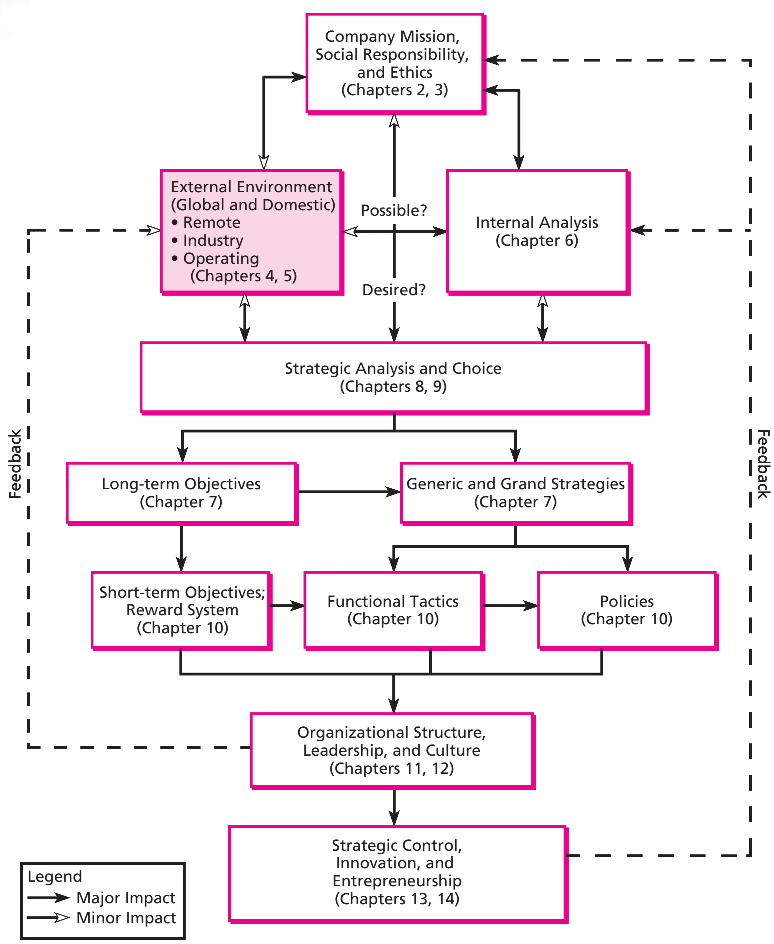
Chapter Five

The Global Environment

After reading and studying this chapter, you should be able to

1. Explain the importance of a company's decision to globalize.
2. Describe the four main strategic orientations of global firms.
3. Understand the complexity of the global environment and the control problems that are faced by global firms.
4. Discuss major issues in global strategic planning, including the differences for multinational and global firms.
5. Describe the market requirements and product characteristics in global competition.
6. Evaluate the competitive strategies for firms in foreign markets, including niche market exporting, licensing and contract manufacturing, franchising, joint ventures, foreign branching, private equity, and wholly owned subsidiaries.



GLOBALIZATION

globalization
The strategy of approaching worldwide markets with standardized products.

Special complications confront a firm involved in the globalization of its operations. **Globalization** refers to the strategy of approaching worldwide markets with standardized products. Such markets are most commonly created by end consumers that prefer lower-priced, standardized products over higher-priced, customized products and by global corporations that use their worldwide operations to compete in local markets. Global corporations headquartered in one country with subsidiaries in other countries experience difficulties that are understandably associated with operating in several distinctly different competitive arenas.

Awareness of the strategic opportunities faced by global corporations and of the threats posed to them is important to planners in almost every domestic U.S. industry. Among corporations headquartered in the United States that receive more than 50 percent of their annual profits from foreign operations are Citicorp, Coca-Cola, ExxonMobil, Gillette, IBM, Otis Elevator, and Texas Instruments. In fact, the 100 largest U.S. globals earn an average of 37 percent of their operating profits abroad. Equally impressive is the effect of foreign-based globals that operate in the United States. Their "direct foreign investment" in the United States now exceeds $90 billion, with Japanese, German, and French firms leading the way.

Understanding the myriad and sometimes subtle nuances of competing in global markets or against global corporations is rapidly becoming a required competence of strategic managers. For example, experts in the advertising community contend that Korean companies only recently recognized the importance of making their names known abroad. In the 1980s, there was very little advertising of Korean brands, and the country had very few recognizable brands abroad. Korean companies tended to emphasize sales and production more than marketing. The opening of the Korean advertising market in the 1990s indicated that Korean firms had acquired a new appreciation for the strategic competencies that are needed to compete globally and created an influx of global firms like Saatchi and Saatchi, J. W. Thompson, Ogilvy and Mather, and Bozell. Many of them established joint ventures or partnerships with Korean agencies. An excellent example of such a strategic approach to globalization by Philip Morris's KGFI is described in Exhibit 5.1, Global Strategy in Action. The opportunities for corporate growth often seem brightest in global markets. Exhibit 5.2 reports on the growth in national shares of the world's outputs and growth in national economies to the year 2020. While the United States had a commanding lead in the size of its economy in 1992, it was caught by China in the year 2000 and will be far surpassed by 2020. Overall, in less than 20 years, rich industrial countries will be overshadowed by developing countries in their produced share of the world's output.

Because the growth in the number of global firms continues to overshadow other changes in the competitive environment, this section will focus on the nature, outlook, and operations of global corporations.

DEVELOPMENT OF A GLOBAL CORPORATION

The evolution of a global corporation often entails progressively involved strategy levels. The first level, which often entails export-import activity, has minimal effect on the existing management orientation or on existing product lines. The second level, which can involve foreign licensing and technology transfer, requires little change in management or operation. The third level typically is characterized by direct investment in overseas operations, including manufacturing plants. This level requires large capital outlays and the development of global management skills. Although the domestic operations of a firm at this level

Global Strategy in Action — Exhibit 5.1

The Globalization of Philip Morris's KGFI

Outside of its core Western markets, Kraft General Foods International's (KGFI) food products have a growing presence in one of the most dynamic business environments in the world—the Asia-Pacific region. Its operations there are expanding rapidly, often aided by links with local manufacturers and distributors.

Japan and Korea are important examples. In both countries, local alliances can be crucial to market entry and success. Realizing this fact in the early 1970s, General Foods established joint ventures in both Japan and Korea. These joint ventures, combined with Kraft General Foods International's (KGFI) stand-alone operations, generate more than $1 billion in revenues. In the aggregate, their combined food operations in Japan and Korea are larger than many *Fortune* 500 companies.

Whereas soluble coffee accounts for just over 25 percent of the coffee consumed in U.S. homes, it fills more than 70 percent of the cups consumed in the homes of convenience-minded Japan. Additionally, Japan is the origin of a unique form of packaged coffee—liquid—and a unique channel of distribution—vending machines. Japanese consumers have purchased packaged liquid coffee for years, and it amounts to a $5 billion category. Some 2 million vending machines dispense 9 billion cans of liquid coffee annually—an average of 75 cans per person.

Japan offers a culturally unique distribution channel for coffee products—the gift-set market. Many Japanese exchange specially packaged food or beverage assortments at least twice a year to commemorate holidays as well as special personal or business occasions. The gift-set business has helped Maxim products reinforce their quality image; it also will be a launching pad and support vehicle for Carte Noire coffees.

Outside the Ajinomoto General Foods joint venture, KGFI is developing a freestanding food business under the name Kraft Japan. It is building a cheese business with imported Philadelphia Brand cream cheese, the leading cream cheese in the Tokyo metropolitan market, as well as locally manufactured and licensed Kraft Milk Farm cheese slices. The cheese market is expected to grow approximately 5 percent per year. This is a rapid growth rate for a large food category. In addition to cheese, KGFI also imports Oscar Mayer prepared meats and Jocobs Suchard chocolates.

KGFI's joint venture in Korea, Doug Suh Foods Corporation, is one of the top 10 food companies in the country. Doug Suh manufactures coffees and cereals and has its own distribution network. One of Doug Suh's other businesses in Korea, Post Cereals, is also a strong number two, with a 42 percent category share.

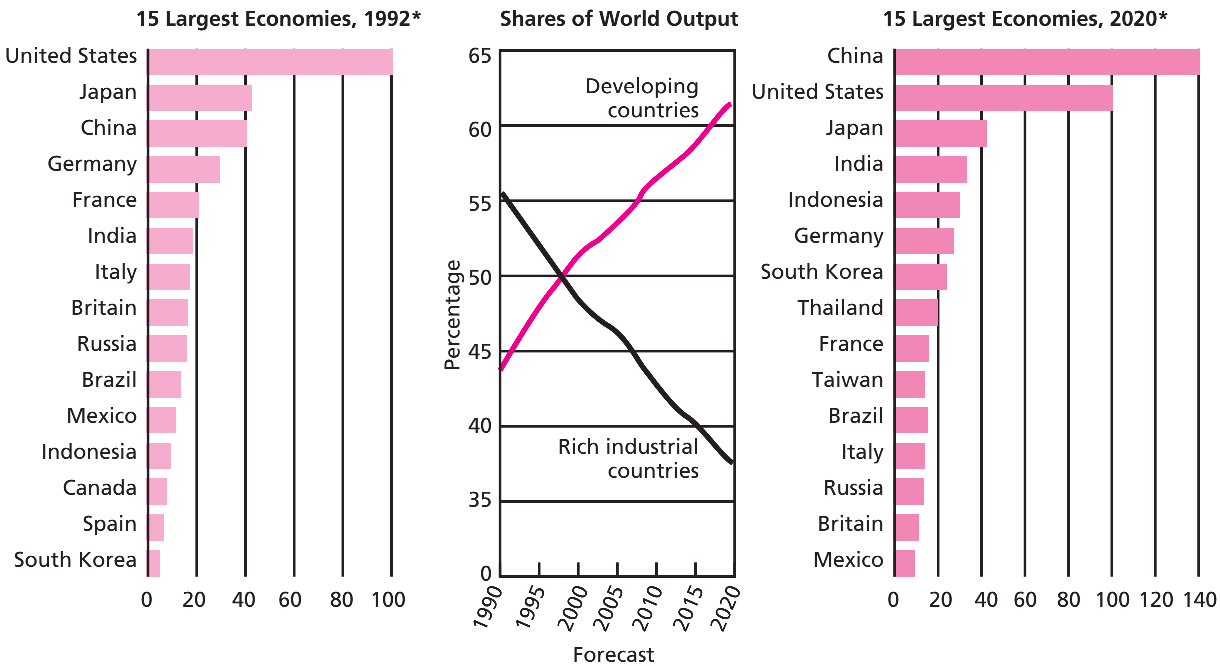
Korea's $400 million coffee market is the fastest-growing major coffee market in the world, expanding at an average annual rate of 14 percent. Growing with the market, Maxim and Maxwell soluble coffees, in both traditional "agglomerate" and freeze-dried forms, account for more than 70 percent of the country's soluble coffee sales. The strength of these brands also brings the company a strong number one position in coffee mix, a mixture of soluble coffee, creamer, and sugar. In addition, its Frima brand leads the market in the nondairy creamer segment.

Beyond Japan and Korea, KGFI is targeting many other countries for geographic expansion. In Indonesia, for instance, KGFI has established a rapidly growing cheese business through a licensee and introduced other KGFI products. In Taiwan, the joint venture company, PremierFoods Corporation, holds a 34 percent share of the soluble coffee market and is aggressively developing a Kraft cheese and Jocobs Suchard import business. KGFI Philippines, a wholly owned subsidiary, has a leading position in the cheese and powdered soft-drink markets in its country. In the People's Republic of China, the company produces and markets Maxwell House coffees and Tang powdered soft drinks through two successful and rapidly growing joint ventures.

continue to dominate its policy, such a firm is commonly categorized as a true multinational corporation (MNC). The most involved strategy level is characterized by a substantial increase in foreign investment, with foreign assets comprising a significant portion of total assets. At this level, the firm begins to emerge as a global enterprise with global approaches to production, sales, finance, and control.

To get a more complete understanding of the many elements of a multinational environment that need to be considered by strategic planners, study Appendix 5-A. It contains lists of important competitive issues that will help you to see the complexity of the multinational landscape and to better appreciate the complicated and sophisticated nature of strategic planning.

EXHIBIT 5.2 Projected Economic Growth



Source: World Bank, *Global Economic Prospects and the Developing Countries.*

Some firms downplay their global nature (to never appear distracted from their domestic operations), whereas others highlight it. For example, General Electric's formal statement of mission and business philosophy includes the following commitment:

> To carry out a diversified, growing, and profitable worldwide manufacturing business in electrical apparatus, appliances, and supplies, and in related materials, products, systems, and services for industry, commerce, agriculture, government, the community, and the home.

A similar global orientation is evident at IBM, which operates in 125 countries, conducts business in 30 languages and more than 100 currencies, and has 23 major manufacturing facilities in 14 countries.

WHY FIRMS GLOBALIZE

The technological advantage once enjoyed by the United States has declined dramatically during the past 30 years. In the late 1950s, more than 80 percent of the world's major technological innovations were first introduced in the United States. By 1990, the figure had declined to less than 50 percent. In contrast, France is making impressive advances in electric traction, nuclear power, and aviation. Germany leads in chemicals and pharmaceuticals, precision and heavy machinery, heavy electrical goods, metallurgy, and surface transport equipment. Japan leads in optics, solid-state physics, engineering, chemistry, and process metallurgy. Eastern Europe and the former Soviet Union, the so-called COMECON (Council for Mutual Economic Assistance) countries, generate 30 percent of annual worldwide patent applications. However, the United States has regained some of its lost technological advantage. Through globalization, U.S. firms often can reap benefits from industries and technologies developed abroad. Even a relatively small service firm that possesses a distinct competitive advantage can capitalize on large overseas operations.

Diebold Inc. once operated solely in the United States, selling automated teller machines (ATMs), bank vaults, and security systems to financial institutions. However, with the U.S. market saturated, Diebold needed to expand internationally to continue its growth. The firm's globalization efforts led to both the development of new technologies in emerging markets and opportunistic entry into entirely new industries that significantly improved Diebold's sales.

In many situations, global development makes sense as a competitive weapon. Direct penetration of foreign markets can drain vital cash flows from a foreign competitor's domestic operations. The resulting lost opportunities, reduced income, and limited production can impair the competitor's ability to invade U.S. markets. A case in point is IBM's move to establish a position of strength in the Japanese mainframe computer industry before two key competitors, Fiyitsue and Hitachi, could dominate it. Once IBM had achieved a substantial share of the Japanese market, it worked to deny its Japanese competitors the vital cash and production experience they needed to invade the U.S. market.

Firms that operate principally in the domestic environment have an important decision to make with regard to their globalization: Should they act before being forced to do so by competitive pressures or after? Should they (1) be proactive by entering global markets in advance of other firms and thereby enjoy the first-mover advantages often accruing to risk-taker firms that introduce new products or services or (2) be reactive by taking the more conservative approach and following other companies into global markets once customer demand has been proven and the high costs of new-product or new-service introductions have been absorbed by competitors? Although the answers to these questions are determined by the specifics of the company and the context, the issues raised in Exhibit 5.3 are helpful to strategic decision makers faced with the dilemma.

ethnocentric orientation
When the values and priorities of the parent organization guide the strategic decision making of all its international operations.

polycentric orientation
When the culture of the country in which the strategy is to be implemented is allowed to dominate a company's international decision-making process.

regiocentric orientation
When a parent company blends its own predisposition with those of its international units to develop region-sensitive strategies.

geocentric orientation
When an international firm adopts a systems approach to strategic decision making that emphasizes global integration.

Strategic Orientations of Global Firms

Multinational corporations typically display one of four orientations toward their overseas activities. They have a certain set of beliefs about how the management of foreign operations should be handled. A company with an **ethnocentric orientation** believes that the values and priorities of the parent organization should guide the strategic decision making of all its operations. If a corporation has a **polycentric orientation,** then the culture of the country in which a strategy is to be implemented is allowed to dominate the decision-making process. In contrast, a **regiocentric orientation** exists when the parent attempts to blend its own predispositions with those of the region under consideration, thereby arriving at a region-sensitive compromise. Finally, a corporation with a **geocentric orientation** adopts a global systems approach to strategic decision making, thereby emphasizing global integration.

American firms often adopt a regiocentric orientation for pursing strategies in Europe. U.S. e-tailers have attempted to blend their own corporate structure and expertise with that of European corporations. For example, Amazon has been able to leverage its experience in the United States while developing regionally and culturally specific strategies overseas. By purchasing European franchises that have had regional success, E*Trade is pursuing a foreign strategy in which they insert their European units into corporate structure. This strategy requires the combination and use of culturally different management styles and involves major challenges for upper management.

Exhibit 5.4 shows the effects of each of the four orientations on key activities of the firm. It is clear from the figure that the strategic orientation of a global firm plays a major role in determining the locus of control and corporate priorities of the firm's decision makers.

EXHIBIT 5.3
Reasons for Going Global

Proactive	
Advantage/Opportunity	**Explanation of Action**
Additional resources	Various inputs—including natural resources, technologies, skilled personnel, and materials—may be obtained more readily outside the home country.
Lowered costs	Various costs—including labor, materials, transportation, and financing—may be lower outside the home country.
Incentives	Various incentives may be available from the host government or the home government to encourage foreign investment in specific locations.
New, expanded markets	New and different markets may be available outside the home country; excess resources—including management, skills, machinery, and money—can be utilized in foreign locations.
Exploitation of firm-specific advantages	Technologies, brands, and recognized names can all provide opportunities in foreign locations.
Taxes	Differing corporate tax rates and tax systems in different locations provide opportunities for companies to maximize their after-tax worldwide profits.
Economies of scale	National markets may be too small to support efficient production, while sales from several combined allow for larger-scale production.
Synergy	Operations in more than one national environment provide opportunities to combine benefits from one location with another, which is impossible without both of them.
Power and prestige	The image of being international may increase a company's power and prestige and improve its domestic sales and relations with various stakeholder groups.
Protect home market through offense in competitor's home	A strong offense in a competitor's market can put pressure on the competitor that results in a pull-back from foreign activities to protect itself at home.
Reactive	
Outside Occurrence	**Explanation of Reaction**
Trade barriers	Tariffs, quotas, buy-local policies, and other restrictive trade practices can make exports to foreign markets less attractive; local operations in foreign locations thus become attractive.
International customers	If a company's customer base becomes international, and the company wants to continue to serve it, then local operations in foreign locations may be necessary.
International competition	If a company's competitors become international, and the company wants to remain competitive, foreign operations may be necessary.
Regulations	Regulations and restrictions imposed by the home government may increase the cost of operating at home; it may be possible to avoid these costs by establishing foreign operations.
Chance	Chance occurrence results in a company deciding to enter foreign locations.

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EXHIBIT 5.4 Orientation of a Global Firm

	Orientation of the Firm			
	Ethnocentric	**Polycentric**	**Regiocentric**	**Geocentric**
Mission	Profitability (viability)	Public acceptance (legitimacy)	Profitability and public acceptance (viability and legitimacy)	Same as regiocentric
Governance	Top-down	Bottom-up (each subsidiary decides on local objectives)	Mutually negotiated between region and its subsidiaries	Mutually negotiated at all levels of the corporation
Strategy	Global integration	National responsiveness	Regional integration and national responsiveness	Global integration and national responsiveness
Structure	Hierarchical product divisions	Hierarchical area divisions, with autonomous national units	Product and regional organization tied through a matrix	A network of organizations (including some competitors)
Culture	Home country	Host country	Regional	Global
Technology	Mass production	Batch production	Flexible manufacturing	Flexible manufacturing
Marketing	Product development determined by the needs of home country	Local product development based on local needs	Standardize within region but not across regions	Global product, with local variations
Finance	Repatriation of profits to home country	Retention of profits in host country	Redistribution within region	Redistribution globally
Personnel practices	People of home country developed for key positions in the world	People of local nationality developed for key positions in their own country	Regional people developed for key positions anywhere in the region	Global personnel development and placement

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AT THE START OF GLOBALIZATION

External and internal assessments are conducted before a firm enters global markets. For example, Japanese investors conduct extensive assessments and analyses before selecting a U.S. site for a Japanese-owned firm. They prefer states with strong markets, low unionization rates, and low taxes. In addition, Japanese manufacturing plants prefer counties characterized by manufacturing conglomeration; low unemployment and poverty rates; and concentrations of educated, productive workers.

External assessment involves careful examination of critical features of the global environment, particular attention being paid to the status of the host nations in such areas as economic progress, political control, and nationalism. Expansion of industrial facilities, favorable balances of payments, and improvements in technological capabilities over the past decade are gauges of the host nation's economic progress. Political status can be gauged by the host nation's power in and impact on global affairs.

Internal assessment involves identification of the basic strengths of a firm's operations. These strengths are particularly important in global operations, because they are often the characteristics of a firm that the host nation values most and, thus, offer significant

Global Strategy in Action — Exhibit 5.5

Checklist of Factors to Consider in Choosing a Foreign Manufacturing Site

The following considerations were drawn from an 88-point checklist developed by Business International Corporation.

Economic Factors:
1. Size of GNP and projected rate of growth
2. Foreign exchange position
3. Size of market for the firm's products; rate of growth

Political Factors:
4. Form and stability of government
5. Attitude toward private and foreign investment by government, customers, and competition
6. Degree of antiforeign discrimination

Geographic Factors:
7. Proximity of site to export markets
8. Availability of local raw materials
9. Availability of power, water, gas

Labor Factors:
10. Availability of managerial, technical, and office personnel able to speak the language of the parent company
11. Degree of skill and discipline at all levels
12. Degree and nature of labor voice in management

Tax Factors:
13. Tax-rate trends
14. Joint tax treaties with home country and others
15. Availability of tariff protection

Capital Source Factors:
16. Cost of local borrowing
17. Modern banking systems
18. Government credit aids to new businesses

Business Factors:
19. State of marketing and distribution system
20. Normal profit margins in the firm's industry
21. Competitive situation in the firm's industry: do cartels exist?

bargaining leverage. The firm's resource strengths and global capabilities must be analyzed. The resources that should be analyzed include, in particular, technical and managerial skills, capital, labor, and raw materials. The global capabilities that should be analyzed include the firm's product delivery and financial management systems.

A firm that gives serious consideration to internal and external assessment is Business International Corporation, which recommends that seven broad categories of factors be considered. As shown in Exhibit 5.5, Global Strategy in Action, these categories include economic, political, geographic, labor, tax, capital source, and business factors.

COMPLEXITY OF THE GLOBAL ENVIRONMENT

By 2003, Coke was finally achieving a goal that it had set a decade earlier when it went to India. That goal was to take the market away from Pepsi and local beverage companies. However, when it arrived, Coke found that the Indian market was extremely complex and smaller than it had estimated. Coke also encountered cultural problems, in part because the chief of Coke India was an expatriate. The key to overcoming this cultural problem was promoting an Indian to operations chief. Coke also changed its marketing strategy by pushing their "Thums Up" products, a local brand owned by Coke. Then, they began to focus their efforts on creating new products for rural areas and lowering the prices of their existing products to increase sales. Once Coke had new products in the market, they focused on a new advertising campaign to better relate to Indian consumers.

Strategy in Action

Exhibit 5.6

A Milestone for Human Rights

BusinessWeek

In the mid-1990s, reports emerged out of Burma that villagers in the remote Yadana region had been forced by the military to clear jungle for the construction of a $1.2 billion natural gas pipeline. The allegations were horrendous: to round up workers for the project, the Burmese military had resorted to torture, rape, and murder to enslave villagers, even throwing one woman's baby in a fire after killing her husband. Before long, U.S. human rights groups had filed suit against Unocal Corp., based in El Segundo, California, one of the four pipeline partners, on behalf of 15 unnamed Burmese villagers.

Now, after years of courtroom sparring, Unocal has quietly agreed to settle the suits, one filed in California state court and another in the U.S. District Court in Los Angeles. Insiders say that Unocal will pay about $30 million in damages to settle the cases. The award will include money for the 15 plaintiffs and for a fund to improve living conditions, health care, and education in the pipeline region.

The settlement may mark a milestone in human rights advocates' struggle to use U.S. courts to force American multinationals to protect their workers against abuse by repressive regimes. The Unocal case "shows that corporations have both direct and indirect human rights responsibilities," says Susan Aaronson, director of globalization studies at the Kennan Institute, a Washington think tank.

Unocal is the first of a series of U.S. multinationals to face allegations that they acquiesced in or benefited from human rights violations, committed mostly by authoritarian governments. Other defendants include ExxonMobil, Coca-Cola, Drummond, Occidental Petroleum, and Del Monte Foods. The companies are all fighting the suits.

Source: Reprinted with special permission from Paul Magnusson, "A Milestone for Human Rights," *BusinessWeek*, January 24, 2005.

Coke's experience highlights the fact that global strategic planning is more complex than purely domestic planning. There are at least five factors that contribute to this increase in complexity:

1. Globals face multiple political, economic, legal, social, and cultural environments as well as various rates of changes within each of them. Occasionally, foreign governments work in concert with their militaries to advance economic aims even at the expense of human rights. International firms must resist the temptation to benefit financially from such immoral opportunities. Specifics of just one abusive situation are presented in Exhibit 5.6, Strategy in Action.
2. Interactions between the national and foreign environments are complex, because of national sovereignty issues and widely differing economic and social conditions.
3. Geographic separation, cultural and national differences, and variations in business practices all tend to make communication and control efforts between headquarters and the overseas affiliates difficult.
4. Globals face extreme competition, because of differences in industry structures within countries.
5. Globals are restricted in their selection of competitive strategies by various regional blocs and economic integrations, such as the European Economic Community, the European Free Trade Area, and the Latin American Free Trade Area.

CONTROL PROBLEMS OF THE GLOBAL FIRM

An inherent complicating factor for many global firms is that their financial policies typically are designed to further the goals of the parent company and pay minimal attention to

Top Strategist

Francisco D'Souza, CEO of Cognizant Technology Solutions

Exhibit 5.7

Even in the fast-growing outsourcing industry, Cognizant is a standout. Propelled by the increased outsourcing of health care data processing and by a growing number of European clients, Cognizant's 2006 sales jumped 61 percent. Its bread and butter, though, remains managing financial and information-tech services for U.S. clients; companies such as Wells Fargo, Citigroup, and Aetna account for 86 percent of its sales. To keep growth humming, CEO Francisco D'Souza plans to hew to the company's policy of investing aggressively in operations and staff, adding 16,000 workers, mostly in India and China. And he plans to spend $200 million on more office space and infrastructure in India, where Cognizant has 70 percent of its operations. The outlay comes at the cost of margins lower than Indian rivals Wipro and Infosys Technologies, but so far these bets have paid off in growth.

Source: Reprinted with special permission from The *BusinessWeek* 50—The Best Performers, *BusinessWeek*, March 26, 2007. Copyright © 2007 The McGraw-Hill Companies.

the goals of the host countries. This built-in bias creates conflict between the different parts of the global firm, between the whole firm and its home and host countries, and between the home country and host country themselves. The conflict is accentuated by the use of various schemes to shift earnings from one country to another in order to avoid taxes, minimize risk, or achieve other objectives.

Moreover, different financial environments make normal standards of company behavior concerning the disposition of earnings, sources of finance, and the structure of capital more problematic. Thus, it becomes increasingly difficult to measure the performance of international divisions.

In addition, important differences in measurement and control systems often exist. Fundamental to the concept of planning is a well-conceived, future-oriented approach to decision making that is based on accepted procedures and methods of analysis. Consistent approaches to planning throughout a firm are needed for effective review and evaluation by corporate headquarters. In the global firm, planning is complicated by differences in national attitudes toward work measurement, and by differences in government requirements about disclosure of information.

Although such problems are an aspect of the global environment, rather than a consequence of poor management, they are often most effectively reduced through increased attention to strategic planning. Such planning will aid in coordinating and integrating the firm's direction, objectives, and policies around the world. It enables the firm to anticipate and prepare for change. It facilitates the creation of programs to deal with worldwide development. Finally, it helps the management of overseas affiliates become more actively involved in setting goals and in developing means to more effectively utilize the firm's total resources. A strategic manager who shares this view is Francisco D'Souza, the CEO of Cognizant Technology Solutions. Some of his company's recent global strategic initiatives are discussed in Exhibit 5.7, Top Strategist.

An example of the need for coordination in global ventures and evidence that firms can successfully plan for global collaboration (e.g., through rationalized production) is the Ford Escort (Europe), the best-selling automobile in the world, which has a component manufacturing network that consists of plants in 15 countries.

GLOBAL STRATEGIC PLANNING

It should be evident from the previous sections that the strategic decisions of a firm competing in the global marketplace become increasingly complex. In such a firm, managers cannot view global operations as a set of independent decisions. These managers are faced with trade-off decisions in which multiple products, country environments, resource sourcing options, corporate and subsidiary capabilities, and strategic options must be considered.

A recent trend toward increased activism of stakeholders has added to the complexity of strategic planning for the global firm. **Stakeholder activism** refers to demands placed on the global firm by the foreign environments in which it operates, principally by foreign governments. This section provides a basic framework for the analysis of strategic decisions in this complex setting.

stakeholder activism
Demands placed on a global firm by the stakeholders in the environments in which it operates.

Multidomestic Industries and Global Industries

Multidomestic Industries

International industries can be ranked along a continuum that ranges from multidomestic to global.

A **multidomestic industry** is one in which competition is essentially segmented from country to country. Thus, even if global corporations are in the industry, competition in one country is independent of competition in other countries. Examples of such industries include retailing, insurance, and consumer finance.

multidomestic industry
An industry in which competition is segmented from country to country.

In a multidomestic industry, a global corporation's subsidiaries should be managed as distinct entities; that is, each subsidiary should be rather autonomous, having the authority to make independent decisions in response to local market conditions. Thus, the global strategy of such an industry is the sum of the strategies developed by subsidiaries operating in different countries. The primary difference between a domestic firm and a global firm competing in a multidomestic industry is that the latter makes decisions related to the countries in which it competes and to how it conducts business abroad.

Factors that increase the degree to which an industry is multidomestic include[1]

- The need for customized products to meet the tastes or preferences of local customers.
- Fragmentation of the industry, with many competitors in each national market.
- A lack of economies of scale in the functional activities of firms in the industry.
- Distribution channels unique to each country.
- A low technological dependence of subsidiaries on R&D provided by the global firm.

An interesting example of a multidomestic strategy is the one designed by Renault-Nissan for the low-cost automobile industry. As described in Exhibit 5.8, Strategy in Action, Renault's strategy involves designing cars to fit the budgets of buyers in different countries, rather than being restricted to the production of cars that meet the safety and emission standards of countries in Western Europe and the United States or by their consumer preferences for technological advancements and stylish appointments.

[1] Y. Doz and C. K. Prahalad, "Patterns of Strategic Control within Multinational Corporations," *Journal of International Business Studies,* Fall 1984, pp. 55–72.

Strategy in Action — Exhibit 5.8

The Race to Build Really Cheap Cars

BusinessWeek

How cheap is cheap? Renault-Nissan Chief Executive Carlos Ghosn is betting that for autos, the magic number is under $3,000. At a plant-opening ceremony in India in 2007, he was already talking up the industry's next challenge: a future model that would sport a sticker price as low as $2,500—about 40 percent less than the least expensive subcompact currently on the market.

Renault already has a runaway hit with its bare-bones Logan sedan. The automaker began offering the roomy Logan in Europe for just $7,200 in 2004—some 40 percent less than rival sedans—and has since sold 450,000 of the cars in 51 countries. A $3,000 car for Asian markets, built in low-cost India with a local partner, is the next logical step.

That realization is now dawning on the industry's giants. When Tata made its vow to build a $2,500 car, many Western auto executives ridiculed the project, dubbing it a four-wheel bicycle. They aren't laughing anymore. Tata's model is a real car with four doors, a 33-horsepower engine, and a top speed of around 80 mph. The automaker claims it will even pass a crash test.The key is India's low-cost engineers and their prodigious ability to trim needless spending to the bone, a skill developed by years of selling to the bottom of the pyramid.

By 2012, the market for vehicles priced under $10,000 is likely to reach 18 million cars, or a fifth of world auto sales, according to Roland Berger Strategy Consultants. That's up from 12 million in 2007.

Car manufacturers, of course, have always sought to cut costs and pack more value into each new-model generation to stay competitive. But now, emerging markets like India offer cheap engineering, inexpensive parts-sourcing, and low-cost manufacturing. For its new car, for example, Tata should be able to slash the cost of the engine to about $700, or 50 percent lower than a Western-developed equivalent, says one consultant close to the company.

To make a success of the Logan, Renault manufactured in low-cost Romania. It developed a design that reduced the total number of parts and made assembly a cinch. It stripped out sophisticated electronics, dispensed with high-tech curved windshields, and even saved $3 per vehicle by using identical rear-view mirrors on each side. The biggest breakthrough: Renault was able to eliminate expensive prototypes and the pricey tooling involved in building them, an innovation that saved the French car company $40 million.

The majority of low-cost cars will range from $5,000 to $10,000, depending on size and features. Analysts say adding equipment required for safety and emissions control in Western markets would automatically bring the price of a cheap Chinese or Indian car up to $6,000 to $7,000.

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Global Industries

global industry
An industry in which competition crosses national borders on a worldwide basis.

A **global industry** is one in which competition crosses national borders. In fact, it occurs on a worldwide basis. In a global industry, a firm's strategic moves in one country can be significantly affected by its competitive position in another country. The very rapidly expanding list of global industries includes commercial aircraft, automobiles, mainframe computers, and electronic consumer equipment. Many authorities are convinced that almost all product-oriented industries soon will be global. As a result, strategic management planning must be global for at least six reasons:

1. *The increased scope of the global management task.* Growth in the size and complexity of global firms made management virtually impossible without a coordinated plan of action detailing what is expected of whom during a given period. The common practice of management by exception is impossible without such a plan.

2. *The increased globalization of firms.* Three aspects of global business make global planning necessary: (*a*) differences among the environmental forces in different countries, (*b*) greater distances, and (*c*) the interrelationships of global operations.

3. *The information explosion.* It has been estimated that the world's stock of knowledge is doubling every 10 years. Without the aid of a formal plan, executives can no longer know all that they must know to solve the complex problems they face. A global planning process provides an ordered means for assembling, analyzing, and distilling the information required for sound decisions.

4. *The increase in global competition.* Because of the rapid increase in global competition, firms must constantly adjust to changing conditions or lose markets to competitors. The increase in global competition also spurs managements to search for methods of increasing efficiency and economy.

5. *The rapid development of technology.* Rapid technological development has shortened product life cycles. Strategic management planning is necessary to ensure the replacement of products that are moving into the maturity stage, with fewer sales and declining profits. Planning gives management greater control of all aspects of new-product introduction.

6. *Strategic management planning breeds managerial confidence.* Like the motorist with a road map, managers with a plan for reaching their objectives know where they are going. Such a plan breeds confidence, because it spells out every step along the way and assigns responsibility for every task. The plan simplifies the managerial job.

A firm in a global industry must maximize its capabilities through a worldwide strategy. Such a strategy necessitates a high degree of centralized decision making in corporate headquarters so as to permit trade-off decisions across subsidiaries.

Among the factors that make for the creation of a global industry are

- Economies of scale in the functional activities of firms in the industry.
- A high level of R&D expenditures on products that require more than one market to recover development costs.
- The presence in the industry of predominantly global firms that expect consistency of products and services across markets.
- The presence of homogeneous product needs across markets, which reduces the requirement of customizing the product for each market. The presence of a small group of global competitors.
- A low level of trade regulation and of regulation regarding foreign direction investment.[2]

Six factors that drive the success of global companies are listed in Exhibit 5.9, Strategy in Action. They address key aspects of globalizing a business's operations and provide a framework within which companies can effectively pursue the global marketplace.

The Global Challenge

Although industries can be characterized as global or multidomestic, few "pure" cases of either type exist. A global firm competing in a global industry must be responsive, to some degree, to local market conditions. Similarly, a global firm competing in a multidomestic industry cannot totally ignore opportunities to utilize intracorporate resources in competitive positioning. Thus, each global firm must decide which of its corporate functional activities should be performed where and what degree of coordination should exist among them.

[2] G. Harveland and C. K. Prahalad, "Managing Strategic Responsibility in the MNC," *Strategic Management Journal,* October–December 1983, pp. 341–51.

Strategy in Action — Exhibit 5.9

Factors That Drive Global Companies

1. Global Management Team

Possesses global vision and culture.

Includes foreign nationals.

Leaves management of subsidiaries to foreign nationals.

Frequently travels internationally.

Has cross-cultural training.

2. Global Strategy

Implement strategy as opposed to independent country strategies.

Develop significant cross-country alliances.

Select country targets strategically rather than opportunistically.

Perform business functions where most efficient—no home-country bias.

Emphasize participation in the triad—North America, Europe, and Japan.

3. Global Operations and Products

Use common core operating processes worldwide to ensure quantity and uniformity.

Product globally to obtain best cost and market advantage.

4. Global Technology and R&D

Design global products but take regional differences into account.

Manage development work centrally but carry out globally.

Do not duplicate R&D and product development; gain economies of scale.

5. Global Financing

Finance globally to obtain lowest cost.

Hedge when necessary to protect currency risk.

Price in local currencies.

List shares on foreign exchanges.

6. Global Marketing

Market global products but provide regional discretion if economies of scale are not affected.

Develop global brands.

Use core global marketing practices and themes.

Simultaneously introduce new global products worldwide.

Source: Reprinted from *Business Horizons*, Volume 37, Robert N. Lussier, Robert W. Baeder and Joel Corman, "Measuring Global Practices: Global Strategic Planning through Company Situational Analysis," p. 57. Copyright © 1994, with permission from Elsevier.

Location and Coordination of Functional Activities

Typical functional activities of a firm include purchases of input resources, operations, research and development, marketing and sales, and after-sales service. A multinational corporation has a wide range of possible location options for each of these activities and must decide which sets of activities will be performed in how many and which locations. A multinational corporation may have each location perform each activity, or it may center an activity in one location to serve the organization worldwide. For example, research and development centered in one facility may serve the entire organization.

A multinational corporation also must determine the degree to which functional activities are to be coordinated across locations. Such coordination can be extremely low, allowing each location to perform each activity autonomously, or extremely high, tightly linking the functional activities of different locations. Coca-Cola tightly links its R&D and marketing functions worldwide to offer a standardized brand name, concentrate formula, market positioning, and advertising theme. However, its operations function is more autonomous, with the artificial sweetener and packaging differing across locations.

Location and Coordination Issues

Exhibit 5.10 presents some of the issues related to the critical dimensions of location and coordination in multinational strategic planning. It also shows the functional activities that

EXHIBIT 5.10
Location and Coordination Issues of Functional Activities

Functional Activity	Location Issues	Coordination Issues
Operations	Location of production facilities for components.	Networking of international plants.
Marketing	Product line selection. Country (market) selection.	Commonality of brand name worldwide. Coordination of sales to multinational accounts. Similarity of channels and product positioning worldwide. Coordination of pricing in different countries
Service	Location of service organization.	Similarity of service standards and procedures worldwide.
Research and development	Number and location of R&D centers.	Interchange among dispersed R&D centers. Developing products responsive to market needs in many countries. Sequence of product introductions around the world.
Purchasing	Location of the purchasing function.	Managing suppliers located in different countries. Transferring market knowledge. Coordinating purchases of common items.

Source: From Michael E. Porter, "Changing Patterns of International Competition," *California Management Review,* Winter 1986. Copyright © 1986, by The Regents of the University of California. Reprinted from the California Management review, Vol. 28, No. 2. By permission of The Regents.

the firm performs with regard to each of these dimensions. For example, in connection with the service function, a firm must decide where to perform after-sale service and whether to standardize such service.

How a particular firm should address location and coordination issues depends on the nature of its industry and on the type of international strategy that the firm is pursuing. As discussed earlier, an industry can be ranked along a continuum that ranges between multidomestic at one extreme and global at the other. Little coordination of functional activities across countries may be necessary in a multidomestic industry, since competition occurs within each country in such an industry. However, as its industry becomes increasingly global, a firm must begin to coordinate an increasing number of functional activities to effectively compete across countries.

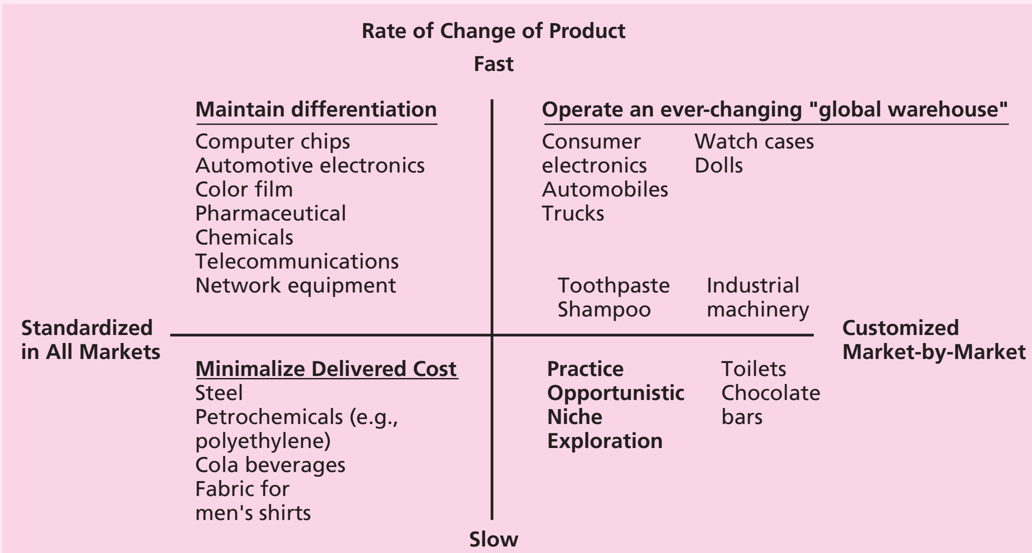
Going global impacts every aspect of a company's operations and structure. As firms redefine themselves as global competitors, workforces are becoming increasingly diversified. The most significant challenge for firms, therefore, is the ability to adjust to a workforce of varied cultures and lifestyles and the capacity to incorporate cultural differences to the benefit of the company's mission.

Market Requirements and Product Characteristics

Businesses have discovered that being successful in foreign markets often demands much more than simply shipping their well-received domestic products overseas. Firms must

Global Strategy in Action — Exhibit 5.11

Market Requirements and Product Characteristics



Source: Lawrence H. Wortzel, *1989 International Business Book* (Strategic Direction Publishers, 1989).

assess two key dimensions of customer demand: customers' acceptance of standardized products and the rate of product innovation desired. As shown in Exhibit 5.11, Global Strategy in Action, all markets can be arrayed along a continuum from markets in which products are standardized to markets in which products must be customized for customers from market to market. Standardized products in all markets include color film and petrochemicals, while dolls and toilets are good examples of customized products.

Similarly, products can be arrayed along a continuum from products that are not subject to frequent product innovations to products that are often upgraded. Products with a fast rate of change include computer chips and industrial machinery, while steel and chocolate bars are products that fit in the slow rate of change category.

Exhibit 5.11 shows that the two dimensions can be combined to enable companies to simultaneously assess both customer need for product standardization and rate of product innovation. The examples listed demonstrate the usefulness of the model in helping firms to determine the degree of customization that they must be willing to accept to become engaged in transnational operations.

International Strategy Options

Exhibit 5.12, Global Strategy in Action, presents the basic multinational strategy options that have been derived from a consideration of the location and coordination dimensions. Low coordination and geographic dispersion of functional activities are implied if a firm is operating in a multidomestic industry and has chosen a country-centered strategy. This allows each subsidiary to closely monitor the local market conditions it faces and to respond freely to these conditions.

High coordination and geographic concentration of functional activities result from the choice of a pure global strategy. Although some functional activities, such as after-sale

Global Strategy in Action — Exhibit 5.12

International Strategy Options

Coordination of Activities	Geographically Dispersed	Geographically Concentrated
High	High foreign investment with extensive coordination among subsidiaries	Global strategy
Low	Country-centered strategy by multinationals with a number of domestic firms operating in only one country	Export-based strategy with decentralized marketing

Location of Activities

Source: From Michael E. Porter, "Changing Patterns of International Competition," *California Management Review*, Winter 1986. Copyright © 1986, by The Regents of the University of California. Reprinted from the *California Management Review*, Vol. 28, No. 2. By permission of The Regents.

service, may need to be located in each market, tight control of those activities is necessary to ensure standardized performance worldwide. For example, IBM expects the same high level of marketing support and service for all of its customers, regardless of their location.

Two other strategy options are shown in Exhibit 5.12. High foreign investment with extensive coordination among subsidiaries would describe the choice of remaining at a particular growth stage, such as that of an exporter. An export-based strategy with decentralized marketing would describe the choice of moving toward globalization, which a multinational firm might make.

COMPETITIVE STRATEGIES FOR FIRMS IN FOREIGN MARKETS

Strategies for firms that are attempting to move toward globalization can be categorized by the degree of complexity of each foreign market being considered and by the diversity in a company's product line (see Exhibit 5.13, Global Strategy in Action). *Complexity* refers to the number of critical success factors that are required to prosper in a given competitive arena. When a firm must consider many such factors, the requirements of success increase in complexity. *Diversity,* the second variable, refers to the breadth of a firm's business lines. When a company offers many product lines, diversity is high.

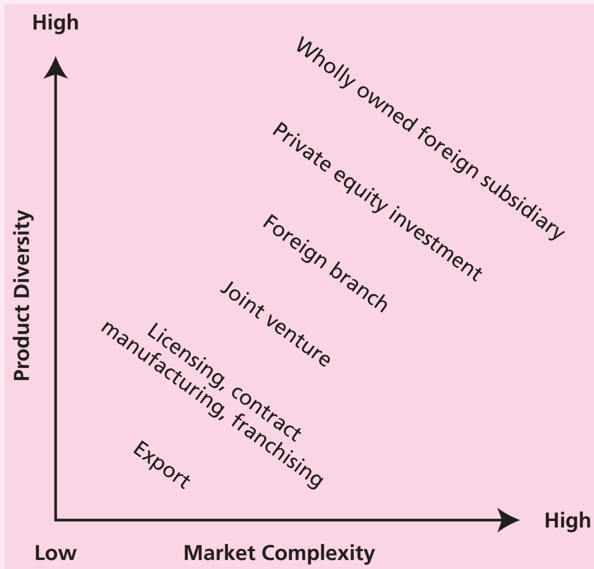
Together, the complexity and diversity dimensions form a continuum of possible strategic choices. Combining these two dimensions highlights many possible actions.

Niche Market Exporting

The primary niche market approach for the company that wants to export is to modify select product performance or measurement characteristics to meet special foreign demands.

Global Strategy in Action — Exhibit 5.13

Escalating Commitments to International Markets



Combining product criteria from both the U.S. and the foreign markets can be slow and tedious. There are, however, a number of expansion techniques that provide the U.S. firm with the know-how to exploit opportunities in the new environment. For example, copying product innovations in countries where patent protection is not emphasized and utilizing nonequity contractual arrangements with a foreign partner can assist in rapid product innovation. N. V. Philips and various Japanese competitors, such as Sony and Matsushita, now are working together for common global product standards within their markets. Siemens, with a centralized R&D in electronics, also has been very successful with this approach.

The Taiwanese company, Gigabyte, researched the U.S. market and found that a sizable number of computer buyers wanted a PC that could complete the basic tasks provided by domestic desktops, but that would be considerably smaller. Gigabyte decided to serve this niche market by exporting their mini-PCs into the United States with a price tag of $200 to $300. This price was considerably less than the closest U.S. manufacturer, Dell, whose minicomputer was still larger and cost $766.

Exporting usually requires minimal capital investment. The organization maintains its quality control standards over production processes and finished goods inventory, and risk to the survival of the firm is typically minimal. Additionally, the U.S. Commerce Department through its Export Now Program and related government agencies lowers the risks to smaller companies by providing export information and marketing advice.

Licensing and Contract Manufacturing

Establishing a contractual arrangement is the next step for U.S. companies that want to venture beyond exporting but are not ready for an equity position on foreign soil. Licensing involves the transfer of some industrial property right from the U.S. licensor to a motivated licensee. Most tend to be patents, trademarks, or technical know-how that are granted to the licensee for a specified time in return for a royalty and for avoiding tariffs or import quotas. Bell South and U.S. West, with various marketing and service competitive advantages valuable to Europe, have extended a number of licenses to create personal computer networks in the United Kingdom.

Another licensing strategy open to U.S. firms is to contract the manufacturing of its product line to a foreign company to exploit local comparative advantages in technology, materials, or labor.

U.S. firms that use either licensing option will benefit from lowering the risk of entry into the foreign markets. Clearly, alliances of this type are not for everyone. They are used best in companies large enough to have a combination of international strategic activities and for firms with standardized products in narrow margin industries.

Two major problems exist with licensing. One is the possibility that the foreign partner will gain the experience and evolve into a major competitor after the contract expires. The experience of some U.S. electronics firms with Japanese companies shows that licensees gain the potential to become powerful rivals. The other potential problem stems from the control that the licensor forfeits on production, marketing, and general distribution of its products. This loss of control minimizes a company's degrees of freedom as it reevaluates its future options.

Franchising

A special form of licensing is franchising, which allows the franchisee to sell a highly publicized product or service, using the parent's brand name or trademark, carefully developed procedures, and marketing strategies. In exchange, the franchisee pays a fee to the parent company, typically based on the volume of sales of the franchisor in its defined market area. The franchise is operated by the local investor who must adhere to the strict policies of the parent.

Franchising is so popular that an estimated 500 U.S. businesses now franchise to over 50,000 local owners in foreign countries. Among the most active franchisees are Avis, Burger King, Canada Dry, Coca-Cola, Hilton, Kentucky Fried Chicken, Manpower, Marriott, Midas, Muzak, Pepsi, and ServiceMaster. However, the acknowledged global champion of franchising is McDonald's, which has 70 percent of its company-owned stores as franchisees in foreign nations.

Joint Ventures

As the multinational strategies of U.S. firms mature, most will include some form of joint venture (JV) with a target nation firm. AT&T followed this option in its strategy to produce its own personal computer by entering into several joint ventures with European producers to acquire the required technology and position itself for European expansion. Because JVs begin with a mutually agreeable pooling of capital, production or marketing equipment, patents, trademarks, or management expertise, they offer more permanent cooperative relationships than export or contract manufacturing.

Compared with full ownership of the foreign entity, JVs provide a variety of benefits to each partner. U.S. firms without the managerial or financial assets to make a profitable independent impact on the integrated foreign markets can share management tasks and cash requirements often at exchange rates that favor the dollar. The coordination of manufacturing and marketing allows ready access to new markets, intelligence data, and reciprocal flows of technical information.

For example, Siemens, the German electronics firm, has a wide range of strategic alliances throughout Europe to share technology and research developments. For years, Siemens grew by acquisitions, but now, to support its horizontal expansion objectives,

Strategy in Action

Exhibit 5.14

Wrapping the Globe in Tortillas

BusinessWeek

Tortillas are a hot topic in Mexico these days. Since December 2006, prices for the staple disks of corn have shot up 67 percent, spurring the government to impose price controls on both finished tortillas and the flour used to make them. In theory, that should be devastating for a company such as Gruma, Mexico's leading flour producer. But that's not so. While Gruma's earnings in Mexico will likely take a hit due to the controls, it is the world's no. 1 tortilla maker, and more than two-thirds of its $3 billion-plus in sales this year will come from outside its home country.

That's because Gruma has spent years building a global market for its quintessentially Mexican comestibles. In September 2006, Gruma opened a new factory in Shanghai that will churn out tens of millions of tortillas annually for KFC restaurants and other customers in China. All told, the company now produces tortillas and chips in 89 factories from Australia to Britain.

But Gruma's global expansion is now speeding up, thanks to CEO Jairo Senise. After getting the top job last year, he took a month-long trip with stops in cities from Manila to Moscow, sampling food in local markets with an eye toward producing tortillas that might fit the local fare. "We're able to think globally but respect the tastes and preferences of each country where we operate," Senise says.

The Shanghai plant is a key part of Gruma's global expansion. The company built the facility at the request of KFC, which had been importing frozen Gruma tortillas from California for the chicken wrap sandwiches it offers in more than 1,800 restaurants in China.

The company's international operations seem to be running more smoothly than those at home. That's because of the price controls, which the government introduced on January 18, 2007, after the cost of imported corn soared. Gruma, which supplies 75 percent of Mexico's corn flour for tortillas, had to agree to keep a lid on its prices. As a result, Merrill Lynch & Co. predicts Gruma will earn $111 million on $3.1 billion in sales in 2007, versus estimated profits of $145 million and revenues of $2.85 billion in 2006.

Senise is now eyeing opportunities in South Africa, Morocco, Egypt, and India. And he'd like to move into industrial tortilla production at home, where mom-and-pop tortillerias dominate the market and Gruma mainly sells flour. That could be tough. Today, Gruma makes tortillas only in a few cities, and Mexico's anti-monopoly watchdog may not allow it to expand.

Source: Reprinted with special permission from Geri Smith, "Wrapping the Globe in Tortillas," *BusinessWeek*, February 26, 2007. Copyright © 2007 The McGraw-Hill Companies.

it is engaged in joint ventures with companies like Groupe Bull of France, International Computers of Britain, General Electric Company of Britain, IBM, Intel, Philips, and Rolm. Another example is Airbus Industries, which produces wide-body passenger planes for the world market as a direct result of JVs among many companies in Britain, France, Spain, and Germany.

JVs speed up the efforts of U.S. firms to integrate into the political, corporate, and cultural infrastructure of the foreign environment, often with a lower financial commitment than acquiring a foreign subsidiary. General Electric's (GE) 3 percent share in the European lighting market was very weak and below expectations. Significant increases in competition throughout many of their American markets by the European giant, Philips Lighting, forced GE to retaliate by expanding in Europe. GE's first strategy was an attempted joint venture with the Siemens lighting subsidiary, Osram, and with the British electronics firm, Thorn EMI. Negotiations failed over control issues. When recent events in Eastern Europe opened the opportunity for a JV with the Hungarian lighting manufacturer, Tungsram, which was receiving 70 percent of revenues from the West, GE capitalized on it.

Although joint ventures can address many of the requirements of complex markets and diverse product lines, U.S. firms considering either equity- or non-equity-based JVs face many challenges. For example, making full use of the native firm's comparative advantage

Strategy in Action — Exhibit 5.15

Russians Have Driven a Ford Lately

BusinessWeek

In 2006, New York Motors, on a commercial strip in southwest Moscow, sold more Fords than any other dealership in the world. All told, salesmen in the crowded showroom moved 10,060 vehicles, helping Ford race past rivals Hyundai, Toyota, and Chevrolet to become the top-selling auto nameplate in Russia.

The brand's success in Russia stands in striking contrast to Ford Motor Co.'s flagging fortunes elsewhere. The automaker clocked a global loss of $12.7 billion in 2006, but sales of Ford-branded vehicles in Russia soared 92 percent, to 115,985 cars and trucks, for some $2 billion in revenues. That's partly due to Russia's thriving economy, which has stoked strong demand for foreign models. In 2006, foreign brands outsold domestic nameplates for the first time, topping 1 million—a 65 percent increase from 2005 and 20 times the level in 2000, according to the Association of European Businesses in Moscow.

In 1999, Ford made a big bet on Russia, spending $150 million on a plant near St. Petersburg—the country's first foreign-owned auto factory. The facility opened in 2002, and in 2006 production climbed to 62,400 Focus sedans, hatchbacks, and wagons.

Competition is heating up as rivals copy Ford's strategy of local production. Volkswagen, Toyota, Nissan, GM, and Fiat have all announced plans to build plants in Russia.

Still, local production has helped Ford keep prices down. Although about 80 percent of the parts used in the Focus are imported, the company sells the cars for as little as $13,000, or about $3,000 less than similarly equipped imports, which are subject to a 25 percent duty. While that's not exactly pocket change in Russia, it's low enough for a growing number of middle-class consumers. Sure, the cheapest Focus is nearly $4,000 more than a Russian-made Lada or low-cost foreign cars such as the Renault Logan and Daewoo Nexia.

Source: Reprinted with special permission from Jason Bush, "They've Driven a Ford Lately: Russians Are Snapping Up Its Locally Made Models in Record Numbers," *BusinessWeek*, February 26, 2007. Copyright © 2007 The McGraw-Hill Companies.

may involve managerial relationships where no single authority exists to make strategic decisions or solve conflicts. Additionally, dealing with host-company management requires the disclosure of proprietary information and the potential loss of control over production and marketing quality standards. Addressing such challenges with well-defined covenants agreeable to all parties is difficult. Equally important is the compatibility of partners and their enduring commitments to mutually supportive goals. Without this compatibility and commitment, a joint venture is critically endangered.

Foreign Branching

A foreign branch is an extension of the company in its foreign market—a separately located strategic business unit directly responsible for fulfilling the operational duties assigned to it by corporate management, including sales, customer service, and physical distribution. Host countries may require that the branch be "domesticated," that is, have some local managers in middle and upper-level positions. The branch most likely will be outside any U.S. legal jurisdiction, liabilities may not be restricted to the assets of the given branch, and business licenses for operations may be of short duration, requiring the company to renew them during changing business regulations. Gruma, Mexico's leading flour producer and the world's leading tortillas manufacturer has manufacturing branches in 89 foreign countries. The story of Gruma's success is presented in Exhibit 5.14, Strategy in Action.

Equity Investment

Small and medium-size enterprises with strong growth potential frequently have the need for additional funds to be able to grow further before deciding to trade their stock publicly

private equity
Money from private sources that is invested by a venture capital or private equity company in start-ups and other risky—but potentially very profitable—small and medium-size enterprises.

in the marketplace. These firms often enlist the support of a venture capital firm or **private equity** company that invests its shareholders' money in start-ups and other risky but potentially very profitable small and medium-size enterprises. In exchange for a private equity stake, which is sometimes a majority or controlling position, the Venture Capital (VC) or private equity company provides investment capital and a range of business services, including management expertise.

Wholly Owned Subsidiaries

Wholly owned foreign subsidiaries are considered by companies that are willing and able to make the highest investment commitment to the foreign market. These companies insist on full ownership for reasons of control and managerial efficiency. Policy decisions about local product lines, expansion, profits, and dividends typically remain with the U.S. senior managers. An excellent example of a wholly owned subsidiary is the manufacturing and sales organization of Ford Motor in Russia, as described in Exhibit 5.15, Strategy in Action.

Fully owned subsidiaries can be started either from scratch or by acquiring established firms in the host country. U.S. firms can benefit significantly if the acquired company has complementary product lines or an established distribution or service network.

U.S. firms seeking to improve their competitive postures through a foreign subsidiary face a number of risks to their normal mode of operations. First, if the high capital investment is to be rewarded, managers must attain extensive knowledge of the market, the host nation's language, and its business culture. Second, the host country expects both a long-term commitment from the U.S. enterprise and a portion of their nationals to be employed in positions of management or operations. Fortunately, hiring or training foreign managers for leadership positions is commonly a good policy, because they are close to both the market and contacts. This is especially important for smaller firms when markets are regional. Third, changing standards mandated by foreign regulations may eliminate a company's protected market niche. Product design and worker protection liabilities also may extend back to the home office.

The strategies shown in Exhibit 5.13 are not exhaustive. For example, a firm may engage in any number of joint ventures while maintaining an export business. Additionally, there are a number of other strategies that a firm should consider before deciding on its long-term approach to foreign markets. These will be discussed in detail in Chapter 6 under the topic of grand strategies. However, the strategies discussed in this chapter provide the most popular starting points for planning the globalization of a firm.

Summary

To understand the strategic planning options available to a corporation, its managers need to recognize that different types of industry-based competition exist. Specifically, they must identify the position of their industry along the global versus multidomestic continuum and then consider the implications of that position for their firm.

The differences between global and multidomestic industries about the location and coordination of functional corporate activities necessitate differences in strategic emphasis. As an industry becomes global, managers of firms within that industry must increase the coordination and concentration of functional activities.

The Appendix at the end of this chapter lists many components of the environment with which global corporations must contend. This list is useful in understanding the issues that confront global corporations and in evaluating the thoroughness of global corporation strategies.

As a starting point for global expansion, the firm's mission statement needs to be reviewed and revised. As global operations fundamentally alter the direction and strategic capabilities of a firm, its mission statement, if originally developed from a domestic perspective, must be globalized.

The globalized mission statement provides the firm with a unity of direction that transcends the divergent perspectives of geographically dispersed managers. It provides a basis for strategic decisions in situations where strategic alternatives may appear to conflict. It promotes corporate values and commitments that extend beyond single cultures and satisfies the demands of the firm's internal and external claimants in different countries. Finally, it ensures the survival of the global corporation by asserting the global corporation's legitimacy with respect to support coalitions in a variety of operating environments.

Movement of a firm toward globalization often follows a systematic pattern of development. Commonly, businesses begin their foreign nation involvements progressively through niche market exporting, license-contract manufacturing, franchising, joint ventures, foreign branching, and foreign subsidiaries.

Key Terms

ethnocentric orientation, *p. 133*
geocentric orientation, *p. 133*
global industry, *p. 140*
globalization, *p. 130*
multidomestic industry, *p. 139*
polycentric orientation, *p. 133*
private equity, *p. 150*
regiocentric orientation, *p. 133*
stakeholder activism, *p. 139*

Questions for Discussion

1. How does environmental analysis at the domestic level differ from global analysis?
2. Which factors complicate environmental analysis at the global level? Which factors are making such analysis easier?
3. Do you agree with the suggestion that soon all industries will need to evaluate global environments?
4. Which industries operate almost devoid of global competition? Which inherent immunities do they enjoy?
5. Explain when and why it is important for a company to globalize.
6. Describe the four main strategic orientations of global firms.
7. Explain the control problems that are faced by global firms.
8. Describe the differences between multinational and global firms.
9. Describe the market requirements and product characteristics in global competition.
10. Evaluate the competitive strategies for firms in foreign markets:
    a. Niche market exporting
    b. Licensing and contract manufacturing
    c. Franchising
    d. Joint ventures
    e. Foreign branching
    f. Private equity investment
    g. Wholly owned subsidiaries

Chapter 5 Discussion Case

BusinessWeek

China Mobile's Hot Signal

1 Dagoucun feels like the kind of place that progress missed entirely in its sweep through China. Nestled at 10,000 feet in the pine-studded foothills of the Tibetan plateau, the village is little more than a few dozen stone houses and a Buddhist shrine. Getting there from the nearest big city, Chengdu, takes five hours by car, much of it on a muddy, rutted road.

2 But given the electronic trills emanating from the fields of barley, potatoes, and corn, it's clear that the twenty-first century has finally made it to Dagoucun. Last year, the village got cell-phone service, dramatically transforming the way its residents live and work. With better information about crop prices delivered to their phones, farmers have started planting more marketable crops such as Chinese cabbage and herbs for traditional medicines. And they no longer have to truck their produce to distant cities in hopes of finding buyers. "Before, we had to travel 20 kilometers to make a phone call," says village chief Xie Sufang, a 65-year-old mother of seven. "Now we contact the buyers, and they come to us."

3 The company responsible for bringing change to this rural outpost: China Mobile Ltd. Since it was spun off from fixed-line operator China Telecom Corp. in 2000, China Mobile has grown into the world's biggest cellular carrier. The company is signing up nearly 5 million new customers a month and recently topped the 300 million mark—more than the entire population of the United States. In 2006, revenues grew 21 percent, to \$37.8 billion, and net income 23 percent, to \$8.7 billion, estimates Deutsche Bank. And its Hong Kong–traded shares more than doubled in the past year, giving China Mobile a market capitalization of \$198 billion and making it the most valuable cellular carrier on earth. The company also has global ambitions: on January 22, 2007, it announced it was buying 89 percent of Paktel Ltd., Pakistan's fifth-largest cellular carrier.

4 China Mobile built its early success on urban China. Problem is, just about everyone in mainland cities who can afford cellular service already has it. Mobile-phone penetration in Beijing, Shanghai, and Shenzhen is approaching 100 percent. So to keep growing, China Mobile is plunging ever deeper into the interior, building cell towers from the deserts of Inner Mongolia to the mountains of Tibet. In rural China, home to 700 million, just over 1 in 10 people has a cell phone. "It is a market with huge potential," says China Mobile Chairman Wang Jianzhou.

5 China Mobile's torrid growth hasn't escaped the attention of Western companies seeking to tap the potential of China, both urban and rural. The carrier has inked agreements with Vodafone Group, News Corp., Viacom's MTV Networks, and the National Basketball Association. Last summer, China Mobile launched a music-download service called M.Music in partnership with Sony bmg, Universal Music Group, emi, and Warner Music. And on January, 4, 2007, Google Inc. announced that its search engine would be featured on China Mobile's Monternet mobile phone portal.

What's behind the flurry of deals? "We want to make the cell phone into a new medium," says Wang. The company is aggressively pushing extras such as ringtones and music downloads. Demand for such services is expected to surge with the launch of third-generation (3G) mobile technology in time for the Beijing Olympics in 2008. Beijing telecom consultancy BDA China estimates revenues from such services will jump from \$10.4 billion last year to \$28.6 billion by 2010. Wang believes his company's continued dominance of China's cell-phone market will depend on the news, entertainment, and music it can beam to subscribers. So in June, China Mobile plunked down \$166 million for a 19.9 percent stake in Phoenix Satellite Television Holdings, the mainland's most popular cable news and entertainment channel. 6

China Mobile is also turning its sights overseas. Its \$284 million purchase of Paktel, likely to conclude in late February, 2007, will be the company's first overseas acquisition, though early last year it bought Hong Kong's No. 4 mobile company, People's Telephone, with 1.1 million subscribers. Last summer, China Mobile made a \$5 billion-plus play for Luxembourg's Millicom International Cellular—Paktel's parent—which has mobile networks in Africa and Latin America as well as Asia. But negotiations broke down due to concerns about the big price tag, analysts say. While Wang declined to comment on the collapse of the Millicom talks, he says China Mobile is interested in acquisitions in other developing countries: "We are familiar with emerging markets. Their experiences may be very similar to ours." 7

Wang has plenty to keep him busy at home as the government turns up the competitive heat on the cell-phone industry. Until now, China Mobile has had to contend with just one rival: China Unicom Ltd. Like China Mobile, Unicom is listed in Hong Kong and is state-controlled. With 143 million subscribers, though, Unicom is a distant no. 2, which some attribute to the complications it faces in maintaining a network that uses two mobile standards. China Mobile, by contrast, can operate more efficiently using a single technology, the gsm standard developed in Europe. Sometime this year, Beijing is expected to award 3G licenses to both current carriers and also possibly to two new rivals, most likely China's state-owned fixed-line operators, China Netcom Group and China Telecom. 8

PROFIT PUSH

China's leadership could complicate life for Wang & Co. in other ways, too. In an effort to boost its international prestige, 9

Beijing is pushing the development of a homegrown 3G standard not used elsewhere. China Mobile, China Netcom, and China Telecom are all currently running trials of the new technology. But analysts expect China Mobile to win the dubious honor of leading the rollout, which could be a costly distraction that will almost certainly be more complex than introducing one of the 3G standards already deployed in other countries. Being forced to build a network using China's technology "definitely is a liability," says Zhang Dongming, director of research at consultancy BDA.

10 Even with a smooth rollout of 3G, China Mobile could have a tough time keeping revenue and earnings growing at double-digit rates. As it pushes ever deeper into the interior, the company faces the same dilemma as the likes of Procter & Gamble Co. and General Motors Corp.: how to win new customers without sacrificing profit margins. Incomes in rural China average just over $400 per year, or less than one-third what city dwellers earn. To drum up business in places such as Dagoucun, China Mobile is cutting prices, and the amount of money it gets from each subscriber has declined modestly in the past year, to about $11. "The key is to maintain profitability even while penetrating rural areas," says Steve Zhang, CEO of Beijing's AsiaInfo Holdings Inc., a telecom software and services company that works with China Mobile.

11 Wang insists he's not jeopardizing earnings. One reason, he says, is that China Mobile runs a much leaner operation in the countryside. It has largely dispensed with stores and is instead relying on village chiefs such as Xie to persuade neighbors to buy handsets and prepaid cards. China Mobile offers cell-phone plans tailored for farmers that include information such as crop prices and tips on duck breeding delivered via text message, the Internet, and a call-in phone service. The plan costs a nominal 25 cents a month, but users must pay extra to place calls and send text messages. Since its launch in October, 2006, the service has been rolled out to 12 provinces in western China and is expected to go nationwide later this year. "Our main purpose now is to provide farmers with information that benefits them," says Qin Dabin, vice general manager of China Mobile's operations in the western city of Chongqing. Although it will take some time before the initiative turns a profit, Qin says it's helping to attract subscribers.

12 China Mobile isn't abandoning cities, either. Far from it. The company has an upscale service called Go-Tone for businesspeople. The $6.40 basic monthly fee (phone and message charges are extra) includes reduced membership rates at golf courses and access to VIP waiting rooms at many Chinese airports. And a $2-a-month plan called M-Zone is aimed at music-mad teenagers and twentysomethings. China Mobile puts on special events for M-Zone members, such as appearances by the likes of Chinese-American pop star Pan Weibo.

Meanwhile, back in the mountains of Sichuan, villagers 13
are figuring out more ways to wring money from their new phones. Cabbages from Dagoucun now travel all the way to the southern cities of Guangzhou and Shenzhen as it's easier to reach buyers across the country. Villagers have sold a rare caterpillar fungus—prized in Asia for its antiviral attributes—to customers in Singapore who were contacted via cell phone. And residents are building a three-story lodge for mountain climbers and anglers in a bid to transform their remote village into a flourishing center for ecotourism. "With our mobile phones, potential tourists can contact us and learn more about our village," says village chief Xie. "We can increase our incomes in many ways."

Telecom Titans: The World's Biggest Cellular Companies

Operator Accounts (millions)	Subscriber Revenue per User	Average
China Mobile	300	$11.19
China Unicom	143	6.80
Cingular	60	49.76
Verizon Wireless	59	50.59
Sprint USA	54	52.25

Source: Reprinted with special permission from Dexter Roberts, "China Mobile's Hot Signal: It's Already the World's Biggest Cellular Carrier. Now It's Planning to Get Even Bigger," *BusinessWeek*, February 2007. Copyright © 2007 The McGraw-Hill Companies.

DISCUSSION QUESTIONS

1. How do you believe that the mobile phone industry in China differs form the one in the United States?
2. Do you think that the investment opportunity in China's mobile phone industry is attractive?
3. What difficulties do you expect China's mobile phone industry to encounter as it tries to expand?
4. Can you detect any patterns or rules of development from the China mobile phone industry that could be applied to the development of the mobile phone industry in other countries?
5. Do you agree that "globalization is the strategy of approaching worldwide markets with standardized products?" Are mobile phones an example?

Chapter 5 Appendix

Components of the Multinational Environment

Multinational firms must operate within an environment that has numerous components. These components include the following:

1. Government, laws, regulations, and policies of home country (United States, for example)
   a. Monetary and fiscal policies and their effect on price trends, interest rates, economic growth, and stability
   b. Balance-of-payments policies
   c. Mandatory controls on direct investment
   d. Interest equalization tax and other policies
   e. Commercial policies, especially tariffs, quantitative import restrictions, and voluntary import controls
   f. Export controls and other restrictions on trade
   g. Tax policies and their impact on overseas business
   h. Antitrust regulations, their administration, and their impact on international business
   i. Investment guarantees, investment surveys, and other programs to encourage private investments in less-developed countries
   j. Export-import and government export expansion programs
   k. Other changes in government policy that affect international business
2. Key political and legal parameters in foreign countries and their projection
   a. Type of political and economic system, political philosophy, national ideology
   b. Major political parties, their philosophies, and their policies
   c. Stability of the government
      (1) Changes in political parties
      (2) Changes in governments
   d. Assessment of nationalism and its possible impact on political environment and legislation
   e. Assessment of political vulnerability
      (1) Possibilities of expropriation
      (2) Unfavorable and discriminatory national legislation and tax laws
      (3) Labor laws and problems
   f. Favorable political aspects
      (1) Tax and other concessions to encourage foreign investments
      (2) Credit and other guarantees
   g. Differences in legal system and commercial law
   h. Jurisdiction in legal disputes
   i. Antitrust laws and rules of competition
   j. Arbitration clauses and their enforcement
   k. Protection of patents, trademarks, brand names, and other industrial property rights
3. Key economic parameters and their projection
   a. Population and its distribution by age groups, density, annual percentage increase, percentage of working age, percentage of total in agriculture, and percentage in urban centers
   b. Level of economic development and industrialization
   c. Gross national product, gross domestic product, or national income in real terms and also on a per capita basis in recent years and projections over future planning period
   d. Distribution of personal income
   e. Measures of price stability and inflation, wholesale price index, consumer price index, other price indexes
   f. Supply of labor, wage rates
   g. Balance-of-payments equilibrium or disequilibrium, level of international monetary reserves, and balance-of-payments policies
   h. Trends in exchange rates, currency stability, evaluation of possibility of depreciation of currency
   i. Tariffs, quantitative restrictions, export controls, border taxes, exchange controls, state trading, and other entry barriers to foreign trade
   j. Monetary, fiscal, and tax policies
   k. Exchange controls and other restrictions on capital movements, repatriation of capital, and remission of earnings
4. Business system and structure
   a. Prevailing business philosophy: mixed capitalism, planned economy, state socialism
   b. Major types of industry and economic activities
   c. Numbers, size, and types of firms, including legal forms of business
   d. Organization: proprietorships, partnerships, limited companies, corporations, cooperatives, state enterprises
   e. Local ownership patterns: public and privately held corporations, family-owned enterprises
   f. Domestic and foreign patterns of ownership in major industries
   g. Business managers available: their education, training, experience, career patterns, attitudes, and reputations
   h. Business associations and chambers of commerce and their influence
   i. Business codes, both formal and informal
   j. Marketing institutions: distributors, agents, wholesalers, retailers, advertising agencies, advertising media, marketing research, and other consultants

k. Financial and other business institutions: commercial and investment banks, other financial institutions, capital markets, money markets, foreign exchange dealers, insurance firms, engineering companies
l. Managerial processes and practices with respect to planning, administration, operations, accounting, budgeting, and control

5. Social and cultural parameters and their projections
   a. Literacy and educational levels
   b. Business, economic, technical, and other specialized education available
   c. Language and cultural characteristics
   d. Class structure and mobility
   e. Religious, racial, and national characteristics
   f. Degree of urbanization and rural-urban shifts
   g. Strength of nationalistic sentiment
   h. Rate of social change
   i. Impact of nationalism on social and institutional change