a multilateral agreement whose objective was to liberalise trade by eliminating tariffs, subsidies, import quotas etc. GATT did not attempt to liberalise trade restriction in one phase but rather to spread over eight rounds.

GATT regulations were enforced by a mutual monitoring mechanism. If one country believed that one of its trading partners was violating a GATT regulation, it could ask the Geneva-based bureaucracy that administered GATT to investigate. If GATT investigators found the complaints to be valid, member countries could be asked to pressure the offending party to change its policies.

In its early years, GATT trade liberalisation system was successful. But however during 1980s and early 1990s the world trading system built by GATT began to strain as protectionist pressure arose around the world. The three main reasons for the rise in protectionist pressures were due to the success of Japanese economy, persistent of U.S. trade deficit and many countries found ways to get around GATT regulations (Hill, 1998).

In 1986 the last round of GATT's negotiations to reduce tariffs, known as The Uruguay Round took place. It was reported that it was the most difficult round of negotiations and dragged for seven years. Member countries sought to extend GATT rules to cover trade in services. Previously, GATT rules had applied only to trade in manufactured goods and commodities. The Uruguay Round agreement has the following effects:-

- Tariffs on industrial goods will be reduced by more than one-third.
- Agricultural subsidies will be substantially reduced.
- GATT fair trade and market access rules will be extended to cover a wide range of services.
- GATT rules will also be extended to provide enhanced protection for patents, copyrights, and trademarks (intellectual property).
- Barriers on trade in textiles will be significantly reduced over ten years.
- GATT rules will be much clearer and stronger.

- World Trade Organization will be created to implement the GATT agreement.

Following the conclusion of the Uruguay Round Negotiations, the interim GATT Secretariat was convened into a permanent WTO Secretariat with greatly strengthened trade policy review and dispute settlement mechanisms. It has also a new role to co-operate with the International Monetary Fund (IMF) and World Bank with a view to achieve greater coherence in global economic policy-making.

GATT/WTO rules to govern international trade for three major purposes (Anderson, 2001). First, WTO protect the welfare of small and weak nations against discriminatory trade policy actions of large and powerful nations. GATT Articles I (Most-Favoured-Nation) and III (national treatment) promise that all WTO members will be given the same conditions of access to a particular country's market as the MFN, and all foreign suppliers will be treated the same as domestic suppliers. These fairness rules are fundamental to instilling confidence in the world trading system.

Secondly, the tariff-binding rule will facilitate countries to prepare to become more interdependent and promote more investment. Article II, requires WTO members to limit trade only with tariffs and are obligated to continue to provide market access which is never less favourable than that agreed to in their tariff schedules.

The third purpose is to help government ward off domestic interest groups seeking special favours. This comes about partly via Article II, which outlaws the raising of bound tariffs, as well as via numerous benefit of the system such as to favour a special interest group at the expense of the rest of the economy (Petersmann, 1991).

Greater openness and interdependence between national economies provides opportunities and challenges for poorer economies. Globalisation rewards the nations that choice good economic governance as demonstrated by East Asia Crisis in late 1990s due to lost of economic confidence. Now financial capital can flow into well-managed economy more easily and quickly then before and can equally withdrawn if confidence in any economy's governance is shaken. The stability of the commitment to openness is crucial because capital inflows and investments will tend to be short-term in nature and susceptible to withdrawal should confidence waver (Anderson, 2001).

In response to the global economy condition, ASEAN (The Association of Southeast Asian Nations) launched the Asean Free Trade Area (AFTA) in January 1992 to establish a free trade area (PTA) by the revised target date of 2003 with tariffs on all commodities covered ranging between zero and five percent, and with all other trade restrictions eliminated. Agriculture raw materials/unprocessed products are excluded. In addition, AFTA will open the possibility of a freer flow of production and information among member countries in order to increase the chances of partnership and production linkages among firms of member countries. This is inline with the core idea of AFTA to facilitate intra-Asean free trade by removing all bottlenecks and impediments in the shortest time possible.

The formation of AFTA was inspired by numerous reasons such as the desire to remain a full participant in the global economy, the fear of investment diversion and desire to continue to attract FDI due to the increase competition for scarce global capital. De Simone (1995) identified another reason behind the creation of AFTA is the need to 'retaliate' for the formation of regional blocks such as NAFTA (North America Free Trade Area). This argument is strengthened by Bowles (1997) that the primary purpose of new regional trading block is the fear of developing countries was not of dependence on global economy but of being excluded from it.

ASEAN members are not only members of AFTA but also members of EAEC (East Asian Economic Caucus), of APEC (Asia-Pacific Economic Corporation) and of the Asian group of countries (ASEAN, China, Japan and South Korea). The existence of multiple regionalisms should be viewed as a concept of open regionalism. These regional trading agreements may seem to be steps on the road to a more open international trading system as different blocks themselves negotiate bilateral tariff reductions that lead to global freer trade. AFTA is important as a medium-term vehicle allowing ASEAN countries to participate in the negotiation process towards liberalised global trading.

IMPACTS ON BUSINESSES

Shall globalisation and open economy benefit all? Some quarters have expressed doubts and view global capitalism as a form of colonialism by the advanced and economically stronger nations (Sachs & Warner 1995). However, it is learnt from research that open economies have benefited far more than closed economies from economic growth and development (Sieh, 2000). According to Sachs & Warner (1995), they have found that countries that have recently reformed and liberalized their markets experienced accelerated growth.

Global changes in term of technologies and communications, physical mobility, and the trend towards greater economic freedom through WTO and other regional free trade agreements such as AFTA are the forces for firms to be more open to outside influences if they are to fulfil their primary economic functions and retain competitiveness. Corporate decisions on business strategies and the way of implementation tend to set directions of the development of globalisation because firms operate within the constraints imposed by the society and economic fabrics within which they exist (Veliyath & Zahra, 2000).

Nowadays a significant large number of business mergers and acquisitions are taking place for the purpose to remain competitive. Intense competition among companies and group is being felt and will become more severe in time to come. With this development, companies are expected to have altered their operational strategies that include innovative ways of managing production, technology, professional manpower resources, information and marketing. Indeed, globalisation offers new opportunities in a growing global economy as well as challenges and even threats. But the most obvious one is the heightened and aggressive competition.

Globalisation has made intra and inter-company relationship vital for businesses. In Malaysia such interconnection can be seen in electronics, textiles and apparel, and food companies (Sieh, 2000). Cost advantages with production sites in Asian region are one of the main reasons for initiating such relationships. The rising costs in Malaysia has encouraged local manufacturers to take advantage of nearby, lesser-developed Asian economies for lower production costs and as well as distribution centres. Indo-China, China and Indian subcontinent are some of countries that provide good access to other markets. The setting up plants abroad paves the way for Malaysian companies to engage in international division of labour.

With globalisation, most foreign companies in the food industry in Malaysia do not depend on their parent companies in home countries to supply raw materials due to cost factor. Instead, they purchase most of their inputs locally from competitive suppliers. Similarly, automobile and electronics manufacturers are gradually increasing procurement from local vendors (Sieh, 2000). Thus, Malaysian suppliers should improve themselves in all aspects to meet the demand and develop mutually beneficial ties with MNCs.

Continuous technology advancement is another requirement of assured future posed by globalisation. The technology innovation could improve work processes and accommodate horizontal workflows by providing cross-functional information flows, performance feedback and learning (Miner et al., 2001). A learning organization could be able to continuously improve the effectiveness of operations and enhance its competitiveness. In Malaysia, foreign investors are more willing to impart some of their technology to the local affiliates in a spirit of partnership (Sieh, 2000). The cost efficiencies generated through technological transfer will lead to a more dynamic, efficient and automated manufacturing system in Malaysia. The gains should be taken seriously by Malaysia entrepreneurs, which will lead to other possibilities of regional and global ventures.

Globalisation also encourages smaller production units and SMEs (small and medium enterprises) which having advantages of shorter inventory and order time and able to offer complementary competencies to larger business entities. MNCs in Malaysia may have to downsize and work closely with some SMEs which quality standards are met for customized production. As a result, Malaysian SMEs need to improve production efficiency by upgrading production technologies and distribution networks to grab business partnership opportunities with MNCs.

The process of trade liberalisation has resulted strategic alliances amongst parties involved in the manufacturing and distribution, which lead to sharing responsibilities among companies. It is becoming harder for any organizations to remain self-sufficient in a turbulent and changing environment that demand focus and flexibility (Crossan and Inkpen, 1995). Strategic alliances can come in many forms like ad-hoc

arrangements, joint venture and consortium. It can be used for variety of compelling reasons: to reduce costs in product development and new business opportunities, to reduce risks in expanding into new markets and new businesses, to enter and penetrate markets faster through collaborative research and product innovation, to build and maintain flexibility, and to neutralize competition by collaborating instead of competing with competitors (Yeoh, 1995). Some of these partnerships have also led to regional division of labour that enable companies to raise productivity, lower costs and reap competitive advantage. Strategic alliances will also open up for innovation from exchange of information, skills and experiences between business partners. A possible result with AFTA, ASEAN may gradually become less dependent to their counterparts from advanced economies.

To benefit fullest from globalisation, business operations may require adjustments. Best global practices need to be adopted such as a shift to higher-technology products and processes and international professional management systems and practices that based on up-to-date information technology and communication systems. Training of skill manpower needs more serious planning and execution than before because knowledgeable and skill workforce will be the key competitive weapon for the twenty first century. As a result, Malaysian companies may have to establish joint training programs with MNCs within the industry. In addition, procurement processes also need to be improved to face expanding global market with trade liberalisation under WTO.

Efficient supplier networking is another requirement for business to remain competitive in the globalisation era. The integration of the supplier into the organisational structure adds value to the organisation's customers. When customers and suppliers work together and form inter-organisational dynamic teams, it will facilitate improved communications and increase the rate of learning. Benefits will be gained from the effects of sharing mutual experience and knowledge, which will result in the whole chain becoming better, aligned with the final customer's requirements and objectives (Motwani & Ahuja, 2000). Fulfilling external customer satisfaction would lead to sustainable advantage over competitors and ensure of better market share in global economy.

CLOSURE

Open economy paved by the globalisation and growing regionalism and WTO rules is an inevitable phenomenon that requires adjustments and adaptation to survive in volatile and transitional environment. To entrepreneurs, they have to develop appropriate strategies to maintain an edge over competitors. Global economy also introduces new avenues to venture into and compete in new industries in global marketplace such as in ICT (information communication technology) industry. However, globalisation and changing global trading system are not without problems. To minimise the effect of undesirable consequences, adequate preparation, proper planning, and ability to act accordingly and timely would be needed.

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