BUSINESS DIPLOMACY:
THE COMPASS ROSE OF FOREIGN MARKETS

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BUSINESS DIPLOMACY: THE COMPASS ROSE OF FOREIGN MARKETS.

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MY MASTERS THESIS IS DEDICATED IN LOVING MEMORY OF

GEORGIA M. VLAHOS
November 8, 1943 – August 15, 2014
MENTOR, TEACHER & FRIEND

ROBERT H. RUTHERFORD SR.
November 8, 1932 – August 28, 2014
BELOVED UNCLE & FRIEND

SOME PEOPLE COME INTO OUR LIVES & QUICKLY GO SOME STAY FOR A WHILE, LEAVE FOOTPRINTS ON OUR HEARTS, AND WE ARE NEVER THE SAME.

-FLAVIA
# TABLE OF CONTENTS

LIST OF TABLES ........................................................................................................................................1

ACKNOWLEDGEMENTS ..........................................................................................................................1

1. INTRODUCTION ........................................................................................................................................2

2. HISTORY OF DIPLOMACY THROUGH THE AGES ..............................................................................4

3. LITERATURE REVIEW: TRANSFORMATION OF BUSINESS IN A GLOBAL MARKET ...............................7

  3.1. THE NEW GLOBAL CONCEPT OF DIPLOMACY ...........................................................................12

4. EMBRAER (EMPRESA BRASILEIRA DE AERONAUTICA, S.A.) .........................................................20

  4.1. HISTORY ........................................................................................................................................20

  4.2. EMBRAER IN CHINA ..................................................................................................................26

5. ANALYSIS: EMBRAER’S BUSINESS DIPLOMACY STRATEGY .........................................................33

6. CHINA: EMBRAER’S BUSINESS DIPLOMACY CHALLENGE ..........................................................37

7. LIABILITY OF GOVERNANCE ............................................................................................................43

  7.1. UNDERSTAND YOUR ETHICAL SCREEN ................................................................................24

  7.2. INVEST IN KNOWING THE MARKET HISTORY & THE BUSINESS ENVIRONMENT .................45

  7.3. BE A STUDENT OF ANTHROPOLOGY & JURISPRUDENCE ......................................................45

  7.4. BUILD YOUR OWN “EMBASSY” .................................................................................................46
7.5. DON'T LET YOUR STRENGTHS BECOME YOUR NEW WEAKNESS

8. CONCLUSION

9. REFERENCES
LIST OF TABLES

Table 1: EMBRAER’S use of business diplomacy in foreign markets (embraer.com) ................. 26

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1. **INTRODUCTION**

With transnational corporations (TNCs) around the world today numbering over 60,000 and more than 800,000 affiliates working abroad, it is easy to understand how modern day international business could have transformed into a major global player serving at the axis of politics, social and environmental responsibility. Additionally, with accountability to a large variety of both public and private stakeholders, all exerting significant power and influence, today’s global corporate structure is reinventing modern international relations, and in some cases, dominating it. (Muldoon 2005) This transformative nature of globalization today can also serve as a source of friction among this growing chorus of players and is bringing irreversible change to these relationships and how they impact and influence business around the world. (Muldoon 2005)

From the largest to the smallest international corporation seeking to expand into new international markets, the challenges that come with corporate ambition can mean the difference between success and failure and they find a home at the intersection of international relations, diplomacy and economics.

To successfully navigate these challenges, especially in emerging economies, a company must now factor in more than just the “bottom line” and address complex issues that include human rights differences, environmental regulations, labor rights and values of each country. (Henisz, 2014) Combined with modern-day mobility achieved through technology and the Internet, corporations today have a great capacity to reach targeted audiences and establish a presence, but it is this same technology that also allows for immediate response to any corporate action. This constant, 24-hour news cycle, where everyone is made to be a real-time reporter through social media, has created a situation that demonstrably necessitates the ability to not only
respond immediately, but also to have real-time understanding of the challenges faced by a corporation as it looks toward global expansion.

*International Business Diplomacy*, or simply *Business Diplomacy* as it will be referred to in this paper, combines all of these nuanced factors into a relatively new discipline that offers companies looking to expand into new markets, guidelines and directives so that they can more strategically map corporate direction, limit risk and achieve their objectives.

This paper will examine the history of diplomacy and how the concept of statecraft became intertwined with the increasing globalization of business. Following a scholarly examination of how modern Business Diplomacy came into being, and the unique challenges that come with its application, particularly the liabilities needed to be overcome, this paper will apply the concept to the Brazilian aerospace manufacturer Embraer, tracking its strategic emergence from a small, regionally focused aircraft producer to global leader in the regional and executive jet market platforms. It will then examine Embraer’s entrance into the Chinese market, where the company suffered from several missteps and eventually had to refocus its business model from commercial to executive jets.

Finally, as globalization continues to “emancipate international business from its institutional and social constraints,” (Muldoon 2005) this paper will address how the relatively new and emerging discipline of Business Diplomacy is continuing to mature and grow in stature and influence through the proposition of a new challenge or “liability” that corporations must also overcome as they expand into new markets.

Through the analysis of Embraer in China, this paper will introduce the *Liability of Governance* to the lexicon of Business Diplomacy and propose specific steps that a company can undertake to avoid it.
The origin of diplomacy can be traced back to the moment when our predecessors realized that it was better to hear a message than to eat the messenger.  

Dr. George F. Vella  
Former Minister of Foreign Affairs, Malta  
(Modern Diplomacy)

2. HISTORY OF DIPLOMACY THROUGH THE AGES

The links between diplomacy and trade can be traced back to the time of the Bronze Age when rulers would often exchange gifts in an attempt to impress each other and demonstrate the trade power of their respective kingdoms. When an emissary would be sent, he was usually a relative or close trusted advisor to the ruler, so impressing them ensured that word would get back to the king as well. These early diplomats were traditionally only dispatched to handle a specific treaty or negotiation and would return home immediately upon completion, so the courtesies extended while in country would often go beyond gift-giving to include protection and shelter. (E-Diplomat) These rituals of hospitality were known as Xenia, or guest-friendship, and would come to define the first official diplomatic engagements between two peoples. (Finley, 1954)

Diplomatic relations of this type would continue until the early Renaissance, when in the 1300s the concept of a mission or embassy would begin to take shape in the states of Northern Italy. Seeing the need for on-going regular interaction, not to mention confidence building to know what other states were doing, the states began sending permanent representatives to live and work within the respective territories. The origins of many of the modern diplomatic traditions still in use today, such as an ambassador presenting his or her credentials to the head of state, can be traced back to this period. (Finley, 1954) The first international diplomatic posting came in 1455 when Milan established on-going representation in France. Ironically, Milan
refused to provide for reciprocal French representation fearing external intervention. As outside influence began to grow, the Milanese relented allowing for both Spain and France to establish permanent representation. The ability for regular, face-to-face meetings and discussion, allowed for confidence building and mutual understanding, a hallmark that exists in modern day diplomacy. (Finley, 1954)

It didn’t take long for other European powers to see the value of direct in-country representation. Spain would become the first nation to send a permanent representative to the Court of St. James in 1487. Within less than 100 years, permanent missions would become the standard practice across the globe. (Finley, 1954)

As the role of diplomatic emissaries expanded and evolved, the formal title of Ambassador was adopted, and Foreign Ministries were established to oversee and coordinate international relations. The growing challenges and responsibilities that these diplomats faced necessitated moving beyond selecting those with close personal connections to the country’s ruler to skilled individuals to staff the new embassies. Graduates of universities, those who had studied international law, modern languages and history were greatly sought after experts. From the very earliest developments of diplomatic relations, countries saw the need for individuals who had a solid understanding and appreciation for the unique circumstances that come with nation-tonation interaction.

The first real test for the system of diplomatic relations would come following the French Revolution and the abolishment of the monarchy. Ranks of precedence were done away with and Napoleon would later refuse immunity to diplomats, detesting what he viewed as the long, drawn out slow moving process of formal diplomacy. (Finley, 1954) It wasn’t until the Congress of Vienna of 1815 that a formal international system of diplomatic rank would be established. The
disputes over country precedence and other similar issues would linger through the middle half of the 20th century. It wasn’t until the Vienna Convention on Diplomatic Relations of 1961 that a formal modern framework of diplomatic relations between independent nations would be established. (Vienna Convention)

While viewed fundamentally as overseeing the relationship between independent states as equal members, with the advent of modern technology and communications, the concept of diplomacy in today’s modern age has required incorporating the outside influences of international business and non-governmental organizations among others. These external forces began introducing new complexities and challenges that had to be factored into international relations on a global scale, and thereby redefining diplomacy as the “mechanism of representation, communication and negotiation through which states and other international actors conduct their business.” (Melissen, 1999)

The inclusion of non-state actors broadens the lens through which international relations is viewed while simultaneously confirming that the state remains at its core. This expansion and the resulting impact, demonstrated since the last half of the 20th century, have significantly increased the role of economics in diplomacy. From more open, coordinated and consolidated global trade policies (World Trade Organization) to regional economic agreements (NAFTA) to full consolidation of economic markets (European Union), globalization of economies has increased the importance of economic diplomacy on the world stage. (Dicken, 2011) This trade diplomacy, which includes numerous players and complexities has been described as “the work of diplomatic missions in support of the home country’s business and finance sectors in their pursuit of economic success and the country’s general objective of national development.” (Saner & Yiu, 2003)
With this historical perspective in mind, in today’s modern, post-Cold War, global age it can be argued that diplomacy as a whole has migrated away from a geopolitical focus and shifted toward a geo-economic outlook, resulting in “trade and economic relationships [moving] to the centre of diplomacy.” (Ögütçü, M., & Saner, R., 2008) For as the Foreign Minister of Australia Julie Bishop described it earlier this year, “If the goal of traditional diplomacy is peace, then the goal of economic diplomacy is prosperity.” (DFAT)

3. LITERATURE REVIEW: TRANSFORMATION OF BUSINESS IN A GLOBAL MARKET

In a global economy where technology is shrinking boundaries and economics and trade now live near the center of diplomatic efforts, one might incorrectly assume that the challenges for entering foreign markets are diminishing. In fact, just the opposite rings true. The increased access to diverse new markets has simultaneously elevated the unique challenges that corporations face when going beyond their own native borders as well as raising the interest and desire of scholars to study the discipline of global market expansion, hoping to better understand and define the challenges and opportunities that lie within. Over the last fifty years, several notable theories have been proposed that today serve as benchmarks in the study of economic globalization and market expansion. First among them, were several “liabilities” that have been introduced to define the challenges that a corporation faces when attempting to enter a foreign market. The concept of “being foreign” was theorized by Stephen Hymer and replaced the more basic premise of simply being the “costs of doing business abroad (CDBA).” (Gaur & Kumar & Sarathy, 2011) From the beginnings of international engagement, corporations have faced a multitude of socio and economic challenges when operating, or attempting to operate in foreign markets. As they began to become more complex and intertwined with diplomatic issues,
researchers began looking into the types of advantages needed to offset these challenges. (Eden & Miller, 2001)

Hymer’s theory argued that because these challenges can take longer to overcome, they serve as a real disadvantage for foreign firms over those of domestic firms. (Eden & Miller, 2004) He believed that CDBA should be measured in reverse, looking at the specific “advantages that national firms have in their home markets relative to foreign-owned firms.” (Eden & Miller, 2001)

*First, national firms would have better information about their own country so foreign entrants needed to incur a one-time cost of acquiring this information. Second, national firms could receive differential and superior treatment from the host country government, buyers and suppliers. This ‘stigma of being foreign’ was expected to persist over time, even after the firm set up operations in the host country. Third, the entrant’s home government could also generate differential treatment; e.g. by prohibiting its firms (both parents and foreign affiliates) from engaging in certain activities or by levying more onerous taxes than apply to host national firms. Lastly, Hymer argued that because receipts and payments of foreign currencies were not synchronized, the MNE subunit faced foreign exchange risks that were not incurred by a national firm in the host country. Because of these costs of doing business abroad, Hymer argued that the MNE needed advantages if it was to go abroad and be successful.* (Eden & Miller, 2001)

Following on Hymer’s premise and research, Akbar Zaheer would coin the term *Liability of Foreignness*, which she defined as “the costs of doing business abroad that results in a competitive disadvantage for a multi-national enterprise subunit…broadly defined as all additional costs a firm operating in a market overseas incurs that a local firm would not incur.” (Zaheer, 1995) Liability of Foreignness comes from being a ‘foreign entity,’ where the company “suffers from a lack of legitimacy in the host country, and therefore faces discriminatory treatment by foreign customers, suppliers, competitor firms and the government.” (Eden & Miller, 2001)
Both Hymer and Zaheer argued that the bottom line for any corporation looking to expand into other markets must work to negate the challenges they face, find parity on the economic playing field with local corporations based within the country and overcome the “unfamiliarity hazards” and “discrimination hazards,” which come with “being a stranger in a strange land.” (Eden & Miller, 2001)

Unfamiliarity hazards are exactly what is implied; namely, the challenges of being unfamiliar with the host country market which serves as an automatic disadvantage over local companies native to the market and familiar with it. With these hazards comes the “Liability of Newness [which] is measured by the additional costs that the MNE must incur to achieve the same level of knowledge as the national firm.” (Eden & Miller, 2001) In their research, Lorraine Eden and Stewart Miller argue that any new corporation faces this challenge, but that foreign corporations also face the unfamiliarity within the new country, doubling the liability in both industry and country. While previous experience as a new market entrant won’t fully mitigate the liability, it can reduce it. (Eden & Miller, 2001) Discrimination hazards they argue place challenges on the foreign corporation as an outsider. From government imposed barriers such as trade regulations and restrictions to supply chain limitations. Eden and Miller argue that these hazards can be political or consumer ethnocentric, and that the ‘costs’ must be focused on finding legitimacy in the host country. (Eden & Miller, 2001)

In an effort to further address the challenges of foreignness, researchers Jan Johanson and Jan-Erik Vahlne at Uppsala University in Sweden proposed a new model for international involvement by corporations. The Uppsala Internationalization Model, which was introduced in the 1970s, proposed a process in which a firm’s presence is gradually developed over time
through four unique steps “which cannot be viewed independently of a company’s situation, market or market knowledge.” (Uppsala)

- Step 1: No regular export activities (sporadic export)
- Step 2: Export via independent representative (export mode)
- Step 3: Establishment of a foreign sales subsidiary
- Step 4: Foreign production/manufacturing

The model contradicted the established and accepted economic norms of the day that were rooted in the belief that a firm should analyze their costs and risks based on market characteristics, and then choose how to enter any market based on their own resources. (Hood & Young, 1979)

*The model focuse[d] on the gradual acquisition, integration and use of knowledge about foreign markets and operations, and on the incrementally increasing commitments to foreign markets. In particular, attention is concentrated on the increasing involvement in the individual foreign country.* (Johanson & Vahlne, 1977)

Johanson and Vahlne based their findings on their empirical research of Swedish firms and their slow, incremental steps to developing international operations. As was the case for many companies of the day, firms would enter into agreements with intermediaries who could then in turn represent the company abroad. This process allowed for a business to slowly increase its involvement as it gained additional knowledge about the market, and as that knowledge led to further expansion, invest more into it. The most important factor in the model was to ensure minimizing uncertainty, one of the most important factors related to the process of internationalization. (1977)

Over the last forty years, with rapid globalization and increased modern technology, the environment of global business has changed, and Johanson and Vahlne concluded in 2009 that it was important to revisit their model to assess and revise their premise based on these fundamental changes. The new analysis acknowledged that when they “constructed the model, there was only
a rudimentary understanding of market complexities that might explain internationalization difficulties.” (2009) While their model explained the internationalization process of a firm, they felt it was important to reassess the model as it related to the relationships that exist in a business network, the environment in which the firm must work. These relationships serve as modern day learning labs for building trust and commitment from which would develop “insidership in relevant network(s) [which] is necessary for successful internationalization.” (2009) But this premise also introduced the converse, namely, that by creating business networks and establishing relationships with distributors and customers alike, companies could avoid the Liability of Outsidership. (Schweizer, 2012)

The network model of internationalization comes from the firm’s own business network as well as the foreign market networks that it must permeate to succeed. Johanson and Vahlne argued, “if a firm attempts to enter a foreign market where it has no relevant network position, it will suffer from the Liability of Outsidership, [as well as] Liability of Foreignness, [as] foreignness complicates the process of becoming an insider.” (Johanson & Valhne, 2009) They argued that the strength of this environment of networks is the benchmark by which a firm can measure potential for success or failure.

In concluding their revisions to the original Uppsala model, Johanson and Vahlne assessed that a corporation is fundamentally at the core of a business network that can simultaneously be enabling and constraining and involve numerous actors and interdependent relationships. (2009) They went on to propose that

the traditional view of entry – that is, overcoming various barriers – is becoming less important than internationalizing undertaken to strengthen a firm’s position in the network. As a result, [they] claim that existing business relationships, because they make it possible to identify and exploit opportunities, have a considerable impact on the particular geographical market a firm will decide to enter. (Johanson & Valhne, 2009)
The revised Uppsala model argues that the globalization of business has moved away from the Liability of Foreignness and more toward the Liability of Outsidership, in that a corporation’s challenges and advantages are “becoming less a matter of countryspecificity and more one of relationship-specificity and network-specificity.” (Johanson & Valhne, 2009) They argue that new market entry challenges are similar regardless of locale, and that without having established relationships within the market it would be challenging at best to understand how they are intertwined and create a market access point.

The researchers noted that further study in the years ahead might be needed to determine when and where Liability of Foreignness or Liability of Outsidership is the primary challenge, or how the two approaches might be combined. It is at the heart of this crossroad that Business Diplomacy lies, and where the study of internationalization meets its real world application.

3.1. THE NEW GLOBAL CONCEPT OF DIPLOMACY

As has been seen, the concept of diplomacy has evolved from one-state engagement with other similar states to today’s complex and somewhat abstract view where state, sub-national actors and non-state actors all interact on a regular basis, and from which forms both nationalistic and multilateral agreements and opportunities for cooperation and partnership. (Saner & Yiu, 2003) For the purposes of this paper, the definition of modern day, contemporary diplomacy will be that of Jan Melissen’s who defined Diplomacy as “the mechanism of representation, communication and negotiation through which states and other international actors conduct their business.” (Melissen, 1999)

When globalization and multinationalization are viewed through this lens, combined with the challenges faced, there are several categories of Diplomacy under which their work can fall
that must be identified to better understand how to address them for both the state and the independent corporation.

When a state seeks to obtain an economic advantage for the nation through higher growth rates, job creation and increased tax revenue through international engagement, that government will employ either Economic Diplomacy or Commercial Diplomacy.

**Economic Diplomacy** provides a mechanism for the state to address and advance its economic footing abroad through foreign direct investment and promotion of exports to advance the interests of the state in foreign countries. (Ögütçü & Saner, 2008) As described in their 2003 study of modern diplomacy, Saner and Yiu, refer to these efforts as “economic statecraft” in that it “employs economic resources, either as rewards or sanctions, in pursuit of a particular foreign policy objective.” (2003) By using modern diplomatic channels and processes, governments are also supporting economic development by corporations within the state through incentives, guidance and assistance. This **Commercial Diplomacy** involves “the work of diplomatic missions in support of the home country’s business and finance sectors in their pursuit of economic success and the country’s general objective of national development.” (Saner & Yiu, 2003)

The importance of this economic statecraft was recently demonstrated by the Australian Government when on August 18, 2014, Julie Bishop, Minister of Foreign Affairs and Andrew Robb, Minister for Trade and Investment jointly launched a bold new Economic Diplomacy agenda. This is new policy is based on four key points: promote trade, encourage growth, and attract investment and support Australian business. (Placek)

It is not coincidence that both ministers were at the announcement. The Government’s new policy agenda is looking to its 95 ambassadors, high commissioners and consul generals as well as its 72 trade commissioners to “‘harness broader aspects of [their] international work’ to
achieve these economic outcomes.” Each head of mission submitted a plan to advance economic diplomacy for Australia and out of their combined plans, more than 2,000 recommendations were compiled. The focus will be for these overseas posts to work more closely with all aspects of the private sector to forge new partnerships to strengthen and advance Australian economic priorities. (Placek)

In her speech at the announcement, Minister Bishop described this new policy as an “overarching principle that puts strong economic outcomes at the centre of our foreign, trade, investment, tourism and development assistance policies.” It is widely believed that this new plan will serve as the benchmark for the Australia Government to reorganize how it approaches foreign policy writ large. With the smallest diplomatic footprint of any of the G20 countries, questions remain as to whether such a transformative policy can be fully enacted during a time of shrinking government budgets and declining staff numbers. (Placek)

The multitude of standards governing business behavior today also require a diplomatic framework under which corporations can navigate the challenges presented earlier as they look to expand their global footprint. As previously discussed, the expansion of globalization in business has brought new challenges, from the political and consumer ethnocentricity hazards that come with the Liability of Foreignness to attempts to overcome the liabilities of being an outsider, Liability of Outsidership, through business networks and establishing relationships. In sum, the costs of doing business outside a home country environment are complex, nuanced and real.

To find success in other countries, it is incumbent upon corporations to create a strategic vision that addresses these challenges. By applying the principles of either **Corporate Diplomacy** or **Business Diplomacy**, a company can establish its own unique and targeted plan to do just that.
It is important to pause to acknowledge one of the significant challenges of researching these topics, that is, just like the study of the globalization of business, they are relatively new to the lexicon of economics and diplomacy. The study of Business Diplomacy was only first mentioned by the editor of Forbes Magazine in a 1950 article entitled “Total Business Diplomacy” that argued using American corporate power could be used to spread American values around the world in an effort to beat back the imposing challenge of Soviet-led communism. The term Corporate Diplomacy would be introduced six years later by the same publication. Fast-forward to the early 1990s when the late Susan Strange, world-renowned British scholar of international relations credited for coining the term “international political economy,” would describe emerging forms of diplomacy that were more nuanced and focused in their work relating to the private sector. In describing Corporate Diplomacy, she stated it “is becoming at least as important a subject as analysis of individual firms and their corporate strategies for finance, production and marketing. (Strange, 1992)

The further examination of these new forms of diplomacy would continue to develop over the next decade, leading to the seminal studies by Saner and Yiu in 2000 and 2003 which would provide formal definitions of both and set clear guidelines as to what each was and was not. For the purposes of this paper, the Saner and Yiu definitions will be used to clarify these terms.

In addressing the challenges of liability, both foreignness and outsidership, a corporation must ensure that before engaging external stakeholders, that there is a strong relationship between the company headquarters and its country offices and at the crux of it are the actors who work in both on behalf of the corporation. Saner and Yiu would describe this as Corporate Diplomacy which

cconsists of two organizational roles considered to be critical for the successful coordination of a multinational company, names that of a country business unit
manager who “should be able to function in two cultures: the culture of the business unit, and the corporate culture that is usually heavily affected by the nationality of the global corporation;” and that of a corporate diplomat who as a home country or other national who is impregnated with the corporate culture, multilingual, from various occupational backgrounds, and experienced in living and functioning in various foreign cultures. These two roles are essential “to make multinational structures work, as liaison persons in the various head offices or as temporary managers for the new ventures. (2003)

Corporate Diplomacy can thus be viewed as an overall methodology and could be compared to the modern day structure of the State Department and diplomacy at large. When a new Presidential Administration enters office, the President sets a foreign policy agenda, and the big behemoth of U.S. foreign affairs that is the State Department will work to enact this agenda. Regardless of the changes to foreign policy that the new Administration may want to enact, there are still diplomats on the ground at American embassies around the world who will go on about their daily business regardless of the new agenda set by leaders back in Washington. The day-to-day work of the embassy must continue, and these roles are critical to ensuring that happens while also overseeing overall diplomatic engagement by the embassy on behalf of the U.S. Government.

The work that these diplomats do can in the same regard be compared to Business Diplomacy. They are the diplomatic frontline for our nation in countries overseas, handling relationships with intergovernmental actors, other national governments, engaging with civic and community leaders and establishing the framework under which relationships are built and strengthened allowing for the work that is in the interest of the American people to be undertaken. Saner and Yiu establish a definition for business diplomats in much the same context. They write that

**Business Diplomacy** pertains to the management of interfaces between the global company and its multiple non-business counterparts and external constituencies. For instances, global companies are expected to abide by multiple sets of national laws and multilateral agreements set down by international organizations such as the World Trade Organization (WTO) and the International Labour Organization.
(ILO). On account of a global company, Business Diplomats negotiate with host country authorities, interface with local and international NGOs in influencing local and global agenda. At the firm level, they will help define business strategy and policies in relation to stakeholder expectations, conduct bilateral and multilateral negotiations, coordinate international public relations campaigns, collect and analyse pertinent information emanating from host countries and international communities. (Saner & Yiu, 2000)

This formalized concept and practice of Business Diplomacy is a still relatively new one. In today’s modern age, you don’t have to be Coca-Cola or IBM to be global in nature and companies of all shapes and sizes are now able to expand and operate around the world. (Goodman, 2006) But as has been addressed, having the desire or ability to expand doesn’t alone guarantee success, nor does corporate achievement in one market mean you will be able to successfully expand to others.

Business Diplomacy combines all of these nuanced factors into this new discipline allowing companies that seek to expand a way to strategically map their direction, limit risk and achieve their corporate objectives.

Corporate success in the global marketplace requires moving beyond Milton Friedman’s theory that a firm’s sole responsibility to its shareholders and the bottom line and factoring both in to a larger set of stakeholders. (Friedman, 1970) From foreign governments to local communities in which they operate, interest groups to regulators, global companies today must operate with a new mindset, factoring in what only a short time ago was considered outlying factors that need not be weighed into decision-making.

Additional “intangibles” such as public relations and Corporate Social Responsibility (CSR) also must now also be factored into the make-up of a corporations plan for global expansion. This move from shareholder to stakeholder is the capstone of a modern corporation defined as “the centre of a network of interdependent interests and constituents, each contributing
(voluntarily or involuntarily) to its performance, and each anticipating benefits (or at least no uncompensated harms) as a result of the corporation’s activities.” (Post, Sachs & Preston, 2002)

Business Diplomacy invokes participation from private firms, government entities and civil society to find that win-win opportunity by which a transnational firm can overcome liabilities and gain an advantage to increase market share through favorable economic conditions.

Saner and Yiu argue that for businesses to succeed they must first analyze, define and engage their own forms of diplomacy, or in other words, define and then manage business diplomacy for themselves and their company. (2000) To overcome Liability of Foreignness and Liability of Outsidership as well as manage the expectations of governments and civil society organizations and address socio-economic considerations, business diplomats must “build bridges between core businesses and the complex political environments within which global firms conduct business.” (2000)

While there is a distinct difference between Corporate Diplomacy and Business Diplomacy, Corporate Diplomacy can play a significant role in Business Diplomacy. To achieve the international business diplomacy objectives of a company, it is critical that corporate headquarters work closely with their in-country, socio-economic “interpreters” whose job it is to ensure that the interests of the company are being looked after. Just as European powers saw the importance of placing subject matter experts on station as far back as the 1500s, today they are just as critical to corporate success especially as corporate globalization plans include continued expansion into new markets.

Obtaining that “license to operate” becomes the most important company asset and “to obtain it requires meeting expectations of multiple stakeholders, which in turn requires gaining the trust and reducing the Liability of Outsidership.” (Ordeix-Rigo & Duarte, 2009) This “social
“charter” can also validate “the legitimacy of the contemporary corporation as an institution within society…[based] on its ability to meet the expectations of an increasingly numerous and diverse array of constituents.” (Post, Sachs & Preston, 2002)

As has been noted, the globalization of the corporate world is transforming how business gets done, which in turn is also refocusing the broader mission of how to achieve corporate objectives. (Ordeix-Rigo & Duarte, 2009) The inclusion of Business Diplomacy in a corporate strategy does not mean to just throw public diplomacy into the mix of tactics and strategies, but rather provide a means by which a company can pursue their own objectives through diplomatic means, just as governments utilize public diplomacy in advocating their key objectives. (Mitchell, Agle & Wood, 1997)

Through Business Diplomacy programs and initiatives, corporations can, just like the modern state, work to gain acceptance in the host country, providing validation beyond their simple writ that allows for operation in the country. “Through financial and other tangible means, corporations will support local charities, initiatives and other similar types of organizations to bond with a community, demonstrate that they are insiders dedicated to the long term investment in bettering the community…[By becoming proactive members in society, corporations can add] new dimensions to their traditional perceived role of generating wealth, employment and quality products or services.” (Ordeix-Rigo & Duarte, 2009)

By demonstrating their civic responsibility, corporations can engage many aspects of CSR in their Business Diplomacy strategy as it “can help achieve and demonstrate their “support of the publics,” and not just random “public support.” (Ordeix-Rigo & Duarte, 2009) It is important to note however, that Business Diplomacy is not CSR, and CSR is not Business Diplomacy. While Business Diplomacy can provide validation by the public for their actions, CSR is but one tactic
“to expand its legitimacy and the influence of the company.” (Ordeix-Rigo & Duarte, 2009) In a stakeholder system, this power and legitimacy, defined by Ronald Mitchell, et al. as “a generalized perception or assumption that the actions of an entity are desirable, proper or appropriate within some socially constructed system of norms, values, beliefs and definitions” are two of the main factors in measuring success. (Mitchell, Agle & Wood, 1997)

This modern view of Business Diplomacy is not without its challenges and controversies. In working to overcome the Liability of Foreignness and Liability of Outsidership, the image of a global corporation becoming a “citizen actor” in the public sphere of the state can be invoked. This vision at best can be complex and challenging, and risky at its worst. With few “consistent global laws or concrete standards, challenges relating to the environment, labor business practices corporate roles in education and human rights… they must balance their fiduciary responsibility to shareholders in highly competitive marketplace with considerations that include their own corporate and moral values, their roles in strengthening the society around them, and the rewards and risks to their reputation.” (Garten, 2002) To not do so, risks the invocation of new liabilities that can have equally disastrous results.

4. EMBRAER (EMPRESA BRASILEIRA DE AERONAUTICA, S.A.)

4.1. HISTORY

One highly internationalized manufacturer from an emerging economy that has demonstrated the value of Business Diplomacy as they have expanded is Embraer, or as it is known by its parent holding company name, Empresa Brasileira de Aeronautica, S.A., a leading global aircraft manufacturer and one of the largest international companies in Brazil. (Green & Simko, 2013)
While Brazil is still viewed as an emerging economy, the same cannot be said for the country’s work in the aerospace industry. Since the beginning of the 20th Century, Brazil has been a major player in the global development of the aerospace industry. From the historic first achievements of Alberto Santos Dumont, known as the Father of Brazilian Aviation, Brazil’s place as a pioneering innovator in aviation has continued to grow and flourish. Santos Dumont’s achievements catalyzed his country’s passion for flying which led to the creation of the Brazilian School of Aviation by the military on January 13, 1913 at Campo dos Afonsos. (Lopes, Maat, Zimath, et. al., 2008)

Over the next 20 years, the aviation industry in Brazil would establish one of the first airmail systems in the early 1930s and during the height of World War II, Brazil manufacturers were producing aircraft at the rate of one a week in support of Allied efforts. (Brazilian Air Force)

At the end of the war, the Brazilian government was determined to continue building on prior aviation success, ensuring that the achievements in aeronautical engineering would not diminish but serve as the foundation from which to modernize the industrial manufacturing base across the country. To that end, Brazil’s Ministry of Aeronautics would establish the Aeronautical Technology Center (CTA) in the 1940s, which in collaboration with the Massachusetts Institute of Technology (MIT), continues to serve as the national research center for aviation and space flight today. (Embraer History)

The successful innovation of Brazilian aerospace would continue to thrive in the years that followed. A military coup replaced the sitting government in 1964, and in an effort to nationalize the industry, the company that would come to be known as Embraer was established by President Artur da Costa e Silva on August 19, 1969. Embraer’s first aircraft, the EMB-110
Bandeirante had already been under development at CTA and had made its maiden flight the previous year. It would go into service in the early 1970s. (Green & Simko, 2013)

As a state-owned company, Embraer was able to draw on the capabilities of CTA, which served as the corporation's lead institution for developing new technology while the blue-collar workforce came from the car industry. (Vertesy & Szirmai, 2010) The success in the aerospace industry would quickly earn Embraer a reputation for being a reliable aircraft manufacturer, gaining orders for both military and commercial variants of their aircraft, and began international sales in 1975. Sales continued to flourish with the development of the EMB-120 Brasilia, a pressurized, 30-seat turboprop that would continue growing their market share into the 1980s. (Vertesy & Szirmai, 2010)

As the impact of the global recession of the 1990s began to hit South America, along with the consequences resulting from the end of the Cold War, Brazilian manufacturing was hit hard. The Brazilian aerospace industry lost more than 70% of its industrial base. In 1994 alone, Embraer suffered losses in excess of $310M on sales of only $177M. (Vertesy & Szirmai, 2010)

Government ownership had gone from being a sure foundation to a challenge to their competitiveness. All major decisions had to be approved in Brasilia, usually by both the executive and legislative branches of the government. Additionally, with the government in charge, the company was forced into fiscally unviable projects that led to declining export sales and rapidly increasing financial losses. (Bonelli, & Pinheiro, 2012) These fiscal challenges would lead to the near-collapse of the Brazilian aviation company, and only its sale to private investors would keep it afloat, with a much-needed injection of private capital funds to sustain it. (Fernandes, Moscoso, Price, Yoshino & Zhang, 2011) This new consortium provided Embraer
with the ability to seek out risksharing agreements with foreign suppliers, reducing R&D costs from 30% down to 5% of total company revenue. Other cost saving actions undertaken once a private company included a significant reduction in its total workforce. The spirit of innovation that thrived at Embraer continued not only in the newly privatized company, but also with the former employees. Taking the knowledge and training they had acquired into their own hands, the former engineers and technicians would spur a new round of corporate growth in the aerospace industry across Brazil and in the long run, strengthen the industry as a whole. (Vertesy & Szirmai, 2010)

In addition to life-saving funding, Embraer’s privatization allowed for the company to more strategically target its focus, namely on the regional jet manufacturing industry. Combined with a sharp increase in demand from international markets, Embraer was able to gain a lion’s share of the market, surpassing its leading competitor, the Canadian aerospace firm Bombardier. (Fernandes, Moscoso, Price, Yoshino & Zhang, 2011) The success of Embraer has allowed Brazil to become the “only developing and tropical country in the 20th century to have successfully developed an indigenous aircraft industry. Among the failed attempts there are India, South Korea, Indonesia, Turkey and, Argentina.” (Fernandes, Moscoso, Price, Yoshino & Zhang, 2011) Throughout its history, Embraer has successfully used the principles of Business Diplomacy to enter foreign markets, establish its presence and grow their market share. This allowed the company to continue its strong record of innovation and product development, to include entering the growing executive jet industry in 2005. (See Table 1)

Given the distance from Brazil to many of the country’s Embraer exported their aircraft to, initial entries into foreign markets were done out of sheer necessity, ensuring that repair and
technical support for its clients, both commercial and private, was available. This strategy was known as “follow the aircraft.” (Parente, Cyrino, Spoehr, Caravalho de Vasconcelos, 2013)

Embraer has exponentially grown, overtaking their direct competitor, Canada’s Bombardier to become the global leader in regional jet manufacturing and already third in executive jets, despite only entering the market in 2005. (Fernandes, Moscoso, Price, Yoshino & Zhang, 2011)

Embraer and the resulting aeronautics industry is the largest in the Southern Hemisphere, 5th largest by volume globally and became one of the fastest growing exporters of the last ten years. (Fernandes, Moscoso, Price, Yoshino & Zhang, 2011)

- Embraer’s first exports came in September 1975 with the purchase of 15 aircraft by the Government of Uruguay.
- The first international type certification and commercial exports began in 1977. Certified by the French Government, Air Littoral received the first EMB 110 Bandeirante.
- In August 1978, the Bandeirante receives certification of both the British Civil Aviation Authority (CAA) and the U.S. Federal Aviation Administration (FAA).
- In October 1979, Embraer opened its first offices in the United States to ensure adequate technical support for new North American customers. Additionally, the new Embraer Aircraft Company subsidiary was established to provide for sales in United States, Canada and Mexico.
- Embraer partners with Italian aerospace firms Aeritalia and Aermacchi to begin developing the AMX, and generation of subsonic fighter/bomber aircraft.
- In 1981, Egypt began building the EMB 312 Tucano under product license from Embraer.
- Embraer Aviation International (EAI), headquartered in Paris was established in 1983 to support technical services and sales to Europe, the Middle East and Africa.
• In July 1988, Embraer joins with China to begin initial studies into the development of the CBERS, China Brazil Earth Resources Satellite.

• In 1993, Embraer enters into agreements with first strategic partners to develop the EMB145. These risk-sharing partners include Gamesa (Spain), C&D (EUA), ENAER (Chile) and Sonaca (Belgium). Program includes 350 suppliers and 10 system partners.

• The financial challenges of the early 1990s prompt Embraer to privatize with the majority stake of the company being acquired by Cia Bozano, Simonsen, Wasserstein and Perella. Under the new privatization of Embraer, the EMB145 program is launched. Grupo Bozano would purchase the Wasserstein Perella shares in 1996.

• In 1998, the Greek government commissions four Airborne Early Warning and Control (AEW&C) aircraft, which is based on the ERJ145 platform.

• The second significant strategic partnership is launched by Embraer in 1999 with a European group formed by EADS, Descuelt, Thales and Snecma and control 20% share of the company.

• 1999 also saw Embraer launch the Embraer170/190 family of aircraft, which moved the company from solely producing regional jets to larger aircraft. Following on previous successful models, the new aircraft line was developed under a multi-national partnership, which included 16 aerospace industries.

• In November 1999, Embraer SA of Brazil Liebherr Equipment (ELEB) was formed in partnership with Liebherr Aerospace Group of Switzerland.

• In May 2000, Embraer officially opens commercial offices in Beijing, China, providing a parts warehouse as well as marketing and sales support for aircraft.

• Embraer opens sales offices in Singapore in December 2000.

• In what was considered an important step in expanding after-sales support to Embraer operators in the United States, Embraer Aircraft Maintenance Services was opened in Nashville, TN in 2002.

• Embraer announces a joint venture with AVIC II to open an ERJ 145 aircraft assembly plant in Harbin, China in 2002 establishing the Harbin Embraer Aircraft Industry (HEAI).

• The first ERJ 145 produced in China rolls out in December 2003.

• Embraer and EADS buy Aeronautics de Portugal (OGMA), expanding its European presence.

• Embraer opens three new service centers in the United States to support executive jet sales.
- Embraer receives certification from the Civil Aviation Administration of China (CAAC) to operate the Embraer 190 and 195 jets in May 2008.

- Also in 2008, Embraer joins the United Nations Global Compact, an effort by the UN to mobilize the international business community to include human rights, labor relations, environmental protection and corruption protection into its business model.

- In August 2008, Embraer’s warehouse in China receives Brazilian certification to ensure compliance with Brazilian Aeronautical Regulations (RBHA).

- In December 2008, Embraer begins construction of its first plant in the United States for final assembly of aircraft. The facility would open in 2011 and begin production of Phenom 100 aircraft.

- Embraer Defense and Security, in partnership with Israel’s AEL Sistemas, launches Harpia Sistemas SA, a partnership to explore the UAV market in 2011.

- In February 2012, Jackie Chan, Embraer brand ambassador receives the first Legacy 650 aircraft produced in Harbin, China.

- Embraer, Boeing and Airbus sign an agreement to partner, promote and accelerate the availability of new sources of sustainable aviation fuel in March 2012. The public-private partnership includes support from governments, producers and other stakeholders.

- In October 2012, Embraer signs agreement with ExecuJet Aviation Haite Services China Co. Ltd. to provide maintenance service and support for Embraer’s executive jets. This is the first authorized support center in Mainland China.

- December 2012 sees Embraer fly the first “Made in the USA” Phenom 300 executive jet, joining the Phenom 100 production line.

- In March 2013, Embraer expands in Florida, opening new facilities to build aircraft for the U.S. Air Force’s Light Air Support (LAS) program.

- In November 2013, Embraer is listed in the Corporate Sustainability Index (ISE).

Table 1: EMBRAER’S use of business diplomacy in foreign markets (embraer.com)

4.2. EMBRAER IN CHINA
The attempts by the government of the People’s Republic of China to enter the aerospace industry during the last quarter of the 20th century were marked more by failure than success and prompted the government in 1993 to abandon its original plans and consolidate all of the state-supported aerospace manufacturing enterprises into one company, Aviation Industry Corporation, or AVIC. Following additional unsuccessful attempts to collaborate with Boeing and Airbus, and only one partnership with McDonnell Douglas to build the MD-83 jets in China, in 1999, the government divested AVIC into two companies, AVIC I and AVIC II, both still fully state-controlled enterprises. AVIC I would focus on military aircraft as well as subcontracts for Airbus and Boeing parts. AVIC II would focus on a broad manufacturing industry base including cars, motorcycles and other non-aviation products. AVIC II did include work on import and exports including aircraft leasing. (Lazzarini & Bourgeois, 2008)

As air traffic began a slow recovery following the September 11th attacks in New York, the greatest increase was seen in the Asia-Pacific countries. China exhibited not only the largest volume of traffic but also one of the largest growth rates. The increase in per capita income, especially in urban regions, increased demand, which was met by expanding seat capacity in planes and developing new routes. Growth was expected to remain strong, especially in domestic traffic. Boeing forecasted China’s annual domestic traffic growth at 8.8% from 2006-2026, compared with around 5% for the world as a whole. (Lazzarini & Bourgeois, 2008)

But even with this growth, regional aviation remained underdeveloped in China, accounting for only 3.5% of all airline traffic. “Major routes were still concentrated on a few airport hubs, especially on its east coast where 20% of its airports were responsible for about 80% of its passenger traffic.” It was anticipated that a thriving regional airline market, a major infrastructure investment would be needed across the country. (Lazzarini & Bourgeois, 2008)
Additionally, the regional operations (30- to 120-seat aircraft) of the three major government-controlled air carriers only accounted for 7% of air travel in China, whereas in the United States it accounts for 34%. New privately controlled airlines only controlled 4% of the market and were challenged by scalability limitations and profitable market shares. With the government in Beijing not eager to diversify the market, private entries faced numerous challenges to overcome, including a shortage of qualified pilots. (Lazzarini & Bourgeois, 2008)

The portending challenges to enter the last great un-tapped aviation market were not limited just to Embraer’s competition. In the late 1990s, as the company began to thrive under privatization, the Brazilian manufacturer decided to bet on Mainland China and the possibility of unlocking the door with their ERJ regional jets. In May 2000, Embraer promoted Guan Dongyuan, a Brazilian of Chinese decent and tasked him with establishing a new commercial office. Within the first six months, Embraer had secured new orders from two of the smaller, privately held airlines for a total of 35 firm orders and options for an additional 15. Before the aircraft could be delivered, and in a move directly targeting Embraer, the central government in Beijing decided to increase tariffs on imported small-size jets from 7.1% to 22.9%, making them instantly cost prohibitive for the regional airlines, and the orders were quickly cancelled. (Goldstein, 2005)

*So in a perfect case of ‘if you can’t beat ‘em, join ‘em,’ Embraer began looking at the possibilities of building the ERJ jets in China to “meet the central government’s requirement that foreign aircraft manufacturers should not only attempt to export assembled products but also carry out local production and engage, whenever possible, local Chinese suppliers.” (Lazzarini & Bourgeois, 2008)*

The goal of the original agreement with AVIC II that Embraer negotiated included sharing manufacturing technology and creating aircraft destined for the Chinese aircraft market. So once
Embraer decided to move forward with building a plant in Mainland China, the deal was transformed into a joint venture with Harbin Aircraft Industry Group (HAIG) and its subsidiary Hafei Aviation (HAFEI). (Embraer Releases, 2014) Previous agreements between China and Brazil, including those involving the aerospace industry, allowed for a rather amicable partnership to coalesce which culminated with the deal being signed in December 2002, in which Embraer would build ERJ 145 aircraft in the Manchurian region at the Harbin assembly plant under the new venture, Harbin Embraer Aircraft Industry Co. Ltd. (Lazzarini & Bourgeois, 2008)

In January 2003, the Chinese plant began operations with an assembly capacity of 11 jets per year. Productivity was expected to increase to 15 jets per year by 2008, and in the future, the workforce would expand in order to reach a capacity of 24 planes per year in the same assembly plant. By contrast, the product of ERJ 145 planes in Sao Jose dos Campos was from 16 to 18 planes per month. Because of the reduced demand for ERJ 145s, especially in the United States, in 2006, Embraer ceased the assembly of these jets in Brazil and used their former assembly line to manufacture Legacy corporate jets, which shared the same production platform; however, there were no plans to assemble the 170/190 E-Jets in China. (Lazzarini & Bourgeois, 2008)

Robert Rossi de Souza, who was appointed general manager in 2004 after 32 years of working for Embraer in Brazil, led the new Harbin Embraer. Jiang Da, a Chinese national was appointed deputy general manager to assist with local affairs. Jiang had worked at Hafei and had a strong background in aircraft manufacturing. The leadership reported to a board of directors consisting of a Chair from HAIG, Embraer served as a Vice Chair and five additional directors, two from Hafei/AVIC II and three from Embraer. (Lazzarini & Bourgeois, 2008)

While initial training for Chinese workers took place in Brazil, Embraer made significant efforts to ensure quality control standards were met. Harbin Embraer managers required a minimum of 10 months of training and on-the-job coaching. The plan was for most training and coaching to occur in Harbin by 2008. (Lazzarini & Bourgeois, 2008)
Cost production was mostly accrued from aircraft part purchases from more than 250 suppliers around the world, which were the same suppliers for parts in Brazil. In an effort to preserve intellectual property, contracts were signed to ensure that China could not purchase anything directly without the direct consent of Embraer. While the plan was to eventually local suppliers and produce parts of the aircraft in China, the main portions of the aircraft, known as “the kit” were shipped from Brazil through 2007. (Lazzarini & Bourgeois, 2008)

By that year, Harbin Embraer employed 247 Chinese nationals to work in the factory, which was overseen by 13 Brazilians who served as managers (most of whom had worked for the company in Brazil). The challenge that came from this was the language barrier; while the official language was English, most Brazilians couldn’t speak Mandarin and the Chinese workers had limited English knowledge, gestures became the language of the production line which proved challenging at best. (Lazzarini & Bourgeois, 2008) “The Brazilians saw the Chinese as eager to learn and showing a marked sense of responsibility. General Manager Rossie thought that there was a ‘natural affinity’ between the Brazilians and the Chinese.” (Lazzarini & Bourgeois, 2008)

Unfortunately, all of the good will among the staff didn’t translate into the expected sales. Only 16 planes had been ordered by early 2003 with Embraer executives citing the slow development of regional traffic as the cause. By the end of 2006, orders for 50 additional aircraft had been received with deliveries expected to begin by the end of 2007. This new order would have the production line operating at full capacity through 2010. (Lazzarini & Bourgeois, 2008) Another challenge that Embraer faced was in sales and marketing. Harbin Embraer did not incorporate its own sales team, relying on the Embraer China sales office, which required
payment of royalties and fees. Additionally, the commercial sales operation in China is challenging at best.

*Embraer’s commercial office first had to convince airlines companies that regional routes were profitable; the process often involved details consulting on which specific routes could be exploited. Then the airlines had to convince CAAC that they would operate the route with high safety standards, and external-relations official would judge whether the nation of the aircraft manufacturer had any serious conflict with China. Finally, NDRC officials would have to analyze whether the product involved adequate technology. Only then could a Chinese carrier enter into a purchase agreement with the manufacturer.* (Lazzarini & Bourgeois, 2008)

By 2008, doubts about the future of Embraer’s investment in China began to surface. While “cautiously optimistic” about the future, Embraer executives still working to find new customers in China and began looking at export market options across Asia. One of the challenges Embraer face was the immaturity of the market space and the yet developed regional market base within the country. (Optimistic Embraer, 2008)

While Embraer saw China as an underdeveloped market and an opportunity to infuse their product line, what they faced in reality was a market that had major obstacles and hesitancies from numerous sources that would affect the evolution of the market. (Optimistic Embraer, 2008)

Embraer’s own market analysts believed that 10% of all aircraft demand from China would come from the 30- to 120- seat market, equating to 730 airplanes and a 7.5% market growth. This estimate would make China the third largest and fastest growing developing market in the world. (Optimistic Embraer, 2008)

The opportunities of the Chinese market were tempered further by the challenges of operating in a country where the national government didn’t hesitate to intervene in the interest of Chinese companies. This was the reason for the increase on tariffs for regional jets earlier in the
decade and was also the reason Embraer chose to establish the partnership with AVIC II, because China has all but ended imports of regional jets into the country. (Optimistic Embraer, 2008) By 2008, China remained a perplexing challenge for the aircraft industry – “a market too large and strategically important to ignore but too unpredictable to embrace wholeheartedly. Embraer [had] certainly done its part with the opening of the joint venture…[b]ut while the Harbin plant [held] the capacity to built 24 airplanes a year, Embraer’s own market outlook [projected] a demand for fewer than 100 50-seat jets over the next decade.” (Optimistic Embraer, 2008) This sentiment was echoed by Embraer executive Mauro Kern who at the time stated, “we don’t have high expectations of big numbers of 50-seaters being sold there,” and indicated that the company had decided to begin looking at export options. (Optimistic Embraer, 2008)

Production, assembly and sales of the ERJ commercial jets ceased operation in May 2011. With the investment already having been made, Embraer saw that there was a growing demand for executive transport and their failed commercial aviation plan opened a door to potentially use their new focus on business jets. The revised plan resulted in a deal to produce Legacy executive jets in a June 2012 agreement using the same infrastructure designed for the original plant. (Optimistic Embraer, 2008) Embraer was able to reconfigure assets to enter the executive aircraft market as all three industries areas, civil, private and military, shared the same platform of aircraft models. (Parente, Cyrino, Spohr & Carvalho de Vasconcelos, 2013)

Embraer’s entry into the executive aviation market began in 2000, when they introduced the Legacy, which was built on the ERJ regional jet platform. The success of their venture led to the company officially launching Embraer Executive Jets as a subsidiary of the company with brand new executive jet designs. Following the model of their commercial market success, Embraer established a “global network of owned and authorized service centers, parts distribution
centers and expanded production of our executive jet aircraft components [and eventually] final assemblies outside of Brazil.” (Embraer History) Embraer delivered its first executive jet to China in 2004. (Embraer Executive, 2014) As part of the new plan for Embraer Harbin, Embraer and Minsheng Financial Leasing would strengthen the partnership between the manufacturer and China with a new “strategic cooperation” agreement to provide financing for executive jet purchases in China and would partner to promote the growing executive aviation business in China. Additionally, ABC Leasing, a subsidiary of the Agricultural Bank of China signed a $1.5 billion Memorandum of Understanding to help support aircraft financing in the first five years of the new venture. (Embraer Inks, 2011)

According to the Hurun Report, the most influential luxury genre publication in the country, “the Chinese business jet fleet has grown at an average annual rate of 27%, nearly matching the 26% annual growth in Chinese citizens classified as wealthy during 2007-2012.” (Embraer Sees, 2013) Embraer’s forecast for the market is very positive in the years ahead ironically as demand for executive jets has increased for both business and leisure travel because of the limited operation of commercial aviation in the country.

In releasing their market outlook for next ten years, Embraer is predicting more than 1,000 executive jets will be delivered in China. (Embraer See, 2013)

The first Legacy 650 executive jet built in Harbin made its first flight in August 2013 and delivered to its first customer in January 2014. All jets built in the Manchurian plant will be destined for China’s growing executive jet market. (Embraer Executive, 2014)

5. ANALYSIS: EMBRAER’S BUSINESS DIPLOMACY STRATEGY
As the world’s third-largest aircraft manufacturer, Embraer represents “a successful case of entry into a closed oligopoly dominated by U.S. and European firms. Embraer and its main rival Bombardier…a successful case in the sense that they were able to profitably enter the aerospace market with a niche strategy in mid-range jets, forcing incumbents such a Saab (Sweden), Fairchild (United States) and Fokker (the Netherlands) to exit” the market. (Bonelli & Pinheiro, 2012)

From its founding as a company, Embraer always seemed to get it right, focusing on smaller, regional jets that were well suited for Brazil’s airport infrastructure and commercial aviation market. This served in contrast to the leading aircraft manufacturers of the day that were focusing on larger aircraft designs which could not be accommodated at the airports in many of the smaller Brazilian markets. (Bonelli & Pinheiro, 2012)

*To become a leading aircraft exporter, Embraer had to overcome several barriers and uncertainties. The most noteworthy, of course, was the ability to develop technologically and commercially viable planes. Developing a new aircraft takes about three years and costs about $1 billion. In particular, the initial project had to be developed while no revenues were accruing; and given the level of technological mastery in Brazil in the 1960s, there was a reasonable risk that it would not be successful.* (Bonelli & Pinheiro, 2012)

From the government’s initial technological investment, to public private partnerships focusing on technology, to military procurement contracts which challenged Embraer to create more technologically advanced aircraft to transferring cost and risk to suppliers in the 1990s, the Brazilian manufacturer used its unique circumstances and strengths to continually advance its technology base and focus on several smaller projects and ensure they were at the top of their class of aircraft. (Bonelli & Pinheiro, 2012)

This technology was also led in part by aircraft customers, who partnered with Embraer to stimulate new innovation while demanding nothing short of total excellence in the final product.
This coordination came from another core factor in Embraer’s strength as an aircraft manufacturer, the company’s laser beam focus on exportation of jets from early on in its history. Stimulating product runs, Embraer was able to move past the government’s plan to be solely domestic in focus and allowed for it to more easily transition to being a private company. (Bonelli & Pinheiro, 2012)

The establishment of the Aeronautical Technology Center (CTA) in the 1940s provided Embraer with a solid, consistent pipeline of talent from which to draw aerospace engineers, all who were at the top of their field. But while the manufacturer could easily insource their workforce, the same could not be said for their ability to vertically integrate, which ironically became a strength in efforts to save the company from collapse. By having to rely on foreign outsourcing, Embraer could focus its attention on research and development and thus produce a higher quality product. As the company matured and evolved under privatization, so too did the Brazilian aerospace industry sector, leading to more locally manufactured components and a regionally based, high-tech cluster. (Bonelli & Pinheiro, 2012)

Throughout its history, Embraer strategically followed the basic tenets of Business Diplomacy, skillfully avoiding the Liabilities of Foreignness and Outsidership as they strategically and systematically went about its global expansion. The company’s Business Diplomacy strategy ensured that it was prepared to immediately respond to circumstances when new business opportunities presented themselves.

During the launch of its first commercial aircraft in the United States, President Carter signed the 1978 Airline Deregulation Act, the most revolutionary change in American air travel through modern day. Embracer was well positioned and ready to respond to the legislation, promoting this new aircraft as the right plane for rapidly changing times, particularly as airlines
were now able to begin exchanging frequency for aircraft size and many of the quickly emerging regional airlines pounced on the new import making it an overnight success for the company. While the two were not coordinated or linked in any way, Embraer was able to quickly capitalize on the turn of events.

From sales to support, Embraer’s Business Diplomacy model is holistic in its approach to clients. Once a sufficient market share was attained, the company would strategically expand its market footprint in the region where the aircraft were flying with technological and system support, engraining itself within the aviation community and further validating its ability to support a “foreign” aircraft on home soil. This strategic approach would ensure avoidance of the Liability of Foreignness and provide strong validation for Embraer’s products around the world.

Additionally, Embraer could be used as the poster child for the Uppsala Internationalization Model, having followed all four steps in its strategic pattern of growth and expansion around the world. Gradually increasing their market presence, from exporting to sales subsidiaries to foreign production and manufacturing, Embraer’s strategic progress also ensured that the company avoided the Liability of Outsidership as well by minimizing uncertainty by establishing a business network of relationships built on trust and commitment, making Embraer a true insider in the aviation community.

Throughout its history, from the Americas to Europe and beyond, Embraer’s approach to Business Diplomacy through its corporate governance has been strategic and methodical, paving the way for continued growth. So with all the success that Embraer had had, including reinventing itself to ward off total collapse, what happened in China? How did Embraer so misjudge this “major market” it was confident it could succeed in?
6.  CHINA: EMBRAER’S BUSINESS DIPLOMACY CHALLENGE

From its founding, Embraer has always been a leading innovative aerospace company, building upon the success of each aircraft with more advanced technology and allowing for a gain in market share with each new product. This was the case when it unveiled the ERJ-145. Introduced as the first jet-engine aircraft from Embraer, airlines around the world, knowing the strong reputation of the company, welcomed this new game-changing competitor, which also included strong support from carriers in the United States including American and Continental who based their regional jet fleets on the aircraft type.

As time progressed, and new more fuel-efficient entrants to the market were introduced, including the 1999 announcement of the revolutionary Embraer 170 family of jets, interest in the less economical and less fuel-efficient ERJ-145 started to wane. Yet when time came to establish a presence in China in the early 2000s, it was this aircraft that Embraer chose to introduce into commercial production, a regional jet that didn’t fully fit with the emerging commercial aviation market conditions.

While it can be argued and understood that Embraer chose the less advanced ERJ145 over the E170 family of jets out of concern for China’s demand for “shared” technology of any aircraft manufactured in the country, the same cannot be said for its corporate governance structure and the decisions that were made when it entered the Chinese aviation market. Embraer’s own history in the commercial aviation market combined with the Chinese desire for modern technology should have been a strong warning to the company that a less advanced airframe would yield less-than-enthusiastic results, but the company chose to gamble on the untapped potential of the Chinese commercial aviation market with the ERJ-145 and lost.
It is important to note that Embraer was not the first aircraft manufacturer to try to build commercial aircraft in China. Boeing and Airbus had both attempted to collaborate with government-supported business but were unsuccessful. With the central government of China holding tight control over the aerospace industry, foreign manufacturers wanting to build jets in China are required by law to share technology and engage local firms in production of aircraft as well as parts.

The now Boeing-merged McDonnell Douglas Aircraft Corporation was successful in building a small production run of the narrow body MD-83 jets in China, but only because they were willing to share the technology with the Chinese, a decision for which it would pay a great price back home in the United States with sales and its reputation. One only needs to look at the COMAC (Chinese Aircraft Manufacturing Company) ARJ21 aircraft to see where that technology went. The commonalities of design between the MD-83 and ARJ21 are significant and other than slight modifications in design, the two aircraft could be mistaken for each other.

In the late 1990s, Fairchild Dornier unsuccessfully attempted to enter the Chinese market because it was unwilling to collaborate with government-supported manufacturers in establishing a local assembly line and pursue joint developments with Chinese companies. (Lazzarini & Bourgeois, 2008)

Embraer saw in the post-9/11 economic recovery, that the Asia-Pacific market was rebounding the fastest, with China exhibiting the largest potential for growth in air travel, with very strong forecasts for expansion. The growth of the market didn’t advance into regional aviation however, where operation of 30- to 120-seat aircraft of the three major air carriers, all controlled by the central government, only made up 7% of air travel in China. The privately controlled airlines in China made up only 4% of the market and were challenged by a
government that wasn’t eager to diversify the market and created numerous roadblocks for expansion. This should have been another warning sign to Embraer’s Corporate Governance, that in China, if the government doesn’t support it, odds are it will not happen or it will be a challenge for it to succeed. (Blair, 1995)

Despite the challenges, Embraer saw the commercial market in China as an underdeveloped opportunity in the regional category and aggressively tried to capitalize on this. But after a quick start and “a decade-long investment in China’s commercial aviation market [that] resulted in a fleet of [only] 120 commercial jets in service,” a poor production rate of only one aircraft a month over ten years, Embraer had to acknowledge that the financial investment and required technology-sharing had not produced the results the company had anticipated. (Embraer Sees, 2014)

Embraer’s Corporate Governance failed in its assumption that the ERJ-145 would be an acceptable airframe for regional airlines in China. It missed the mark by not “looking in the mirror” to see what was happening within the company back home in Brazil. The ERJ-145 production lines were slowing down due to decreasing demand for the airframe over the newer Embraer 170 model In fact, the company would eventually turn over the production line altogether in favor of its own new Legacy executive jets, which is built on the same platform as the commercial variant of the ERJ-145.

Had the Corporate Governance of Embraer looked at the commercial aviation market trends in China with the same strategic vision it did for its product line in Brazil, or considered the potential of the executive jet market in China as it was exploring the category for itself, the possibility exists that their achievements in building executive jets in China would have been their initial success and the company could have avoided the pitfalls of trying to manufacture an
out-of-date commercial regional jet in a country where strict government controls were also hindering expansion of private airlines. (Bonelli & Pinheiro, 2012)

The failure of Embraer’s commercial jet venture in China, the first major setback for the company since it was privatized, highlights the complexities that can come with Business Diplomacy and its importance to a company’s success. Embraer’s rush to capitalize on the emerging market in China broke every strategic rule they had followed previously with their Business Diplomacy strategy. While partnering with Chinese companies may have provided Embraer with legitimacy in the host country, it still suffered from the Liability of Foreignness.

In this case, one “additional cost” was the language barrier between Brazilian and Chinese workers on the production line, requiring gestures to replace language in an environment where a plurality of managers were Brazilian and the workforce was entirely Chinese. The cultural differences of their respective approach to the work environment also caused challenges previously unknown to Embraer both in Brazil and in other European-styled markets. These unfamiliarity hazards would be compounded when Embraer broke from its own history of an Uppsala Model-type strategy that incorporated slow and incremental growth in a new market.

While the Chinese government perhaps left Embraer no choice when it raised the tariffs on aircraft imports, as has been previously discussed, the company chose the quick path to market entry to remain viable in the commercial sector versus pausing to take a step back to consider alternative ideas such as executive jets. So while Embraer entered China with the blessing of the government, the fates conspired against the company relegating it to “stranger in a strange land” status. (Eden & Miller, 2001)
It could easily be argued that Embraer failed in China simply because it didn’t follow the current, established tenets of Business Diplomacy. The company ignored the Uppsala Model and became subject to the Liability of Foreignness and the Liability of Outsidership. As Johanson and Vahlne stated, “the traditional view of entry [into a market] – that is, overcoming various barriers – is becoming less important than internationalizing undertaken to strengthen a firm’s position in the network.” (2009) They went on to state that the globalization of business is causing corporate challenges and advantages to be “less a matter of country-specificity and more one of relationship-specificity and network-specificity.” (2009)

Today’s model of Business Diplomacy focuses on the importance of the corporation as the hub of relationships and networks that determine success or failure in a new market. However, this same model fails to address the “hub” itself – namely the responsibility of the corporation to achieve the desired outcomes. Beyond the network of relationships, Corporate Governance plays a significant role in the expansion of a corporation into new markets. Company leadership must study and analyze market history, understand the influence of society and the impact of the law. They must align corporate objectives with market opportunity while simultaneously adhering to ethical guidelines and ensuring that decisions aren’t being made simply because it worked somewhere else.

By adhering to these principles, a corporation can avoid the Liability of Governance, which for today’s model of Business Diplomacy is just as critical as relationships and networks within the targeted foreign market.

In the case of Embraer and China, avoiding the Liability of Governance could have positively impacted the outcome of the partnership and potentially avoided the initial failures that the company experienced. It is clear that one of the biggest challenges Embraer faced was the
concern over sharing technology and what it was and was not willing to give away. While the company had established its ethical screen, it differed from that of their Chinese counterparts, and the friction between the two was challenging.

Throughout Embraer’s history, the aerospace manufacturer has been incredibly strategic and thoughtful in mapping out its global expansion, yet when it came to China, there was a “gold rush” mentality to be the first to take advantage of this new growing market. Simple issues that should have been factored into their planning when entering China seem to have been overlooked or ignored. These included the declining global market interest in the ERJ-145, the increasing interest in the company’s executive jets and the rising upper class in China that was beginning to acquire them. Embraer failed to study the dismal history of other manufacturers who had attempted to partner with China and attempted to apply an accelerated version of their successful Business Diplomacy model, only to have it implode in Harbin.

Embraer was successful in building platforms in other countries such as the United States, but that strategy didn't work in China. It's critical that a company ensure that its business model is localized for the market it wishes to enter, and then ensure that that target-specific product or service will be of interest to the market. While Embraer was able to eventually repurpose the Harbin production line successfully for the executive jet market, it is not difficult to imagine the potential for success if they had avoided the Liability of Governance.
7. LIABILITY OF GOVERNANCE

When a company begins global expansion, there are factors that must be included in its planning. Understanding the country system it is attempting to penetrate, from socio-economic and political perspectives, to corporate governance within the country by “home” companies, to the communities it will attempt to become a part of, it is crucial that an expanding corporation factor in the tenets of Business Diplomacy into their model for expansion and success.

As previously examined, the Liability of Foreignness and Liability of Outsidership can hinder expansion if not included in overall strategic planning, but there is another aspect not previously examined, that can also hinder this effort. As was seen in the example of the Embraer entrance into China, the potential liabilities to a company that are not just external, but internal to their corporate governance.

This is not to be confused with what was previously defined as Corporate Diplomacy, which again, is the work undertaken by a company to ensure the foreign policies and procedures enacted are overseen properly within the company headquarters as well as its country offices by a structured organization of corporate diplomats whose job it is to ensure that the multinational structures are working. (Blair, 1995)

While Liability of Foreignness and Liability of Outsidership work to focus on the relationships between a company with the external stakeholders in the foreign market, the Liability of Governance focuses on the other mitigating factors that must be applied to be successful in the application of Business Diplomacy.

When the term ‘Governance’ is considered, it is understood to incorporate the entire set of legal, cultural and institutional components that make up the functioning of a corporation. (Blair, 1995) It is the process and practice “by which a company is directed and controlled...[it] essentially involves balancing the interests of the many stakeholders [involved] in a company –
these include its shareholders, management, customers, suppliers, financiers, government and community.” (Corporate Governance) Because Corporate Governance is responsible for the framework for all corporate objectives, it includes all management aspects, from action plans to performance measurement and disclosure. (Blair, 1995)

When a corporation is planning to expand into new markets and is developing its Business Diplomacy strategic plan, it must not only look at the ability to network and engage within the country, but understand the law and challenges related to things like environment, labor practices, education and human rights. It must also “balance their fiduciary responsibility to shareholders in highly competitive marketplace with considerations that include their own corporate and moral values, their roles in strengthening the society around them, and the rewards and risks to their reputation.” (Garten, 2002) It is critical for a corporation looking to expand into new markets understand that to develop a modern Business Diplomacy must include taking the necessary steps to avoid the Liability of Governance

7.1. UNDERSTAND YOUR ETHICAL SCREEN

In today’s corporate world, it is hard to talk about governance without ethics. Not only is there an ethical decision on when and where to invest, it is also important to understand that every company (and stakeholder) goes in seeking something different and with a different set of values. Leadership must look beyond the company’s own selfinterest and learn what is important to those within the foreign market it wants to enter. Having an ethical screen established for the company will help guide Corporate Governance in diverse markets, especially those that may operate under a different set of principles than the company or its home country.
7.2. INVEST IN KNOWING THE MARKET HISTORY & THE BUSINESS ENVIRONMENT

Study the history of competitors in the foreign market you are seeking to enter as well as examine the historical business trends and challenges of similar businesses from your home country. This will allow corporate leadership to better understand the challenges it will face. Understand from the perspective of others the historical track of the market, customer behaviors and habits. Knowing what was or is important can help define how you approach your business and how you approach consumers, and at the core influence how you create the strategy behind going into the market. Understanding the benchmark of history of the market one intends to enter is critical when looking to establish a strategic plan for success especially given that roots of customer behavior are often embedded in culture heritage.

It is also important to note that the historical challenges differ from precedence, which is normally associated with traditional statecraft. Historical challenges refer to the importance for a company to be strategic in looking back to compile a history of practice. History matters, and the implementation of Business Diplomacy must incorporate the historical perspectives of how the market has operated in the past, which can provide clues on how it will operate in the future. This “what if…” factor can help planning to avoid the mistakes others have and have not made in the same market or business category.

7.3. BE A STUDENT OF ANTHROPOLOGY & JURISPRUDENCE

Entering a new market also means studying and learning about the institutional and legal environment of the country. Each country’s legal system and local cultural standards are different. As part of examining the market history & business environment outcomes, corporate executives must examine the influence of society and the courts on the market and what
implications could come from their actions and what their reaction could be to your business initiatives within the country.

7.4. BUILD YOUR OWN “EMBASSY”

Embassies around the world today are not created from a cookie-cutter design, but are created based on the dynamics and priorities of the country. For example, an Embassy established in Pristina, Kosovo would not be identical to one established in Juba, South Sudan and neither would identically reflect the make-up of an Embassy in Ottawa, Canada. Why? Because each host country comes with a unique set of circumstances and staffing of an embassy will reflect those country-specific priorities.

Similarly, when a corporation enters a new market, the company must look at the country as a unique market segment. A purpose-built Business Diplomacy strategy must be tailored to specific business outcomes as well as the political landscape and cultural make-up of the country. It's not Corporate Social Responsibility when a country establishes an Embassy, it's a strategic and organizational investment in the priorities of both nations, and corporations must use similar diplomatic tactics as they approach a foreign market. Whether a nation or a corporation, building your own “Embassy” defines your purpose for being there and ensures your priorities reflect the outcomes you seek to achieve.

This is also where Business Diplomacy and Corporate Diplomacy align in a strategic plan. Ensuring a strong relationship within the market as well as with corporate headquarters in the home country. These corporate diplomats, as described by Saner and Yiu, “make multinational structures work, as liaison persons…experienced in living and functioning in various foreign cultures.” (2003)
7.5. DON'T LET YOUR STRENGTHS BECOME YOUR NEW WEAKNESS

A company that wants to avoid the Liability of Governance must invest in Diplomatic Thought. As a business, it is important to think about segmentation, where you belongs and where the market valuation is for your company. What is done elsewhere successfully does not mean it will necessarily do well in a new market. It is important for a company looking to expand into new markets to strategically invest in its own "opposition research," or in other words, figure out not only how will your business model will work, but also how the model will not work in a specific market and ensure that your Business Diplomacy plan addresses and overcomes those challenges.

8. CONCLUSION

Throughout history, diplomacy and business have been intertwined, and no more so than in modern day international business, which serves as the fulcrum for political influence, social and environmental responsibility and where various stakeholders that have significant influence in contemporary international relations operate. (Muldoon, 2005) To successfully navigate these challenges, especially in emerging economies, a company must now factor in more than just the “bottom line” and address complex issues that include human rights differences, environmental regulations, labor rights and the values of each country. (Henisz, 2014) To guide the ship of business through these challenges, it is imperative that a global corporation integrates Business Diplomacy into its strategic planning to successfully overcome the liabilities that come with operating in a foreign market. The Liability of Foreignness or the costs for doing business abroad that a local firm would not incur, results in a competitive disadvantage for the foreign corporation. (Zaheer, 1995) The Liability of Outsidership pertains to the lack of relevant
networks within a foreign market and that if established, can be used to help a company succeed, and that the strength of this network can be used as the benchmark by which firms (and others) measure success and failure. (Schweizer, 2012)

In addition to these external liabilities, the successful implementation of a modern Business Diplomacy strategy includes the mitigation of internal corporate challenges that can help avoid the Liability of Governance. This open-door style of corporate analysis, where the company is not closed off from ideas and reflection, provides the ability for corporate executives, managers and subject-matter experts to portend future success or failure by analyzing past actions and the results of those actions by other companies operating in the foreign market with similar product offerings.

Whether an aircraft manufacturer or a food distributor, incorporating the tenants to avoid the Liability of Governance can create a comprehensive strategic vision that will serve as a link between Business Diplomacy, strategic planning and corporate governance established under a socio-political-economic-and historical framework. It is from this new vantage point that global corporations can also more effectively validate the focus of a stronger strategic plan that factors in all of the perspectives required when looking to enter a new foreign market. (Ruel, 2012)

Business Diplomacy remains a relatively new and emerging discipline that will continue to mature and grow in stature and influence in the years ahead, and it will benefit from additional inquiry and research from an applied perspective. As the globalization of business continues to shrink distance between foreign markets for corporations, new business practices will continue to emerge and evolve. But it is the application of Business Diplomacy, while also continuing to evolve, that can and will be the guiding force for these companies as long as they take the time to employ it and respect the value that can be achieved from its application.
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