

1. Political systems can be assessed according to two dimensions: the degree to which they emphasize collectivism as opposed to individualism and the degree to which they are democratic or totalitarian.
2. Collectivism is an ideology that views the needs of society as being more important than the needs of the individual. Collectivism translates into an advocacy for state intervention in economic activity and, in the case of communism, a totalitarian dictatorship.
3. Individualism is an ideology that is built on an emphasis of the primacy of the individual's freedoms in the political, economic, and cultural realms. Individualism translates into an advocacy for democratic ideals and free market economics.
4. Democracy and totalitarianism are at different ends of the political spectrum. In a representative democracy, citizens periodically elect individuals to represent them, and political freedoms are guaranteed by a constitution. In a totalitarian state, political power is monopolized by a party, group, or individual, and basic political freedoms are denied to citizens of the state.
5. There are three broad types of economic systems: a market economy, a command economy, and a mixed economy. In a market economy, prices are free of controls, and private ownership is predominant. In a command economy, prices are set by central planners, productive assets are owned by the state, and private ownership is forbidden. A mixed economy has elements of both a market economy and a command economy.
6. Differences in the structure of law between countries can have important implications for the practice of international business. The degree to which property rights are protected can vary dramatically from country to country, as can product safety and product liability legislation and the nature of contract law. Page 59

Critical Thinking and Discussion Questions

1. Free market economies stimulate greater economic growth, whereas state-directed economies stifle growth. Discuss.
2. A democratic political system is an essential condition for sustained economic progress. Discuss.
3. What is the relationship between corruption in a country (i.e., government officials taking bribes) and economic growth? Is corruption always bad?
4. You are the CEO of a company that has to choose between making a \$100 million investment in Russia or Poland. Both investments promise the same long-run return, so your choice is driven by risk considerations. Assess the various risks of doing business in each of these nations. Which investment would you favor and why?
5. Read the Management Focus “Did Walmart Violate the Foreign Corrupt Practices Act?” What is your opinion? If you think it did, what do you think the consequences will be for Walmart?



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Use the globalEDGE™ website (globaledge.msu.edu) to complete the following exercises:

1. The definition of words and political ideas can have different meanings in different contexts worldwide. In fact, the *Freedom in the World* survey published by Freedom House evaluates the state of political rights and civil liberties around the world. Provide a description of this survey and a ranking (in terms of “freedom”) of the world’s country leaders and laggards. What factors are taken into consideration in this survey?
2. As the chapter discusses, differences in political, economic, and legal systems have considerable impact on the benefits, costs, and risks of doing business in various countries. The World Bank’s “Doing Business Indicators” measure the extent of business regulations in countries around the world. Compare Brazil, Ghana, India, New Zealand, the United States, Sweden, and Turkey in terms of how easily contracts are enforced, how property can be registered, and how investors can be protected. Identify in which area you see the greatest variation from one country to the next.

CLOSING CASE

Transformation in Saudi Arabia

The desert kingdom of Saudi Arabia is a rarity in the modern world, an absolute monarchy whose laws are based upon interpretations of a religious text, the Qur’an, the holy book of Islam. Despite Saudi Arabia's adherence to an archaic

form of government, the Saudi economy has historically performed well, primarily due to the country's position as the world's largest oil exporter. In 2017, the country's GDP per capita on a purchasing power parity basis was \$54,500, not far behind the \$59,800 GDP per capita of the United States.

The oil sector accounts for around 87 percent of government revenues, 42 percent of GDP, and 90 percent of export earnings. In times of high oil prices, the Saudi government has used oil revenues to finance a sprawling government apparatus and to subsidize energy prices, which are among the lowest in the world. In 2014, however, oil prices collapsed, wiping out an annual government surplus. In 2014, the government deficit ballooned to 15 percent of GDP, and it hit 20 percent of GDP in 2016, forcing the country to issue more debt and draw down its foreign exchange reserves. Higher oil prices improved the situation in 2017 and 2018, but the crisis exposed the vulnerability of Saudi Arabia to a fall in oil prices.

To compound matters, Saudi Arabia has a young population—some 70 percent of the population is under the age of 30—and unemployment is high at 12 percent, a combination of factors that many see as a recipe for social unrest. The high unemployment reflects the fact that while there are jobs available outside of the government sector, most of them are taken by low-paid foreign workers, who account for 80 percent of the labor force.

Following the death of his brother, in January 2015 Salman bin Abd al-Aziz Al Saud became King. Breaking with tradition, the aging King quickly devolved substantial power to his son, crown prince Muhammad bin Salman Page 60 (commonly known as “MBS”). The young crown prince articulated a different vision for Saudi Arabia. Known as Vision 2030, this calls for reducing the kingdom's dependence on oil revenues, privatizing the state-owned oil company Saudi Aramco, cutting energy and water subsidies, growing the private sector, investing \$500 billion in a new city called NEOM that will serve as a hub for private and foreign investment, and introducing a value-added tax in order to close the government deficit. At the same time, the crown prince is seeking to loosen the stifling moral codes that have limited cultural life and to promote a “moderate Islam open to the world and all religions.”

Not surprisingly, this vision has met with resistance, particularly from members of the sprawling royal family and conservative clergy who have benefited from the status quo. To counter this, the crown prince consolidated his power, removing members of the royal family that disagreed with him and putting his allies in positions of power. This culminated in an unprecedented shake-up in November 2017 when scores of people, including some of the most powerful princes in the kingdom, were arrested in a massive anticorruption sweep and jailed in, of all places, Riyadh's opulent Ritz Carlton.

Whether this power grab will help the crown prince achieve his goals for Saudi Arabia remains to be seen. The government has had to backtrack on plans to reduce subsidies after strong resistance from the population, but it did introduce a 5 percent value-added tax in January 2018.

Plans for the privatization of Saudi Aramco are under way, and the government budget deficit has been cut in half since 2015—although stronger oil prices have had a lot to do with that. Some of the stricter laws have also been relaxed. Women are now allowed to drive, and some banned cultural entertainments once seen as decadent, including going to the cinema, are now allowed. In the long run though, transforming the Saudi economy will require growth in the non-oil private sector, and that is a challenging task.

Moreover, a scandal surrounding the murder of *Washington Post* journalist Jamal Khoshoggi by Saudi operatives in Turkey in October 2018 has at the very least potentially weakened the power of the crown prince. Khoshoggi, a Saudi citizen and U.S. resident, was a critic of the Saudi regime. Although the Saudi government has claimed that his killing was the result of a rogue operation gone wrong, few believe that narrative. Many critics suspect that Muhammad bin Salman was aware of plans to arrest Khoshoggi. Indeed, there is growing evidence that, back in 2017, MBS authorized a secret campaign to silence dissenters, which included the surveillance, kidnapping, detention, and torture of Saudi citizens. Khoshoggi was just the highest-profile case in that operation. In the wake of Khoshoggi's murder, some foreign investors have reconsidered their ties with the kingdom, and there is little doubt that the fallout from the scandal has made it more difficult for the Saudis to attract foreign investment.



Bandar Algaloud/Saudi Kingdom Council/Handout/Anadolu Agency/Getty Images

Sources: Asa Fitch, "Saudi Arabia Plans Record Spending in New Budget," *The Wall Street Journal*, December 19, 2017; Brittany De Lea, "Saudi Citizens Plagued by New Taxes, High Unemployment after Oil Price Collapse," *Fox Business*, October 26, 2017; "Saudi Arabia's Unprecedented Shake-up," *The Economist*, November 5, 2017; Mark Mazzetti and Ben Hubbard, "It Wasn't Just Khashoggi: A Saudi Prince's Brutal Drive to Crush Dissent," *The New York Times*, March 17, 2019.

Case Discussion Questions

1. What long-term economic and political problems does Saudi Arabia face?
2. How might the reforms proposed by Muhammad bin Salman potentially address these problems? Who will gain from these reforms? Who might object and push back against them?
3. Current plans for Saudi Aramco call for the state-owned oil company to be privatized. An initial public offering (IPO) is tentatively scheduled for 2021. What are the potential benefits to Saudi Arabia of privatizing Saudi Aramco? Is there a downside?
4. Is it morally correct for international businesses to invest in a country that denies basic rights to women?
5. Is it morally correct for international businesses to invest in an autocratic country where the current leader has been implicated in ordering the murder of one of his critics?

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Endnotes

1. As we shall see, there is not a strict one-to-one correspondence between political systems and economic systems. A. O. Hirschman, "The On-and-Off Again Connection between Political and Economic Progress," *American Economic Review* 84, no. 2 (1994), pp. 343–48.
2. For a discussion of the roots of collectivism and individualism, see H. W. Spiegel, *The Growth of Economic Thought* (Durham, NC: Duke University Press, 1991). A discussion of collectivism and individualism can be found in M. Friedman and R. Friedman, *Free to Choose* (London: Penguin Books, 1980).
3. For a classic summary of the tenets of Marxism, see A. Giddens, *Capitalism and Modern Social Theory* (Cambridge, UK: Cambridge University Press, 1971).
4. Smith, Adam. *The Wealth of Nations. The Modern Library*. Random House, Inc., 1937.
5. R. Wesson, *Modern Government—Democracy and Authoritarianism*, 2nd ed. (Englewood Cliffs, NJ: Prentice Hall, 1990).
6. For a detailed but accessible elaboration of this argument, see Friedman and Friedman, *Free to Choose*. Also see P. M. Romer, "The Origins of Endogenous Growth," *Journal of Economic Perspectives* 8, no. 1 (1994), pp. 2–32.
7. T. W. Lippman, *Understanding Islam* (New York: Meridian Books, 1995).
8. "Islam's Interest," *The Economist*, January 18, 1992, pp. 33–34.
9. M. El Qorchi, "Islamic Finance Gears Up," *Finance and Development*, December 2005, pp. 46–50; S. Timewell, "Islamic Finance—Virtual Concept to Critical Mass," *The Banker*, March 1, 2008, pp. 10–16; Lydia Yueh, "Islamic Finance Growing Fast, But Can It Be More Than a Niche Market?" *BBC News*, April 14, 2014.
10. This information can be found on the UN's treaty website at www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG.html.
11. International Court of Arbitration, www.iccwbo.org/index_court.asp.
12. D. North, *Institutions, Institutional Change, and Economic Performance* (Cambridge, UK: Cambridge University Press, 1991).