

Insights

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Although fifty years have passed since the inception of International Business as a field of research and teaching we are still plagued by doubts and questions. What is this field really about? Is it an extension of macroeconomics focusing on capital flows among countries? Is it an extension of International Trade theory? Or maybe International Business is an extension of the traditional fields of study in MBA programs like marketing, management, production, finance, and accounting. Is there a need for a separate and distinct theory of International Business, or is it just a collection of applications of existing theories, concepts, and management tools to a set of issues relating to operating a business in more than one country?

In a way this question has already been decided as is evident by the existence of AIB, JIBS, and *Insights*. Yet, the issue still haunts researchers, teachers, and Business Schools. Two of the articles published in this issue of *Insights* are a testimony that major and experienced researchers and teachers in the field of International Business are still asking themselves what is the nature of International Business. Robert Pearce focuses on economic theory as the basis for International Business in the tradition of Reading, MIT, Harvard, and others. He concludes that past and current research in International Business is sufficiently rich and focused so that there is no need to look for validation from other methodologies. Yet, maybe even this statement in itself shows that the need for validation is still there. Alan Rugman looks at the issue from a different, maybe opposing point of view. By asking the question whether there is a need for a separate International Business department, or that "everything in business is international" and therefore there is no need for a separate field and a separated department, Rugman is focusing on teaching whereas Pearce is focusing on research. Moreover, the contributors to the book edited by Rugman at Indiana University focus on organizational issues like building a department, developing faculty or organizing the whole Business School into Global Programs. Pearce focus is on ideas and how they can help in a better understanding of observable facts of the business world. In the practice of International Business in Business Schools we need both. The two articles prove that even today after almost fifty years of teaching and research in International Business the question of what is International Business is still unanswered.

The tradition of *Insights* established by BJ Punnett is to include in the issue not just articles but experiences as well. The short case by Moshe Banai falls into this category. It also serves as a reminder that beyond the ideas and the organizations of International Business we deal with people who have to negotiate the often difficult terrain of international Business.



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1st Quarter:	December 15
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- Articles should be approximately 2-3 printed pages.
- Exercises, simulations, and other material should include all the information needed for use in the classroom. Material submitted should not contravene any copyrights.
- Blunders should be based on real-world events and should be new - i.e., not previously published, or disseminated in other media.

*We look forward to your
comments and submissions.*

THE ECONOMIC THEORY OF THE MNE: A VIEW FROM READING.

There are three subtexts to this brief review of selected early approaches to theorising about the MNE. Firstly, that the value of these varied analytical strands is their essential concern to address economic *issues* (resource allocation, distribution, growth, development, environmental externalities, etc.) rather than to generate a single hermetic theory from conventional economic *techniques*. Thus, secondly, that each of these important steps come about to extend the ability of theory to explain observable aspects of ‘real world’ behaviour (rather than simplify such behaviour to make it amenable to mainstream theoretical constructs). Thirdly, that most of these steps involve (explicitly or implicitly) perceptions of MNE *strategy*, and that the way forward now is to bring current views of the MNE’s strategic nature to bear on economic issues.

I call this a ‘view from Reading’ partly, obviously, because of the core contributions made by Reading-based (or –associated) scholars, partly because the work done here (including allied work on technology and business history) has normally sought to address the type of agenda implied above, and partly because the other disparate approaches discussed can, indeed, be viewed as having valuable resonances and interfaces with what I see as Reading-style preoccupations. From these perspectives I would start this story with John Dunning’s classic 1958 book ‘American Investment in British Manufacturing Industry’. Though not formally setting up theoretical aims, Dunning’s book clearly does point forward analytically by basing its detailed investigation around individual foreign *firms*’ operations in UK (rather than address macro problems of FDI). The book immediately provides *practical* insights and challenges by observing behaviour patterns and raising issues that fuel formal analyses to come (indeed very promptly so in Hymer’s crucial PhD). I see it also as a *symbolic* pointer towards the works I advocate here, by providing a truly rich body of *knowledge* of the types that can drive subsequent investigations by challenging limitations in extant theories.

Despite its relatively slow initial percolation into informed analysis, we can now see Hymer’s (1960/1976) PhD as defining the agenda for economic thinking on MNEs. Vitally, for our themes here, he indicates the need for a new micro-level theory of MNEs (who implement the internationalisation of production/business) rather than macro-level theories of investment flows, *precisely because* available theories of FDI could not explain a number of relevant observed facts. Aspects of these observations also then drive the two strands of future theorising that are attributed origins in Hymer’s thought. Firstly, that firms often carried out *acts* of FDI without moving capital reflects their pos-

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session of those firm-level advantages (technology and other intangible assets, for example) that later provide the ownership advantage (OA) element of Dunning's eclectic framework. Secondly, that international operations are generally more prevalent in some industries than others indicates roots of MNEs in industry characteristics, with Hymer himself favouring industry concentration (and its implications within economic analysis) as the most influential.

Though not actively addressing the agenda derived from Hymer's work Vernon's (1966) product cycle model (PCM) provided insights that moved thinking forward in consonant directions. Though the predictive power of the fully-integrated PCM sequence was mostly short-lived, we can still see significant reflections of its separate elements in current thinking.

In its original articulation the first (innovation or product development) stage of the PCM addresses the issue of how *national* firms can become international. To do this it, in effect, discussed how US firms derived internationally-competitive capabilities (Dunning's OAs) from home-country creative inputs. Two factors underpinned this. Firstly, that the US was distinctively strong in relevant creative attributes. Second, that even where suitable technologies/ideas were available elsewhere US firms without operations on the ground there could not sense or operationalise them. The way that this has evolved in practice provides key strands of recent MNE-strategy literature. Now all well-developed

MNEs recognise distinct creative scopes in many of their host economies and are able to activate decentralised programmes of innovation, R&D, etc. within heterarchical global strategies.

In the second (mature product) stage Vernon sees firms responding to the *ad hoc* initial emergence of overseas markets by, eventually, implementing production in key markets. He suggests two explanations for this, both of which were later developed in significant ways. Firstly, in response to a nexus of cost factors, subsequently embodied in determinate optimising decision models. Secondly, as a more defensive, less determinate, response to potential local rival suppliers, thus anticipating the later testing of competitive oligopoly behaviour (Knickerbocker, 1973; Graham, 1978, etc.).

In the third (standardised product) stage Vernon foresees (remarkably precisely) another of the central strategic aims of modern MNEs, in the form of efficiency-seeking relocation of the production of cost-competitive parts (or stages) of supply to low-input-cost countries. Again a very precise form of location advantage (LA) conditions firms' evolution. Overall the second and third stages of the PCM presage how globally competing enterprise would come to encompass a strategic heterogeneity that could address different objectives in different countries at different times. The way in which these different strategic responses to potentials and problems have very different economic implications points towards the centrepiece of the analysis of Kojima (1978).

There has been a long-standing perception of a fundamental alienation of Kojima's methodology from that of the emphases of a 'Reading-style' approach (Buckley, 1985). This in particular reflects Kojima's desire to locate his FDI approach at the macro-level (within the practices of mainstream trade theory) and to assertively eschew use of firm-level strategic behaviour. I would argue that, within the compass of eclecticism, we can still usefully accept the core of Kojima's analysis in terms of his distinction between trade-creating and trade-destroying FDI. This distinction, and its derivation, fits well with both our concerns with economic issues and an interpretation of the concept of location advantage. Trade creating FDI generates improvements in efficiency and welfare because *MNEs* respond to positive LAs by relocating operations in a particular industry away from a country where the industry has become comparatively disadvantaged, into one where the local economy endows it with comparative advantage. Here response to positive LAs represents efficiency-seeking strategy of MNEs. Trade destroying FDI occurs where MNEs relocate (in a more market-seeking fashion) production into a particular country in order to defend its profitable supply of the country's market (but at a presumed lower level of efficiency), due to negative LAs in the form (usually) of restraints on trade. Another, less widely noted, element of Kojima's analysis, in the form of his distinction between orderly and disorderly technology transfer within FDI, also has resonances with economic issues (here balanced growth and

development) and with current concerns of MNE analysis (generation and application of technology).

Famously the application of internalisation (Buckley and Casson, 1976) to thinking about international business allowed the completion of the eclectic framework (Dunning, 1977) as an analytical construct. Thus with OAs providing the *ability* to compete internationally and LAs determining the *need* for their use in particular countries (to enhance efficiency and/or defend profitability) it remained to be explained why firms opted to own and control their OAs dispersed application (rather than sell or lease the right to use to another, usually local, enterprise).

Needless to say the above contextualisation does not define or exhaust the scope of internalisation in explaining the practicalities of IB (just as it only hinted at the available elaborations and positionings of the eclectic framework; e.g. Dunning, 2000). Logically there are as many cases of internalisation as there are intermediate goods, (intangibles, components, raw materials, etc). Thus the understanding of internalisation has been enriched both through formalised invocation of ideas from *inter alia* the theory of the firm (uncertainty, opportunism, asymmetrical information, switching costs, small numbers conditions, appropriability, and so on) and through the evidence of a range of detailed case study analyses.

Two broad contexts can indicate the much debated relationship between OAs and internalisation advantages (IAs) and, thereby, the variable geometry of the eclectic framework. In the case above 'outward internalisation' explains the hor-

izontally integrated MNE (as a firm which replicates core competitive activities in a number of separate market situations) through the failure to *create* an efficient external market for those unique attributes (OAs) that it already possesses and which essentially define its distinctive competitive capacity.

By contrast the 'inward internalisation' of the vertically integrated MNE sees the firm rejecting use of possible external markets for inputs to parts or stages of its production process, by expanding so as to remove independent suppliers and position them within an owned and controlled network (generating intra-firm, international intermediate goods trade). Where one firm responds to such exogenous imperfections of the market context, by internalising a particular intermediate supplier, other potential participants in that market could have done so (and logically may now suffer competitively from exclusion). Thus a full analysis needs to explain which firm implements the internalisation (or alternatively which of the two 'ends' of a distinctive and separable stage within a vertically integrated sequence 'takes over' the other). The firm-level difference may indeed be no more than the ability to detect, and evaluate as strategically influential, the relevant market imperfections. But it can also take the form of more substantive types of complementary OAs that can further enhance the distinctive competitive value of the integrated operation. Managerial capacities in realising the efficiency gains and synergistic creative potentials of coordinating an expanding differential network are likely to be crucial. Ultimately possession of endogenous firm-level competences (OAs) will determine the ability to

“Thus the understanding of internalisation has been enriched both through formalised invocation of ideas from inter alia the theory of the firm (uncertainty, opportunism, asymmetrical information, switching costs, small numbers conditions, appropriability, and so on) and through the evidence of a range of detailed case study analyses.”

secure the initially exogenous sources of IAs.

More zealous early advocates of the internalisation approach provided it with normative support by pointing to the innate efficiency gains of replacing a problematic market transaction by a more cost-effective hierarchical transfer. However, it is also innate to internalisation that it extends the firm's borders (geographical and/or functional) and often in ways that remove elements of competition. Such increases in market power questions the realisation of potential efficiency gains and generates concerns on the distribution of any benefits accruing.

These foundations have now supported a further quarter-century of elaboration, enrichment, diversification and disputation in building the distinctive body of knowledge

and analysis that now constitutes the study of international business (Pearce, 2004). A distinguishing feature of such theorising of MNEs (and concomitant analysis of their implications) is that it embodies variegated decision processes contingent on a range of different environmental conditions and strategic aims, rather than suggesting automatic and immutable responses to a limited number of very precise market signals.

In his recent memoir published in JIBS John Dunning (2002) records his vexation at "the reluctance of most mainstream international economists to embrace the activities of MNEs within their ambit of interest". It is indeed desperately sad to suffer the persisting hegemony¹ of a mode of analysis that is predominantly negligent of the true nature of the key players in

its environment. For IB economists, however, this need only be a frustration and not a problem.

If we accept that the crucial challenge facing anyone concerned with understanding economics in an international context is currently the processes and implications of globalisation, in terms of a categorical intensification of competition across borders, then it is surely unavoidable to understand the MNE as the central agent in these developments. The body of knowledge and analytical procedures now in the possession of AIB members is sufficiently rich and decisively focused on this that we should no longer require the validation or mediation of antecedent methodologies.

End Note

¹ On the day I finished this piece I looked at the new edition of a (presumably successful) International Economics textbook. In 500+ pages four covered FDI and three the MNE. Of the authors cited by name here only Dunning (worth one footnote) and Vernon (because the PCM is a new trade theory) are mentioned in the textbook.

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THE INFUSION MODEL OF INTERNATIONAL BUSINESS EDUCATION AND RESEARCH

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International Business (IB) education and research became institutionalized in leading U.S. business schools in the 1960s. The Academy of International Business was founded by a group of IB teachers in 1958, and the *Journal of International Business Studies* was launched in 1969. The founding members of the AIB and *JIBS* came from a small set of U.S. business schools, most notably Columbia, N.Y.U., Michigan, and Pennsylvania. Yet the most influential business school at the time and one of the first to develop a full IB department was Indiana University (IU). In a new book, Rugman (2003), the leadership of IU in the developments of the field of IB is recorded and assessed, including a paper by the first chair of the IB Department, Stefan H. Robock. In other parts of the book, the influence of IU on the major associated IB fields of research and teaching (finance, marketing, and management) is assessed, and recent research themes in these fields are explored.

The book develops several overlapping themes:

- the process of internationalization within major Business Schools—the IU experience as a leader in comparison to others,
- the current state of knowledge about IB research, and
- new issues in IB research.

Underlying these themes is a fundamental question pertinent to today's approach to internationalization in top business schools: As IB has become the accepted norm in business today and therefore no longer the provenance of exclusive "IB departments" only, to what extent has it been effectively "infused" in key functional areas of traditional business education—marketing, finance, management, accounting, etc? Despite high hopes that the infusion model would work across all business schools, not only in the United States, but worldwide, this has not always been the case. Often IB is "diffused" where there is no longer a champion to foster the subject. In this context, IU may well be representative as well as a pioneer.

In Rugman (2003) Professor Robock vividly describes the early years of the IB field: making the institutional commitment to IB; defining the parameters of the field; identifying key issues to be addressed through

research; and developing the faculty, the literature, and the curricula necessary for its delivery. Jeff Arpan, a distinguished IU/IB doctoral alumnus and past president of the AIB, describes IU's role in educating a generation of faculty leaders in the field, particularly throughout the 1970s. And John Daniels, another past president of the AIB who played a significant role in the maturation of IB at IU in the 1980s and 1990s, discusses his own perspective on internationalizing the broad range of functional areas. He is pessimistic about the success of infusion at IU and elsewhere, although there have been some success stories, particularly in doctoral education.

The contributors to Rugman (2003) conclude that IU was both a pioneer in building an early IB Department, helping to shape the development of the field generally and, later, fully implementing the infusion model. There are, however, divergent views on the success of infusion, both at IU and elsewhere, as discussed by David Ricks, Carol Howard, Laurence Booth, and Richard Wright, among others. Yet, in an up-to-date perspective, Louise Siffin, IU's Global Programs Director, argues that infusion has been achieved in the MBA and undergraduate programs at IU and, to a large extent, also in the research activities of faculty. Today a "network" of IB activities exists. In this sense, IU is again leading the way in implementing the internationalization process at leading business schools.

In terms of research we can note a parallel development of IB teaching about organizations and structures with the development of the IB field. Today the dominant role of the U.S. multinationals in the 1960s has been replaced by regional/triad business and two-way trade and investment. Issues in global, regional and subnational strategy are now relevant, not just from a business economics perspective but requiring a "multiple perspectives" approach across the disciplines of finance, marketing, management, etc. So, in addition to infusion of IB into the key disciplines, it is likely today that IB itself has been reformulated by relevant insights from the disciplines. One thinks of knowledge, learning and networks as relevant contributions from management which have deepened analysis of multinational enterprises beyond the earlier assumption of centralized hierarchies. Such work places the earlier historical discussion of IB in context and illustrate how mature and wide-ranging the field of IB has become over the last fifty years.

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Alan M. Rugman (Ed.) *Leadership in International Business Education and Research: Research in Global Strategic Management* Vol. 8. Elsevier/JAI Press, 2003.

BUSINESS ETHICS IN RUSSIA: NATASHA'S CHOICE*

** Some information in this case has been altered to protect people's identity.*

Natasha is a new Russian entrepreneur. For the last three years she has been running her own wholesale stationary business in the town of Perm, in Tatarstan, Russia. Tatarstan is a Russian state with about 3.25 million inhabitants of whom half are Tatars and therefore Muslims, and the other half are Russian and therefore Orthodox Christians. The two groups have lived peacefully together for the last four hundred and fifty years, married each other to the extent that many people cannot define themselves as Russians or as Tatars anymore.

Natasha's company imports various stationary items from Korea and from Finland and sales it to local schools, shops, and bodegas. The company consists of five people: Natasha who is doing the procurement, her partner Guzel who is in charge of marketing and sales, an office clerk, a bookkeeper, and a driver. The company's monthly turnover is \$200,000 of which about 30% is in revenue. Natasha pays her suppliers in advance and she pays her workers fairly. Her federal, state, and city taxes amount to about 35% of the profit. She invests the rest of the money in the company's growth and keeps very little in saving for herself and her old mother with whom she shares a two bedrooms apartment in a suburb of the city. Her life ambition is to save enough money to build a house in the suburb for herself and her mother. She wants her mother to have comfortable life during her retirement age.

Natasha was a student at the local university when the 1991 peaceful revolution took place in the Soviet Union. She has completed her studies successfully in Mathematics and Engineering, hoping to join one of the research departments of the local military complex. Her mother was a dedicated member of the Communist party and as such Natasha's way into a research function was paved. However, the changes that took place in Russia at the time made many of the factories in her area redundant and it was impossible for her to pursue her dream of becoming a researcher.

She joined the military complex as an engineer trying to convert this mammoth into a civil factory but her plan was shuttered again when the factory closed its doors in 1993 and all the workers found themselves unemployed. However, during her two years work for the military complex she had met Nail, an entrepreneur who was dealing with that factory, buying and selling Polyethylene and its products.

M O S H E B A N A I

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Anil was an engineer in a chemical complex. He had decided to exploit the available government loans and to go on his own – establishing a private business. With a partner, he had leased a vacant building from the chemical company within the security wall that guarded the company, thereby, securing his new factory. He secured a loan from a bank and purchased a few plastic injection machines. The raw plastic was provided by the chemical complex and was used to produce plastic bags and other simple plastic products such as tablecloths and decorative plastic panels. There was a high demand for the factory's products and Nail recruited about 80 workers to man the production line over two daily shifts.

Since Nail did not speak English he needed Natasha as a translator to communicate with foreign suppliers of machinery and with potential buyers. He offered her this very sensitive job and she got involved in the in-and-out of the company, accessing most of the confidential information that was available only to the company's owner and his partner. After a couple of years Nail trusted Natasha to the extent that he decided to assign her as the Director of Human Resources. Natasha learned a lot about business management and worked happily for Nail and his partner till Nail was assassinated while getting ready to drive from home to the factory on one of the first mornings of the spring of 1997.

Nail's partner took over and became the CEO of the company. Not only that he did not trust Natasha but also at one point in time he sexually abused her. She decided to quit the company and to look for another job. Luckily enough she was introduced to an US citizen of a Korean origin who was building a large restaurant in the center of the city in partnership with the city's government. She was in charge of translating the details of the deal to the government's officials who did not speak English. While working for this enterprise she had established good contacts with Korean suppliers of various office stationary and supplies. The cooperation between the US investor and the government went array and he had to leave town and his investment behind.

Natasha found herself out of a job again. She decided that this was her opportunity to use all the knowledge that she had accumulated and to establish her own private business. She has found a woman partner and together they have gathered all their personal assets, rented a small office, and ordered the first shipment of stationary from Korea. They found a good market niche and their success was immediate.

A few months after they started the company two men appeared in their office. They asked to speak with the owners and Natasha, assuming that they were potential customers, invited them in. They presented themselves only by their first names and suggested to Natasha that "it was not good for two women to work alone" and that Natasha and Guzel needed partners to secure their business. They said that the competition may drive their rival to try and sabotage the stationary business and therefore they made an offer that the two women 'could not refuse' - to protect the business for a service charge of 30% of the profit. In the absence of alternatives the two women treated their new partners as "their charity". Despite the heavy unexpected added 'tax', the two

women were doing well and the business grew up, with more and more satisfied customers buying from them every month.

A year ago, Natasha has discovered that her bookkeeper, also a woman, had stole \$6000.00 from the company's coffer. Natasha had fired the bookkeeper immediately and asked her to return the stolen money. The bookkeeper said that she did not have that amount of money and that she could not repay the debt. Natasha knew that if she would decide to take her client to court she might never see her money again. Any business dispute brought to court requires the companies to expose their business financing and thereby attract the tax police that have a reputation for being unjustifiably hard on business. Natasha excluded this option and decided to call "her charity men" to collect the debt for her.

Natasha was surprised with the speed that the "charity organization" came back to her. The two men told her that the mother of the ex-bookkeeper, who did not want to pay her debt, lived in her own apartment in the city. They suggested that they should force the old lady out of her home to go to live with her daughter. Then they would sell the apartment and split the cash in such a way that Natasha would collect her debt and they would collect their 30% "mediating fees."

Natasha does not know what to do. If she gives the green light to the "charity men" to execute their plan she knows she would feel guilty about her decision to the rest of her life. After all it has been her life ambition to make sure her own mother lives comfortably in her late days. If she goes to court she may lose twice: Once, the court's decision may take a long time to sort out during which the tax police may raid her business and probably make her pay large sums of money. Second, the 'charity' men might get very upset since they may lose some potential money that they hoped to collect as 'mediators.' Moreover, they may execute their plan anyway and regardless of her objection, taking the money for them and leaving Natasha with a bad reputation and with no money. If she decides to write the debt off as a bad loan she may hamper her reputation as a tough businesswoman and more potential (mostly men) bad debtor may take advantage of her weakness and stop paying her on time or stop paying her at all.

What is Natasha to do?

This real case demonstrates the complexity of the application of western management style and ethics to other societies such as Russia where the value systems is different from that applied in the USA. It also delineates the possible conflict between personal ethics and business survival, and the difficulties faced by US companies embarking on business in Russia. Most US cases present ethical dilemmas between two or more alternative actions within a western value system. This case presents the western decision maker with a dilemma in a foreign culture where the local value system challenges the western manager's value system. The case is a good indicator of what should foreign investors expect in Russia. It sheds a dark light over the future of Russian business and the Russian economy in general.

