MULTINATIONAL ENTERPRISES AND TERRORISM

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MULTINATIONAL ENTERPRISES AND TERRORISM

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CONTENTS

LIST OF TABLES

LIST OF FIGURES

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PREFACE

International business was the second casualty of 9/11 terrorist incident; the first was, of course, nearly 3,000 people who lost their lives on that sad day. The birth of global terrorism brought about palpable perils for businesses around the world. The multinational enterprises felt the jolts of the massive magnitude of this risk. The most important question for the MNEs was how to manage this risk to save huge investments and to avoid falls in revenues.

Albeit one can find considerable research on MNEs' business in emerging markets, little attention has been paid on the impact of terrorism on MNEs operating in emerging markets and how established MNEs should befittingly respond to this situation. Emerging markets are favorite destinations of large MNEs because of greater opportunities of better profitability there when compared to the developed markets, which are believed to have reached the saturation point. A large number of American and Western MNEs are operating in EMs for last many decades, and many more aspire to reap high dividends from these markets. But terrorism is one big uncertainty and risk that can have significant impacts on their businesses. The research on this issue has been scant and limited.

We aimed at discerning the impacts of terrorism on MNEs in emerging markets to foresee and forestall threats to their operations by formulating appropriate strategies. It strived to explore how direct and indirect impacts of terrorism pose serious operational and management challenges to the MNEs operating in EMs and how MNEs modify their strategies and structures to handle them. We carried out extensive research and explored the literature pertaining to it.

After identifying the gap in the literature, we conducted case studies of four established MNEs operating in the two EMs afflicted with terrorism. Pakistan and Turkey, being large EMs facing acute terrorism, were selected for the case studies. The managers of these MNEs and relevant governmental officials were interviewed for this purpose.

Terrorism is a glaring peculiarity in EMs, which has not been profoundly researched, specifically focusing on the role of the MNEs operating there. Institutional theory enabled us to explore and explain the approaches of MNEs embedded in country-specific institutional arrangements of the EMs that have a peculiar social system accentuated with prolonged existence of terrorism. It provided rich theoretical foundation for examining a wide range of critical issues and also allowed for theorizing at multiple levels of analysis, which was essential for MNE research (Djelic & Quack, 2003). It helped understand how MNEs responded to the institutional pressures caused by terrorism and why they adopted particular systems in particular emerging markets. We have been able to develop the scope of institutional theory by employing it to understand the impacts of terrorism, a phenomenon which is surreptitious in nature and remains elusive but creates upheaval in the system.

It has further developed the theory by considering terrorism as a distinctive political risk which creates distinct institutional factors requiring adjustments of strategies accordingly. The analysis of case studies depicted that, in such an environment, out of the three pillars of institutional factors, regulative factor gains more strength than normative and cognitive. Deliberate and sustained efforts of the MNEs to maintain good relations with the host governments and their diligent adherence to laws of the land confirmed this standpoint.

The study confirmed that the MNEs operating in EMs afflicted with terrorism thrived and continued their business which highlights a new and positive relationship between institutional uncertainty and entrepreneurship in EMs. Furthermore, this finding has abolished the myth that firms hesitate to operate in the countries with institutional distance or institutional uncertainty between them. Where there is a profit, there is a way. MNEs make strategic adjustments to cope well with formal and informal institutions to overcome the uncertainties.

The study will contribute toward deeper understanding of the impacts of terrorism on MNEs and will demonstrate how MNEs can respond to these impacts to continue successful operations. The management of these MNEs has to address multiple aspects of such threats. To begin with, the management must have deep and wide knowledge and understanding of the terrorist threats and the environment they operate in. The corporate manager must apprise the top management of the lethality of direct and indirect impacts of terrorism which can affect the employees, supply chain, customers, and even production.

The study proves that the managers of MNEs usually consider the indirect threat as more worrisome aspect because these are beyond control of the firm. But at times, the direct threat can be more damaging to the security and morale of the employees. For example, if extortion and kidnappings for ransom are rampant, the company cannot consider its employees, especially the top managers, safe.

At times, the top managers of MNE do not consider their firm as the direct target of terrorists; therefore, adequate security measures are not adopted. The studies show that in an environment of widespread terrorism, any firm can become a target, with or without a warning from the terrorists. The security manager ought to make arrangements at par with the security arrangements of a company directly under threat.

This book provides a unique understanding of the strategies and management of the MNEs operating in a challenging environment where terrorism upsets all systems, processes, and regulations. The prospective investors, the top management of the MNEs already operating in such places, and, to top all, the corporate security managers can greatly benefit from the scenarios, strategies, and solutions offered in this book.

Naveed Elahi and Pervez N. Ghauri

ABSTRACT

Terrorism exerts negative impacts on international business and multinational enterprises (MNEs). Emerging markets (EM), though fraught with terrorism-related perils, offer greater opportunities of profits to the MNEs than in the developed markets, which are believed to have reached the saturation point. The significance of this research is accentuated by the fact that despite perils, EMs are attractive destinations for MNEs. Therefore, it is imperative to discern the impacts of terrorism on MNEs in EMs to foresee and forestall threats to their operations by formulating appropriate strategies.

The purpose of this research is to explore how direct and indirect impacts of terrorism pose serious operational and management challenges to the MNEs operating in EMs and how MNEs modify their strategies and structures to handle them. Albeit one can find considerable research on MNEs' business in EMs, little attention has been paid on the impact of terrorism on MNEs operating in EMs and how established MNEs should befittingly respond to this situation. Literature review, carried out for this study, based on more than 130 research papers published in top-tier journals, indicates clear dearth of research on this topic.

This research intends to fill this gap by carrying out case studies of four established MNEs operating in the two EMs afflicted with terrorism. Pakistan and Turkey, being large EMs facing acute terrorist incidents, have been selected for the case studies. The managers of these MNEs and relevant governmental officials were interviewed for this purpose. Prior to it, a pilot case study was carried out to test the research questions and to remove distortions in interview questions and their understanding.

The study will contribute toward deeper understanding of impacts of terrorism on MNEs and will demonstrate how MNEs respond to these impacts to continue successful operations in the EMs.

Keywords: Terrorism; terrorism and management; multinational enterprises; emerging markets; terrorism and strategies; security and policy makers

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CHAPTER 1

INTRODUCTION

Emerging markets (EMs) have become increasingly favorite destinations of multinational enterprises (MNEs) (Enderwick, 2008; IMF, 2017[1]; London & Hart, 2004; Ruddick, 2014) because the cumulative gross domestic product (GDP) of EMs is estimated to climb around 2 percentage points higher than that of developed economies in the coming years. These markets are likely to account for around $20 trillion consumer spending, 40% of the total spending, by 2020 (Lang et al., 2018). EMs grew by 4.3% in 2017, compared with 3.7% in 2016. Global growth has been predicted to remain at around 3% in 2018–2019, while EMs' growth was predicted to reach 4.5% in 2018 and 4.7% in 2019 (Casanova & Miroux, 2018).

Although there are enormous opportunities in these markets, they are full of difficulties and drawbacks (Pinkasovitch, 2018; Zhang, 2008). Terrorism is one such drawback, which has become top concern for MNEs operating in such markets, because of its potential to undermine their business. We aim to ascertain how the MNEs operating in the EMs, afflicted with terrorism, handle the impacts of terrorism.

1.1. SIGNIFICANCE OF EMs

EMs are endowed with majority of the world's people (about six billion) and land and faster growth than the developed world (IMF, 2016[2]; London & Hart, 2004). In year 2013, the emerging economies accounted for more than half of world GDP on the basis of purchasing power. This exceptional growth is considered a significant economic transformation in modern history (IMF, 2013). Occasional dips apart, EMs continued to grow at a greater pace than the advanced countries. Growth in EMs was projected to strengthen to 4.5% in 2018 and 4.7% in 2019 when compared with 2.2% in advanced economies.[3] The MNEs from the US and other developed Western countries expanded in the EMs at a great speed and scale, which is evident from the fact that till 2008, emerging economies boasted 70 companies in the Fortune Global 500 list of the world's biggest companies, up

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Table 1.1. Comparison of Developed Markets and EMs.

S. No.	Developed Markets	Emerging Markets
1.	Saturated	Opportunities galore Vast land mass and majority of world population
2.	Slow growth	Fast growth
3.	GDP is shrinking	Half of world GDP on the basis of purchasing power
4.	Foreign exchange reserves – less than EMs	Have taken over the developed markets
5.	Little increase in consumption	Consumption will be more than double by 2025
6.	Costs are higher. Infrastructure and regulations are already developed	Costs are going down as more investment in infrastructure development, especially in transportation, power, and communication, is taking place

Source: Based on the information given in the paragraphs above and below.

from just 20 a decade ago (Accenture, 2008). This number had been rising in the subsequent years. About 132 largest companies of the world had established their headquarters in EMs till 2014, up from 21 in 2000.[4]

A brief comparison of conspicuous aspects and characteristics of the EMs and developed markets, gleaned from the sources used in this research, mentioned in Table 1.1, highlights the growing significance of EMs, which makes them a favorite destination of MNEs.

According to IMF Report (2013), from 2003 to 2011, the share of world output provided by the emerging economies grew at more than a percentage point a year. After a mild dip during 2014–2015, they regained momentum in 2016. According to IMF Report (2018), growth in EMs and developing economies was expected to remain steady at 4.7% in 2018–2019 and to rise modestly over the medium term.[5]

The trend of the contribution of emerging economies to the world output is given in Fig. 1.1.

Fig. 1.2 shows that the share of world GDP of the developed economies is gradually shrinking whereas of EMs in Asia and Europe is fast expanding. It is increasing in Pakistan as well.

Similarly, Fig. 1.3 shows that the foreign exchange reserves in EMs are increasing at a greater rate than in the developed markets.

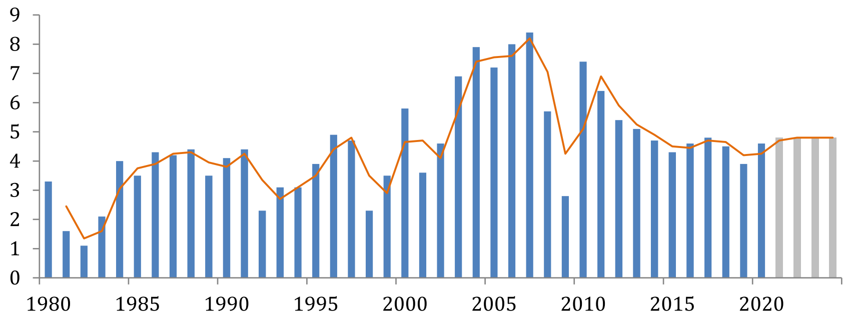

Fig. 1.1. Emerging Market Share of World GDP. *Source*: Based on data from IMF Data Mapper, World Economic Outlook (April 2019).

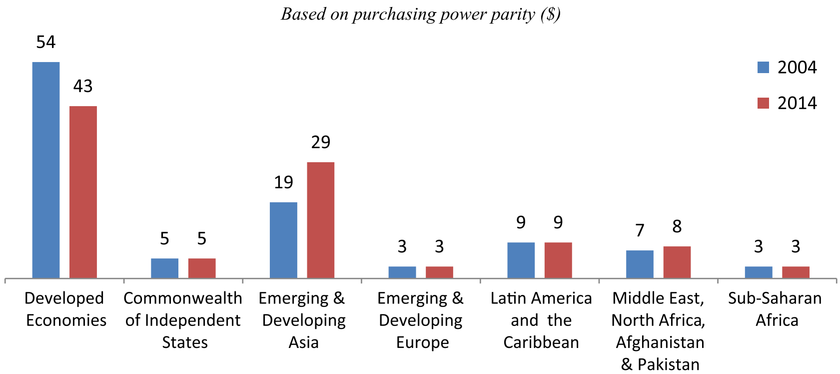

Fig. 1.2. Share of World GDP 2004–2014. *Source*: Based on data gleaned from IMF Report (2018).[6]

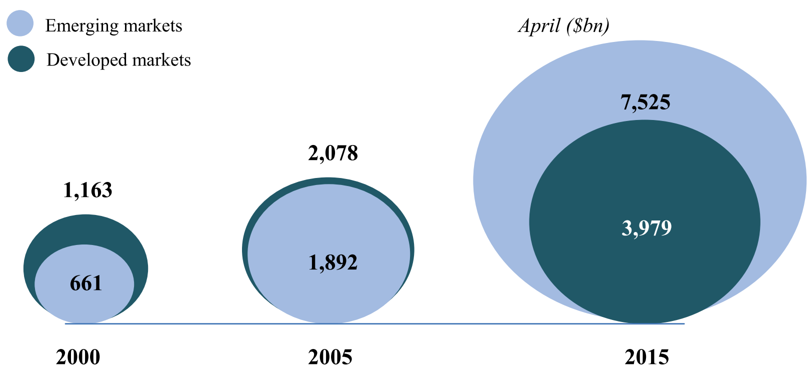

Fig. 1.3. Foreign Exchange Reserves – Developed Markets and EMs. *Source*: Thomson Reuters DataStream (2018).[7]

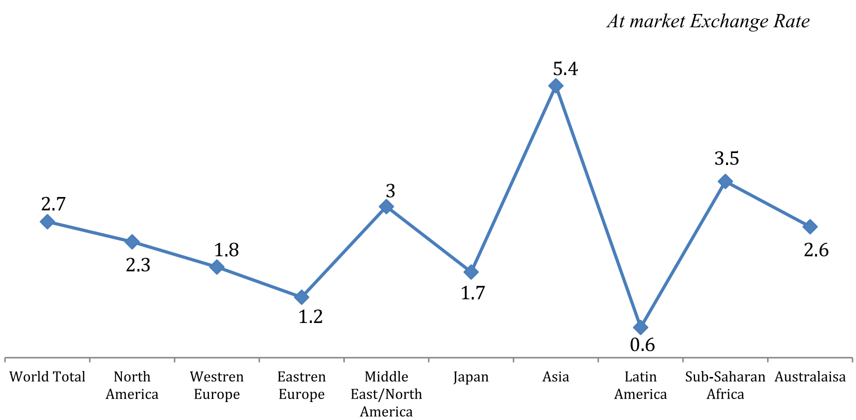

Fig. 1.4. World GDP. *Source*: Based on information gleaned from Economist Intelligent Unit (2018).[8]

Fig. 1.4 further supports the estimates of Fig. 1.3 that the rate of world GDP increase is 0%–2% in developed countries, 2%–4% in North America, North Africa and Middle East, and 4% in Asia. This indicates a remarkable growth in EMs.

The dip in growth of EMs is linked with global growth trend which remained downward from 2013 onward. According to IMF World Economic Outlook (WEO), the global growth was in low gear in 2013, weaker-than-expected in 2014, and 0.3% lower in 2015. However, as per IMF WEO Report (2016), the global growth was projected at 3.4% in 2016 and 3.6% in 2017. According to IMF Report (2017), EMs and developing economies accounted for almost 80% of the global economic growth, two times more their share 20 years ago.[9] Axiomatically, the conditions augur well for the EMs.

EMs emerged more than three decades ago, and 30 years down the lane, they are still considered to be emerging. EMs having enormous size, where over 80% of the world population resides in about three quarters of the world's land mass, showing rapid and constant growth, deserve a more appropriate nickname now, like rapid growth markets, which may sound more encouraging and befitting.

Coupled with natural endowment of size, several emerging economies are investing in infrastructure development, especially in innovation, transportation, power, and communication, which has helped bring down the costs of selling in EMs (Cavusgil, Knight, & Riesenberger, 2013; Rao-Nicholson, Vorley, & Khan, 2017). Many EMs have developed or accessed technologies that have made them competitive on a global basis. Indubitably, some EMs have highly differentiated structures, the demand forecast has become easier, with professional consulting and advertising organizations established in most of these markets. To cap it all, liberal policies of the governments in emerging economies, providing full support for foreign investment, have made the process of reaching business agreements much more convenient.

By continuing to develop their economic and social infrastructures, institutions and markets, and by investing in their people's education, EMs are expected to grow further, to consolidate their economic and business power, and to exceed the GDP of the developed countries within two decades (Griffith, Cavusgil, & Xu, 2008; Oliver Wyman Report, 2019[10]). Large MNEs are well aware of these facts; therefore, majority of international businesses (IBs) include the EMs into their strategic decision making (Enderwick, 2009; UNCTAD Annual Report, 2007). Furthermore, emerging economies have unique capabilities and strategies in advanced technologies which is also a source of attraction for foreign direct investment (FDI) by MNEs (He, Khan, & Shenkar, 2017).

There is a realization in the MNEs that the global consumer base is on the rise, with EMs playing a significant role in that growth. As depicted in Fig. 1.5, management consultant McKinsey estimates that EM consumption will reach $30 trillion, roughly half of all global spending. For almost two decades, a growing number of MNEs have recognized and explored the enormous business opportunity at the base of the economic pyramid (Hart & Milstein, 1999; London & Hart, 2004).

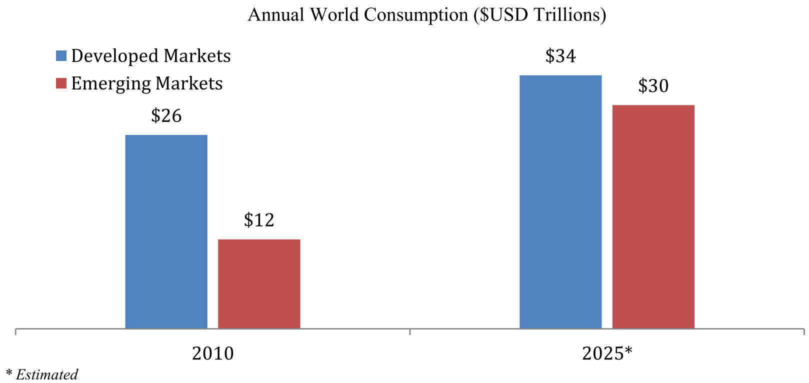

Fig. 1.5. Emerging Market Consumption. *Source*: Based on information gleaned from Angus Maddison, Groningen Growth and Development Centre, University of Groningen; Homi Kharas; Wolfenson Center for Development at Brookings Institution; McKinsey. Retrieved from https://www.thecapitalgroup.com/capitalideas/article/global-companies-emerging-markets.html. Accessed on November 1, 2016.

1.2. TERRORISM, EMs, AND MNEs

Despite several positive indicators, EMs are characterized with some peculiarities, many of which could be considered risks for MNEs to operate there. The most notable among these risks are loss of control over ownership or loss of benefits of enterprise by government action; constraints imposed at the specific industry or specific firm level; riots; expropriation, restrictions on remittance of profits, discriminatory taxation, and public-sector competition; and discontinuities, which are difficult to anticipate, occur in the business environment as a result of political change, etc. (Fitzpatrick, 1983).

Terrorism tops among such risks, and its impacts are not restricted to EMs only. After 9/11 terrorist attacks in New York, it has become a global phenomenon. Since then, risk related to terrorism became more widespread as there had been a meteoric rise in terrorism, with an almost fivefold increase in fatalities since then (GTI, 2014; Mazzarella, 2005). Later studies show that global terrorist attacks increased by 80% in 2014, and the death toll from terrorist activity increased ninefold since the year 2000 (GTI, 2015).

Cofer Black, the former Head of the CIA Counterterrorism Center, said, "There was a before 9/11, and there is an after 9/11." Condoleezza Rice, former National Security Advisor to the US President Bush, 2001–2004, stated, "The world has changed so much that it is hard to remember what our lives were like before that day."

After this incident, the valuations of many MNEs declined by more than 10%. The expected cash flows of MNEs were reduced, even when they were not directly hit (Madura, 2013). Terrorism emerged as a major risk to IB as it causes losses in FDI, damaged infrastructure, output losses, security costs, reduced economic growth, reduced tourism, trade losses, and higher insurance premiums (Keefer & Loayza, 2008). This substantial strain on the global economy caused by terrorism is a matter of concern for the truly internationally focused manager. Many high-ranking international executives considered terrorism second only to double-digit inflation as a threat to their IBs (Mazzarella, 2005).

With every passing day, the lethality and complexity of terrorism increased. The birth of terrorist organization, so-called Islamic State, also called ISIS, ISIL, and Daesh, in Iraq and its swift spillover in Middle East, Asia, and even Europe gave further boost to international terrorism. Over years, terrorism became more pronounced and actually turned more lethal in some EMs because of their limited capacities to bridle it. This state of affairs causes a

Table 1.2. Effects of Terrorism.

S. No.	Countries	Domestic Terrorism Incidents	Transnational Terrorism Incidents	FDI (% of GDP)	Aid (% of GDP)
1	Algeria	27.17	2.93	0.76	0.6
2	Angola	*	1.74	6.57	3.32
3	Argentina	10.31	5.79	1.48	0.06
4	Bangladesh	10.67	*	0.28	4.35
5	Brazil	*	1.88	1.64	0.07
6	Cambodia	*	1.79	5.41	11.49
7	Chile	42.38	5.67	4.03	0.19
8	Colombia	101.31	23.1	1.88	0.45
9	Ecuador	*	1.38	1.17	0.73
10	Egypt	10.21	*	2.55	5.7
11	El Salvador	72.31	6.33	1.95	2.52
12	Ethiopia	*	1.52	1.95	10.16
13	Guatemala	24.6	7.74	1.43	1.39
14	Honduras	*	2.07	2.52	6.17
15	India	92.33	8.1	0.62	0.65
16	Indonesia	*	1.38	0.76	1.34
17	Iran	8.76	2.86	0.52	0.08
18	Israel	24.95	2.1	1.74	3.48
19	Lebanon	12.69	14.52	11.58	2.47
20	Mexico	*	3.26	1.79	0.06
21	Nicaragua	17.98	2.66	2.41	11.37
22	Nigeria	*	2	2.71	0.84
23	Pakistan	61.17	7.1	0.79	2.81
24	Peru	110.57	8.79	1.92	0.91
25	Philippines	40.26	8.05	1.06	1.22
26	South Africa	32.34	*	0.76	0.32
27	Sri Lanka	32.36	2.9	0.88	4.96
28	Sudan	*	1.52	2.61	4.6
29	Thailand	22.17	1.43	2.12	0.59
30	Turkey	40.55	6.5	0.72	0.37
31	Venezuela	*	1.9	1	0.04
32	Yemen	*	1.67	1.37	3.52
Average, 122 countries		7.51	1.38	2.9	6.74

Source: Bandyopadhyay, Sandler, and Younas (2015).
Note: Most countries with more than average terrorist incidents have lower FDI and foreign aid.
* indicates that the number of terrorist incidents was below the average of the 122 developing economies in the total sample.

massive decrease in a country's net stock of FDI and inflicts significant damage on its economy (Abadie & Gardeazabal, 2008). Generally, a higher frequency of terrorism could deter potential investors to invest in a terrorism-infested area (Bandyopadhyay & Younas, 2014). Table 1.2 shows domestic and transnational terrorism incidences in different countries in comparison with percentage of FDI and foreign aid.

The linkage between domestic terrorism incident index and FDI of Pakistan and Turkey can be taken as a litmus test, which confirms the relationship between the two. Nevertheless, despite risks and challenges, MNEs had been spreading their operations in EMs as they could make good profits there. MNEs use international expansion as a springboard to acquire strategic resources, diversification, access to talent, competitive advantage, and to reduce their institutional and market constraints at home (Luo & Tung, 2007; Van Rossum, 2017).

Earlier research reveals that the managements of MNEs usually tend to play down the impacts of terrorism on MNEs and fail to understand the complexity of direct and indirect impacts on businesses (Czinkota, Knight, Liesch, & Steen, 2010). Although many MNEs have been aware of terrorist threats since 1980s and had devised counterterror plans for their operations abroad (Mazzarella, 2005), the real understanding of the post-9/11 form and nature of terrorism has been overlooked, and attempts to formulate effective strategies to ward off the impacts of terrorism have been below the mark. According to an estimate, only 18% managers said anti-terrorism expenditures were seriously considered in their firm (Czinkota et al., 2010). In the same survey, while nearly 50% of firms were concerned about the effects of terrorism or threats of terrorism, only a quarter had prepared a terrorism contingency plan. Only 12% said shareholders reward corporate efforts to prepare for terrorist threats.

1.3. WHY THIS STUDY?

There had been clear dearth of substantial research on impact of terrorism on IB (Suder & Czinkota, 2005). But over years, a consensus emerged among the scholars, policymakers, and practitioners that terrorism is an issue of growing importance to IB (Czinkota & Ronkainen, 2009) and a particular concern to firms with complex, global supply chains (Abadie & Gardeazabal, 2008). Now terrorism studies have become an integral part of the IB literature (Suder & Czinkota, 2013).

Although research on terrorism's impact on management and IB has increased substantially since 9/11, theoretical and conceptual thinking about the nature of the terrorist threat and its implications for MNEs, their stakeholders, and the IB environment remains underdeveloped. Similarly, the research is insufficient to understand how MNEs respond to the impacts or risks of terrorism to run their operations smoothly in EMs.

Scope of this research is to ascertain how the managers and policymakers of the MNEs operating in the EMs perceive terrorism-related impacts and respond to them. It will give them new ideas to think out of box instead of remaining fixated on Westerners' solutions (Prahalad & Lieberthal, 1998) which might not work in different environments of EMs.

In addition to the theoretical and empirical contributions, this study is expected to contribute to practice and policy to be adopted by the MNEs and governments to handle and counter the impacts of terrorism.

1.4. CASE STUDY METHOD

The research has been designed on a case study basis covering, primarily, semi-structured interviews of key persons of selected MNEs. Pursuing the case study method, it seemed appropriate to choose at least four MNEs from two EMs afflicted with high level of terrorism for the purpose of this study. The four MNEs, Beverages, Nest, Fast Food, and Oil Co., fulfilled the criteria developed to select the MNEs. Similarly, Pakistan and Turkey were selected as the two EMs continuously figuring on the Global Terrorism Index (GTI), having a number of established MNEs operating there for last many decades. Table 1.3 shows that Pakistan was ranked 4th and Turkey 27th, without much difference in score in GTI.

The key persons like managers and/or security heads of these MNEs were interviewed for this purpose. The key persons belonging to government regulatory authorities related to business and security were also interviewed. Besides the interviews, documents and record pertaining to the implementation of standard operating procedures shall also be examined.

Prior to conducting actual case studies, a pilot case study was carried out.

1.5. RESEARCH AIMS AND RESEARCH QUESTIONS

Scholars have cited terrorism as a key international policy issue (Czinkota & Ronkainen, 2009) and one of the critical frontiers in IB issues (Ricart, Enright, Ghemawat, Hart, & Khanna, 2004). They have realized that there is a dramatic change in terrorism after 9/11, and it is on the rise (Ricart et al., 2004). It is an increasingly serious threat to MNEs that merits additional attention from both the IB scholars and practitioners. According to Kotabe (2005), terrorism is an accepted fact of geopolitical life, and by implication, it is a worthwhile topic of scholarly inquiry by the IB academics.

Table 1.3. Global Terrorism Rank of Pakistan and Turkey (2015).

GTI Rank	Country	2015 GTI Score	Change in Score (Actual Year 2013–2014)
1	Iraq	10	0.4062
2	Afghanistan	9.233	0.238
3	Nigeria	9.213	1.018
4	Pakistan	9.065	−0.009
27	Turkey	5.737	−0.144

Source: Based on data drawn from GTI. Measuring and understanding the impact of terrorism (2015).