Strategy in Action

Exhibit 5.7

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.
   Produce 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.

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

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.

Global Strategy in Action — Exhibit 5.8

Market Requirements and Product Characteristics

Rate of Change of Product

Fast

	Standardized in All Markets	Customized Market-by-Market
Fast	**Maintain differentiation** Computer chips Automotive electronics Color film Pharmaceutical Chemicals Telecommunications Network equipment	**Operate an ever-changing "global warehouse"** Consumer electronics Watch cases Dolls Automobiles Trucks Toothpaste Shampoo Industrial machinery
Slow	**Minimalize delivered cost** Steel Petrochemicals (e.g., polyethylene) Cola beverages Fabric for men's shirts	**Practice opportunistic niche exploration** Toilets Chocolate bars

Slow

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

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 assess two key dimensions of customer demand: customers' acceptance of standardized products and the rate of product innovation desired. As shown in Exhibit 5.8, 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 5.8 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. Starbucks has taken advantage of an industry with a slow rate of change in the product and relatively high standardization in all markets, namely, the retail coffee industry. Exhibit 5.9, Strategy in Action, provides some interesting details on how Starbucks' global success is achieved.

Strategy in Action Exhibit 5.9

Starbucks' Global Expansion

Starbucks began its international expansion with two stores in Japan in the mid-1980s. By 2000, the company's non-U.S. operations reached 792 stores in 16 countries. Starbucks' global strategy included three key elements:

- Increase market penetration and focus on profitability in existing markets.
- Target long-term store potential of 15,000 locations beyond the United States.
- Focus on emerging markets—especially China, Brazil, and Russia—as a catalyst for long-term revenue and profit growth.

Starbucks was extremely successful with the global strategy. By 2007, Starbucks' 15,012 stores in 44 countries generated net revenues of $9.4 billion for the fiscal year, which was an increase of 21 percent over 2006. Its U.S. revenue grew by 19.4 percent and operating income grew by 12.1 percent. Even more impressive, Starbucks' international segment's revenue growth was 32.1 percent and its operating income grew 27.0 percent, principally because of aggressive expansion into new markets and a refocus on profitability in the large core markets of Canada and the United Kingdom.

In 2008, Starbucks undertook an even more aggressive global strategy. The plan is to accelerate expansion and increase the profitability of Starbucks outside the United States by redeploying a portion of the capital originally earmarked for U.S. store growth to the international business.

Sources: "Starbucks Outlines International Growth Strategy; Focus on Retail Expansion and Profitability," *Business Wire*, October 2004, p. 1; and "Starbucks Announces Strategic Initiatives to Increase Shareholder Value; Chairman Howard Schultz returns as CEO," Starbucks, news release, January 2008, p. 1.

Glob
Escala

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 5.10, 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

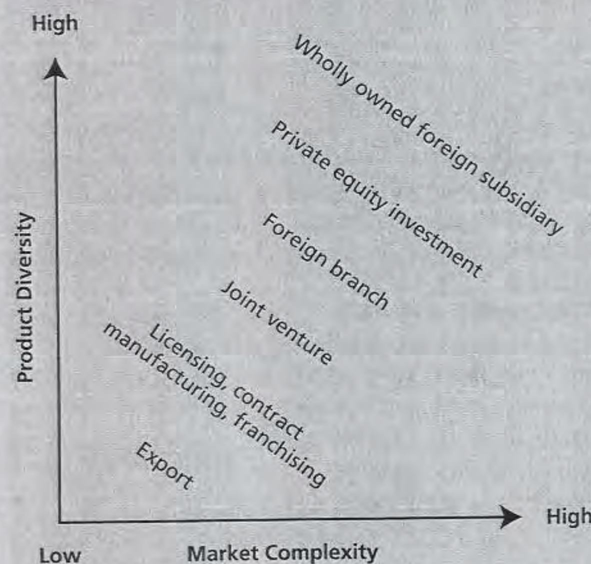
The primary niche market approach for the company that wants to export is to modify select product performance or measurement characteristics to meet special foreign demands. Combining product criteria from both the U.S. and the foreign markets can be slow and tedious. There are, however, a number of 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

Global Strategy in Action

Exhibit 5.10

Escalating Commitments to International Markets



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 more than 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, 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 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 and sales of $3 billion annually.

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 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.

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

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.

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. For example, in 2007, PepsiCo's CEO Indra Nooyi led her company's large-scale global

Top Strategist

CEO Nooyi Spearheads PepsiCo's International Expansion Strategy

Exhibit 5.11

PepsiCo is one of the largest food and beverages companies in the world. It manufactures, markets, and sells a variety of salty, sweet, and grain-based snacks and carbonated and noncarbonated beverages. Indra Nooyi has been the chairman and chief executive officer of PepsiCo since 2007.

Nooyi wanted to become less reliant on the U.S. market, where sales growth has slowed for some of its flagship sodas and snacks. In 2008, 40 percent of PepsiCo revenue came from international business. About her strategic intention, Nooyi said, "Revitalizing this business is a huge priority for us and investments will be made to expand the company's footprint in fast-growing emerging markets."*

Nooyi planned to strengthen PepsiCo's presence in emerging high-growth markets—including China, India, and Russia, where it has an established market in carbonated beverages and planned to expand with more focus on snack foods and other beverages.

PepsiCo planned to invest $1 billion in China between 2008 and 2011 to build more plants in western and interior areas of China, expand local R&D to develop products tailored to Chinese consumers, and build a larger sales force to expand marketing and distribution.

In an effort to expand its presence in the Russian juice category, PepsiCo bought a 75.53 percent stake in Russia's leading branded juice company, JSC Lebedyansky. PepsiCo also built a potato chip factory in southern Russia.

In 2008, Nooyi announced an investment plan of $500 million aimed at upgrading its manufacturing capacity, infrastructure, and R&D in India. With an established carbonated business, Pepsi India began to launch localized product offerings, such as the drink "nimbu paani."

*B. McKay and A. Cordeiro, "Pepsi Results Send Chills in Beverage, Snack Sector," *The Wall Street Journal,* October 15, 2008, p. B.1.

Source: B. McKay, "Pepsi to Boost China Outlay by $1 Billion," *The Wall Street Journal,* November 4, 2008, p. B. 3.

expansion based on developing wholly owned subsidiaries. The plan was to build brands in emerging markets to compensate for the slow growth in the United States, as described in Exhibit 5.11, Top Strategist.

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 5.10 may be undertaken singly or in combination. 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 7 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. 119*
geocentric orientation, *p. 119*
global industry, *p. 124*
globalization, *p. 115*
multidomestic industry, *p. 124*
polycentric orientation, *p. 119*
private equity, *p. 131*
regiocentric orientation, *p. 119*
stakeholder activism, *p. 123*

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.