Chapter 8: International Strategy (IS)

• Overview: 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
Introduction

- Many firms choose direct investment in assets over indirect investment – Provides better protection for assets
Identifying International Opportunities: Incentives to Use an International Strategy (IS)

- **International Strategy (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 International Strategy (IS) (Cont’d)

• 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
Identifying International Opportunities: Incentives to Use an International Strategy (IS) (Cont’d)

• Four primary reasons (Cont’d)
  – 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
International Strategies (IS)

- Firms choose one or both of two basic types 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
  - 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

Factors of production

Firm strategy, structure, and rivalry

Demand conditions

Related and supporting industries
International Corporate-Level Strategies
International Strategies (IS) (Cont’d)

• **International corporate-level strategies** (Cont’d)

• **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

- 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
- Offers less effective learning processes (pressure to conform and standardize)
International Strategies (IS) (Cont’d)

• 3. Transnational
  – 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
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
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 (Cont’d)

• 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
International Entry Modes (Cont’d)

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
• 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
International Entry Modes (Cont’d)

4. Acquisitions
   - Allow for quick access to market
   - Involve possible integration difficulties
   - Are costly
   - Have complex negotiations and transaction requirements
International Entry Modes (Cont’d)

• 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
International Entry Modes (Cont’d)

• 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
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 international strategy and mode of entry

- 1. International diversification and returns
- 2. International diversification and innovation
- 3. Complexity of managing multinational firms
Strategic Competitive Outcomes (Cont’d)

• 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
Risk 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 International Environment (Cont’d)

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
Risks in International Environment (Cont’d)

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