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Formulating and Implementing Strategy for International and Global Operations

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Formulating Strategy



OUTLINE

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OBJECTIVES

1. To understand why companies engage in international business.
2. To learn the steps in global strategic planning and the models available to direct the analysis and decision making involved.
3. To appreciate the techniques of environmental assessment and internal and competitive analysis, and how those results can be used to judge the relative opportunities and threats to be considered in international strategic plans.

4. To become familiar with strategic planning for emerging markets.
5. To profile the types of strategies available to international managers—both on a global level and on the level of specific entry strategies for different markets.
6. To gain insight into the issues managers face when strategic planning for global e-business.

OPENING PROFILE: GLOBAL COMPANIES TAKE ADVANTAGE OF OPPORTUNITIES IN SOUTH AFRICA

Global companies with a presence in South Africa all cite numerous advantages for setting up shop in the country, from low labor costs to excellent infrastructure—and a base to export products internationally. Jim Myers, president of the American Chamber of Commerce in South Africa, says that nearly 50% of the chamber's members are Fortune 500 companies, and that over 90% operate beyond South Africa's borders into southern Africa, sub-Saharan Africa, and across the continent. "The sophisticated business environment of South Africa provides a powerful strategic export and manufacturing platform for achieving global competitive advantage, cost reductions and new market access," says Myers.¹

Businesses are taking advantage of opportunities because of the legal protection of property, high labor productivity, low tax rates, reasonable regulation, a low level of corruption, and good access to credit, all of which were seen as factors contributing to the country's investment climate. Threats include the low level of skills and education of workers, labor regulation, exchange rate instability, and crime. Nevertheless, the business environment is favorable.

Following are some examples of the many global companies taking advantage of the opportunities and incentives in South Africa.² In addition, The 2010 FIFA World Cup generated huge opportunities for businesses, especially emerging entrepreneurs, in South Africa's tourism industry.

ACER AFRICA

In 1995, Acer Africa acquired ownership of a locally based company they had been working with to distribute peripherals and printers since 1980.

MAP 6.1 South Africa has a population of 50.58 million and consists of 1,221,037 sq. km.



(Continued)

MAP 6.2 Africa



Source for maps: https://www.cia.gov/library/publications/the-world-factbook/maps/maptemplate_sf.html

As a leading international PC manufacturer and vendor, Acer recognized the wealth of opportunities in South Africa as local IT companies rapidly came abreast of world standards following the country's first democratic elections in 1994.

For Acer, South Africa's modern banking and telephone systems and exceptional water and power rates made the country a sound business location.

Acer Africa was established as a base to export to the Southern African Development Community (SADC), Angola, and the islands along the Indian Ocean.

"South Africa is the only port of entry to Africa, the only place that one would be able to succeed . . ." —Peter Ibbotson (Acer Africa)

ALCATEL

"Alcatel has built its worldwide reputation on its production. Investing with local partners [electronics group Altech and black empowerment company Rethabile] in South Africa has meant that we have

demanded a high standard of technology and capability, and believe that in many respects South Africa compares very favourably with the most advanced countries in the world.” —*Bernard Vaslin, executive vice president, Alcatel*

GENERAL ELECTRIC

“The re-entry of General Electric (USA) to the South and southern African market has been exciting and has well exceeded our operating plan expectations.

“South Africa’s excellent infrastructure, together with first-class financial, legal and commercial systems, makes this country a natural location to pursue the significant opportunities of South and southern Africa.

“The friendly business environment ensures that we can run our business efficiently, and we look forward to successful and profitable operations in southern Africa that meet our global goals and create wealth for the GE shareholder.” —*GE South Africa president Michael C. Hendry*

Source: www.southafrica.info, used with permission.

As the opening profile on South Africa illustrates, companies continue to look for opportunities around the world in search of profitable new markets, outsourcing facilities, acquisitions, and alliances—and this search is increasingly directed at emerging markets.

However, the recent economic slowdown caused many companies to retrench rather than expand in order to conserve cash flow in the economic slowdown. Thus, while much of the focus in this chapter is on “going international” and expansion abroad, we need to keep in mind that retrenchment is also a very real strategy, especially in difficult economic times. However, the long-term trend is clear. After the Boston Consulting Group identified 100 emerging-market companies that they felt have the potential to reach the top rank of global corporations in their industries, *BusinessWeek* challenged that:

*Multinationals from China, India, Brazil, Russia, and even Egypt are coming on strong. They’re hungry—and want your customers. They’re changing the global game.*³

Management consultant Ram Charan advises that we are now truly in a global game, one that he calls a “seismic change” to the competitive landscape brought about by globalization and the Internet. This first wave of emerging-nation players, he says, are taking advantage of three forces spurred on by the Internet—mobility of talent, mobility of capital, and mobility of knowledge. The strategies of companies such as America Movil of Mexico, China Mobile, Petrobras of Brazil, and Mahindra and Mahindra of India (which is penetrating Deere’s market on its own U.S. turf) are to use their bases in their emerging markets—from which they have had to eke out meager profits—as “springboards to build global empires.”⁴ Add these new challengers to the already hyper-competitive arena of global players, and it is clear that managers need to pay close and constant attention to strategic planning. *BusinessWeek* gives an example of two global companies, challenging us to decide which is more “American”:

*Mumbai-based Tata Consultancy Services (TCS), or Armonk (New York)-based IBM? Evaluate the two based on where they make their sales, and the answer is surprising. TCS, India’s largest tech-services company, collected 51 percent of its revenues in North America the first quarter of 2008, while 65 percent of IBM’s were overseas.*⁵

As it will be explained in this chapter, however, corporate strategies must change in response to shifting global economic conditions and other environmental and competitive factors. With continuing economic challenges in the U.S. and Europe, TCS must consider how it will respond, but it is strengthened by its geographic diversification. IBM, meanwhile, now making about half its revenues in its services business—in particular in emerging markets—has diversified with a two-track approach. The company is helping clients in the U.S. to cut costs, and in emerging markets, it helps customers develop their technology infrastructure.⁶ These are examples of corporate strategies that are being developed to respond to or anticipate current global trends, as

noted by Beinhocker et al. of McKinsey & Company and discussed in various chapters throughout this book. They note that:

Companies' strategic behavior should be tied closely to ten important trends: strains on natural resources, a damper on globalization, the loss of trust in business, the growing role of government, investment in quantitative decision tools, shifting patterns of global consumption, the economic rise of Asia, industry structure upheaval, technological innovation, and price instability.⁷

Because international opportunities are far more complex than those in domestic markets, managers must plan carefully—that is, strategically—to benefit from them. Many experienced managers are wary about expanding into politically risky areas or those countries where they find government practices to be prohibitive.

The process by which a firm's managers evaluate the future prospects of the firm and decide on appropriate strategies to achieve long-term objectives is called **strategic planning**. The basic means by which the company competes—its choice of business or businesses in which to operate and the ways in which it differentiates itself from its competitors—is its **strategy**. Almost all successful companies engage in long-range strategic planning, and those with a global orientation position themselves to take full advantage of worldwide trends and opportunities. Multinational Enterprises (MNEs), in particular, report that strategic planning is essential both to contend with increasing global competition and to coordinate their far-flung operations.

In reality, however, that rational strategic planning is often tempered, or changed at some point, by a more incremental, sometimes messy, process of strategic decision-making by some managers. When a new CEO is hired, for example, she or he will often call for a radical change in strategy. That is why new leaders are carefully chosen, on the basis of what they are expected to do. So, although the rational strategic planning process is presented in this text because it is usually the ideal, inclusive method of determining long-term plans, managers must remember that people are making decisions, and their own personal judgments, experiences, and motivations will shape the ultimate strategic direction.

REASONS FOR GOING INTERNATIONAL

Companies of all sizes “go international” for different reasons—some reactive (or defensive), and some proactive (or aggressive). The threat of their own decreased competitiveness is the overriding reason many large companies adopt an aggressive global strategy. To remain competitive, these companies want to move fast to build strong positions in key world markets with products or services tailored to the needs of increasingly global and diverse sets of customers.

Reactive Reasons

GLOBALIZATION OF COMPETITORS

One of the most common reactive reasons that prompts a company to go overseas is global competition. If left unchallenged, competitors who already have overseas operations or investments may get so entrenched in foreign markets that it becomes difficult for other companies to enter at a later time. In addition, the lower costs and market power available to these competitors operating globally may also give them an advantage domestically. Nor is this global perspective limited to industries with tangible products. Following the global expansion of banking, insurance, credit cards, and other financial services, financial exchanges have been going global by buying or forming partnerships with exchanges in other countries, their strategies facilitated by advances in technology.⁸

Strategic moves by competing global giants prompt countermoves by other firms in the industry in order to solidify and expand their global presence. Such was the case after the Pfizer takeover of Wyeth in January 2009; Pfizer, the world's biggest drug maker, bid \$68 billion for Wyeth. Subsequently, Roche, the Swiss pharmaceutical company, paid \$46.8 billion to acquire the biotechnology company Genentech, in which it already owned a majority stake. Not to be outdone, Merck, the American pharmaceutical giant, announced in March 2009 that it would pay

\$41 billion to acquire its rival Schering-Plough—the combined company to keep the Merck name. Clearly, Merck will benefit from the worldwide reach of Schering-Plough, which generates about 70 percent of its sales outside of the United States, including more than \$2 billion per year from emerging markets. Mr. Clark, Merck's CEO, stated that

*We are creating a strong, global health care leader built for sustainable growth and success. The combined company will benefit from a formidable research and development pipeline, a significantly broader portfolio of medicines and an expanded presence in key international markets, particularly in high-growth emerging markets.*⁹

TRADE BARRIERS

Although trade barriers have been lessened in recent years as a result of trade agreements that have led to increased exports, some countries' restrictive trade barriers do provide another reactive reason for companies often switching from exporting to overseas manufacturing. Barriers such as tariffs, quotas, buy-local policies, and other restrictive trade practices can make exports to foreign markets too expensive and too impractical to be competitive. Toyota, for example, has manufacturing plants in the United States in order to circumvent import quotas. In May 2011, for example, ZTE—China's second largest telecom equipment maker and a state-controlled company listed in Hong Kong—moved to Brazil; the purpose was to avoid that country's high import tariffs, even though it is cheaper to manufacture in China.¹⁰

REGULATIONS AND RESTRICTIONS

Similarly, regulations and restrictions by a firm's home government may become so expensive that companies will seek out less restrictive foreign operating environments. Avoiding such regulations prompted U.S. pharmaceutical maker SmithKline and Britain's Beecham to merge. Both thereby guaranteed that they would avoid licensing and regulatory hassles in their largest markets: Western Europe and the United States. The merged company is now an insider in both Europe and America.

CUSTOMER DEMANDS

Operations in foreign countries frequently start as a response to customer demands or as a solution to logistical problems. Certain foreign customers, for example, may demand that their supplying company operate in their local region so that they have better control over their supplies, forcing the supplier to comply or lose the business. McDonald's is one company that asks its domestic suppliers to follow it to foreign ventures. Meat supplier OSI Industries does just that, with joint ventures in 17 countries, such as Germany, so that it can work with local companies making McDonald's hamburgers.

Proactive Reasons

*Many more companies are using their bases in the developing world as springboards to build global empires, such as Mexican cement giant Cemex, Indian drugmaker Ranbaxy, and Russia's Lukoil, which has hundreds of gas stations in New Jersey and Pennsylvania.*¹¹

ECONOMIES OF SCALE

Careful, long-term strategic planning encourages firms to go international for proactive reasons. One pressing reason for many large firms to expand overseas is to seek economies of scale—that is, to achieve world-scale volume to make the fullest use of modern capital-intensive manufacturing equipment and to amortize staggering research and development costs when facing brief product life cycles.¹² The high costs of research and development, such as in the pharmaceutical industry (for example, Merck and Pfizer), along with the cost of keeping up with new technologies, can often be recouped only through global sales.

GROWTH OPPORTUNITIES

*According to the Small Business Administration (SBA), 96 percent of the world's customers live outside the United States, and two thirds of the world's purchasing power is in foreign countries.*¹³

Clearly there are vast opportunities for small businesses—those with fewer than 500 workers—to do business overseas. In fact, as of 2011, small businesses accounted for about 30% of total export revenue, or about \$500 billion in annual sales. “Still, only about 1% of the nation’s roughly 30 million small businesses sell overseas, according to U.S. Census data. Those that do usually work with no more than one foreign market—typically Canada, Mexico, the United Kingdom, Germany or China, Census data show.”¹⁴ As domestic growth declines because of slow-growth economies, opportunities abroad look more attractive, in particular since the Internet now greatly facilitates the ability to quickly link to contacts in other countries. New start-ups in Europe, for example, feeling the weight of the continent’s continuing debt crisis, realize that they must go global from the beginning to establish sufficient market size to be viable. Indeed, most European entrepreneurs and managers are well equipped personally to go global because they are accustomed to moving easily among different languages and customers. This is particularly true of Internet-based companies such as audio-sharing Web service SoundCloud, cofounded in Stockholm by Alex Ljung, a multilingual entrepreneur, who observed that:

“It was obvious that our business had to be global from the start. We’re more like citizens of the Internet than citizens of a country.”

“COMPANIES BORN IN EUROPE, BUT BASED ON THE PLANET,” WWW.NYTIMES.COM,
JUNE 12, 2012.¹⁵

Whatever their size, companies in mature markets in developed countries experience a growth imperative to look for new opportunities in emerging markets. In an effort to continue its long-term strategy to expand into China—with its 1.3 billion consumers—Nestle, the Swiss food giant, announced on July 11, 2011 that it had agreed to pay \$1.7 billion for a 60 percent stake in Hsu Fu Chi, a big Chinese confectioner, in one of the biggest deals ever by a foreign company in China. The founding Hsu family eventually retained 40 percent, and Hsu Chen, current CEO, heads the joint venture.¹⁶ And in March 2012, United Parcel Service (UPS) reached an agreement to acquire TNT Express, a Dutch shipping company, for 5.2 billion euro, or \$6.8 billion, in order to increase market share in Europe and provide growth opportunities in China. UPS stated that “The additional capabilities and broadened global footprint will support the growth and globalization of our customers’ businesses.”¹⁷

Cemex, the Mexican cement giant, has been one company aggressively taking advantage of growth opportunities through acquisitions. After learning his family’s business from the bottom up for eighteen years, Lorenzo Zambrano became CEO and started his gutsy expansion into world markets. His strategy has been to acquire foreign companies, allow time to integrate them into Cemex and pay off the debt, and then look for the next acquisition. In 2009, however, environmental factors forced strategic changes, as discussed in the accompanying Management in Action feature, causing Mr. Zambrano to reflect in 2011 on how he has enacted his strategies and to wonder about the future.

RESOURCE ACCESS AND COST SAVINGS

Resource access and cost savings entice many companies to operate from overseas bases. The availability of raw materials and other resources offers both greater control over inputs and lower transportation costs. Lower labor costs (for production, service, and technical personnel)—another major consideration—lead to lower unit costs and have proved a vital ingredient to competitiveness for many companies.

Sometimes just the prospect of shifting production overseas improves competitiveness at home. When the Xerox Corporation started moving copier-rebuilding operations to Mexico, the U.S. union agreed to needed changes in work rules and productivity to keep the jobs at home. Lower operational costs in other areas—power, transportation, and financing—frequently prove attractive.

INCENTIVES

Governments in countries such as Poland seeking new infusions of capital, technology, and know-how willingly provide incentives—including tax exemptions, tax holidays, subsidies, loans, and the use of property. Because they both decrease risk and increase profits, these incentives are attractive to foreign companies. Russia, for example, has a number of special economic zones,



*The turnabout underscores a hard lesson of the financial crisis: For all the promise globalization holds for aggressive companies and executives, it carries hidden risks that can slam both operations and reputations.*¹⁹

*"I have to admit it: it was an error . . . this time we forgot to ask: 'what is the worst that can happen'."*²⁰

The Mexican cement giant Cemex is based in Monterrey and operates in more than 50 countries. The company continued its global expansion when it made an unsolicited bid of \$12.8 billion for the Rinker Group of Australia, a group with considerable U.S. interests. The Rinker Group accepted a revised \$14.25 billion acquisition by Cemex in 2007. The deal created one of the world's largest construction materials companies, and looked sure to strengthen Cemex's leading position in the American housing market, particularly in Sun Belt states like Florida and Arizona. Eighty percent of Rinker's sales come from the United States. However, the deal increased Cemex's gross debt from about \$4 billion to \$19.1 billion—crucially, by using short-term loans.

Cemex's acquisition of the Rinker Group was the largest ever by a Mexican company. Over the prior 15 years, Cemex's chairman, Lorenzo Zambrano, had transformed his company into a multinational company with operations on five continents and \$21 billion in revenue, earning him the reputation as a leader in the push for globalization. He was undoubtedly a role model by creating Mexico's first multinational company with operations on five continents, starting from a small local company.²¹

The global cement and construction materials industry has been slowly consolidating as giants such as Lafarge of France, Holcim of Switzerland, and Cemex have sought to grow through acquisitions.

After taking over 23 years ago at a business co-founded by his grandfather, Mr. Zambrano pushed into country after country with daring acquisitions. Mr. Zambrano, a graduate of Stanford Business School, has been aggressive in expanding Cemex's global presence by taking on billions in debt to expand first in Spain, then in Latin America and the United States. Zambrano's acquisitions in Europe helped the company learn about efficiencies in managing inventory and dealing with clients in other countries.

Cemex became the world's largest producer of ready-mix concrete in 2005 when it bought RMC of Britain for \$5.8 billion, giving it a strong presence in Europe. Zambrano also invested heavily in high technology, allowing managers at its Monterrey headquarters in northern Mexico to track global operations.

In 2009, however, the global economic downturn led to declining construction demand, notably in the United States, UK, and Spain. The construction industry stalled for residential and commercial projects, while the prospect for infrastructure projects awaited government spending to prime the economy in those countries.

With rising costs for crucial raw materials such as coal, heavy oil, and gas, the focus for Cemex in 2009 changed from expansion and acquisitions to cost-cutting and retrenchment. The company announced it would cut costs and jobs in its attempt to absorb the effects of the U.S. housing crisis and global market volatility. Added to its reduced sales, the company also suffered because of the weakness of the peso, which had fallen by more than 30 percent against the dollar since July 2008.

Confounding the problems for Cemex—as with many victims of the financial crisis—the company was not able to refinance a significant portion of its debt (estimated at between \$16 billion to \$20 billion). Emerging market companies across the board were falling prey to the perception of a higher risk in refinancing debt. In a rapid reversal of fortune, the company known for relentless expansion was forced into selling assets, negotiating with creditors, and cutting its work force and spending. However, the tightened credit market also reduced the price Cemex could get for selling its assets in Spain, Hungary, and Austria.

It is unfortunate that the ill-timed takeover of the Rinker group, along with the global financial crisis, has so negatively affected not only the Cemex company, but also the reputation of Mr. Zambrano. He had become corporate Mexico's informal ambassador to the world. Cemex gave other Latin American businesspeople the confidence to expand abroad. Mr. Zambrano was a philanthropist and arts patron, and he raised millions of dollars for a prominent university, El Instituto Tecnológico de Monterrey, from which he received an engineering degree. However, strategists may challenge whether Mr. Zambrano had sufficiently considered potential global threats that could cause such a rapid downturn in the company.

What is your opinion? Was the situation a result of a rare confluence of negative events, or was Mr. Zambrano insufficiently apprised and cautious about the risks in continuing expansion and debt burdens?

Update As of August 2011, Cemex had secured a \$15 billion restructuring deal, had cut 11 percent of its workforce worldwide, and halved it in Spain, and Mr. Zambrano was becoming more optimistic. Reflecting on all that had happened, he said "I had to hide my true feelings, you have to be brave and appear brave . . . It was a terrible time."²² Although this admission is contrary to Mexican culture for a leader, it did signal a change of direction within the company.

both for industrial production and for technical research, offering various tax concessions such as exemption from property and land taxes for the first five years, as well as customs privileges.²³

In February 2009, for example, companies were rushing to conclude M&A deals in Brazil while a tax break that allows companies to deduct 34 percent of the premium paid in an acquisition is still guaranteed, amid fears that it would be rescinded. This kind of tax incentive is rare, so it attracts considerable interest from foreign investors. Coupled with the recent devaluation of the Brazilian real—which made acquisitions cheaper for foreign bidders—tax deductions are currently one of the great attractions for acquisition deals in Brazil.²⁴ Nor are those incentives limited to emerging economies. The state of Alabama in the United States has spent hundreds of millions of dollars in incentives to attract the Honda, Hyundai, and Toyota plants.²⁵

STRATEGIC FORMULATION PROCESS

Typically, the strategic formulation process is necessary both at the headquarters of the corporation and at each of the subsidiaries. Most organizations operate on planning cycles of five or more years, with intermediate reviews. However, adjustments are frequently necessary to respond to changes in a dynamic global environment, in particular in rapidly changing industries such as those driven by technological developments.

The global strategic formulation process, as part of overall corporate strategic management, parallels the process followed in domestic companies. However, the variables, and therefore the process itself, are far more complex because of the greater difficulty in gaining accurate and timely information; the diversity of geographic locations; and the differences in political, legal, cultural, market, and financial processes. These factors introduce a greater level of risk in strategic decisions. However, for firms that have not yet engaged in international operations (as well as for those that do), an ongoing strategic planning process with a global orientation identifies potential opportunities for (1) appropriate market expansion, (2) increased profitability, and (3) new ventures by which the firm can exploit its strategic advantages. Even in the absence of immediate opportunities, monitoring the global environment for trends and competition is important for domestic planning.

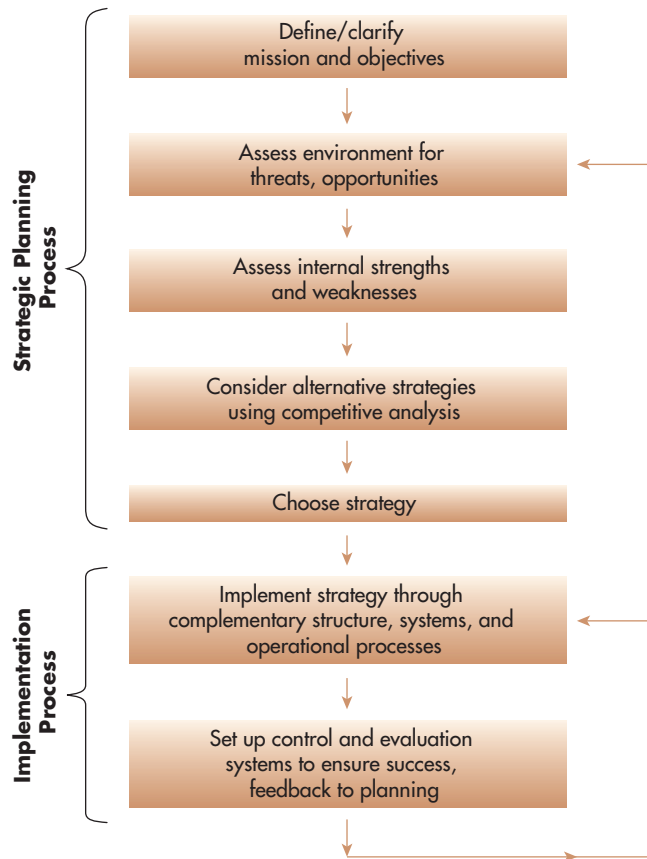
The strategic formulation process is part of the strategic management process in which most firms engage, either formally or informally. The planning modes range from a proactive, long-range format to a reactive, more seat-of-the-pants method, whereby the day-by-day decisions of key managers, in particular owner-managers, accumulate to what can be discerned retroactively as the new strategic direction.²⁶ The stages in the strategic management process are shown in Exhibit 6-1. In reality, these stages seldom follow such a linear format. Rather, the process is continuous and intertwined, with data and results from earlier stages providing information for the next stage.

The first phase of the strategic management process—the *planning phase*—starts with the company establishing (or clarifying) its mission and its overall objectives. The next two steps comprise an assessment of the external environment that the firm faces in the future and an analysis of the firm's relative capabilities to deal successfully with that environment. Strategic alternatives are then considered, and plans are made based on the strategic choice. These five steps constitute the planning phase, which will be further explained in this chapter.

The second part of the strategic management process is the *implementation phase*. Successful implementation requires the establishment of the structure, systems, and processes suitable to make the strategy work. These variables, as well as functional-level strategies, are explored in detail in the remaining chapters on strategic implementation, organizing, leading, and staffing. At this point, however, it is important to note that the strategic planning process by itself does not change the posture of the firm until the plans are implemented. In addition, feedback from the interim and long-term results of such implementation, along with continuous environmental monitoring, flows directly back into the planning process.

STEPS IN DEVELOPING INTERNATIONAL AND GLOBAL STRATEGIES

In the planning phase of strategic management—strategic formulation—managers need to carefully evaluate dynamic factors, as described in the stages that follow. However, as discussed earlier, managers seldom consecutively move through these phases; rather, changing events and variables prompt them to combine and reconsider their evaluations on an ongoing basis.

EXHIBIT 6-1 The Strategic Management Process

Step 1. Establish Mission and Objectives

The *mission* of an organization is its overall *raison d'être* or the function it performs in society. This mission charts the direction of the company and provides a basis for strategic decision making. It also conveys the cultural values that are important to the company, as contrasted in the following two mission statements:

SANYO (A Japanese Company)

*Corporate philosophy: to make products and services indispensable for people all over the world, offering a more enjoyable life. Digital technology and core competence (the source of our competitiveness) generate joy, excitement, and impact, a more comfortable life in harmony with the global environment.*²⁷

SIEMENS (A German Company)

*Success depends on success of our customers. We provide experience and solutions so they can achieve their objectives fast and effectively. We turn our people's imagination and best practices in successful technologies and products. This makes us a premium investment for our shareholders. Our ideas, technologies and activities help create a better world.*²⁸

While both mission statements indicate a focus on customers, Sanyo offers them a more enjoyable life, is more relationship-oriented, and emphasizes harmony and the environment, indicating a long-term focus, factors typical of Japanese culture. Siemens offers efficiency to its customers and a premium return to its shareholders; this mission statement is explicit and decisive, typical of German communication; this compares with the more descriptive and implicit statement given by Sanyo.²⁹

A company's overall *objectives* flow from its mission, and both guide the formulation of international corporate strategy. Because we are focusing on issues of international strategy, we

EXHIBIT 6-2 Global Corporate Objectives**Marketing**

Total company market share—worldwide, regional, national
 Annual percentage sales growth
 Annual percentage market share growth
 Coordination of regional markets for economies of scale

Production

Relative foreign versus domestic production volume
 Economies of scale through global production integration
 Quality and cost control
 Introduction of cost-efficient production methods

Finance

Effective financing of overseas subsidiaries or allies
 Taxation—globally minimizing tax burden
 Optimum capital structure
 Foreign-exchange management

Profitability

Long-term profit growth
 Return on investment, equity, and assets
 Annual rate of profit growth

Research and Development

Develop new products with global patents
 Develop proprietary production technologies
 Worldwide research and development labs

will assume that one of the overall objectives of the corporation is some form of international operation (or expansion). The objectives of the firm's international affiliates should also be part of the global corporate objectives. A firm's global objectives usually fall into the areas of marketing, profitability, finance, production, and research and development, among others, as shown in Exhibit 6-2. Goals for market volume and for profitability are usually set higher for international than for domestic operations because of the greater risk involved. In addition, financial objectives on the global level must take into account differing tax regulations in various countries and how to minimize overall losses from exchange rate fluctuations.

Step 2. Assess External Environment

After clarifying the corporate mission and objectives, the first major step in weighing international strategic options is the **environmental assessment**. This assessment includes environmental scanning and continuous monitoring to keep abreast of variables around the world that are pertinent to the firm and that have the potential to shape its future by posing new opportunities (or threats). Firms must adapt to their environment to survive. The focus of strategic planning is how to adapt.

The process of gathering information and forecasting relevant trends, competitive actions, and circumstances that will affect operations in geographic areas of potential interest is called **environmental scanning**. This activity should be conducted on three levels—global, regional, and national (discussed in detail later in this chapter). Scanning should focus on the future interests of the firm and should cover the major variables such as political and economic risk; major technological, legal, and physical constraints; and the global competitive arena, as well as the opportunities available in different countries. Some generalized areas of risk to consider are shown in Exhibit 6-3. As an example of nationalism, Wal-Mart and other retailers were given an unexpected set-back in December 2011, as discussed in the nearby Under the Lens section.

The firm can also choose varying levels of environmental scanning. To reduce risk in investments, many firms take on the role of the “follower,” meaning that they limit their own investigations. Instead, they simply watch their competitors' moves and go where they go, assuming that

EXHIBIT 6-3 Levels of Risk for Strategic Entry Scanning

the competitors have done their homework. Other firms go to considerable lengths to carefully gather data and examine options in the global arena.

Ideally, the firm should conduct global environmental analysis on three different levels: multinational, regional, and national. Analysis on the multinational level provides a broad assessment of significant worldwide trends—through identification, forecasting, and monitoring activities. These trends would include the political and economic developments of nations around the world, as well as global technological progress. From this information, managers can choose certain appropriate regions of the world to consider further.

Next, at the regional level, the analysis focuses in more detail on critical environmental factors to identify opportunities (and risks) for marketing the company's products, services, or technology. For example, one such regional location ripe for investigation by a firm seeking new markets is Asia.

Having zeroed in on one or more regions, the firm must, as its next step, analyze at the national level. Such an analysis explores in depth specific countries within the desired region for economic, legal, political, and cultural factors significant to the company. For example, the analysis could focus on the size and nature of the market, along with any possible operational problems, to consider how best to enter the market. In many volatile countries, continuous monitoring of such environmental factors is a vital part of ongoing strategic planning. Another important factor that must be considered in the environmental assessment at all levels is that of how institutions might affect potential opportunities to compete.

INSTITUTIONAL EFFECTS ON INTERNATIONAL COMPETITION³⁰

Various institutions can create opportunities or constraints for firms considering entry into specific global markets. Recently, researchers such as Peng have argued that "... firm strategies and performance are, to a large degree, determined by institutions popularly known as the 'rules of the game' in a society."³¹ Institutions include both those formal institutions that promulgate laws,



UNDER THE LENS

India Says No to Foreign Ownership of Supermarkets³²

On Wednesday, Finance Minister Pranab Mukherjee said the decision to allow 51% foreign direct investment in multi-brand retail, as it's called here, was suspended pending "consultations among various stakeholders."

Mumbai (MarketWatch), December 7, 2011.

The decision followed fierce opposition to a proposal granting to foreign "big-box" supermarkets such as Wal-Mart Stores, Inc. unfettered access to India's \$450 billion retail consumer market. The reversal was ruled only a short time after the November 24 approval of the foreign retail measure by Mr. Singh's cabinet; the measure had been widely welcomed by business groups as a bold reform that would benefit consumers and farmers while providing a much-needed jolt to the Indian economy. Opposition parties had condemned the proposal as a direct threat to millions of small businesses across India. This was just one more instance of political resistance from Indian traders and shop owners that had blocked previous efforts to push through similar measures. The ruling would have allowed multi-brand stores such as Wal-Mart to open stores with a minority Indian partner. However, the Indian government already allows foreign companies to own wholesale stores, and Wal-Mart has set up 14 of those in a joint venture with an Indian firm.

The retail measure had been proposed as an attempt to create jobs by improving supply-chain infrastructure, therefore reducing the strain of inflation. But India's many small shop owners saw it as certain death for their own businesses and the protest began. The government has not, however, stopped a policy that will allow single-brand retailers such as Nike and Ikea to own 100% of their businesses, whereas before they were only allowed 51%. In fact, Ikea announced in June 2012 that the company had been granted permission to open 25 stores in India under a policy change that allows some retailers to own 100 percent of their units there.³³ Reforms later in 2012 eased the restrictions on Wal-Mart and other firms, producing uncertainty as to what reversals may occur next.

The fear among foreign retailers is that it is becoming harder for outside companies to enter into India, one of the most promising emerging consumer markets in the world. Starbucks and Dunkin' Brands are forming alliances in order to open outlets in the populous country. "It was easier to operate in the country a year ago than it is today," the CEO of General Electric's Indian unit told Bloomberg. "It is frustrating to look at unresolved issues and know that they're resolvable if you can get some leadership and orientation around them." In addition, in early 2012 investors were postponing new plans for business in India while they awaited the budgetary decisions regarding a number of proposed new taxes on foreign investment.³⁴

regulations, and rules, as well as informal ones that exert influence through norms, cultures, and ethics (discussed elsewhere in this book.)³⁵

Specific ways in which formal institutions affect international competition are (1) the attractiveness of overseas markets, (2) entry barriers and industry attractiveness, and (3) antidumping laws.³⁶

ATTRACTIVENESS OF OVERSEAS MARKETS The extent to which countries have institutions to promote the rule of law affects the attractiveness of those economies to outside investors. Specifically, institutions provide a broad framework of liberty and democracy, as well as human rights protections. In addition, institutions contribute to a stable environment for firms by creating specific laws such as those protecting property rights. Countries with more developed institutions are seen as more stable and attractive to foreign firms.³⁷

ENTRY BARRIERS AND INDUSTRY ATTRACTIVENESS Institutions create barriers to entry in certain industries and hence make those industries more attractive (profitable) for incumbent firms. For example, in the U.S. pharmaceutical industry, barriers are created by the U.S. Food and Drug Administration in the form of stringent drug approval requirements. Since new entrants (with potentially cheaper drugs) are restricted, Americans pay double what Canadians and Europeans pay for the same drugs produced in the United States. Americans spend about \$240 billion a year on drugs, more than Britain, Canada, France, Germany, Italy, and Japan combined. In turn, U.S. firms in this industry earn above-average profits as the institutional barriers restrict entrants and reduce rivalry.³⁸

ANTIDUMPING LAWS AS AN ENTRY BARRIER A second example of an entry barrier is illustrated by current U.S. antidumping laws, which place a foreign entrant at a disadvantage if accused of “dumping” (defined as selling a product below the cost of producing that product with the intent to later raise prices), because of the extensive legal forms and evidence that the U.S. requires.³⁹

Clearly, there are many formal institutions that affect international strategy. But, what explains successes of companies despite the failure or absence of these formal institutions? China is a common illustration of where domestic firms have built competitive advantages despite poorly developed formal institutions. The answer lies in the extensive use of informal institutions or networks of interpersonal connections known in Chinese as *guanxi*. These networks function as substitutes for the weaknesses of the formal institutions. Research has shown that these informal networks are common in a variety of emerging markets with different cultural traditions and are a response to transitions in many emerging markets where formal institutions are evolving.⁴⁰

SOURCES OF ENVIRONMENTAL INFORMATION

The success of environmental scanning depends on the ability of managers to take a global perspective and to ensure that their sources of information and business intelligence are global. A variety of public resources are available to provide information. In the United States alone, more than 2,000 business information services are available on computer databases tailored to specific industries and regions. Other resources include corporate “clipping” services and information packages. However, internal sources of information are usually preferable—especially alert field personnel who, with firsthand observations, can provide up-to-date and relevant information for the firm. Extensively using its own internal resources, Mitsubishi Trading Company employs worldwide more than 50,000 people in 50 countries, many of whom are market analysts, whose job it is to gather, analyze, and feed market information to the parent company.⁴¹ Internal sources of information help to eliminate unreliable information from secondary sources, particularly in developing countries, where even the “official” data from such countries can either be misleading or tampered with for propaganda purposes or it may be restricted.⁴²

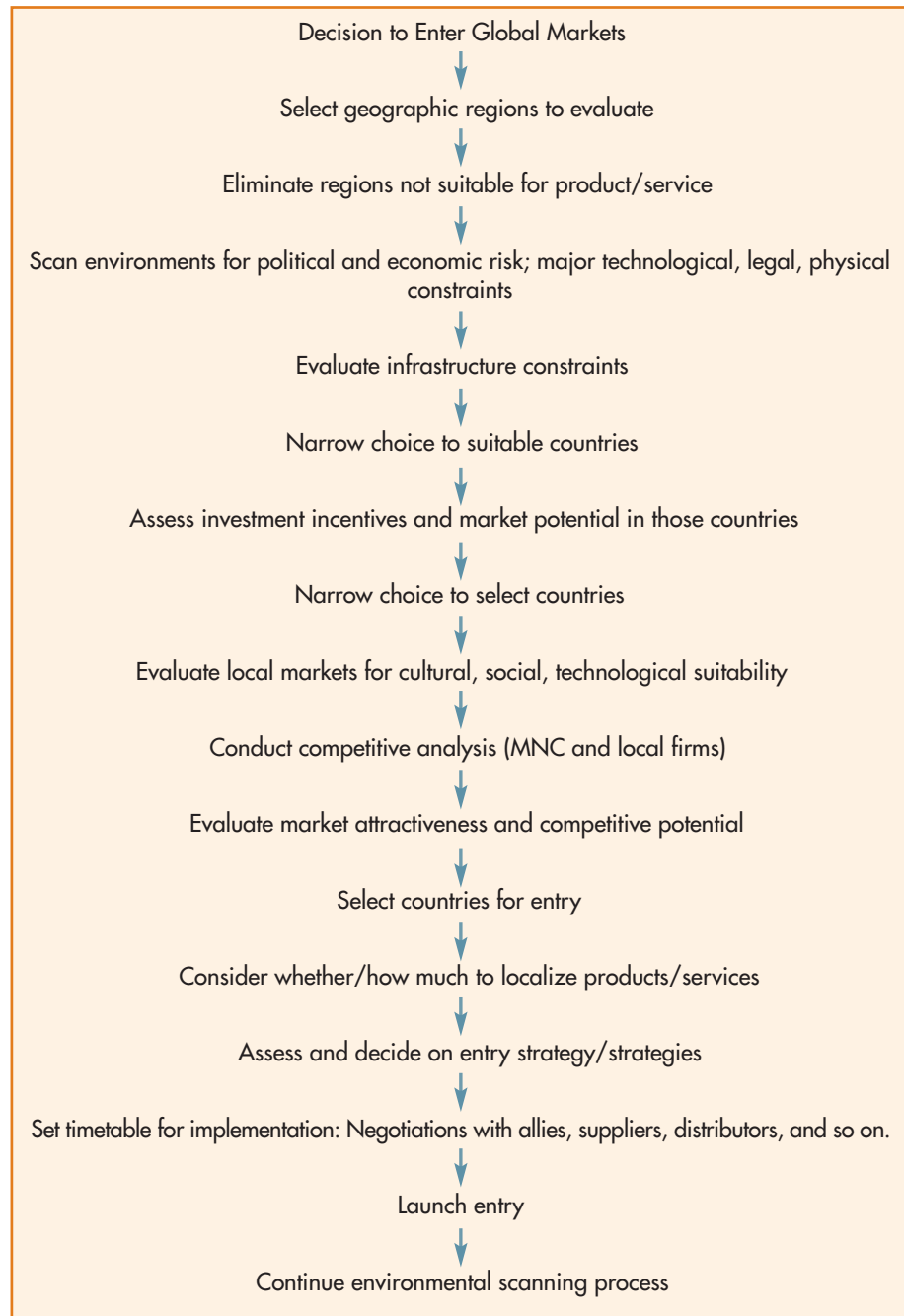
In summary, this process of environmental scanning, from the broad global level down to the local specifics of entry planning, is illustrated in Exhibit 6-4. The first broad scan of all potential world markets results in the firm being able to eliminate from its list those markets that are closed or insignificant or do not have reasonable entry conditions. The second scan of remaining regions, and then countries, is done in greater detail—perhaps eliminating some countries based on, for example, political instability. Remaining countries are then assessed for competitor strengths, suitability of products, and so on. This analysis leads to serious entry planning in selected countries; managers start to work on operational plans, such as negotiations and legal arrangements.

Step 3. Analyze Internal Factors

After the environmental assessment, the second major step in weighing international strategic options is the **internal analysis**. This analysis determines which areas of the firm’s operations represent strengths or weaknesses (currently or potentially) compared to competitors, so that the firm may use that information to its strategic advantage.

The internal analysis focuses on the company’s resources and operations and on global synergies. The strengths and weaknesses of the firm’s financial and managerial expertise and functional capabilities are evaluated to determine what key success factors (KSFs) the company has and how well they can help the firm exploit foreign opportunities. Those factors increasingly involve superior technological capability (as with Apple and Huawei Technologies) as well as other strategic advantages such as effective distribution channels (Carrefour and Wal-Mart), superior promotion capabilities (Nike and Disney), a low-cost production and sourcing position (Toyota), a superior patent and new product pipeline (Merck), and so on.

All companies have strengths and weaknesses. Management’s challenge is to identify both and then take appropriate action. Many diagnostic tools are available for conducting an internal resource audit. Financial ratios, for example, may reveal an inefficient use of assets that is restricting profitability; a sales-force analysis may reveal that the sales force is an area of distinctive competence for the firm. If a company is conducting this audit to determine whether to start

EXHIBIT 6-4 Global Environmental Scanning and Strategic Decision-Making Process

international ventures or to improve its ongoing operations abroad, certain operational issues must be taken into account. These issues include (1) the difficulty of obtaining marketing information in many countries, (2) the often poorly developed financial markets, (3) the complexities of exchange rates and government controls, (4) institutional voids in target countries, and (5) poor infrastructure.

Competitive Analysis

At this point, the firm's managers perform a *competitive analysis* to assess the firm's capabilities and key success factors compared to those of its competitors. They must judge the relative current and potential competitive position of firms in that market and location—whether that is a global position or that for a specific country or region. Managers must also specifically assess their current competitors—global and local—for the proposed market. They must ask

EXHIBIT 6-5 Global Competitor Analysis**A. U.S. Firm Compared with Its International Competitors in Malaysian Market**

Comparison Criteria	A (U.S. MNC)	B (Korean MNC)	C (Local Malaysian Firm)	D (Japanese MNC)	E (Local Malaysian Firm)
Marketing capability	0	0	0	0	–
Manufacturing capability	0	+	0	0	0
R&D capability	0	0	0	–	0
HRM capability	0	0	0	0	0
Financial capability	+	–	0	0	–
Future growth of resources	+	0	–	0	–
Quickness	–	0	+	–	0
Flexibility/adaptability	0	+	+	0	0
Sustainability	+	0	0	0	–

Key:

+ = Firm is better relative to competition.

0 = Firm is same as competition.

– = Firm is poorer relative to competition.

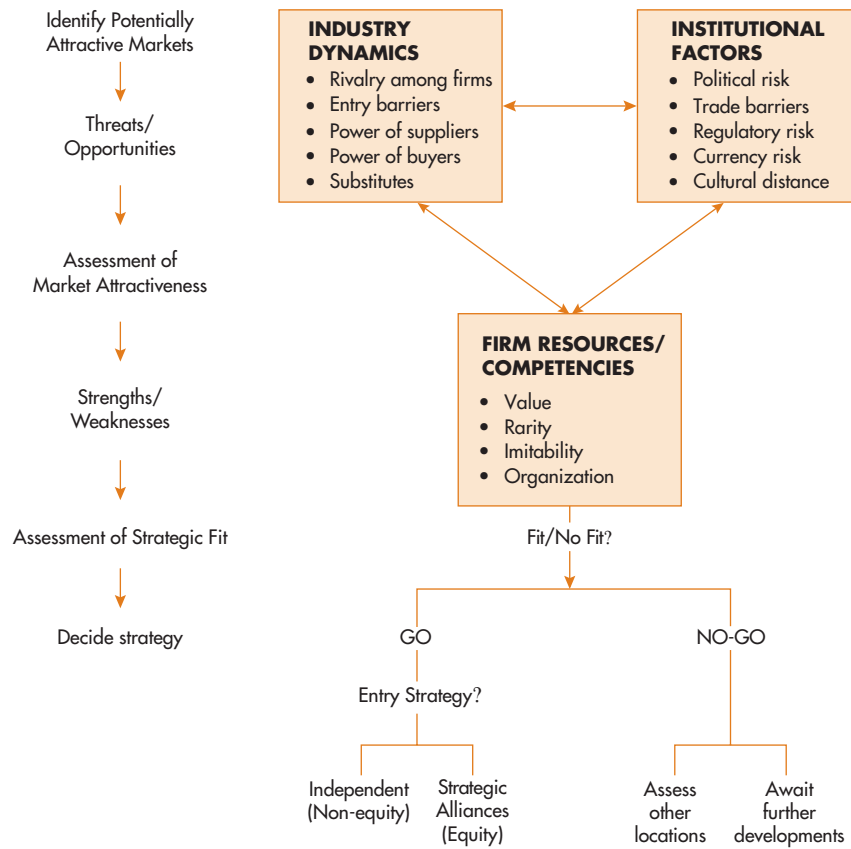
Source: Diane J. Garsombke, “International Competitor Analysis,” *Planning Review* 17, no. 3 (1989): 42–47, used with permission of Emerald Insight.

some important questions: What are our competitors’ positions, their goals and strategies, their resources, and their strengths and weaknesses, relative to those of our firm? What are the likely competitor reactions to our strategic moves? Like a chess game, the firm’s managers also need to consider the strategic intent of competing firms and what might be their future moves (strategies). This process enables the strategic planners to determine where the firm has distinctive competencies that will give it strategic advantage as well as what direction might lead the firm into a sustainable competitive advantage—that is, one that will not be immediately eroded by emulation. The result of this process will also help to identify potential problems that can be corrected or that may be significant enough to eliminate further consideration of certain strategies.

This stage of strategic formulation is often called a **SWOT analysis** (Strengths, Weaknesses, Opportunities, and Threats), in which a firm’s capabilities relative to those of its competitors are assessed as pertinent to the opportunities and threats in the environment for those firms. In comparing their company with potential international competitors in host markets, it is useful for managers to draw up a competitive position matrix for each potential location. For example, Exhibit 6-5 analyzes a U.S. specialty seafood firm’s competitive profile in Malaysia. The U.S. firm has advantages in financial capability, future growth of resources, and sustainability, but a disadvantage in quickness. It also is at a disadvantage compared to the Korean MNC in important factors such as manufacturing capability and flexibility and adaptability. Because the other firms seem to have little **comparative advantage**, the major competitor is likely to be the Korean firm. At this point, then, the U.S. firm can focus in more detail on assessing the Korean firm’s relative strengths and weaknesses.

Most companies develop their strategies around key strengths, or **distinctive competencies**. Distinctive—or “core”—competencies represent important corporate resources because, as Prahalad and Hamel explain, they are the “collective learning in the organization, especially how to coordinate diverse production skills and integrate multiple streams of technologies.”⁴³ Core competencies are usually difficult for competitors to imitate and represent a major focus for strategic development at the corporate level.⁴⁴ Apple, for example, has used its capacity to constantly innovate and apply its technology to new products and services.

Managers must also assess their firm’s weaknesses. A company already on shaky ground financially, for example, will not be able to consider an acquisition strategy, or perhaps any growth strategy. Of course, the subjective perceptions, motivations, capabilities, and goals of the managers involved in such diagnoses frequently cloud the decision-making process. The result is that because of poor judgment by key players, sometimes firms embark on strategies that are contraindicated by objective information.

EXHIBIT 6-6 A Hierarchical Model of Strategic Decision Making

STRATEGIC DECISION-MAKING MODELS

We can further explain and summarize the hierarchy of the strategic decision-making process described here by means of three leading strategic models. Their roles and interactions are conceptualized in Exhibit 6-6. At the broadest level are those global, regional, and country factors and risks discussed above and in Chapter 1 that are part of those considerations in an **institution-based theory** of existing and potential risks and influences in the host area.⁴⁵ For example, firms considering operating in Russia are realizing the potential vulnerability to a changing political attitude to the market reforms and openness from recent progress since President Putin's actions to exert control over key industries. Secondly, or concurrently, the firm's potential competitive position in its industry can be reviewed using Michael Porter's **industry-based model** of five forces that examines the dynamics within an industry, discussed below:

Porter's Five Forces Industry-Based Model

1. The relative level of global and local competition already in the industry; for example, in computers, social networking sites, and auto manufacturing. A high level of competition presents barriers to entry; firms may then decide on a different entry strategy or be deterred from that market altogether.
2. The relative ease with which new competitors may or may not enter the field, which determines the level of threat of new entrants. In other words, if your firm is already competing in that industry, what level of protection, or barriers to new entrants, do you have? Toyota, for example, presents huge barriers to entry for new car manufacturers—worldwide scale, volume, alliance partners and suppliers, and reputation.
3. How much power the buyers have within the industry; that is, what is the level of bargaining power that buyers have to influence competition? Wal-Mart, for example, has a lot of buying power because of the volume of its business, and therefore has a downward pressure on prices. Potential entrants would therefore have to provide some

differentiation or innovation in order to combat that pressure on prices and thus the profitability of the firm.

4. The level of bargaining power of suppliers in the industry. High bargaining power would exert pressure and vulnerability to a potential entrant as well as squeeze profits. Suppliers of raw materials or component parts could disrupt production if alternate sources are not available.
5. The level of threat of substitute products or services, including the likelihood of new innovations.⁴⁶ Kodak, for example, declared bankruptcy in 2012—put out of business by digital photography, in spite of the fact that the company originally invented it. And, as everyone is aware, the Internet is threatening the survival of print newspapers, movie rental stores, the U.S. Post Office, and so on.

These strategic models can provide the decision makers with a picture of the kinds of opportunities and threats that the firm would face in a particular region or country within its industry. This assumes, of course, that the locations that are under consideration have already been pinpointed as attractive and growing markets for the industry. However, that picture would be true for any firm within the particular industry. In other words, all firms within an industry face the same environmental and industrial factors; the difference among firms' performance is as a result of each firm's own resources, capabilities, and strategic decisions. The factors that determine a firm's unique niche or competitive advantage within that arena are a function of its own capabilities (strengths and weaknesses) as relative to those opportunities and threats which are perceived for that location; this is the **resource-based** view of the firm—when considering the unique value of the firm's competencies and that of its products or services.⁴⁷

While these models may indicate varying choices, this strategic decision-making process should enable the managers to give an overall assessment of the strategic fit between the firm and the opportunities in that location and so result in a “go/no go” decision for that point in time. Those managers may want to start the process again relative to a different location in order to compare the relative levels of strategic fit. If it is determined that there is a good strategic fit and a decision is made to enter that market/location, the next step, as indicated in Exhibit 6-6, is to consider alternative entry strategies. A discussion of these entry strategies follows after we first examine the broader picture of the overall strategic approach that a firm might take toward world markets.

Step 4. Evaluate Global and International Strategic Alternatives

The strategic planning process involves considering the advantages (and disadvantages) of various strategic alternatives in light of the competitive analysis. While weighing alternatives, managers must take into account the goals of their firms and the competitive status of other firms in the industry. Depending on the size of the firm, managers must consider two levels of strategic alternatives. The first level, *global strategic alternatives* (applicable primarily to MNCs), determines what overall approach to the global marketplace a firm wishes to take. The second level, *entry strategy alternatives*, applies to firms of any size; these alternatives determine what specific entry strategy is appropriate for each country in which the firm plans to operate. Entry strategy alternatives are discussed in a later section. The two main global strategic approaches to world markets—global strategy and regional, or local, strategy—are presented in the following subsections.

Approaches to World Markets

GLOBAL STRATEGY

In the last decade, increasing competitive pressures have forced businesses to consider global strategies—to treat the world as an undifferentiated worldwide marketplace. Such strategies are now loosely referred to as **globalization**—a term that refers to the establishment of worldwide operations and the development of standardized products and marketing. Many analysts, such as Porter, have argued that globalization is a competitive imperative for firms in global industries: “In a global industry, a firm must, in some way, integrate its activities on a worldwide basis to capture the linkages among countries. This includes, but requires more than, transferring intangible assets among countries.”⁴⁸ The rationale behind globalization is to compete by establishing worldwide economies of scale, offshore manufacturing, and international cash flows. The term *globalization*, therefore, is as applicable to organizational structure as it is to strategy. (Organizational structure is discussed further in Chapter 8.)

The pressures to globalize include (1) increasing competitive clout resulting from regional trading blocs; (2) declining tariffs, which encourage trading across borders and open up new markets; and (3) the information technology explosion, which makes the coordination of far-flung operations easier and also increases the commonality of consumer tastes.⁴⁹ Use of Web sites has allowed entrepreneurs, as well as established companies, to go global almost instantaneously through e-commerce—either B2B or B2C.⁵⁰ Examples are eBay, Yahoo!, and Lands' End. In addition, the success of Japanese companies with global strategies has set the competitive standard in many industries—most visibly in the automobile industry. Other companies, such as Caterpillar, ICI, and Sony, have fared well with global strategies. Another company bent on a global strategy is Lenovo, a Chinese computer-maker that became a global brand when it bought IBM's PC business in 2005 for \$1.75 billion. Says Mr. Yang, Lenovo's Chairman:

*We are proud of our Chinese roots, but we no longer want to be positioned as a Chinese company. We want to be a truly global company.*⁵¹

As a result, Lenovo has no headquarters and its senior managers rotate meetings around the world. The company's global marketing department is in Bangalore, and its development teams comprise people in several centers around the world, often meeting virtually. Mr. Yang himself moved his family to North Carolina in order to immerse himself in the culture and language of global business.⁵²

One of the quickest and cheapest ways to develop a global strategy is through strategic alliances. Many firms are trying to go global faster by forming alliances with rivals, suppliers, and customers. The rapidly developing information technologies are spawning cross-national business alliances from short-term virtual corporations to long-term strategic partnerships. (Strategic alliances are discussed further in Chapter 7.)

A global strategy is inherently more vulnerable to environmental risk, however, than a regionalization (or "multi-local") strategy. Global organizations are difficult to manage because doing so requires the coordination of broadly divergent national cultures. It also means that firms must lose some of their original identity—they must "denationalize operations and replace home-country loyalties with a system of common corporate values and loyalties."⁵³ In other words, the global strategy necessarily treats all countries similarly, regardless of their differences in cultures and systems. Problems often result, such as a lack of local flexibility and responsiveness and a neglect of the need for differentiated products. Many companies, such as Google, now feel that regionalization/localization is a more manageable and less risky approach, one that allows them to capitalize on local competencies as long as the parent organization and each subsidiary retain a flexible approach to each other. Wal-Mart is one global company that has learned the hard way that it should have acted more "local" in some regions of the world, including Germany and South Korea, where it has had to abandon operations.

REGIONALIZATION/LOCALIZATION

*Nokia, Nestle, Google, and Wal-Mart have failed to adjust to the tastes of South Korean consumers.*⁵⁴

For those firms in multidomestic industries—those industries in which competitiveness is determined on a country-by-country basis rather than a global basis—regional strategies are more appropriate than globalization. The **regionalization strategy [multidomestic (or multi-local) strategy]** is one in which local markets are linked together within a region, allowing more local responsiveness and specialization. Top managers within each region decide on their own investment locations, product mixes, and competitive positioning; in other words, they run their subsidiaries as quasi-independent organizations.

While there are pressures to globalize—such as the need for economies of scale to compete on cost—there are opposing pressures to regionalize, especially for newly developed economies (NDEs) and developing, or emerging, economies. These localization pressures include unique consumer preferences resulting from cultural or national differences (perhaps something as simple as right-hand-drive cars for Japan), domestic subsidies, and new production technologies that facilitate product variation for less cost than before.⁵⁵ By "acting local," firms can focus individually in each country or region on the local market needs for product or service characteristics,

distribution, customer support, and so on. The British retailer Tesco has enjoyed considerable success with its localizing strategy; in South Korea, for example, Samsung Tesco, which is 89 percent owned by Tesco Ltd., owes much of its acceptance to hiring local managers from Samsung. Their success compares well with those from other well-known companies which did not localize to the South Korean market, including Wal-Mart and Google.⁵⁶

Ghemawat argues that strategy cannot be decided either on a country-by-country basis or on a one-size-fits-all-countries basis, but rather that both the differences and the similarities between countries must be taken into account. He bases his perspectives on the cultural administrative, geographic, and economic (CAGE) distances between countries, for example:

Cultural distance: differences in values, languages, religion, trust.

Administrative Distance: Lack of common trading bloc or currency, political hostility, non-market or closed economy.

Geographical Distance: Remoteness, different time zones, weak transportation or communication links.

Economic Distance: Differences in level of development, natural or human resources, infrastructure, information or knowledge.

He concludes:

A semiglobalized perspective helps companies resist a variety of delusions derived from visions of the globalization apocalypse: growth fever, the norm of enormity, statelessness, ubiquity, and one-size-fits-all.

Semi-globalization is what offers room for cross-border strategy to have content distinct from single-country strategy.⁵⁷

As with any management function, the strategic choice as to where a company should position itself along the globalization-regionalization continuum is contingent on the nature of the industry, the type of company, the company's goals and strengths (or weaknesses), and the nature of its subsidiaries, among many factors. In addition, each company's strategic approach should be unique in adapting to its own environment. Many firms may try to "Go Global, Act Local" to trade off the best advantages of each strategy. Matsushita, which grew to be Japan's largest electronics firm and renamed itself as the Panasonic Corporation in October 2008, is one firm with considerable expertise at being a "GLOCAL" firm (GLObal, LoCAL). Panasonic has operations in 60 countries and employs over 300,000 people in its 634 domain companies; those companies follow policies to develop local R&D to tailor products to markets, to let plants set their own rules, and to be a good corporate citizen in every country.⁵⁸ Google is another company that has had to step back from its ideal of being just "Global" to instead adapting to local markets. Ghemawat explains why the company had problems with a "one-size-fits-all-countries" strategy by using his CAGE distance framework, as follows:

Cultural distance: Google's biggest problem in Russia seems to have been associated with a relatively difficult language.

Administrative distance: Google's difficulties in dealing with Chinese censorship reflect the difference between Chinese administrative and policy frameworks and those in its home country, the United States.

Geographic distance: Although Google's products can be digitized, it had trouble adapting to Russia from afar and has had to set up offices there.

Economic distance: The underdevelopment of the payment infrastructure in Russia has been another handicap for Google relative to local rivals.⁵⁹

Global Integrative Strategies

Many MNCs have developed their global operations to the point of being fully integrated—often both vertically and horizontally, including suppliers, productive facilities, marketing and distribution outlets, and contractors around the world. Dell, for example, is a globally integrated company, with worldwide sourcing and a fully integrated production and marketing system. It has factories in Ireland, Brazil, China, Malaysia, Tennessee, and Texas, and it has an assembly

and delivery system from 47 locations around the world. At the same time, it has extreme flexibility. Since Dell builds each computer to order, it carries very little inventory and, therefore, can change its operations at a moment's notice. Thomas Friedman described the process that his notebook computer went through when he ordered it from Dell:

*The notebook was co-designed in Austin, Texas, and in Taiwan. . . . The total supply chain for my computer, including suppliers of suppliers, involved about four hundred companies in North America, Europe, and primarily Asia, but with thirty key players. (It was delivered by UPS 17 days after ordering.)*⁶⁰

Although some companies move very quickly to the stage of global integration—often through mergers or acquisitions—many companies evolve into multinational corporations by going through the entry strategies in stages, taking varying lengths of time between stages. Typically, a company starts with simple exporting, moves to large-scale exporting with sales branches abroad (or perhaps begins licensing), then—for a manufacturing company—proceeds to assembly abroad (either by itself or through contract manufacturing), and eventually evolves to full production abroad with its own subsidiaries. Finally, the company will undertake the global integration of its foreign subsidiaries, setting up cooperative activities among them to achieve economies of scale. By this point, the MNC has usually adopted a geocentric orientation, viewing opportunities and entry strategies in the context of an interrelated global market instead of regional or national markets. In this way, alternative entry strategies are viewed on an overall portfolio basis to take maximum advantage of potential synergies and leverage arising from operations in multi-country markets.⁶¹ While Procter & Gamble, for example, took around 100 years to fully go global, more recently many companies are “**born global**”—that is, they start out with a global reach, typically by using their Internet capabilities and also through hiring people with international experience and contacts around the world.

Born globals globalize some aspects of their business—manufacturing, service delivery, capital sourcing, or talent acquisition, for instance—the moment they start up.

*. . . Standing conventional theory on its head, start-ups now do business in many countries before dominating their home markets.*⁶²

Isenberg notes that successful entrepreneurs are able to establish multinational organizations from the outset by setting up and managing global supply chains and striking alliances from positions of weaknesses. The major challenges of born globals are those of accessing resources, and physical and cultural distances in their markets and operations.⁶³

Using E-Business for Global Expansion

Companies of all sizes are increasingly looking to the Internet as a means of expanding their global operations. Clearly the Internet is available to anyone and serves to level the playing field for small businesses.

“Just think,” said Ms. Sinha, “my little six-person operation is now a global business.”

WWW.NYTIMES,
SEPTEMBER 10, 2011.⁶⁴

Ms. Sinha, a Silicon Valley entrepreneur, has six employees in her software company—two in the United States and four in New Delhi. There are many micro-multinationals such as hers and, just as with large companies, they run their businesses using e-mail, Web pages, voice-over-Internet phone services, and other Internet technology to coordinate their far-flung operations.

The globalization of the Web is evident, as shown in Table 6–1. Out of a total number of Internet users of 2,267,233,742 as of January 1, 2012, Asia already had 44.8 percent of world usage, with those numbers growing rapidly, as is so around the world. The telling statistic is the penetration rate of users for Asia of only 26.2 percent, which indicates a far greater growth capacity than, for example, the U.S. penetration of 78.3 percent. In China alone there are over 513 million Internet users, including over 150 million online shoppers. However, there, as in other countries, the logistics to providing customer service is often a barrier to efficient e-commerce. The growth of

TABLE 6-1 World Internet Usage as of January 1, 2012

Regions	Usage % of World	Penetration Rates (%)
Africa	6.2	13.5
Asia	44.8	26.2
Europe	22.1	61.3
Middle East	3.4	35.6
North America	12.0	78.6
Latin America/Caribbean	10.4	39.5
Oceania/Australia	1.1	67.5

Source: Selected data from www.internetworldstats.com, accessed October 5, 2012.

express delivery over a broad geographic base has lagged behind the growth of the e-commerce market there.⁶⁵ Three strategies are recommended to deal with the logistics problems in China and elsewhere:

- Build your own internal logistics network.
- Outsource delivery services to third-party providers.
- Form partnerships with or acquire existing logistics companies.⁶⁶

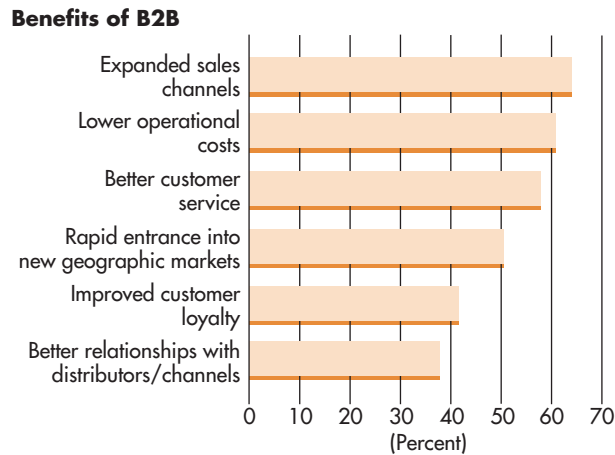
Many developing nations, in particular, are realizing the opportunities for e-commerce and are improving their infrastructure to take advantage of those opportunities. Governments and business are experiencing pressure to “go online,” especially those companies that export goods to countries where a significant amount of business is conducted through the Internet, such as the United States. For example, Everest S.A., a family-run business in San Salvador, sold a 69-kilogram lot (152 pounds) of coffee beans from one of its five farms in an Internet auction for a record price of \$14.06 a pound.⁶⁷

As a result, American technology giants are devoting great amounts of money and time to build and develop foreign-language Web sites and services. “Gone are the days in which you can launch a Web site in English and assume that readers from around the globe are going to look to you simply because of the content you’re providing.”⁶⁸

There are many benefits of e-business, including rapid entrance into new geographic markets and lower operational costs, as indicated by respondents to the IDC Internet Executive Advisory Council surveys (see Exhibit 6-7). Less touted, however, are the many challenges inherent in a global B2B (Business-to-Business) or B2C (Business-to-Consumer) strategy. These include cultural differences and varying business models as well as governmental wrangling and border conflicts—in particular the question over which country has jurisdiction and responsibility over disputes regarding cross-border electronic transactions.⁶⁹ Potential problem areas that managers must assess in their global environmental analysis include conflicting consumer protection, intellectual property, and tax laws; increasing isolationism, even among democracies; language barriers; and a lack of tech-savvy legislators worldwide.⁷⁰

Savvy global managers will realize that e-business cannot be regarded as just an extension of current businesses. It is a whole new industry in itself, complete with a different pool of competitors and entirely new sets of environmental issues. A reassessment of the environmental forces in the newly configured industry, using Michael Porter’s five forces analytical model, should take account of shifts in the relative bargaining power of buyers and suppliers, the level of threat of new competitors, existing and potential substitutes, as well as a present and anticipated competitor analysis.⁷¹ The level of e-competition will be determined by how transparent and imitable the company’s business model is for its product or service as observed on its Web site. In addition, competitors may also be other brick-and-mortar stores as well as their own—such as for Staples or J.C. Penney.

There is no doubt that the global e-business competitive arena is a challenging one, both strategically and technologically. But many companies around the world are plunging in, fearing that they will be left behind in this fast-developing global e-marketplace.

EXHIBIT 6-7 Benefits of B2B

Source: Data from IDC Internet executive Advisory Council Surveys, 2001

For companies like eBay, e-business is their business—services are provided over the Internet for end users and for businesses. With a unique business model, eBay embarked on a global e-strategy. The company has positioned itself to be global and giant: part international swap meet, and part clearinghouse for the world’s manufacturers and retailers.

E-Global or E-Local?

*Alibaba has more than 8 million small and midsize companies using its business-to-business online marketplace. . . . The company has launched local versions of its B2B service in Japan, South Korea, and India.*⁷²

Although the Internet is a global medium, a company is still faced with the same set of decisions regarding how much its products or services can be “globalized” or how much they must be “localized” to national or regional markets. Local cultural expectations, differences in privacy laws, government regulations, taxes, and payment infrastructure are just a few of the complexities encountered in trying to “globalize” e-commerce. Further complications arise because the local physical infrastructure must support e-businesses that require the transportation of actual goods for distribution to other businesses in the supply chain, or to end users. In those instances, adding e-commerce to an existing “old-economy” business in those international markets is likely to be more successful than starting an e-business from scratch without the supply and distribution channels already in place. However, many technology consulting firms, such as NextLinX, provide software solutions and tools to penetrate global markets, extend their supply chains, and enable new buyer and seller relationships around the globe.

Going global with e-business, as Yahoo! has done, necessitates a coordinated effort in a number of regions around the world at the same time to gain a foothold and to grab new markets before competitors do. Certain conditions dictate the advisability of going e-global:

*The global beachhead strategy makes sense when trade is global in scope; when the business does not involve delivering orders; and when the business model can be hijacked relatively easily by local competitors.*⁷³

This strategy would work well for global B2B markets in steel, plastics, and electronic components.

The e-local, or regional strategic, approach is suited to consumer retailing and financial services, for example. Amazon and eBay have started their regional approach in Western Europe. Again, certain conditions would make this strategy more advisable:

[The e-local/regional approach] is preferable under three conditions: when production and consumption are regional rather than global in scope; when customer behavior and market

*structures differ across regions but are relatively similar within a region; and when supply-chain management is very important to success.*⁷⁴

The selection of which region or regions to target depends on the same factors of local market dynamics and industry variables as previously discussed in this chapter. However, for e-businesses, additional variables must also be considered, such as the rate of Internet penetration and the level of development of the local telecommunications infrastructure.

One company which learned the hard way how to localize its e-business is Handango, Inc., of Hurst, Texas—a maker of smartphone and wireless-network software. As Clint Patterson, the company's vice president of marketing, said while reflecting on their move into Asian markets several years ago: "We didn't understand what purchasing methods would be popular or even what kinds of content. We didn't have a local taste. We realized we needed someone on the street to hold our hand."⁷⁵ For example, Handango found it needed a local bank account to do business in Japan, because Japanese consumers use a method called *konbini* to make online payments. This means that when they place their order online, instead of paying with a credit card, they go to a local convenience store and pay cash to a clerk, who then transfers the payment into the online vendor's account. In order to adapt to this system, Handango formed an alliance with @irBitway, a local consumer-electronics Web portal, which now acts as Handango's agent in the konbini system and also has taken over Handango's local marketing and translation.⁷⁶ Handango ran into a similar problem in Germany, finding out that Germans do not like debt and prefer to pay for their online purchases with wire transfers from their bank accounts. To get around this, the company found a local partner to interface with local banks, and then adapted its Web site to the new payment method.⁷⁷

Step 5. Evaluate Entry Strategy Alternatives

For a multinational corporation (or a company considering entry into the international arena), a more specific set of strategic alternatives, often varying by targeted country, focuses on different ways to enter a foreign market. Managers need to consider how potential new markets may best be served by their company in light of the risks and the critical environmental factors associated with their entry strategies. The following sections examine the various entry and ownership strategies available to firms, including exporting, licensing, franchising, contract manufacturing, offshoring, service-sector outsourcing, turnkey operations, management contracts, joint ventures, fully owned subsidiaries set up by the firm, and e-business. These alternatives are not mutually exclusive; several may be employed at the same time. They are addressed in order of ascending risk (typically), although e-business is usually low-risk.

EXPORTING

Exporting is a relatively low-risk way to begin international expansion or to test out an overseas market. Little investment is involved, and fast withdrawal is relatively easy. Small firms seldom go beyond this stage, and large firms use this avenue for many of their products. Because of their comparative lack of capital resources and marketing clout, exporting is the primary entry strategy used by small businesses to compete on an international level. Jordan Toothbrush, for example, a small company with one plant in Norway and with limited resources, is dependent on good distributors. Since Jordan exports around the world, the company recognizes the importance of maintaining good distributor relations. Many firms from emerging or developing markets use exporting extensively to compete overseas in a narrow product category; an example is the Hong Kong-based Johnson Electric (Johnson), which exports most of the 3 million tiny electric motors it produces per day.

An experienced firm may want to handle its exporting functions by appointing a manager or establishing an export department. Alternatively, an export management company (EMC) may be retained to take over some or all exporting functions, including dealing with host-country regulations, tariffs, duties, documentation, letters of credit, currency conversion, and so forth. Frequently, it pays to hire a specialist for a given host country.

Certain decisions need special care when managers are setting up an exporting system, particularly the choice of distributor. Many countries have regulations that make it very hard to remove a distributor who proves inefficient. Other critical environmental factors include export-import tariffs and quotas, freight costs, and distance from supplier countries.

LICENSING

An international licensing agreement grants the rights to a firm in the host country to either produce or sell a product, or both. This agreement involves the transfer of rights to patents, trademarks, or technology for a specified period of time in return for a fee paid by the licensee. Anheuser-Busch, for instance, has granted licenses to produce and market Budweiser beer in England, Japan, Australia, and Israel, among other countries. Many food-manufacturing MNCs license their products overseas, often under the names of local firms, and products like those of Nike and Disney can be seen around the world under various licensing agreements. Like exporting, licensing is also a relatively low-risk strategy because it requires little investment, and it can be a useful option in countries where market entry by other means is constrained by regulations or profit-repatriation restrictions.

Licensing is especially suitable for the mature phase of a product's life cycle, when competition is intense, margins decline, and production is relatively standardized. It is also useful for firms with rapidly changing technologies, for those with many diverse product lines, and for small firms with few financial and managerial resources for direct investment abroad. A clear advantage of licensing is that it avoids the tariffs and quotas usually imposed on exports. The most common disadvantage is the licensor's lack of control over the licensee's activities and performance.

Critical environmental factors to consider in licensing are whether sufficient patent and trademark protection is available in the host country, the track record and quality of the licensee, the risk that the licensee may develop its competence to become a direct competitor, the licensee's market territory, and legal limits on the royalty rate structure in the host country.

FRANCHISING

Similar to licensing, **franchising** involves relatively little risk. The franchisor licenses its trademark, products and services, and operating principles to the franchisee for an initial fee and ongoing royalties. Franchises are well known in the domestic fast-food industry; Pizza Hut, for example, operates primarily on this basis. For a large up-front fee and considerable royalty payments, the franchisee gets the benefit of the firm's reputation, existing clientele, marketing clout, and management expertise. Pizza Hut is well recognized internationally, as are many other fast-food and hotel franchises, such as Hampton Hotels, along with, for example, MyGym of Mexico, Nike's and Disney's products as well as other services such as Supercuts and H & R Block. A critical consideration for the franchisor's management is quality control, which becomes more difficult with greater geographic dispersion.

Franchising can be an ideal strategy for small businesses because outlets require little investment in capital or human resources. Through franchising, an entrepreneur can use the resources of franchisees to expand; most of today's large franchises started out with this strategy. An entrepreneur can also use franchisees to enter a new business. Higher costs in entry fees and royalties are offset by the lower risk of an established product, trademark, and customer base, as well as the benefit of the franchisor's experience and techniques.

Franchising in some countries can be complicated. In China, for example, franchising is a rather new concept. Almost all firms that franchise in China "either manage the operations themselves with Chinese partners (typically establishing a different partner in each major city or region), or sell to a master franchisee, which then leases out and oversees several franchise areas within a territory."⁷⁸ There are considerable problems, including finding suitable franchisees, and collecting royalty payments.

CONTRACT MANUFACTURING

A common means of outsourcing cheaper labor overseas is contract manufacturing (also commonly called outsourcing), which involves contracting for the production of finished goods or component parts. These goods or components are then imported to the home country, or to other countries, for assembly or sale. Alternatively, they may be sold in the host country. If managers can ensure the reliability and quality of the local contractor and work out adequate means of capital repatriation, this strategy can be a desirable means of quick entry into a country with a low capital investment and none of the problems of local ownership. Firms such as Nike use contract manufacturing around the world. However, in 2011, the Boston Consulting Group warned about

assuming that this strategy would continue to deliver big cost reductions by itself and that it should be considered as just one part of a global sourcing strategy, saying:

But suddenly, the case for outsourcing isn't so clear. Recent headlines trumpet the skyrocketing wages at Foxconn and Honda factories in China. These and other factors like quality concerns, the weakening U.S. dollar, rising fuel costs, and the risks inherent in longer supply chains have many companies rethinking their sourcing strategies.

WWW.BCGPERSPECTIVES.COM,
JANUARY 12, 2011⁷⁹

OFFSHORING

Offshoring is when a company moves one or all of its factories from the “home” country to another country, as is the case with some of Nissan’s factories in the U.S. In fact, over 40 percent of cars built in the United States are made by Japanese and other foreign companies.⁸⁰ Offshoring provides the company with access to foreign markets while avoiding trade barriers, as well as, frequently, an overall lower cost of production. According to the U.S. Commerce Department, approximately 90 percent of the output from U.S.-owned offshore factories is sold to foreign consumers.⁸¹

However, some companies attribute their global success to their local connections for part or all of their manufacturing. An example is the BAG shoe company in Italy. Just over half the upper shoe parts are made in low-cost countries such as Serbia and Tunisia. The rest of the uppers and the soles are made locally. Having such a large part of its shoes made by local suppliers enables BAG’s CEO, Mr. Bracalente, to emphasize the “Made in Italy” label as a big marketing advantage. And having suppliers close by means production problems are quickly solved. “Our technicians can go and visit the suppliers, often in just half an hour,” says Mr. Bracalente. He feels that splitting the assembly functions between BAG and many outside companies is a strength, not a weakness.⁸² He argues that this mix of production locations gives the company a vital source of flexibility and the capacity to make rapid changes in shoe style.⁸³

One means of gaining increased efficiencies and therefore lower costs is through **clustering**—used when contract manufacturing, offshoring, or service-sector outsourcing (explained below). Sirkin et al. note that many companies from emerging market economies—companies that they call “challengers”—have gained rapid success by clustering:

*Challengers are particularly expert at keeping their costs low by clustering—operating in concentrations of related, interdependent companies within an industry that use the same suppliers, specialized labor, and distribution channels.*⁸⁴

Examples of industry clusters are an appliance cluster in Monterey, Mexico, serving the North American market and firms both global and local, and including around two hundred local suppliers; the many manufacturing clusters in China; and service center clusters in India, as discussed elsewhere in this chapter.

SERVICE SECTOR OUTSOURCING

According to the 2011 A. T. Kearney Global Services Location Index, the service sector outsourcing industry has grown significantly and

*The part of the value chain that can be performed offshore has increased in value-add and complexity as we continue to see new types of services being handled remotely and across borders.*⁸⁵

Clearly an increasing number of firms are outsourcing “white-collar” jobs overseas in an attempt to reduce their overall costs. Indeed, the practice is not limited to large firms. Research by Gregorio et al. found that “Offshore outsourcing enhances international competitiveness by enabling SMEs to reduce costs, expand relational ties, serve customers more effectively, free up scarce resources, and leverage capabilities of foreign partners.”⁸⁶

Firms that outsource services usually enter overseas markets by setting up local offices, research laboratories, call centers, and so on in order to utilize the highly skilled but lower-wage

“**human capital**” that is available in countries such as India, the Philippines, and China, as well as the ability to offer global, round-the-clock service from different time zones.

Overall, it seems that India has benefited in IT jobs; as noted by Bill Gates of Microsoft, “India is the absolute leader in IT services offered on the world market.”⁸⁷ However, as Indians get more sophisticated at taking over high-skilled jobs outsourced from European and U.S. multinationals, they are starting to turn away call-center work, saying that it doesn’t pay well any longer. In addition, companies are finding that salaries in India are increasing with the demand for jobs from MNCs, and with the Indian technology companies themselves growing in global clout. Outsourcing of low-end office jobs may then migrate to other countries such as the Philippines or South Africa. In turn, both Indian and American IT service providers are opening offices in Hungary, Poland, and the Czech Republic to take advantage of the German and English-speaking workforce for European clients. Indeed, as found by the A. T. Kearney survey, “*the geography of offshore delivery has expanded to include a large number of countries specializing in different parts of the service-production ecosystem.*”⁸⁸

Exhibit 6-8 shows the results of the A. T. Kearney survey of the global outsourcing landscape in 50 countries and those countries’ potential across three major categories: financial attractiveness, people skills and availability, and business environment. The survey results identify the top countries for delivering information technology (IT), business-process outsourcing (BPO), and voice services. While India and China remain the leaders—in particular as far as people skills and availability are concerned—there are many countries that are attractive, depending on the types of services required. Picking the right location depends on many factors specific to the firm’s industry and tasks required for IT, BPO, or voice services. The survey found that India is by far the leader in all fields of offshore services—in large part due to its highly educated and English-language staff availability. China is gaining strength in the IT area, but remains problematic regarding the use of other languages.⁸⁹

Whether firms outsource (or “offshore”) white-collar or blue-collar jobs, they must consider the strategic aspects of that decision beyond immediate cost savings.

In addition to the lack of consideration for factors other than production costs, sending jobs to a particular country is typically a short-term cost-reduction strategy, because at some point competitive pressures will increase costs there, necessitating moving those jobs again to still lower-cost countries (a transition known as “the race to the bottom.”)

Managers are in fact broadening their strategic view of sending skilled work abroad, now using the term “transformational outsourcing” to refer to the growth opportunities provided by making better use of skilled staff in the home office that are brought about by the gains in efficiency and productivity through leveraging global talent.⁹⁰ The risk of backlash from customers, community, and current employees necessitates careful consideration of the reasons for a company to go offshore. Managers also must consider the risk of losing control of proprietary technology and processes and must decide whether to set up the company’s own subsidiary offshore (a “captive” operation) instead of contracting with outside specialists. Bank of America, for example, split its strategy by opening its own subsidiary in India, but also allied with Infosys Technologies and Tata Consultancy Services for 30 percent of its IT resources to be outsourced.⁹¹

TURNKEY OPERATIONS

In a so-called **turnkey operation**, a company designs and constructs a facility abroad (such as a dam or chemical plant), trains local personnel, and then turns the key over to local management—for a fee, of course. The Italian company Fiat, for example, constructed an automobile plant in the former Soviet Union under a turnkey agreement. Critical factors for success are the availability of local supplies and labor, reliable infrastructure, and an acceptable means of repatriating profits. There may also be a critical risk exposure if the turnkey contract is with the host government, which is often the case. This situation exposes the company to risks such as contract revocation and the rescission of bank guarantees.

MANAGEMENT CONTRACTS

A management contract gives a foreign company the rights to manage the daily operations of a business but not to make decisions regarding ownership, financing, or strategic and policy changes. Usually, management contracts are enacted in combination with other agreements, such

EXHIBIT 6-8 The A. T. Kearney Global Services Location Index, 2011

Rank	Country	Financial Attractiveness	People Skills and Availability	Business Environment	Total Score
1	India	3.11	2.76	1.14	7.01
2	China	2.62	2.55	1.31	6.49
3	Malaysia	2.78	1.38	1.83	5.99
4	Egypt	3.10	1.36	1.35	5.81
5	Indonesia	3.24	1.53	1.01	5.78
6	Mexico	2.68	1.60	1.44	5.72
7	Thailand	3.05	1.38	1.29	5.72
8	Vietnam	3.27	1.19	1.24	5.69
9	Philippines	3.18	1.31	1.16	5.65
10	Chile	2.44	1.27	1.82	5.52
11	Estonia	2.31	0.95	2.24	5.51
12	Brazil	2.02	2.07	1.38	5.48
13	Latvia	2.56	0.93	1.96	5.46
14	Lithuania	2.48	0.93	2.02	5.43
15	United Arab Emirates	2.41	0.94	2.05	5.41
16	United Kingdom	0.91	2.26	2.23	5.41
17	Bulgaria	2.82	0.88	1.67	5.37
18	United States	0.45	2.88	2.01	5.35
19	Costa Rica	2.84	0.94	1.56	5.34
20	Russia	2.48	1.79	1.07	5.34
21	Sri Lanka	3.20	0.95	1.11	5.26
22	Jordan	2.97	0.77	1.49	5.23
23	Tunisia	3.05	0.81	1.37	5.23
24	Poland	2.14	1.27	1.81	5.23
25	Romania	2.54	1.03	1.65	5.21
26	Germany	0.76	2.17	2.27	5.20
27	Ghana	3.21	0.69	1.28	5.18
28	Pakistan	3.23	1.16	0.76	5.15
29	Senegal	3.23	0.78	1.11	5.12
30	Argentina	2.45	1.58	1.09	5.12
31	Hungary	2.05	1.24	1.82	5.11
32	Singapore	1.00	1.66	2.40	5.06
33	Jamaica	2.81	0.86	1.34	5.01
34	Panama	2.71	0.72	1.49	4.98
35	Czech Republic	1.81	1.14	2.03	4.98
36	Mauritius	2.41	0.87	1.70	4.98
37	Morocco	2.83	0.87	1.26	4.96
38	Ukraine	2.86	1.07	1.02	4.95
39	Canada	0.56	2.14	2.25	4.95
40	Slovakia	2.33	0.93	1.65	4.91
41	Uruguay	2.42	0.91	1.42	4.75
42	Spain	0.81	2.06	1.88	4.75
43	Colombia	2.34	1.20	1.18	4.72
44	France	0.38	2.12	2.11	4.61
45	South Africa	2.27	0.93	1.37	4.57
46	Australia	0.51	1.80	2.13	4.44
47	Israel	1.45	1.35	1.64	4.44
48	Turkey	1.87	1.29	1.17	4.33
49	Ireland	0.42	1.74	2.08	4.24
50	Portugal	1.21	1.09	1.85	4.15

Note: The weight distribution for the three categories is 40:30:30. Financial attractiveness is rated on a scale of 0 to 4, and the categories for people skills and availability, and business environment are on a scale of 0 to 3.

Source: The A.T. Kearney Global Services Location Index™, 2011, Copyright A.T. Kearney, 2011. All rights reserved. Reprinted with permission.

as joint ventures. By itself, a management contract is a relatively low-risk entry strategy, but it is likely to be short term and provide limited income unless it leads to another more permanent position in the market.

INTERNATIONAL JOINT VENTURES

At a much higher level of investment and risk (though usually less risky than a wholly owned plant), joint ventures present considerable opportunities unattainable through other strategies. A joint venture involves an agreement by two or more companies to produce a product or service together. In an **international joint venture (IJV)** ownership is shared, typically by an MNC and a local partner, through agreed-upon proportions of equity. This strategy facilitates an MNC's rapid entry into new markets by means of an already established partner who has local contacts and familiarity with local operations. IJVs are a common strategy for corporate growth around the world. They also are a means to overcome trade barriers, to achieve significant economies of scale for development of a strong competitive position, to secure access to additional raw materials, to acquire managerial and technological skills, and to spread the risk associated with operating in a foreign environment.⁹² Not surprisingly, larger companies are more inclined to take a high-equity stake in an IJV in order to engage in global industries and to be less vulnerable to the risk conditions in the host country.⁹³ The joint venture reduces the risks of expropriation and harassment by the host country. Indeed, it may be the only means of entry into certain countries, such as Mexico and Japan, that stipulate proportions of local ownership and local participation.

In recent years, IJVs have made up about 20 percent of direct investments by MNCs in other countries, including such deals as the one between Mittal Steel of India and Arcelor of France in 2006—creating the world's biggest steel company.⁹⁴ Many companies have set up joint ventures with European companies to gain the status of an “insider” in the European Common Market. IJVs are quite common in India because the government encourages foreign collaborations to facilitate capital investments, import of capital goods, and transfer of technology.⁹⁵ Most of these alliances are not just tools of convenience but are important—perhaps critical—means to compete in the global arena. To compete globally, firms have to incur, and defray, immense fixed costs—and they need partners to help them in this effort.⁹⁶

In a joint venture, the level of relative ownership and specific contributions must be worked out by the partners. The partners must share management and decision making for a successful alliance. The company seeking such a venture must maintain sufficient control, however, because without adequate control, the company's managers may be unable to implement their desired strategies. Initial partner selection and the development of a mutually beneficial working agreement are, therefore, critical to the success of a joint venture. In addition, managers must ascertain that there will be enough of a “fit” between the partners' objectives, strategies, and resources—financial, human, and technological—to make the venture work. Unfortunately, too often the need for preparation and cooperation is given insufficient attention, resulting in many such marriages ending in divorce. About 60 percent of IJVs fail, usually because of ineffective managerial decisions regarding the type of IJV, its scope, duration, and administration, as well as careless partner selection.⁹⁷ In 1998, the chief executive of Daimler-Benz, Jürgen Schrempp, said that its joint venture with Chrysler would be a “marriage made in heaven.” But it ended in a messy divorce in 2007 because of cross-cultural conflicts and because the German company's luxury-car lineup had little in common with Chrysler's portfolio of vehicles.⁹⁸ IJVs, as well as the many forms of strategic global alliances, are further discussed in Chapter 7.

For companies in emerging markets or developing economies, joint ventures, mergers, and acquisition strategies provide opportunities to internationalize by gaining access to customers, supply networks, technology, local brand image and knowledge, and natural resources. The local alliances also typically provide to the new management a learning curve for manufacturing and management skills and technologies.

FULLY OWNED SUBSIDIARIES

In countries where a **fully owned subsidiary** is permitted, an MNC wishing total control of its operations can start its own product or service business from scratch, or it may acquire an existing firm in the host country. In September 2011, the South African company SABMiller announced it would buy Australia's Foster's—which commands 50 percent of the Australian

beer market—for \$10.15 billion, rounding out its global beer portfolio. South African Breweries bought Miller in 2002; since then, it has expanded into Latin America, Asia, and Africa.⁹⁹ Another deal that closed in 2011 was the purchase of Sara Lee by Grupo Bimbo, the Mexican-based bakery company, for \$959 million; the deal allows Grupo Bimbo the right to sell Sara Lee baked goods everywhere except Western Europe, Australia, and New Zealand.¹⁰⁰

Often the decision to acquire foreign companies will turn on opportunities presented by financial and economic situations at the time, as with companies who, for tax reasons, keep cash overseas. In 2011, for example, money sheltered from U.S. taxes resulted in cheaper acquisitions for a number of companies, including Apple, Cisco, and Pfizer, amounting to \$174 billion in foreign asset purchases. Microsoft said it used \$8.5 billion of offshore cash to acquire Luxembourg-based Internet–phone service Skype Technologies in May 2011.

U.S. companies such as General Electric and Microsoft are using cash parked overseas to snap up foreign companies at more than double last year's pace. Through the first seven months of 2011, there have been about \$174 billion in deals in which U.S. companies bought foreign assets.”¹⁰¹

BLOOMBERG-BUSINESSWEEK,
AUGUST 15–28, 2011.

The Tata Group, an Indian conglomerate for cars, steel, software, and tea, continues to make acquisitions around the world including Corus, a European steel company, and Ford's Jaguar and Land Rover.¹⁰² Such acquisitions by MNCs allow rapid entry into a market with established products and distribution networks and provide a level of acceptability not likely to be given to a “foreign” firm. These advantages somewhat offset the greater level of risk stemming from larger capital investments, compared with other entry strategies. Other examples of acquisitions to gain further growth and entry into global markets include the Procter and Gamble acquisition of Gillette, which paved the way for the creation of the world's largest consumer goods company.¹⁰³

At the highest level of risk is the strategy of starting a business from scratch in the host country—that is, establishing a new wholly owned foreign manufacturing or service company or subsidiary with products aimed at the local market or targeted for export. This strategy exposes the company to the full range of risk, to the extent of its investment in the host country. As evidenced by events in the Middle East, political instability can be devastating to a wholly owned foreign subsidiary. Add to this risk a number of other critical environmental factors—local attitudes toward foreign ownership, currency stability and repatriation, the threat of expropriation and nationalism—and you have a high-risk entry strategy that must be carefully evaluated and monitored. There are advantages to this strategy, however, such as full control over decision making and efficiency, as well as the ability to integrate operations with overall company-wide strategy.

E-BUSINESS

Discussed earlier as a global strategy, e-business is an entry strategy at the local level. As such, the failure risk of entry depends greatly on the country or region, even though it is relatively low globally. Yahoo!, for example, bought the largest Arabic-language web portal in August 2009. Although fewer than 50 million of the world's 320 million Arabic-language speakers are online, then-CEO Carol Bartz said that “emerging markets and new languages are a key part of the strategy. Acquisition costs are modest, and while advertising spending is too low for immediate payback, the medium-term prospects for significant growth are surer than in more mature markets.”¹⁰⁴

Exhibit 6-9 summarizes the advantages and critical success factors of these entry strategies that must be taken into account when selecting one or a combination of strategies, depending on the location, the environmental factors and competitive analysis, and the overall strategy with which the company approaches world markets.

Complex situational factors face the international manager as she or he considers strategic approaches to world markets along with which entry strategies might be appropriate, as illustrated in *Comparative Management in Focus: Strategic Planning for Emerging Markets*.

Step 6. Decide on Strategy

The strategic choice of one or more of the entry strategies will depend on (1) a careful evaluation of the advantages (and disadvantages) of each in relation to the firm's capabilities and resources,

EXHIBIT 6-9 International Entry Strategies: Advantages and Critical Success Factors

Strategy	Advantages	Critical Success Factors
Exporting	Low risk No long-term assets Easy market access and exit	Choice of distributor Transportation costs Tariffs and quotas
Licensing	No asset ownership risk Fast market access Avoids regulations and tariffs	Quality and trustworthiness of licensee Appropriability of intellectual property Host-country royalty limits
Franchising	Little investment or risk Fast market access Small business expansion	Quality control of franchisee and franchise operations
Contract manufacturing/Offshoring	Limited cost and risk Short-term commitment	Reliability and quality of local contractor Operational control and human rights issues
Service-sector outsourcing	Lower employment costs	Quality control
Turnkey operations	Access to high skills and markets Revenue from skills and technology where FDI restricted	Domestic client acceptance Reliable infrastructure Sufficient local supplies and labor Repatriability of profits Reliability of any government partner
Management contracts	Low-risk access to further strategies	Opportunity to gain longer-term position
Joint ventures	Insider access to markets Share costs and risk Leverage partner's skill base, technology, local contacts	Strategic fit and complementarity of partner, markets, products Ability to protect technology Competitive advantage Ability to share control Cultural adaptability of partners
Wholly owned subsidiaries	Realize all revenues and control Global economies of scale Strategic coordination Protect technology and skill base	Ability to assess and control economic, political, and currency risk Ability to get local acceptance Repatriability of profits
E-Business	Rapid entry into (or exit from) new markets (often through alliance or purchase of local websites); relatively low-risk	Differences in business models, culture, language, and laws regarding intellectual property, consumer protection, and taxes.

(2) the critical environmental factors, and (3) the contribution that each choice would make to the overall mission and objectives of the company. Exhibit 6-9 summarized the advantages and the critical success factors for each entry strategy discussed. However, when it comes down to a choice of entry strategy or strategies for a particular company, more specific factors relating to that firm's situation must be taken into account. These include factors relating to the firm itself, the industry in which it operates, location factors, and venture-specific factors, as summarized in Exhibit 6-15.

After consideration of those factors for the firm as well as considering what is available and legal in the desired location, some entry strategies will no doubt fall out of the feasibility zone. With those options remaining, then, strategic planners need to decide which factors are more important to the firm than others. One method is to develop a weighted assessment to compare the overall impact of factors such as those in Exhibit 6-15 relative to the industry, the location, and the specific venture—on each entry strategy. Specific evaluation ratings, of course, would depend on the country conditions at a given point in time, the nature of the industry, and the local company.



COMPARATIVE MANAGEMENT IN FOCUS

Strategic Planning for Emerging Markets

Davos, Switzerland, 29 January 2011 – The global economy is rebounding, led by developing economies including China and India, with developed countries growing much more slowly.¹⁰⁵

WORLD ECONOMIC FORUM ANNUAL MEETING, 2011.

The 2011 GRDI ranking mirrors the dramatic changes that have taken place in global markets, and the varying impacts they have had on different emerging economies. South American countries have fared well during the recession, posting an impressive 6 percent GDP growth in 2010.¹⁰⁶

The 2011 Global Retail Development Index, www.atkearney.com

As we can see from the quotes above, there continue to be many indicators of the increasing business opportunities available for companies wanting to set up operations in or export to the emerging markets, in particular in light of the slowdown in growth in many developed economies brought about by economic problems.

In planning for global opportunities for retail businesses, for example, one can consider the A. T. Kearney Global Retail Development Index, which ranks 30 emerging countries on the urgency for retailers to enter the country. The scores are based on 25 variables across four primary categories: economic and political risk, market attractiveness, market saturation, and time pressure (whether retail growth is keeping up with gross domestic product (GDP)). Table 6–2 shows the top ten ranks and Russia (14th place). Interestingly, South American countries rated as the top three positions, China slipped to 6th place, and India dropped to 4th place.

Table 6–2 Emerging Market Attractiveness for Retail Strategies

Country	2011 Rank	2010 Rank
Brazil	1	5
Uruguay	2	8
Chile	3	6
India	4	3
Kuwait	5	2
China	6	1
Saudi Arabia	7	4
Peru	8	9
U.A.E.	9	7
Turkey	10	18
Russia	14	10

Source: Based on selected data from the A. T. Kearney Global Retail Development Index 2011, www.atkearney.com.

While the study highlights those countries heading the list, Hana Ben-Shabat, A. T. Kearney partner and co-leader of the study, cautions that, since they started the annual study ten years ago, it has become clear that “there is no ‘one size fits all’ formula for global expansion. Different countries are at different levels of development and have different risk/return profiles, which require retailers to tailor their approaches accordingly and assemble a portfolio of markets to balance short-term risk with long-term growth aspirations.”¹⁰⁷ The World Economic Forum report also cautions that emerging markets are not a single homogenous group: “They develop differently, have different infrastructural,

(Continued)

socio-economic and regulatory challenges, face different environmental and geographical constraints, and, to a certain extent, afford different opportunities for business. We argue that the lack of adequate development in the areas of trade facilitation and trade logistics can curtail the growth for these markets and the world.”¹⁰⁸

In jumping on the bandwagon, firms of all sizes, in particular small businesses, must realize that investing in developing economies usually entails considerably higher levels of risk than they are familiar with—in particular those risks of political turmoil, corruption, and contract enforcement. However, avoiding emerging markets will, over time, make firms less competitive than those who invest there in some form. The question is then how to minimize the risks without losing out to the competition and losing growth opportunities. After going through the steps of the strategic decision-making process as outlined in this chapter, including those operational factors in the institutional context such as infrastructure, availability of suppliers, labor markets, and capital markets (such as the effectiveness of banking and financial institutions), CEOs must then decide whether to enter that market and, if so, decide what needs to be changed. As *Harvard Business Review* authors Khanna, Palepu, and Sinha recommend: “decide whether to work around the country’s institutional weaknesses, create new market infrastructures, or stay away because adapting your business model would be impractical and uneconomical.”¹⁰⁹ McDonald’s, for example, worked around infrastructure problems in Russia by setting up their own food supply farms and chains. Dell also chose to adapt its business model in China when the company realized that consumers there did not order computers over the Internet, and so it had to use Chinese ordering and supply chains rather than the company’s usual model of just-in-time inventory. Financial MNCs have helped to improve the financial systems in Brazil and therefore their own firm’s prospects. For its part, Home Depot has declined to enter markets with poor transportation and banking infrastructures, because its model and its success depend on competitive inventory systems and employee stock ownership.¹¹⁰

However, as noted by Washburn and Hunsaker:

“Too many companies in mature markets assume that the only reason to enter emerging countries is to pursue new customers. They fail to perceive the potential for innovation in those countries or to notice that a few visionary multinationals are successfully tapping that potential for much needed products and services.”

*Source: Harvard Business Review, September 2011.*¹¹¹

In their research, Washburn and Hunsaker have found that forward-thinking global managers (they call them “bridgers”) have identified and developed innovations in emerging markets (often with the insight of the local managers) and been able to integrate those ideas and improvements into their companies’ product lines. Innovations percolating from emerging market companies already indicate the potential, such as Tata’s \$2,500 Nano car in India.¹¹²

In addition, when considering opportunities for firms within emerging markets, we can see that, for example, firms such as Tata and Infosys of India, BYD and Tencent Holdings of China, and Samsung Electronics of Korea have become prominent players in a number of technology-intensive industries that have traditionally been the domain of firms from the U.S., Europe, and Japan.¹¹³

Entry Strategies

The following section discusses the findings of a study by Deloitte of 247 executives regarding the choices companies make among entry strategies for emerging markets, along with a comparison of strategic objectives and operating strategies.

Strategic Expansion in Emerging Markets

[A study by Deloitte] involving interviews with several executives and a survey of 247 executives from consumer and industrial product companies with presence in emerging markets revealed that companies are increasingly making emerging geographic markets a centerpiece of their global business model. Over the next three years, upwards of 88 percent of companies plan to expand their presence in emerging markets. In fact, nearly half of these organizations expect 20 percent or more of their global revenues to have their origins in emerging markets. Furthermore, a third of these companies plan to place more than 20 percent of their investments in these regions. None of these figures suggest an imminent end to offshoring as we know it, but rather a renewed interest in its pursuit.

That’s not to say manufacturers would call their endeavors business-as-usual in emerging markets. Forward-thinking companies have not been content to simply increase their presence in low-cost centers. They have become more strategic in their operations by establishing core functions of their

FIGURE 6-1



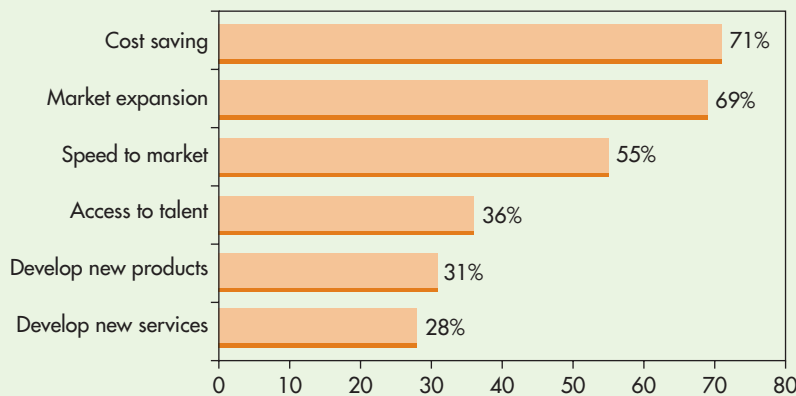
Source: Deloitte Services LP

value chains in these regions. While cost savings is still a key motivator for nearly three-quarters of manufacturing companies, it's no longer the sole reason to set up shop abroad. Almost seventy percent of the manufacturers in our study consider market expansion an important factor (see Exhibit 6-10).

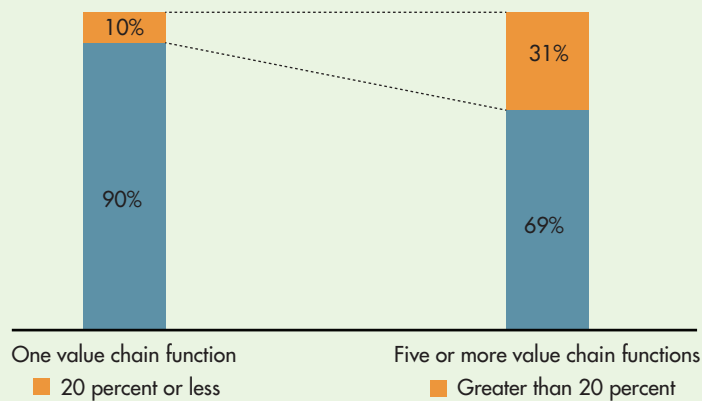
In fact, more than two-thirds of companies think it's equally important to cost savings. Similarly, 55 percent of manufacturing companies reported that they establish operations in emerging markets to improve their speed to market. Nokia has been in India since 1995, an early investment that earned it 50 percent of a mobile phone market—one that adds 8–10 million new users every month. D. Shivakumar, managing director of Nokia India, attributes this success to the company's completely localized value chain. Indian operations for everything from R&D to manufacturing, marketing, and sales give Nokia the power to launch new phones in a matter of weeks, rather than months, with designs that cater directly to the needs of its local customers.

Increasingly, organizations are broadening the scope of their pursuits in emerging economies. Nearly 40 percent of the companies in our study have established commercial operations in addition to their manufacturing endeavors that cater to global as well as local markets. After-sales service, material sourcing, and sales and marketing—relative newcomers to low-cost centers—are becoming increasingly prevalent. Forward-thinking companies are beginning to realize that future returns will

EXHIBIT 6-10 Top Three Strategic Objectives for Establishing Functions in Emerging Markets



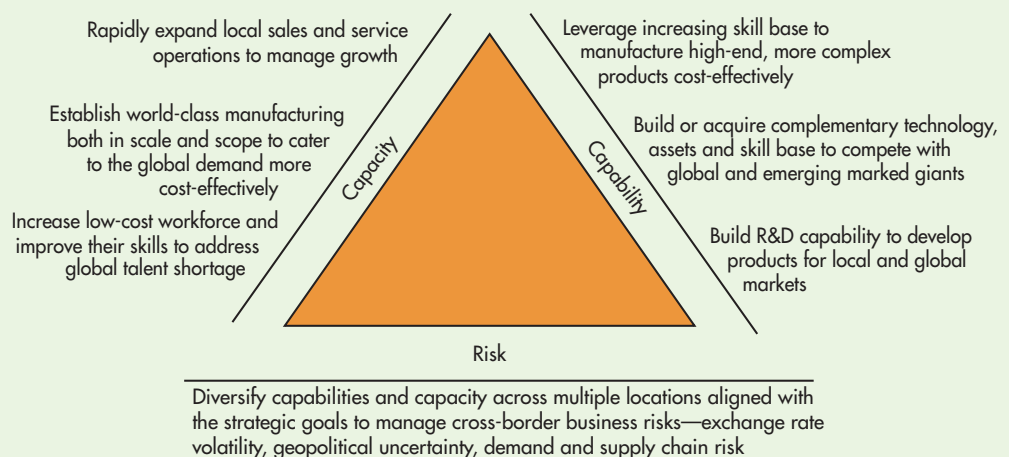
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EXHIBIT 6-11 Number of Functions in Emerging Markets vs. Percentage of Global Profits from Emerging Markets

depend on emulating global business models in emerging markets. Intuitively, a strong correlation exists between the number of functions a company establishes in emerging markets and the percentage of global profits that come from these regions. A third of the organizations in our study with five or more functions in emerging markets earn 20 percent or more of their global profits from these operations (see Exhibit 6-11). By comparison, the majority of manufacturers with only a single operation in these low-cost centers reported that they derive 10 percent or less of their global profits from their endeavors.

But these numbers don't paint a complete picture, either. Many manufacturers reported that they are increasing their expectations along with their investments in emerging markets. As a result, operational and financial performance goals can become as elusive as they are lofty. In fact, raw materials and manufacturing have become more expensive over the last three years for over 40 percent of the companies who cited cost savings as a key objective in their emerging market strategies. Likewise, only 13 percent of the companies that cited market expansion as their key objective have realized a significant increase in their global market share. The problem is a fundamental one: companies' endeavors in developing countries haven't kept pace with the evolving capacity and capabilities of these regions, and they're not part of a global business model. As a result, performance in these countries pale by comparison to other parts of their global business.

When companies were content merely to outsource low-complexity work to low-cost centers, strategies were narrow and straightforward. This simplicity has evaporated as companies begin to strategically shift specific functions of their value chains to account for new objectives pertaining to growth, innovation, and sustainability. From a strategy standpoint, three factors determine the emerging market business model: capacity, capability, and risk (see Exhibit 6-12).

EXHIBIT 6-12 New Strategies for Emerging Markets

Getting the Operating Model Right

In recent years, the rate of IJV (international joint venture) formation has continued to increase steadily, especially among emerging markets in Asia, Eastern Europe, and Latin America. These emerging markets account for about 70 percent of all IJV entries by multinational corporations. As companies deepen their business activities in low-cost centers and incorporate these endeavors into global value chains, their existing operating models may not be effective in emerging markets. According to our survey, 35 percent of companies used joint ventures to enter emerging markets, but only 21 percent still use them.

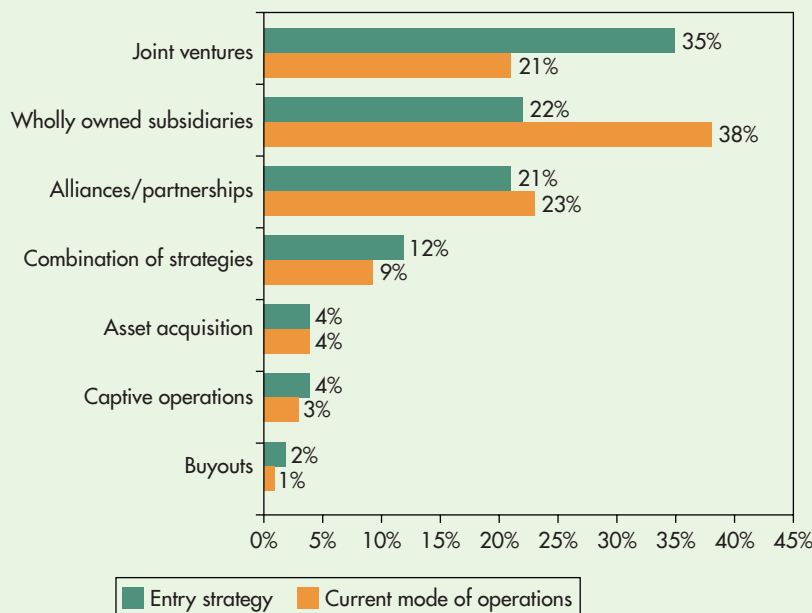
The type of business activities, market opportunities, country regulations, tax advantages, and experience in emerging markets are the key determinants of operating model (see Exhibit 6-13). Thirty-eight percent of manufacturing companies in our study reported that they currently use wholly owned subsidiaries in emerging markets. As they build complete product lines and develop new products, companies require a significant level of control over strategic business activities. For example, Sweden's Volvo group, the world's second largest truck manufacturer, owns a subsidiary in India that builds trucks to sell in India, Myanmar, Indonesia, Vietnam, and China. Volvo India has also established a product development center in Bangalore, India that employs over 200 people. The wholly owned subsidiary model allows companies to take advantage of global brands and existing business processes and protects intellectual property by keeping development effectively in-house.

Similarly, companies expanding sales activities in emerging markets need access to deeper knowledge of local customers, support networks, distribution, and advertising. In many cases, companies choose joint ventures with experienced players in a local market, as noted earlier with Volvo's recently formed joint venture with Eicher Motors in India to sell heavy vehicles and leverage its network of over 200 service centers across the country.

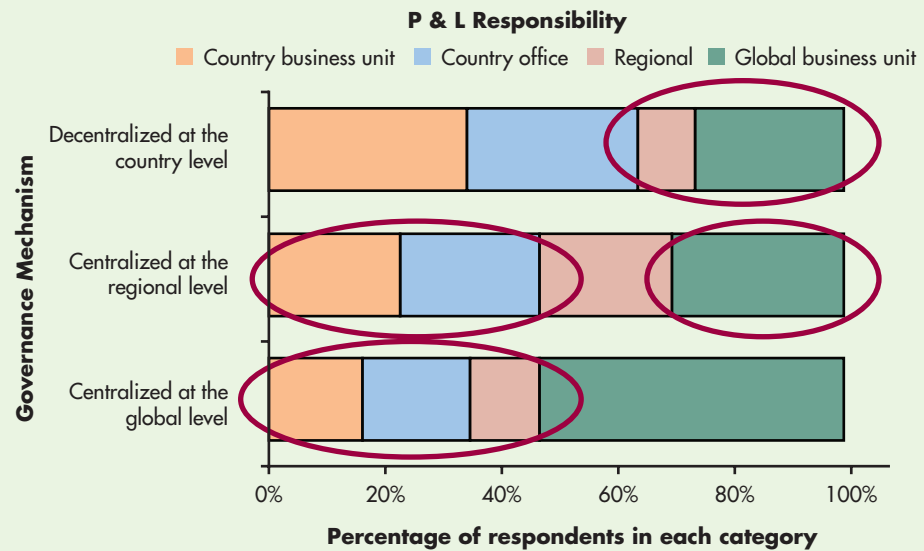
In many cases, market opportunities also drive the choice of operating models in emerging markets. Multinational companies that struggle to stay competitive and innovative sometimes find emerging market companies with a new line of products that has potential to add significant cash flow. In such cases, the choice of operating model depends on size of investment, risk appetite, competition and expected return on the investment. Companies should choose between joint ventures and acquisitions only after thorough due diligence, depending on how these factors play out.

Country regulations and experience in specific countries also drive decisions about operating models. The types of operating model vary significantly by country. For example, in new and comparatively smaller emerging markets like Brazil, Czech Republic, and Mexico, more companies prefer wholly owned subsidiaries compared to China and India. Many countries have strict regulations on operating models for foreign direct investment to support protectionism and growth of domestic industries. However, as many countries are committed to becoming open market economies, these regulations are

EXHIBIT 6-13 Operating Model for Emerging Markets



(Continued)

EXHIBIT 6-14 Disconnected Governance Model

loosening. For instance, just a few years ago, China required all automotive companies to enter Chinese markets via joint venture. Over the years, as countries become economically stronger, they tend to ease such regulations on the operating model. However, to stay competitive over the long run, wholly owned subsidiaries might not be the best model for building an understanding of local markets.

Based on our study, companies with more experience in emerging markets tend to choose wholly owned subsidiaries to expand their presence. With the spotlight on emerging markets, thousands of studies have been commissioned by governments, private companies, and academia that now provide deep know-how of these markets. Based on our survey, more than half the companies that have been in the emerging markets for more than ten years choose “wholly owned subsidiary.”

In addition to choosing the right operating model, alignment to the global governance model is also a critical success factor. Global governance models and P&L responsibilities are misaligned in over a third of manufacturing companies in our study (see Exhibit 6-14). For instance, almost 50 percent of the companies that have a governance model centrally managed by their global headquarters reported that they hold their local or regional businesses responsible for managing profit and loss. As a consequence, local or regional businesses do not have much flexibility to change policies that will be favorable to their region. Organizations that have misaligned governance models lose out on operational efficiencies and the chance to take advantage of emerging markets on a global scale.

From Off-shoring to the Right One

For manufacturers, maybe the term “emerging market” is misleading. Emergence, after all, suggests a singular, upward path, but many companies are quick to call their operations a two-way street. If companies are to evolve along with host countries that are already becoming highly developed in their own right, they must take a closer look at how to adapt their operating models and global value chains and how to offset the risks and challenges associated with these locations, mindful of the fact that the competition is doing the same thing.

Source: Excerpted section from Deloitte Review, Issue 4 (January 2009) article titled “Rethinking Emerging Market Strategies: From offshoring to strategic expansion,” by Vikram Mahidhar, Craig Giffi, and Ajit Kambil with Ryan Alvanos. Used with permission of the Deloitte Review.

Based on a study of more than 10,000 foreign entry activities into China, Pan and Tse concluded that managers tend to follow a hierarchy-of-decision sequence in choosing an entry mode. They found that the location choice—specifically the level of country risk—was the primary influence factor at the level of deciding between equity and non-equity modes. Host-country government incentives also encouraged the choice of equity mode. Managers first decide between non-equity based for high-risk locations, and equity based where it is perceived there is lower risk. Then, non-equity modes are divided into contractual agreements such as franchising,

EXHIBIT 6-15 Factors Affecting Choice of International Entry Mode¹¹⁴

Factor Category	Examples
Internal factors	Global experience of firm and managers Distinctive competencies, patents, technology Corporate culture and structure Global objectives Long-term strategy Financial assets
External factors	Industry globalization Industry growth rate Barriers to entry Level of global competition Opportunities and incentives Extent of scale and location economies Country risk—political, economic, legal Cultural distance Knowledge of local market Potential of local market Competition in local market
Venture-specific factors	Value of firm—assets risked in foreign location Ability to protect proprietary technology Costs of making or enforcing contracts with local partners Size of planned foreign venture Intent to conduct research and development with local partners

licensing, outsourcing, e-business, and exporting; equity modes are split into wholly owned operations, acquisitions, offshoring, and equity joint ventures (EJVs) with varying levels of equity investment.¹¹⁵

Gupta and Govindarajan also propose a hierarchy-of-decision factors sequence but consider two initial choice levels. The first is the extent to which the firm will export or produce locally; the second is the extent of ownership control over activities that will be performed locally in the target market.¹¹⁶ There is an array of choice combinations within those two dimensions. Gupta and Govindarajan point out that, among the many factors to take into account, alliance-based entry modes are more suitable under the following conditions:

- Physical, linguistic, and cultural distance between the home and host countries is high.
- The subsidiary would have low operational integration with the rest of the multinational operations.
- The risk of asymmetric learning by the partner is low.
- The company is short of capital.
- Government regulations require local equity participation.¹¹⁷

The choice of entry strategy for McDonald's, for example, varies around the world according to the prevailing conditions in each country. As of August 2011, McDonalds had 33,000 restaurants in 118 countries, employing 1.7 million people worldwide.¹¹⁸ In Europe, the company prefers wholly owned subsidiaries, since European markets are similar to those in the United States and can be run similarly. Those subsidiaries in the United States both operate company-owned stores and license out franchises. Approximately 80 percent of McDonald's stores around the world are franchised. In Asia, joint ventures are preferred so as to take advantage of partners' contacts and local expertise, and their ability to negotiate with bureaucracies such as the Chinese government. McDonald's has more than 1,000 stores in Japan and it continues its expansion in China, in spite of conflicts with the Chinese government, such as when it made McDonald's move from its leased Tiananmen Square restaurant. In other markets, such as in Saudi Arabia, McDonald's prefers to limit its equity risk by licensing the name—adding strict quality standards—and keeping an option to buy later.

Timing Entry and Scheduling Expansions

As with McDonald's, international strategic formulation requires a long-term perspective. Entry strategies, therefore, need to be conceived as part of a well-designed, overall plan. In the past, many companies have decided on a particular means of entry that seemed appropriate at the time, only to find later that it was shortsighted. For instance, if a company initially chooses to license a host-country company to produce a product, then later decides that the market is large enough to warrant its own production facility, this new strategy will no longer be feasible because the local host-country company already owns the rights.

The Influence of Culture on Strategic Choices

*Certain cultures are considered attractive to other cultures. A foreign culture's perceived attributes may be a major reason for the preferences expressed by potential partners and host countries.*¹¹⁹

JOURNAL OF INTERNATIONAL BUSINESS,
JANUARY 2012.

It is clear that cultural distance (CD), or at least the perception of it, affects strategic choice. Potential partners and their host counterparts tend to feel more confident about their international allies when they seem “culturally attractive,” in particular when new to international business. The more similar the culture, the more likely managers are to select that region for investment—for example, between the United States and England. However, often that assumption of similarity leads to problems because preparation and allowance is not made for existing subtle differences. Shenkar gives the examples that the “friction” between dissimilar cultures is more likely in a merger or acquisition than in an IJV—because there is more interaction among parties in the former—whereas an IJV is set up as a separate entity with less interaction from the parent firms.¹²⁰ Managers armed with such insight might then choose an IJV over other strategic options which necessitate more cross-cultural interaction.

In addition, strategic choices at various levels often are influenced by specific cultural factors, such as a long-term versus a short-term perspective. Hofstede found that most people in such countries as China and Japan generally had a longer-term horizon than those in Canada and the United States.¹²¹ Whereas Americans, then, might make strategic choices with a heavy emphasis on short-term profits, the Japanese are known to be more patient in sacrificing short-term results in order to build for the future with investment, research and development, and market share.

Risk orientation was also found to explain the choice between equity and non-equity modes.¹²² Risk orientation relates to Hofstede's uncertainty avoidance dimension.¹²³ Firms from countries where, generally speaking, people tend to avoid uncertainty (for example, Latin American and African countries) tend to prefer non-equity entry modes to minimize exposure to risk. Managers from firms from low-uncertainty avoidance countries are more willing to take risks and are, therefore, more likely to adopt equity entry modes.¹²⁴

The choice of the equity versus non-equity mode has also been found to be related to level of power distance. According to Hofstede, a high power-distance country (such as Arab countries and Japan) is one where people observe interpersonal inequality and hierarchy.¹²⁵ Pan and Tse found that firms from countries tending toward high power distance are more likely to use equity modes of entry abroad.¹²⁶

These are but a few of the examples of the relationships between culture and the choices that are made in the strategic planning and implementation phase. They serve to remind us that it is people who make those decisions and that the ways people think, feel, and act are based on their ingrained societal culture. People bring that context to work, and it influences their propensity toward or against certain types of decisions.

CONCLUSION

The process of strategic formulation for global competitiveness is a daunting task in the volatile global arena and is further complicated by the difficulties involved in acquiring timely and credible information. However, early insight into global developments provides a critical advantage in positioning a firm for future success.

When an entry strategy is selected, the international manager focuses on translating strategic plans into actual operations. Often this involves strategic alliances; always it involves functional-level activities for strategic implementation. These subjects are covered in Chapter 7.

Summary of Key Points

1. Companies “go international” for many reasons, both proactive and reactive. Those companies that are proactive from their outset in establishing a presence in many countries are referred to as “Born Globals.” The Internet is facilitating companies of all sizes to expand around the world within a short time frame—thus leveling the field for small businesses relative to companies with greater resources.
2. International expansion and the resulting realization of a firm’s strategy are the products of both rational planning and responding to emergent opportunities. For example, those opportunities may develop as a result of economic, competitive, demographic, or political changes in other countries. Firms are increasingly taking advantage of opportunities for expansion into emerging markets such as the “BRICs.”
3. The steps in the rational planning process for developing an international corporate strategy comprise defining the mission and objectives of the firm, scanning the environment for threats and opportunities, assessing the internal strengths and weaknesses of the firm, considering alternative international entry strategies, and deciding on strategy. The strategic management process is completed by putting into place the operational plans necessary to implement the strategy and then setting up control and evaluation procedures.
4. Competitive analysis is an assessment of how a firm’s strengths and weaknesses vis-à-vis those of its competitors affect the opportunities and threats in the international environment. Such assessment allows the firm to determine where the company has distinctive competencies that will give it strategic advantage or where problem areas exist.
5. Corporate-level strategic approaches to international competitiveness include globalization and regionalization. Many MNCs have developed to the point of using an integrative global strategy. Entry and ownership strategies are exporting, licensing, franchising, contract manufacturing, offshoring, outsourcing services, turn-key operations, management contracts, joint ventures, and fully owned subsidiaries, as well as the local level of e-business. Critical environmental and operational factors for implementation must be taken into account.
6. Companies of all sizes are increasingly looking to the Internet as a means of expanding their global operations, but localizing Internet operations is complex, involving various logistical and cultural challenges.

Discussion Questions

1. Discuss why companies “go international,” giving specific reactive and proactive reasons.
2. What effects on company strategy have you observed as a result of the global economic downturn?
3. Give examples of the impact of the Internet on small businesses.
4. Discuss the ways in which managers arrive at new strategic directions—formal and informal. Which is the best?
5. Explain the process of environmental assessment. What are the major international variables to consider in the scanning process? Discuss the levels of environmental monitoring that should be conducted. How well do you think managers conduct environmental assessment?
6. Discuss the impact of the rise of emerging market countries on the strategic planning of firms around the world.
7. How can managers assess the potential relative competitive position of their firm in order to decide on new strategic directions?
8. Discuss the relative advantages of globalization versus regionalization/localization.
9. Compare the merits of the entry strategies discussed in this chapter. What is their role in an integrative global strategy?
10. Discuss the considerations in strategic choice, including the typical stages of the MNC and the need for a long-term global perspective.

Application Exercises

1. Choose a company in the social media industry or a chain in the fast-food industry. In small groups, conduct a multilevel environmental analysis, describing the major variables involved, the relative impact of specific threats and opportunities, and the critical environmental factors to be considered. The group findings can then be presented to the class, allowing a specific time period for each group so that comparison and debate of different group perspectives can follow. Be prepared to state what regions or specific countries you are interested in and give your rationale.
2. In small groups, discuss among yourselves and then debate with the other groups the relative merits of the alternative entry strategies for the company and countries you chose in Exercise 1. You should be able to make a specific choice and defend that decision.

3. For this exercise, research (individually or in small groups) a company with international operations and find out the kinds of entry strategies the firm has used. Present the information you find, in writing or verbally to the class, describing the nature of the com-

pany's international operations, its motivations, its entry strategies, the kinds of implementation problems the firm has run into, and how those problems have been dealt with.

Experiential Exercise

In groups of four, develop a strategic analysis for a type of company that is considering entry into an emerging market country.

Which entry strategies seem most appropriate? Share your results with the class.

Internet Resources

Visit the Deresky Companion Website at www.pearsonhighered.com/deresky for this chapter's Internet resources.

CASE STUDY

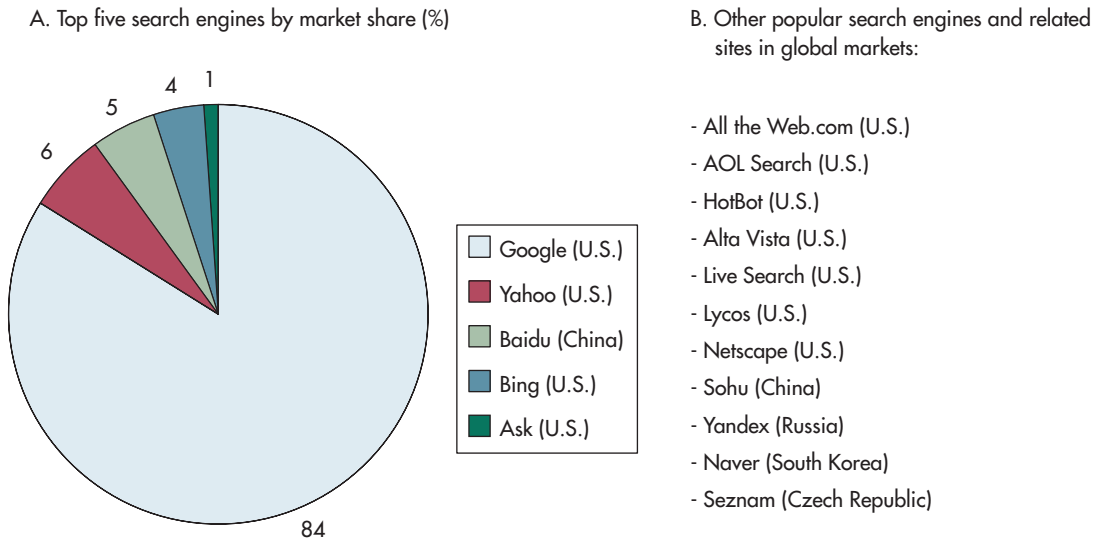
Search Engines in Global Business

A search engine is designed in such a way to actually find useful information on the World Wide Web (WWW) and file transfer protocol (FTP) servers. In technical terms, the search queries and their results show up in the forms of search engine results pages (SERPS) and related information. This information may encompass Web images and other types of useful files. Data mining is also part of this process.¹ In today's fast-changing global business and MNCs' diverse operations in domestic and global markets, search engines are highly useful and have been introduced in a multitude of languages. Local cultures and environments matter a lot when designing country-specific search engines.

In global business, data is an important part of search engines. As of 2012, the need for large-scale data is everywhere (consumers and businesses) in global business. The *Economist* in its annual *World in 2012* wrote: "Many more firms will start to analyze huge piles of data to optimize everything from their supply chains to their customer relationships."² Search engines come in different forms and types and may include: general search engines, P2P search engines, meta-search engines, information-specific search engines, geographically based search engines, business search engines, enterprise search engines, and others.³

Figure 6-2 provides information on the main search engines in global business. Interestingly, most of the search engines are available worldwide but are based in the U.S. This shows the power of information-related companies that own these search engines. As of 2012, Google is the most popular and powerful search engine in the world, followed by Yahoo, Baidu (China), Bing, and Ask. Of course Google is highly diversified in its products and maintains sites in various languages. This is a perfect reflection of today's global business with diverse markets and consumers. Google also maintains Google Docs, Google Calendar, Google Site Search, Google Maps, etc.⁴ In 2012, Google sales surpassed \$37 billion with a market capitalization of \$200 billion. This shows the immense power and coverage of this search engine.

Search engines in global business are mostly impacted by local cultures, country-specific data, and national identities. For example, as of 2012, "Baidu" is the largest search engine in China with sales of \$2.5 billion, and it carries a market capitalization of \$48 billion.⁵ "Yandex" is a major search engine in Russia. In addition, South Korea maintains "Naver," Czech Republic has "Seznam"; "Sohu" is distinctly available in the Chinese market and continues to be a dominant player. Regardless of their types and forms, search engines in global business are highly differentiated on the basis of their functions, country image, and usage. Search engines' transaction data and search results can reveal an interesting array of data. The search engines and their commercial identity are highly country- and region-specific. No wonder we witness a few search engines that continue to dominate global business. This is also the result of complex value chains where information is commoditized and content specific. In short, search engines such as Google, Yahoo, Baidu, Yandex, Naver, and others will play a major role in their country-specific

FIGURE 6-2 Search Engine Market Share in Global Markets (2012)

Sources: Marketshare.hitslink.com (2012); Pinnaclepixel.com (2012); *Search Engine Colossus* (2012); Wikipedia (2012).

environments because of business efficiencies and productivity issues. The area is still in its infancy and growth stage and will have massive repercussions for MNCs, domestic companies, governments, and consumers worldwide.⁶ Above all, consumers' privacy and national policies are major variables in the growth of global search engines.

Case Questions

1. Compare and contrast the top five search engines in global business.
2. Within today's changing global business, what do you see happening in the next five years regarding search engines' growth and country-specific issues?
3. Search engines carry national identities and cultures. Compare major search engines from each continent on the basis of their local characteristics and national identities.

Source:

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