Strategic Management

Undergraduate course in Management

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ISEG 100 1911-2011 ANOS

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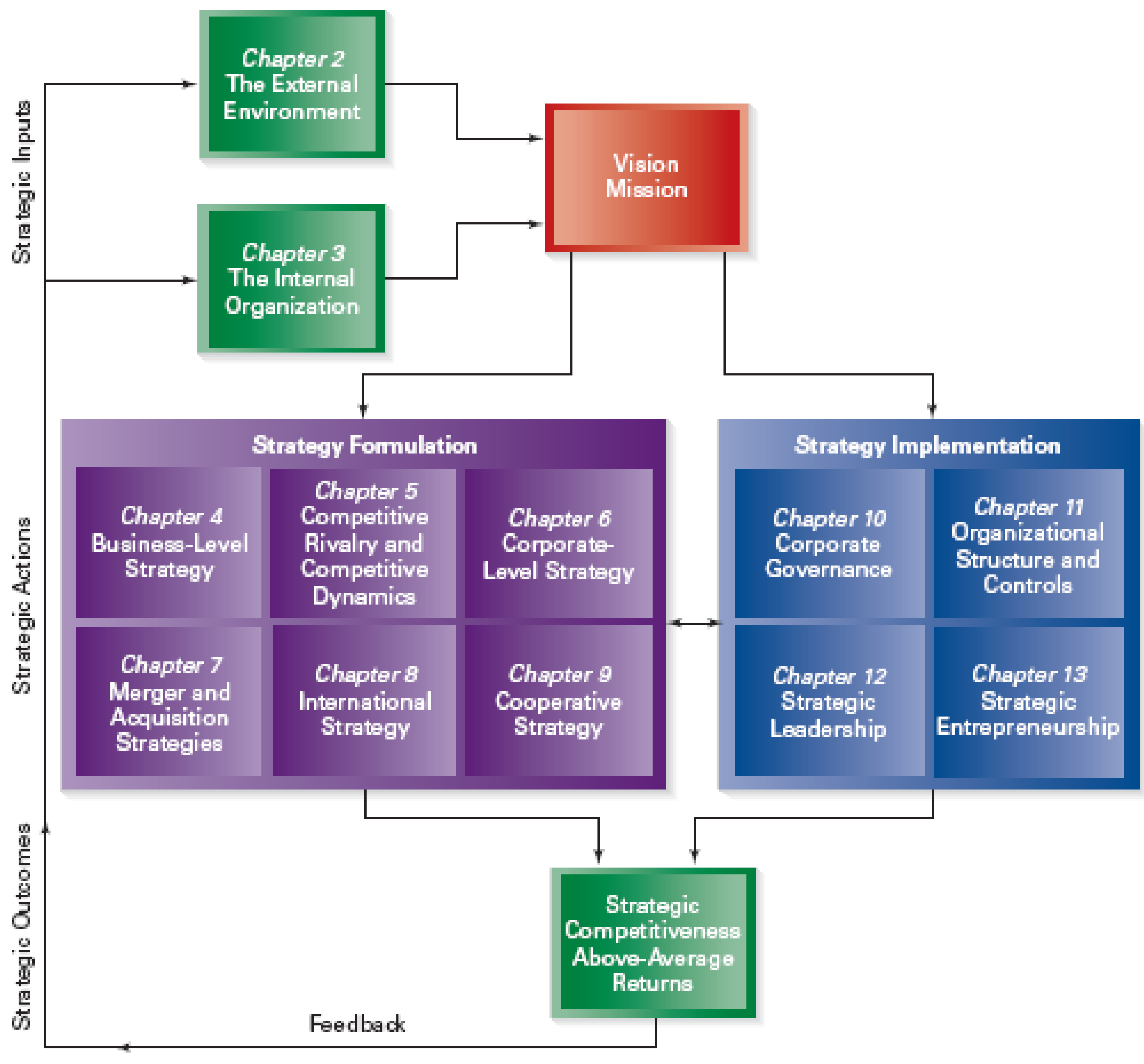
The Strategic Management Process

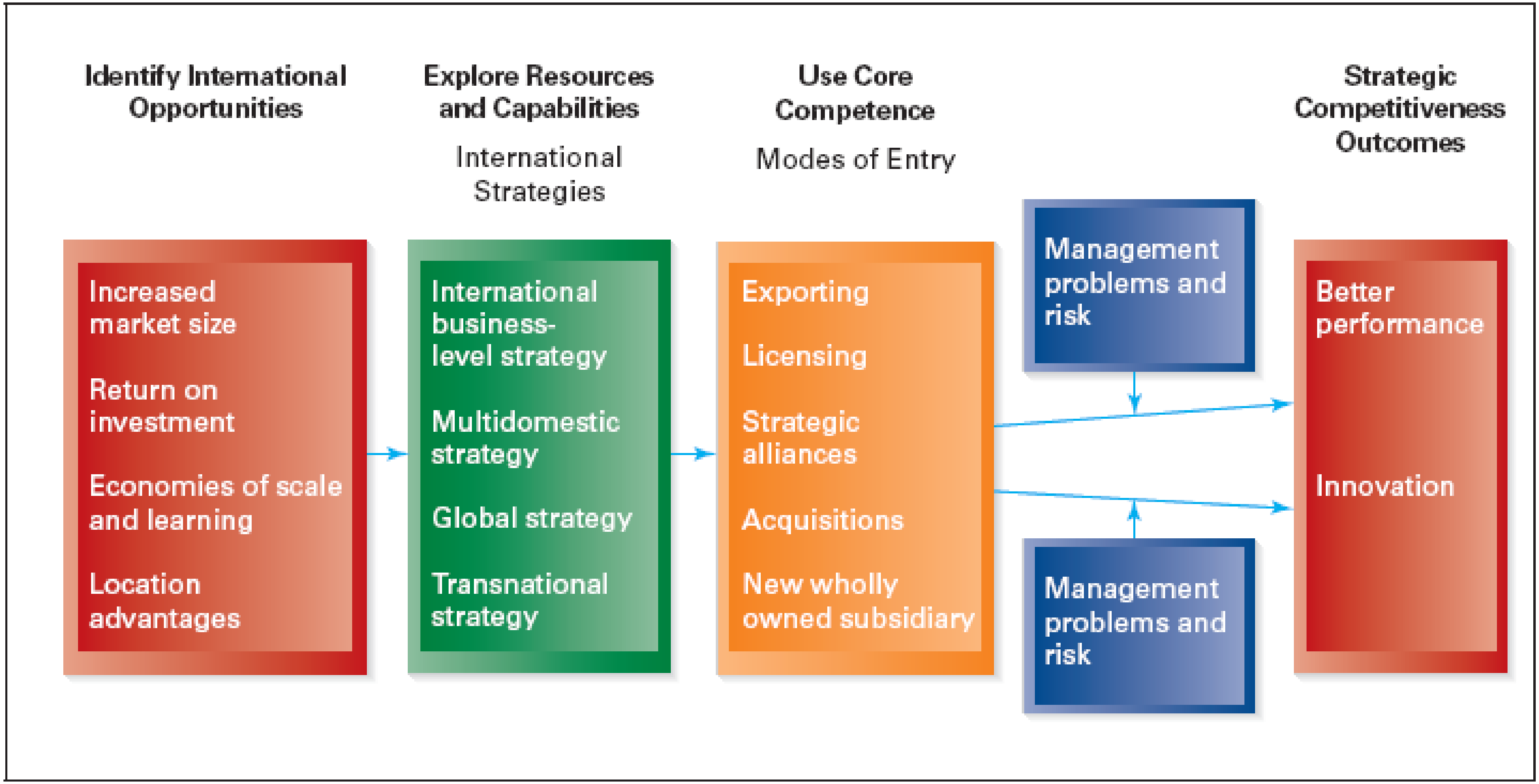


Chapter 8. International Strategy

Eight content areas

- **Traditional vs. emerging motives**
- **Four major benefits of International Strategies (IS)**
- Four factors as basis for international business strategy
- Three international corporate-level strategies
- Environmental trends affecting IS
- Five alternative modes for entering international markets
- Effects of international diversification on returns & innovation
- Two major risks of international diversification

Opportunities and Outcomes of IS



Identifying International Opportunities: Incentives to Use an IS

- **IS:** firm sells its goods or services outside the domestic market
- **Reasons for an IS**
  - International markets yield potential new opportunities
  - International diversification: innovation occurs in home-country market, especially in an advanced economy, and demand for product develops in other countries, so exports provided by domestic organization
  - Multinational strategy: Secure need resources
  - Other motives exist (i.e., pressure for global integration, borderless demand for globally branded products)

Identifying International Opportunities: Incentives to Use an IS

Four primary reasons:

1. Increased market size
   - Domestic market may lack the size to support efficient scale manufacturing facilities
2. Return on Investment (ROI)
   - Large investment projects may require global markets to justify the capital outlays
   - Weak patent protection in some countries implies that firms should expand overseas rapidly in order to preempt imitators
3. Economies of Scale and Learning
   - Expanding size or scope of markets helps to achieve economies of scale in manufacturing as well as marketing, R&D, or distribution
   - Costs are spread over a larger sales base
   - Profit per unit is increased
4. Location advantages: Low cost markets may…
   - … aid in developing competitive advantage
   - … achieve better access to critical resources: i.e. raw materials, lower cost labor, key customers, energy

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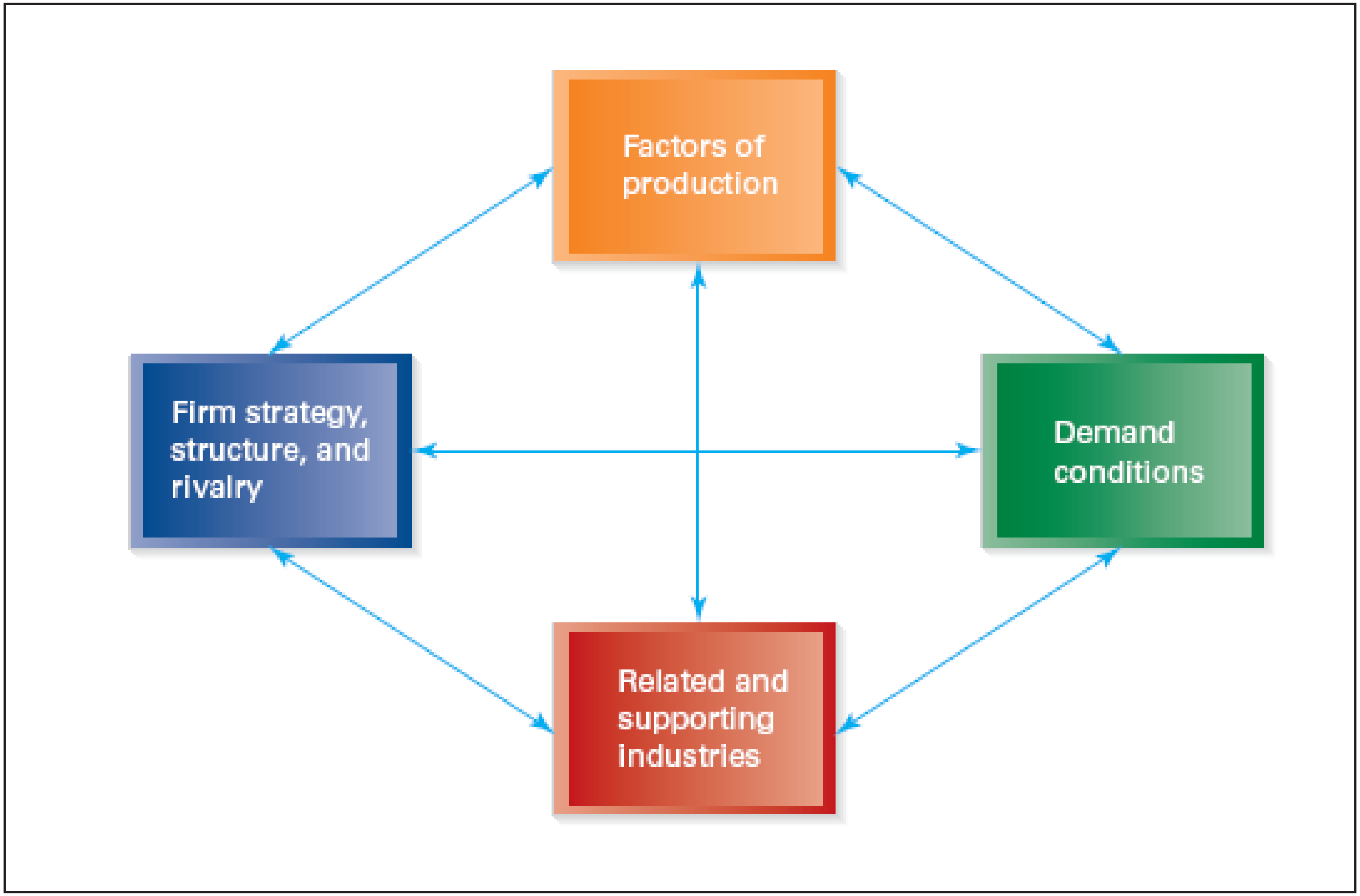
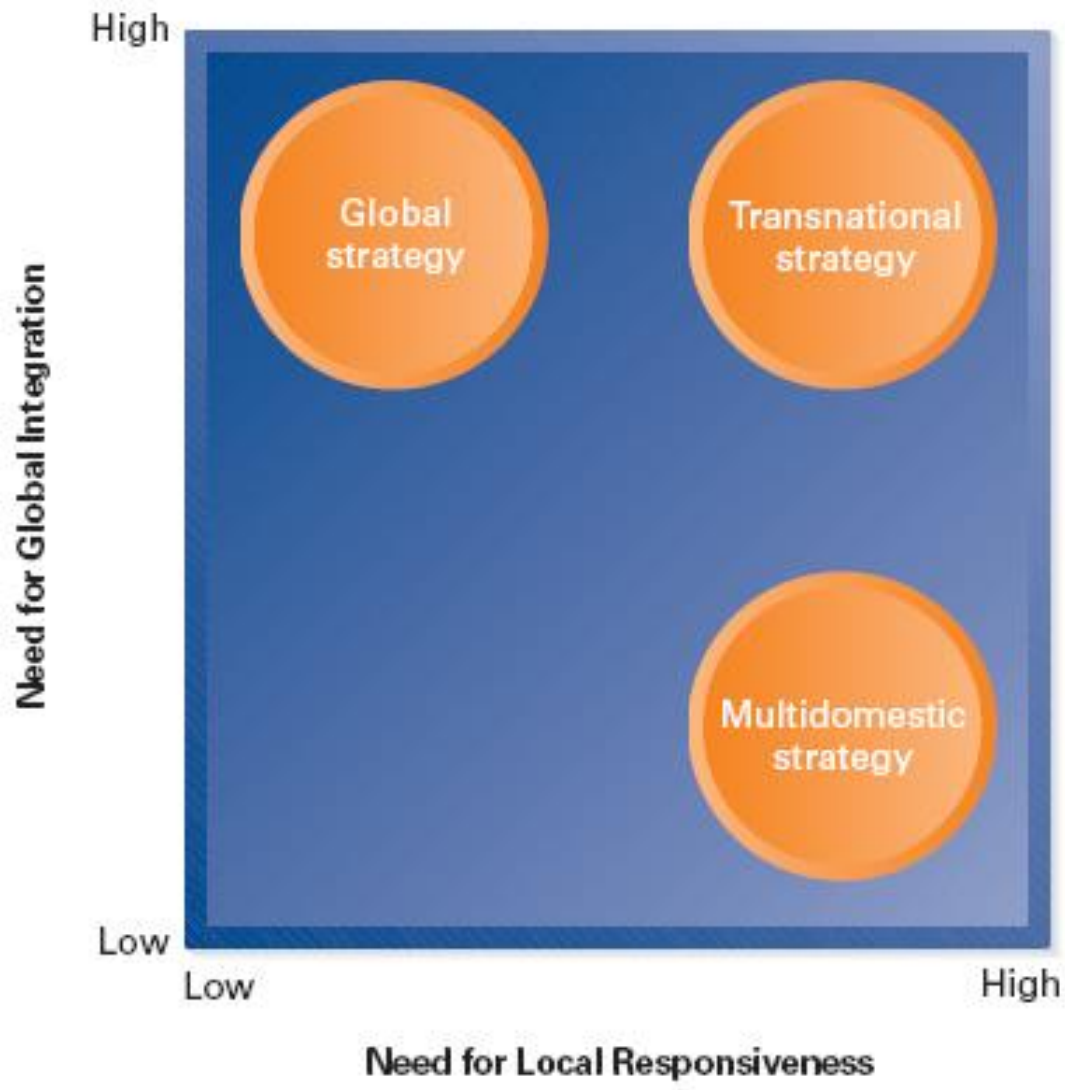
International Strategies

- Firms choose one or both of two basic type of IS: Business level and/or Corporate level
- International business-level strategy
  - Follows generic strategies of cost-leadership, differentiation, focused or broad
- International corporate-level strategy (N=3)
  - Home country usually most important source of competitive advantage
    - Resources and capabilities frequently allow firm to pursue markets in other countries
    - The determinants of national advantage includes 4 factors

Determinants of National Advantage



International Corporate-level Strategies



1. Multidomestic

- Decentralized strategic & operating decisions by strategic business-unit (SBU) in each country allows units to tailor products to local markets
- Focuses on variations of competition within each country
- Customized products to meet local customers' specific needs and preferences
- Takes steps to isolate the firm from global competitive forces
  - Establish protected market positions
  - Compete in industry segments most affected by differences among local countries
- Deals with uncertainty from differences across markets

2. Global

- Firm offers standardized products across country markets, with the competitive strategy being dictated by the home office
- Emphasizes economies of scale
- Facilitated by improved global reporting standards (i.e., accounting and financial)
- Strategic & operating decisions centralized at home office
- Involves interdependent SBUs operating in each country
- Home office attempts to achieve integration across SBUs, adding management complexity
- Produces lower risk
- Is less responsive to local market opportunities, preferences and needs
- Offers less effective learning processes (pressure to conform and standardize)

3. Transnational

- Firm seeks to achieve both global efficiency and local responsiveness – these are competing goals!
- Requires both global coordination and local flexibility with this strategy/structure combination
  - Flexible Coordination: Building a shared vision and individual commitment through an integrated network
- Challenging, but becoming increasingly necessary to compete in international markets
- Growing number of global competitors heightens need to keep costs down while greater information flow and desire for specialized products pressures firms to differentiate and even customize products – nonetheless,
- Increasingly used as a strategy

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Environmental Trends

- Transnational strategy hard to implement
- Two new trends:

1. Liability of foreignness
   - Increased after terrorists' attacks and Iraq War
   - Global strategies not as prevalent today, still difficult to implement even with Internet-based strategies
   - Regional focus allows firms to marshal resources to compete effectively in regional markets
2. Regionalization
   - Focus to a particular region of the world
     - Increases understanding of market
     - Achieve some economies
     - Trade agreements (i.e., EU, OAS, NAFTA) promote flow of trade across country boundaries with their respective regions

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International Entry Modes

Follows the selection of an IS

Five main entry modes

1. Exporting
2. Licensing
3. Strategic Alliances
4. Acquisitions
5. New Wholly-Owned Subsidiary

International Entry Modes

1. Exporting

- Involves low expense to establish operations in host country
- Often involves contractual agreements
- Involves high transportation costs
- May have some tariffs imposed
- Offers low control over marketing and distribution

2. Licensing

- Involves low cost to expand internationally
- Allows licensee to absorb risks
- Has low control over manufacturing and marketing
- Offers lower potential returns (shared with licensee)
- Involves risk of licensee imitating technology and product for own use
- May have inflexible ownership arrangement

International Entry Modes

3. Strategic Alliances

- Involve shared risks and resources
- Facilitate development of core competencies
- Involve fewer resources and costs required for entry
- May involve possible incompatibility, conflict, or lack of trust with partner
- Are difficult to manage

4. Acquisitions

- Allow for quick access to market
- Involve possible integration difficulties
- Are costly
- Have complex negotiations and transaction requirements

5. New Wholly-Owned Subsidiary

- Is costly
- Involves complex processes
- Allows for maximum control
- Has the highest potential returns
- Carries high risk
- Greenfield venture: Establish entirely new subsidiary

Dynamics of Mode of Entry: Use the best suited to the situation at hand; affected by several factors

- Export, licensing and strategic alliance: good tactics for early market development
- Strategic alliance: used in more uncertain situations
- Wholly-owned subsidiary may be preferred if
  - IP rights in emerging economy not well protected
  - Number of firms in industry is growing fast
  - Need for global integration is high
- Acquisitions or greenfield ventures: secure a stronger presence in international markets

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Strategic Competitive Outcomes

- International diversification: firm expands sales of its goods or services across the borders of global regions and countries into different geographic locations or markets
- Implementation follows selection of IS and mode of entry
- Topics to take into account:
  1. International diversification and returns
  2. International diversification and innovation
  3. Complexity of managing multinational firms

Strategic Competitive Outcomes

1. International diversification and returns
   - As international diversification increases, firms' returns initially decrease, but then increase quickly as the firm learns to manage international expansion
2. International diversification and innovation
   - Exposure to new products and markets
   - Opportunity to integrate new knowledge into operations
   - Generation of resources to sustain innovation efforts
3. Complexity of managing multinational firms
   - Geographic dispersion
   - Costs of coordination
   - Logistical costs
   - Trade barriers
   - Cultural diversity
   - Host government

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Risks in International Management

- Two major risks
  1. Political
  2. Economic
- Limits to international expansions: management problems

Risks in the International Environment

- Political Risks
  - War in Iraq and Afghanistan following the September 11, 2001, terrorist attacks
  - Continual warfare between the Palestinians and Israel
  - Potential of war between Pakistan and India
  - The challenge of integrating former Eastern European Block countries into the European Union and the Soviet reaction
  - Protectionist political trends as the economic downturn worsens
- Economic Risks
  - Failure of countries to pay debt obligations and the devaluation of their currencies in the economic downturn
  - Challenges for China in implementing the World Trade Organization agreements
  - The proposed constitution as well as entry of new countries into the European Union strengthening the euro currency and uniting Europe more tightly with existing and new partner countries
  - Success and failure of privatization and firm restructuring among Eastern European countries
  - The increased trend of counterfeit products and the lack of global policing of these products

Risks in the International Environment

1. **Political risks**
    - Government instability
    - Conflict or war
    - Government regulations
    - Conflicting and diverse legal authorities
    - Potential nationalization of private assets
    - Government corruption
    - Changes in government policies
2. **Economic risks**
    - Differences and fluctuations in currency values
    - Investment losses due to political risks

Limits to international expansions: management problems

- Geographic dispersion
- Trade barriers
- Logistical costs
- Cultural diversity
- Other differences by country
- Relationship between organization and host country