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Unit 1: Introduction

The phenomenon of Globalisation Localisation and Glocalization

In today's business world, managers, politicians, journalists and academics commonly use the concepts of 'globalisation', 'global industries', 'global competition', 'global strategies' and 'global corporations'. More and more companies are confronted with the need to globalise or die. While those concepts are widely used, their meaning is often not well understood. For some people, globalisation means to expand the company's presence abroad, for others it means standardising a product and selling it to the world, for yet others it denotes an approach to management in which decision-making is centralised at corporate headquarters.
There are many reasons for this confusion; one is due to the fact that the concept of globalisation is relatively new. Before the 1970s almost no one talked about globalisation; the most frequently used terminology, when referring to companies operating in various part of the world, was 'multinational' or occasionally 'transnational'.**Multinational companies** have been around for many years. Even if we ignore the East India Company, which started in the early seventeenth century, modern corporations like Unilever, Nestlé, and Procter & Gamble were operating all over the world at the end of the nineteenth century. They are known as multinational companies, but nobody would have called them global. The global concept appeared in the early 1970s and progressively invaded boardrooms, classrooms and editorial offices. What happened, and why?

In each country of Europe, different firms fighting for a share of the market contested the elevator market. Competitors were either local companies or subsidiaries of large multinational companies like Otis or Schindler. Each competitor designed, marketed, manufactured, installed and serviced elevators for their respective markets. The subsidiaries of the multinationals had all the activities of the value chain (marketing, design, production, installation and service) under their control. The French subsidiary of Otis designed elevators for the French market, manufactured them in French factories, sold them with French sales forces and maintained them with a French after-sales organisation; the management was essentially French. In Germany, Otis designed, manufactured, sold, installed and serviced elevators for the German market; and so on in nearly every major country. In smaller countries products or components were exported from major countries' subsidiaries. The operations were *self-contained* in each country and the results were evaluated on a *country-by-country* basis. Such a situation had prevailed since the 1880s. It corresponds to what was referred as a multinational or multidomestic world, in which multinational companies like Otis were competing in each main market of the planet.

By the end of the 1960s several key elements played a role in changing this competitive structure. One country manager at Otis perceived that the European business context was changing. First, the Treaty of Rome in 1957 had created the European Economic Community (EEC), at that time called the Common Market. This meant that tariff barriers across Europe were coming down; it became possible to produce components in one country and export them to other countries.
This allowed companies to concentrate on the production of components in one specialised factory and to have a network of specialised factories across Europe, each of them making one product category or one component. Components would be cross-shipped for ultimate installation in the various client countries.
The benefits of such a system were obvious – by concentrating production the company could benefit from economies of scale, some costs could be passed to the customers in the form of price reduction, leading to higher market share. Products could be designed for the whole market (standardised): instead of having country segmentation one would have pan-European segmentation based on utilisation, i.e. high-rise buildings, low-rise buildings, etc.
This would be possible only if customers in Europe – architects, engineers, real estate developers, housing departments, etc. – had a common view about what an elevator should be. Despite the differences in housing organisation across countries, elevators were essentially technical products with very little cultural content and therefore able to be standardised. Only selling methods would vary from country to country.

From a management point of view this was a radical change: country managers were no longer responsible for the whole value chain as before, but only for part of it. They were obliged to co-ordinate with other countries and they were dependent on a co-ordinating organisation called the European headquarters. This led to a very successful story. By 1975, Otis had captured 40 per cent of the European market, containing Japanese penetration, and competitors if they wanted to survive were obliged to adopt a similar strategy. This concept was further expanded and today Otis is organised by product lines on a worldwide basis. There are still country subsidiaries, which take care of installation, maintenance, public relations and very successful story. By 1975, Otis had captured 40 per cent of the European market, containing Japanese penetration, and competitors if they wanted to survive were obliged to adopt a similar strategy. This concept was further expanded and today Otis is organised by product lines on a worldwide basis. There are still country subsidiaries, which take care of installation, maintenance, public relations and personnel, but otherwise product development, and manufacturing is co-ordinated globally by product lines. From being a ‘multinational’, Otis has become a ‘global’ company.

This phenomenon of an *active co-ordinated and integrated presence* in the main regions of the world is what ‘global company’ means. It is important to observe that this change gave Otis a competitive advantage and that competitors were obliged to adopt a similar approach if they wanted to survive. Globalisation is neither a consultant’s fad nor a management buzzword; it is a competitive imperative in an increasing number of industries.

Some global definitions

Global industries are industries in which, in order to survive, competitors need to operate in the key world markets in an integrated and co-ordinated way. Industries like aerospace, computers, telecommunication equipment, appliances, power generation, large industrial projects, insurance and re-insurance and corporate data transmission are examples of what a global industry means. In these sectors it is difficult to sustain competition if one does not cover the whole world (or nearly) as a market, and if one does not integrate operations to make them cost and time effective.

Global companies are the companies that operate in the main markets of the world in an integrated and co-ordinated way. Companies like Coca Cola, Asea Brown Bovery, Sony and Citibank are global companies.

Globalisation is the phenomenon of the transition of industries whose competitive structure changes progressively from multinational to global. Industries such as telecommunications, processed food, personal care and retail are in the process of globalisation.
Global integration and co-ordination are the organisational structure and management processes by which various activities scattered across the world are made interdependent on each other. As examples, global manufacturing integration implies the specialisation of factories and the cross-shipment of parts between different production sites; global product development requires the co-ordination of various research centres and marketing teams; global account management demands that different country subsidiaries provide a service according to a plan negotiated centrally, etc.

Factors that push globalisation

a) **Political factors: liberalisation of trade and investments**

The main political factor has been the development of *free trade* among nations. Two main organisations have been the source of trade liberalisation: the General Agreement on Tariffs and Trade (GATT) (now replaced by the World Trade Organization, WTO) and the EEC, to which one may add the progressive opening of emerging nations to foreign investments.
The GATT, which was founded in 1946 by 23 nations, initiated a series of negotiations, called 'rounds', aimed at reducing tariff concessions to create liberalisation of trade. The GATT became the WTO in 1995.
The Kennedy Round in the mid-1960s, and the Tokyo Round in the early 1970s created an environment that fostered international trade.
The European Community (EC) was established on 25 March 1957 by the Treaty of Rome, signed by Belgium, France, Italy, Germany, Luxembourg and the Netherlands, with the aim of creating a common market and economic and political integration among the six member states. As a result goods, people and financial flows could move freely across countries. During the 1970s, the EC was enlarged with the entry of the United Kingdom, Ireland and Denmark, followed by Spain, Portugal and Greece in the 1980s and by Sweden, Austria and Finland in the 1990s. Companies like Otis could take advantage of European integration to create their own integrated trading network.
Finally, in parallel with what was happening in the industrialised countries, third-world nations progressively adopted more positive attitudes towards foreign direct investments (FDI). At first, investment laws were designed to attract foreign investors in order to induce them to produce locally, but over the years the legislation has evolved toward a more open stance, favouring cross-border investments.

b) **Technological factors: transport, communication, and economies of scale**

Another set of 'push factors' for globalisation is related to *technological progress* that lowered the cost of transport and communication as well as the unit cost of production through economies of scale or the localisation of productive capacities and sourcing in low-cost economies.
Air, rail and road transport and the use of containers in maritime transport have reduced the cost of shipping goods from country to country as well as, in the case of air transport, favouring the travel of managers. The development of telecommunications has reduced the cost of information exchange between business units scattered around the globe. Between 1950 and 1990, the transportation costs of air transport, ocean freight and transatlantic phone calls decreased by some 56 per cent, 14 per cent and 29 per cent, respectively. For satellite charges, there was an approximate decrease of 90 per cent between 1970 and 1990.
Progress in manufacturing technology gave a tremendous impetus to the need to concentrate production in world-class factories benefiting from huge economies of scale, thus encouraging the rationalisation and integration of production systems.

Besides manufacturing concentration, companies have been able to source components or services from low-cost countries, either by setting up their own operations or by purchasing locally.
Another source of economies of scale comes from the need to quickly amortise research and development (R&D) expenditures. Companies are confronted with a dual pressure: R&D budgets are increasing and product life cycles (PLCs) are reducing. Companies need to launch products and services at the same time in all major markets in order to be able to recoup their investments.

c) Social factors: convergence of consumer needs

International air transport and the diffusion of lifestyles by movies and TV series have increased the *brand awareness* of consumers worldwide. Brands like Sony, Nike, Levi or Coca Cola are known nearly everywhere. Kenichi Ohmae, 2 in his book '*Triad Power*', has discussed the 'Californisation of society' – teenagers in São Paolo, Bombay, Milan or Los Angeles listening to the same music, using the same walkman and wearing the same pair of blue jeans. Convergence of customer behaviour and needs is also facilitated by urbanisation and industrialisation of societies. The less cultural and the more technical is the product, the more likely it can be standardised and appeal to masses of consumers in all countries: VCRs, PCs, mobile phones or elevators, cranes and robots are products for which national differences do not matter much.

d) Competitive factors

The 1960s saw the emergence of Japanese competitors in markets that traditionally had been dominated by American or European competitors. Japanese firms, and later on Korean firms, adopted a global approach at the very beginning of their international expansion. One of the reasons is that they did not have many national subsidiaries and their international expansion was occurring at the time of the opening of trade barriers. Right at the beginning they designed products for the world market, creating *global brands* such as 'Sony' or 'Panasonic', and their efficient production system gave them a cost advantage in electronics and automotive parts.
Competitors had to adopt a similar strategic posture if they wished to survive. Another competitive force that pushed companies to globalise is the *globalisation of customers*. During the 1970s, Citibank created a Global Account Management Unit to service those corporate customers who had international subsidiaries.

The benefits of globalisation

(1) ***Cost benefits*.** From economies of scale owing to products/processes standardisation as well as increased bargaining powers over suppliers of raw materials, components, equipment and services and, on the other hand, from the ability to organise a logistic and sourcing network based on location factors. Examples of economies of scale through standardisation are numerous; in the example mentioned earlier, Otis was able to lower the cost of elevators in Europe by 30 per cent after introducing a pan-European manufacturing system.
(2) ***Timing benefits*.** These are due to the co-ordinated approach in product launching in the early stage of the product life cycle. In a multinational setting, each subsidiary is more or less free to adopt products for its own market. This is sometimes called 'the shopping caddy' approach to product adoption. Such an approach generates inefficiencies in the management of the product life cycle since the optimal volume is obtained only after a lengthy process of product adoption by all subsidiaries. A classic example of the deficiency of the 'shopping caddy' approach is the refusal of Philips America to adopt the video system, the V2000, developed by Philips' mother company in the Netherlands. In the late 1960s a theory of multinational product introduction, known as the '**International product life cycle**' theory, postulated a progressive adoption of products over time according to the level of economic and scientific development

of countries Such a theory is no longer valid when industries globalise waiting too long to launch a product can be fatal, particularly if the product has a short life cycle, which is more and more frequently the case. Microsoft launched Window 2000 at the same time everywhere in the world.

(3) Learning benefits. These accrue from the co-ordinated transfer of information, best practices and people across subsidiaries. Such transfer eliminates the costly 'reinvention of the wheel' and facilitates the accumulation of experiences and knowledge. In Thailand, Unilever formulated and implemented an innovative strategy to produce and market ice creams. The Thai experience served as a template for other countries in the Asia Pacific region, giving to the company a first-mover advantage. This example illustrates the benefits that can be gained from a co-ordinated transfer of best practices.

(4) Arbitrage benefits. These come from the advantages that a company managing globally can gain in using resources in one country for the benefit of another country subsidiary. These advantages can be direct competitive advantages or indirect cost advantages. A competitive advantage can be gained by playing a 'global chess game': for instance, engaging in a price war in one country in order to mobilise the resources of competitors in that country, depriving them of cash flow which could be used elsewhere. This strategy was used by Goodyear, the US tyre giant, when in the early 1970s, Michelin from France moved to North America. Goodyear, who had a small market share in Europe, engaged in a price war that Michelin was obliged to counter by lowering its prices, and de facto reducing its financing scope for its American expansion. Another type of arbitrage comes from differential cost elements such as taxes, interest and possibly risk reduction though the pooling of currencies.

Those four benefits are real but achieving them is subject to certain conditions, and their adoption has to be measured against the real competitive advantage they provide to the firms adopting them. The benefits in costs reduction obtained by economies of scale are contingent upon the market responsiveness to standardisation and whether customers are price sensitive. If, on the contrary, customers are not responsive and prefer tailored products and services to standardisation, a global approach is less appropriate. A similar reasoning applies to the benefits of timing. As for purchasing power, it may be limited for culturally sensitive services such as advertising. The benefits of learning are positive if the experience gained in one country is applicable to another. If it is not the case, there is a timing deficit: the time of realising that one has made a mistake plus the time to learn the new environment. At Euro Disneyland near Paris, two years were lost because the transfer of knowledge from Florida or California did not help the European operation.

The benefits of arbitrage can be offset by the cost of managing the arbitrage and the legal barriers that may exist to prevent such arbitrage. In the case of tax arbitrage, governments are very careful to make sure that global companies do not abuse their arbitrage power.

Factors that work against globalisation / The localisation pushes

(1) Cultural factors: attitudes, tastes, behaviour and social codes

When the consumption of a product or a service is linked to traditions and national or religious values, global standardisation is not effective. Some products – for instance, Kretek (tobacco and clove) cigarettes in Indonesia, or the Pachinko (pinball) game in Japan – are unique to one society and their globalisation is nearly impossible, although one can argue that with innovative marketing it may be possible to do so. The example of the arrival of 'Beaujolais nouveau' wine, typically a Burgundy and Parisian bistro event before the 1970s, can be now available in Tokyo, Paris, New York on the same day, 'Halloween' (trick or treat) masquerades, a typical US festivity, are now celebrated in Europe. This shows that even some highly cultural goods can be appreciated by customers all over the world, but it remains that food and drink tastes, social interactions in the process of negotiating a sale, attitudes towards hygiene, cosmetics or gifts varies from culture to culture, thus hampering a global product design or approach. In the Asia Pacific region, for instance, personal relationship building more than legal contracts is the normal

way to conduct business. One has to spend time and effort to build these personal ties, which in a US context would be considered as a waste of time.

(2) Commercial factors: distribution, customisation, and responsiveness

In some sectors, distribution networks and practices differ from country to country and as a consequence the ways of managing the network, motivating dealers and distributors, pricing, and negotiation are hardly amenable to global co-ordination. For instance, the marketing and distribution of pharmaceutical products differs according to the country's health system. In some countries, like Japan, doctors sell medicine, while in other countries pharmacists are selling to patients who get a refund (or not) from their insurance company, while in yet other cases pharmaceutical products are delivered freely to the patient. Responsiveness to customers' demands, as well as customisation are other factors which almost by definition defeat standardisation. Private saving or current accounts to individuals, loans to small and medium-size enterprises (SMEs), mortgages, consulting activities and individual architectural designs are activities in which a local presence and a fast reaction to customers' requirements are needed for competitive success. Although some practices, processes or methodologies can be standardised on a worldwide basis (consultants, engineering, architects, or auditors for example), it remains that specific customer requests have to be taken into consideration, thus limiting globalisation.

(3) ***Technical factors: standards, spatial presence, transportation and languages***

Technical standards in electrical, civil, chemical or mechanical engineering can create a burden for global companies. Scale economies and cost benefits of global integration and standardisation cannot be exploited fully when technical standards vary greatly. In certain cases, standards can be changed without major modification – as, for instance, in consumer electronics where creating multi-standard products with PAL, SECAM and NTSC does not represent a major hurdle for global manufacturing. In other instances, standards are not that easy to accommodate and require specific local production lines; that is mainly the case for beer, for instance.

Spatial presence is needed in those industries which need to occupy a physical space in order to create and distribute their products and services: retail banking, retailing, hotels, local telephones services, hospital, entertainment, car dealers, etc. are example of industries where the services have to be produced locally. In those industries there are still some advantages in globalising certain functions such as back office functions (accounting, data processing, global sourcing, transfer of best practices, etc.) but the location constraint still limits globalisation benefits. In the future, E-commerce is likely to reduce the spatial constraint considerably, particularly when it comes to immaterial services such as banking or movies on demand. E-commerce with physical products can also eliminate the spatial constraint as far as the customer interface is concerned but is still hampered by the logistical constraints. The example of Amazon.com demonstrates that it is possible for a customer in Paris or in Rio de Janeiro to order a book through Amazon but the same customer will have to bear shipping costs that will eliminate the basic cost advantage of the E-bookstore. This is the reason why Amazon is looking for local partnerships outside the United States, thus moving toward a more multinational business design.

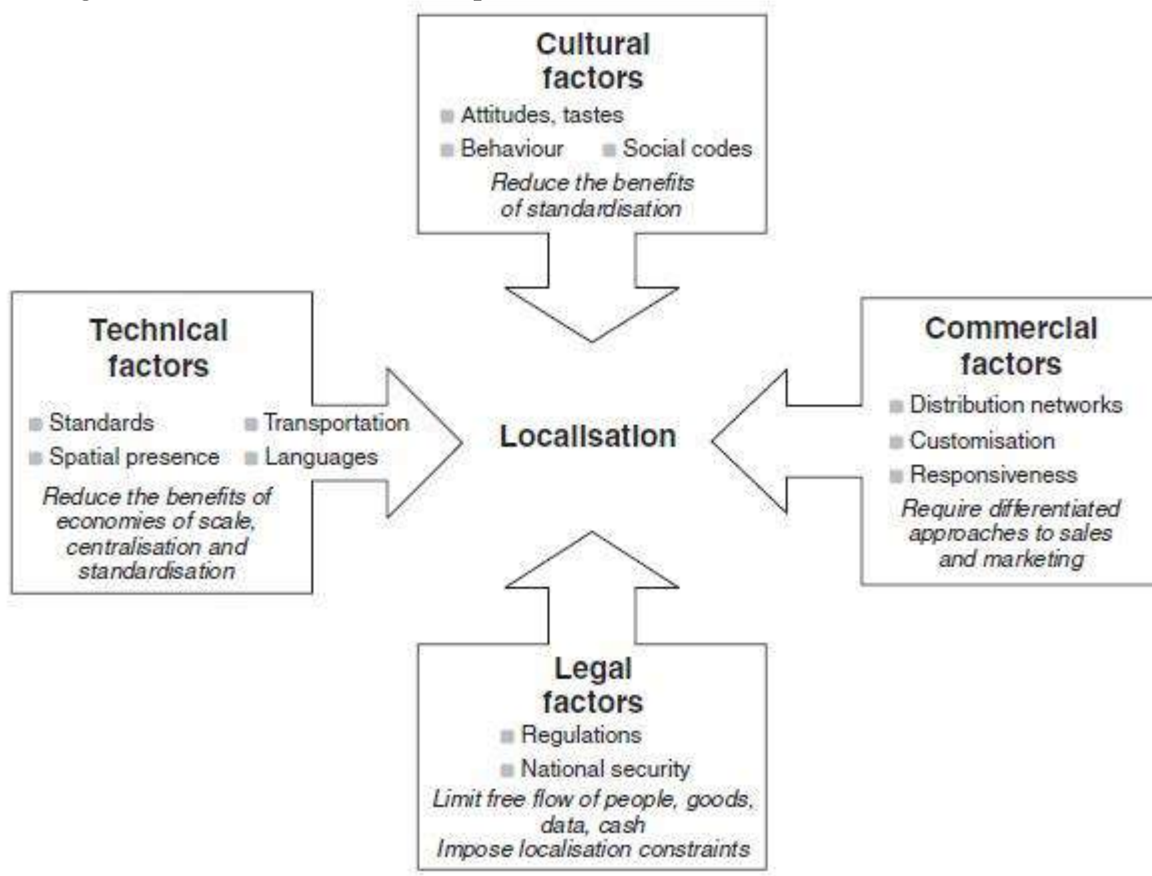
The impediments of transportation are important if the cost of transport cancels out the benefits of concentration of production. Bulk commodities like cement or basic chemicals are more economically produced in local plants rather than in global centralised units, despite the scale economies that could be gained: the cost and the risks of transport cancel out the benefits of centralised production. Similarly, when production systems are not scale-intensive and small productive units can achieve similar costs to large plants – in plastic moulding, for instance – there are no major benefits in building a global productive system.

Finally, languages can add additional constraints to global approaches. Those constraints can be significant when it comes to services to individual customers: training services, personal banking and personal

telecommunication or retailing are possible examples. However, there are two major trends that can reduce language constraints. English has become more and more a 'global language' and industries such as graduate business training or high-level consulting can use English without bothering with translation.

(4) Legal factors: regulation and national security issues

Governments impose regulatory constraints that often work against globalisation, either because they limit the free flow of personnel (regulation on working permits), cash (exchange control, tax), goods (custom duties, quotas), data (censorship, the Internet and EDI control) or because they impose localisation constraints (local content policies, local ownership and joint venture policies). Over the years, thank to the GATT and now the WTO and also multilateral agreements (European Union (EU), ASEAN, NAFTA, etc.) or International Monetary Fund (IMF) requests, government legislation is leaning towards more open legislative contexts that favour globalisation. However, some constraints still exist. Some sectors such as telecommunications, media, banking and insurance are still tightly controlled and some countries, (such as China and India) or regional blocks (EU), still impose local content requirements. Finally, governments are much concerned with national security and will prevent foreigners gaining too much control of their defence or strategic sectors industries. In the defence sector, for instance, where R&D costs are huge and economies of scale significant, globalisation would be fully justified, but is in fact limited because of national security constraints. Fig. summarises the localisation push.



Localisation push factors

The benefits of localisation

The benefits of localisation, instead of a global integrated and co-ordinated approach, are essentially customer-oriented benefits that give firms an increased market power and ultimately an increased market share. Those benefits are flexibility, proximity and quick response time.

a **Flexibility** is the capability to adapt to customer demands in the various dimensions of the marketing mix: product/service design, distribution, branding, pricing and services. Ultimately flexibility leads to *customisation*.

a **Proximity** is the capability to be close to the market, to understand the customer's *value curve*.

a **Quick response time** is the ability to respond at once to specific customers' *demands*.

Flexibility, proximity and quick response time are very much related to each other: proximity provides the basis for flexibility and flexibility provides the basis for quick response time. All three give a competitive advantage when local cultural, technical, commercial and legal contexts vary so much from country to country.

The benefits of globalisation

Arguments in favour of globalisation	Arguments against globalisation
■ Creates overall wealth for all nations because specialisation increases trade	■ Imposes massive strain on labour force both in developed countries (job destruction) and developing countries (sweatshops, child labour)
■ Reduces inflation because of cost efficiencies	■ Standardises customer tastes. Reduces diversity
■ Benefits customers because of price reduction owing to cost efficiencies	■ Induces concentration of power in a few global corporations
	■ Introduces a 'jungle' leading to the domination of the strongest multinational
■ Better allocation of natural, financial and human resources	■ Harms the environment because of unrestrained exploitation of natural resources such as forests
■ Reduces corruption because of free market trade	■ Reduces capacity for nations to protect their national interests, cultures and values

The Global Integration/Local Responsiveness Grid

The two sets of forces – globalisation and localisation forces – are shaping the competitive structure of industries and inducing companies to configure their worldwide business systems with the right mix of co-ordination, integration or decentralisation. The Global Integration/Local Responsiveness3 grid is a mapping tool that has been developed to position industries and industry segments according to the relative importance of each set of forces. Figurerepresents a Global Integration/Local Responsiveness grid for various industries, while Figure represents a similar grid for various segments of the telecommunication industry. The mapping in Figures and reveals that industries and segments can be broadly positioned into three types of competitive situations:

a **Type I**: *Global forces* dominate and there are few advantages to push for local adaptation and responsiveness. What matters is efficiency, speed, arbitrage and learning. These industries are global, as in the case of microchips, bulk chemicals or civil aircraft.

a **Type II**: *Local forces dominate* and flexibility, proximity and quick response are determining capabilities for competitive advantage. Food retailing, consumer banking or voice telephony fall in this category.

a **Type III**: In these industries there is a *mix of global and local forces at play* and competitiveness cannot be achieved without achieving the benefits of global integration and co-ordination and, at the same time, the benefits of flexibility, proximity and quick response time. This positioning is increasingly becoming the dominant competitive battleground for a vast majority of sectors.

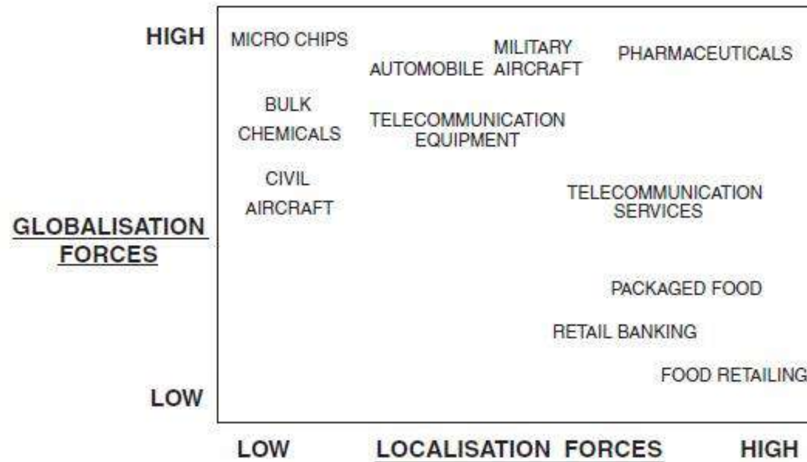


Figure Global Integration/Local Responsiveness Grid

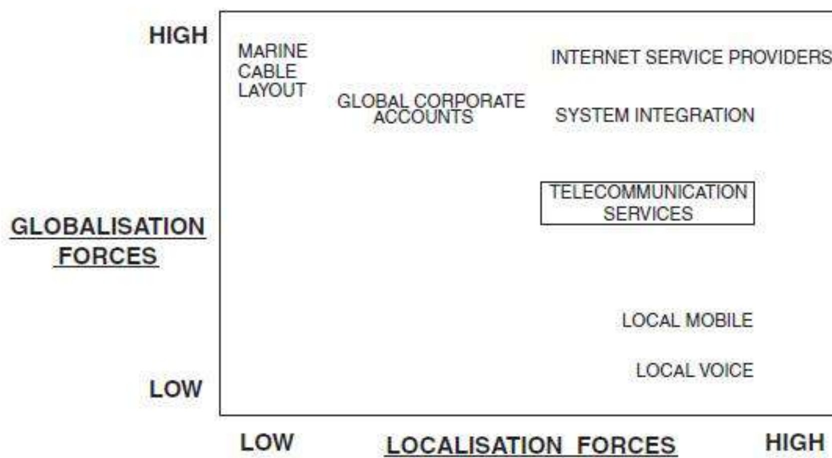


Figure Global Integration/Local Responsiveness Grid: different segments have different competitive requirements – example of telecom services

The Global Integration/Local Responsiveness Grid can be used for assessing a situation at a point in time or to anticipate evolution over time. It can also serve as mapping for the various activities of the value chain. A good understanding of industry positioning will help the formulation of business and country strategies, as well as the implementation of an effective organisational design.

Assessing Countries' Attractiveness:

Country attractive

A country will be attractive for a foreign investor if, in investing in that country, she/he gets a return that is equal to or higher than her/his *risk adjusted weighted cost of capital*. In fact, the foreign investment decision is fundamentally the same as any investment decision. If we apply the concept to a business investment (as opposed to a financial portfolio investment of securities), the logic of the decision is embodied in two key questions:

(a) Are the market prospects and the competitive conditions in a particular country such that given a set of competitive advantages, the business is likely to generate a return *equal to or higher than the cost of capital*?

(b) Are the risks of operating in this country *acceptable for the shareholders and employees*?

Analysis of the various dimensions that contribute to **country attractiveness**. These can be grouped into **two** broad categories:

- *Market and industry opportunities*
- *Country risks*

One has to bear in mind first that market and competitive opportunities vary according to the *type of industry*, and risks affect them differently. Generalisations are thus difficult to make.

Secondly, the merit of a country is first evaluated in *absolute terms* to check whether it presents minimum characteristics of opportunities and risks, and then it is generally compared with other countries having *similar features*.

For instance, a company may evaluate investing in Chile and then compare Chile with Argentina. Thailand may be compared with the Philippines, Malaysia or even Indonesia, Vietnam with Cambodia, France with the United Kingdom or Germany and India with China.

Market and industry opportunities

Market opportunities assessment measures the *potential demand* in the country for the products or services of the firm:

- Market *size*
- Market *growth*
- Quality of *demand*.

Industry Opportunities assessment measures how easy it is to *compete* in the country:

- The quality of the *competitive* climate
- The quality of the *industry competitive structure*
- The *investment incentives* granted by governments.

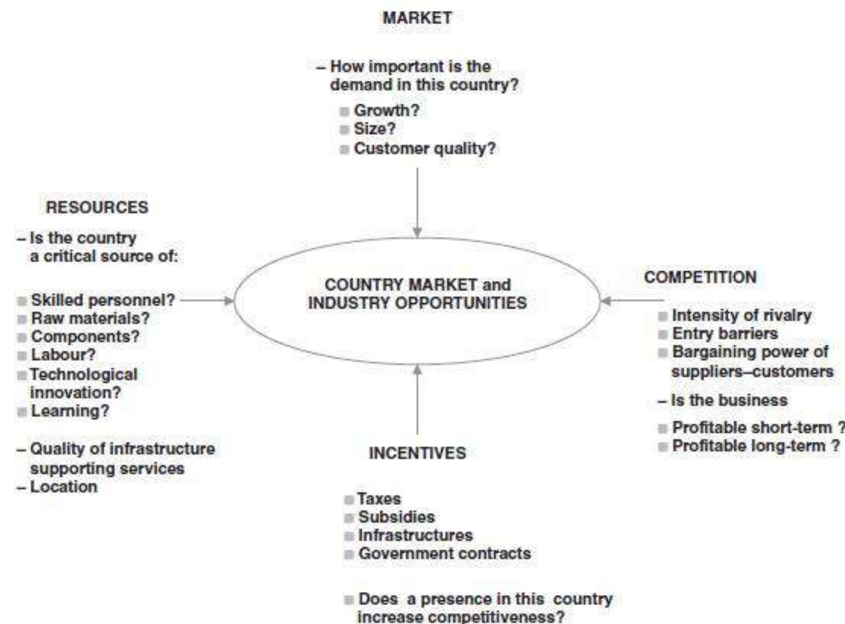


Figure Framework for country market and industry attractiveness assessment

Assessing Market opportunities

Quality of demand The quality of demand describes the nature and diversity of **market segmentation** prevailing in a country, and the profile of the customers value curve in each segment. Marketers and strategists generally distinguish two generic segments, 'low-end' and 'high-end'

In developing countries, the main bulk of the market is a large undifferentiated, price-sensitive segment co-existing with a growing more differentiated middle-class segment. In mature advanced economies, segmentation is more diverse in societies that are essentially middle-class.

Assessing industry opportunities:

Industry and competitive structure

Professor Michael Porter has proposed the concepts and techniques of **industry analysis** for strategic decision-making in his seminal book *Competitive Strategy*. Figure reproduces the five-forces framework that, according to Porter, determines the *long-term profitability potential* of an industry. For international business investment purposes we have added a *sixth force* under the heading of government intervention; it is beyond the scope of this chapter to describe in detail the various forces that are presented in Porter's original work as well as in all classic textbooks on business strategy. In an international context, the following five parameters may affect the competitive context:

Entry barriers can be increased by the licensing policy or government auctions. Distribution networks, locational space, incumbent competitive positions as well as cultural specificities are likely to affect entry costs.

Suppliers' bargaining power is somewhat bigger in protected economies where raw materials are in the hands of state monopolies or when there is a scarcity
of skilled labour or of intermediate suppliers of goods and services. Suppliers' bargaining power is greater when governments adopt a 'local content' policy.

Buyers' bargaining power may also be bigger when distribution networks are tightly controlled, as in the case in Japan.

Government may introduce ***artificial entry*** barriers by putting special constraints on foreign investors. Alternatively, governments may lower entry barriers by deregulating or subsidising factors costs.
Government policies may influence profitability and competitiveness though preferential treatment, price control, taxation and the like.

Resource endowment
The resources that attract foreign investors fall into **three** broad categories:
1. *Natural* resources
2. *Human* resources
3. *Infrastructure and support industries* resources.

1. Natural resources
Resource endowment for minerals, mining, palm oil and forestry. Countries that do not use their production for national consumption are prone to export raw materials, to promote processing by domestic companies or to invite foreign firms to invest in processing and export. Governments are very sensitive about the protection of their natural resources and more than often require controls on foreign activities in this domain by negotiating production sharing agreements as well as joint ventures. Oil and gas is probably the most globally sensitive industry, given the highly strategic nature of the commodity, the inherent risks of exploration, the capital intensity of the investments and the geographical location of the reserves. It is not by chance that the most sophisticated country-risks methodologies have been developed in this industry. A particular type of natural resource is *geographical location* which, combined with good infrastructure and support services and industry, may give to certain countries or regions within country the role of a '**hub**' or a regional centre. Singapore, located at the end of the Strait of Malacca, Hong Kong, located at the doors of continental China, Brussels for the EU or Miami for Latin America, have developed as hubs based on their geographical location.

2. **Human resources**
The quality and cost of labour is the cause of the migration of international investments that took place in the 1950s and 1960s. Offshore factories in South East Asia and Latin America have set up in Export Processing Zones (EPZs) for the production and assembly of labour-intensive products. International sourcing under the form of Original Equipment Manufacturing (OEM) or straight procurement gave an opportunity for local companies in Japan in the 1950s, in Korea, Taiwan and Brazil in the 1960s, Singapore, Hong Kong and Tunisia in the 1970s, and China, Vietnam and India in the 1980s to develop manufacturing volume and competencies and establish their international presence.
Low labour-cost countries tend to attract labour-intensive low-value added production. Since the mid-1980s India, the Philippines and to a certain extent China have tried successfully to strengthen the production of computer software, particularly in the data capture segments. India, for instance, has focused its attractiveness on offering international companies a combination of low-labour cost but highly skilled computer software personnel.

3. **Infrastructure and support industry resources**
The third type of resource that can be of interest to foreign investors is the quality of communication and logistics infrastructures, as well as the availability of supporting industries and services. *World Economic Forum* gives an overall ranking of countries, established by the, based on the quality of their infrastructure.

Government incentives

In order to attract foreign investors, governments have designed and implemented a series of incentives: fiscal, financial, and competitive operational.

Impact of incentives on foreign investor behaviour

A series of research studies on the role of incentives in foreign investment decisions has shown that their role is limited. Market attractiveness, competitive conditions, resource endowments are more important than incentives, but if those conditions are comparable in several locations, incentives may play a positive role in the decision to invest in one country in particular.

Country Risk Analysis

The purpose of country risk analysis is to assess the probability that adverse circumstances owing to political, economic or social actions will negatively affect business performance. Country risks can be grouped into four categories (see Figure).

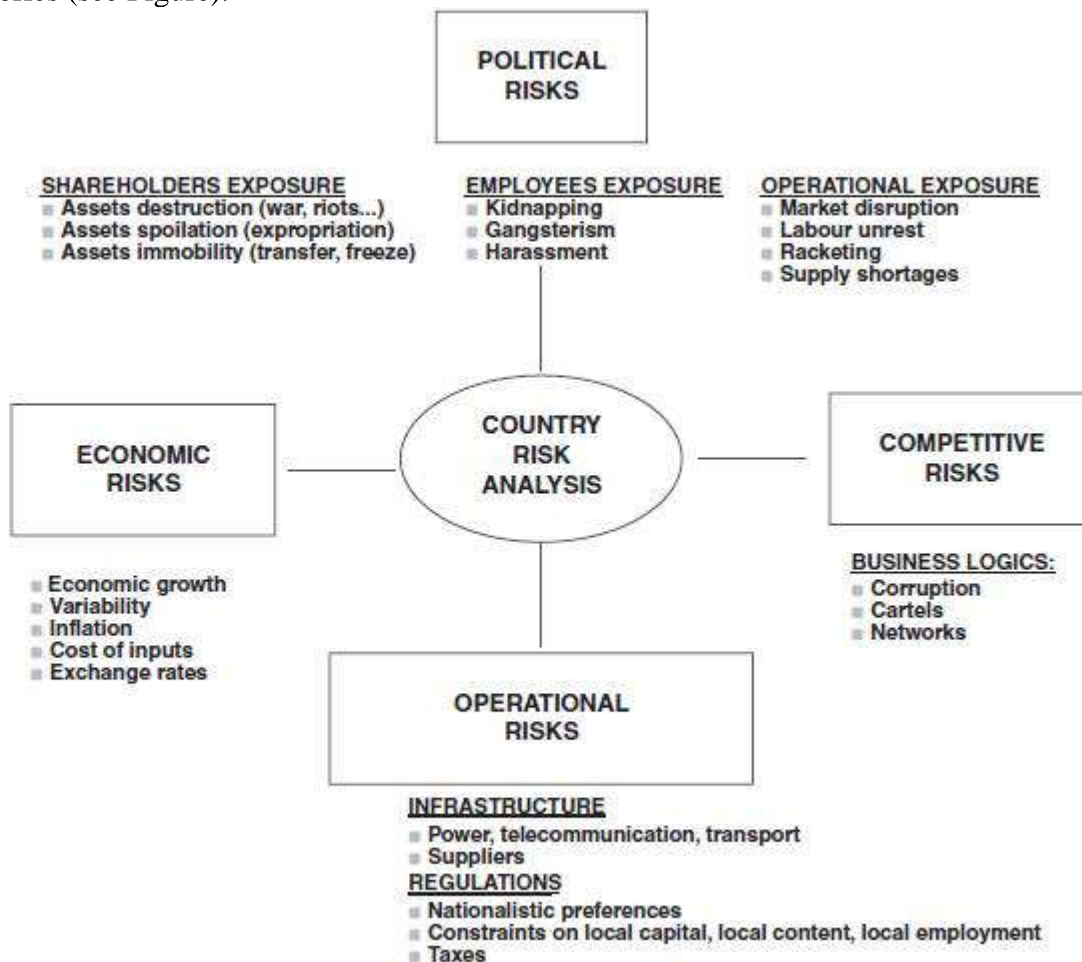


Figure Framework for country risk analysis

a) ***Political risks*:**

Political risks are probable disruptions owing to internal or external events or regulations resulting from political action of governments or societal crisis and unrest. Political risks may expose business performance in various ways.

- A first type of risk exposes *shareholder's value*, in terms of loss of capital or loss through the inability to repatriate dividends. This type of risk is associated with asset destruction linked to external or civil wars or riots, asset spoliation owing to expropriation or asset lock-in through funds freezing or interdiction on capital transfer. The regions of the world that score high on this type of risk are the Middle East and Africa.

Asset destruction (e.g. war or riots)
Asset spoliation
Asset immobility (e.g. freeze)

- Another type of political risk lies in employees' exposure linked to gangsterism, crime and kidnapping as well as operational exposure linked to labour unrest, racketeering or market disruptions or supplies shortages linked to criminal activities.

b) **Economic risks** expose business performance to the extent that the economic business drivers can vary and therefore put profitability at stake. Growth rate of Brazil as compared to India from 1970 to 2000. While the two countries have a similar annual growth rate (4.52 per cent against 4.25), Brazil has more variability than India (coefficient of variation of 1.06 against 0.55) and therefore ceteris paribus presents a higher economic risk.

c) **Competitive risks** are related to non-economic distortion of the competitive context owing to cartels and networks as well as corrupt practices. The competitive battlefield is not even and investors who base their competitive advantage on product quality and economics are at disadvantage.

d) **Operational risks** are those that directly affect the bottom line, either because government regulations and bureaucracies add costly taxation or constraints to foreign investors or because the infrastructure is not reliable.
Infrastructure: a) Power, telecoms and transport, b) Suppliers
Regulations: a) National preferences, b) Constraints on local capital, local content or local employment, c) Taxes

A comparative picture of the score of India and China country risks is reported in the EIU assessment overall China is perceived as riskier than India except for economic risk.

Unit 2 : Market Intelligence and Designing a Global Strategy

Market Intelligence: Drivers and Benefits:
Market Intelligence
MI helps organizations understand their business environment, compete successfully in it, and grow as a result. As a program, MI collects information about market players and strategically relevant topics, and processes it into insights that support decision-making. Organizationally, MI is typically placed under strategic planning, business development, or marketing. Summarizing what has been discussed already, MI is business critical for two reasons above others:
1. The operating environment of organizations is getting increasingly complex and dynamic, and, as a reflection of this complexity, accurate business information is needed not just by the headquarters but virtually all levels of the organization.
2. At the same time, decision-makers are challenged by "information disconnect" that is not caused by lack of information as such, but by lack of time to digest it and to distinguish and process what is truly relevant for decision-making purposes.
MI as a discipline is both old and new. All organizations operating in a competitive environment have always needed intelligence to learn about what the market wants from their products and services, and what is being offered to customers by the competition. Traditionally, the intelligence activity has often been narrowly perceived as "keeping an eye on the competition", which has sometimes even earned it a shady reputation. Whatever the focus, the intelligence activity has often been performed rather randomly by small teams or individuals in different parts of the organization.
Yet more recently – as dictated by the global economy and the complex requirements set for modern strategic planning, sales, marketing, and innovation management – MI has reached a position in the organization that compares to other professional support functions such as risk management, PR, or sourcing. To be successful, an increasingly knowledge-intensive enterprise simply cannot do without an organized intelligence program as one of its support groups.

Market Intelligence as A Program
Processing business information into actionable insights that help organizations understand, compete, and grow in their market is a cyclical process. Within the cycle, a needs analysis always drives the process where data are collected and processed into analyses that will be utilized in decision-making.
Decision-makers need MI both in the format of ad hoc projects and on a continuous basis. Ad hoc projects usually relate to very specific decision-making situations such as entering certain geographical market areas, as in our example in the beginning of this chapter. Continuous market monitoring, in turn, is necessary for the organizations to maintain awareness about the current developments in the marketplace, for example, in the newly entered market area.
In a world class MI program, information from external and internal sources is combined into a systematic intelligence process that serves decision-making with timely and accurate MI that helps them capitalize on opportunities and avoid threats.

MI Program Benefits
MI programs have by now been established in most large companies around the world. However, heads of MI still often find it challenging to clearly communicate the hard and soft benefits that the investment in a corporate MI program is expected to yield, especially at times when budgets are under scrutiny. The benefits of systematically organizing an MI program can be grouped under three categories as has been illustrated in Figure

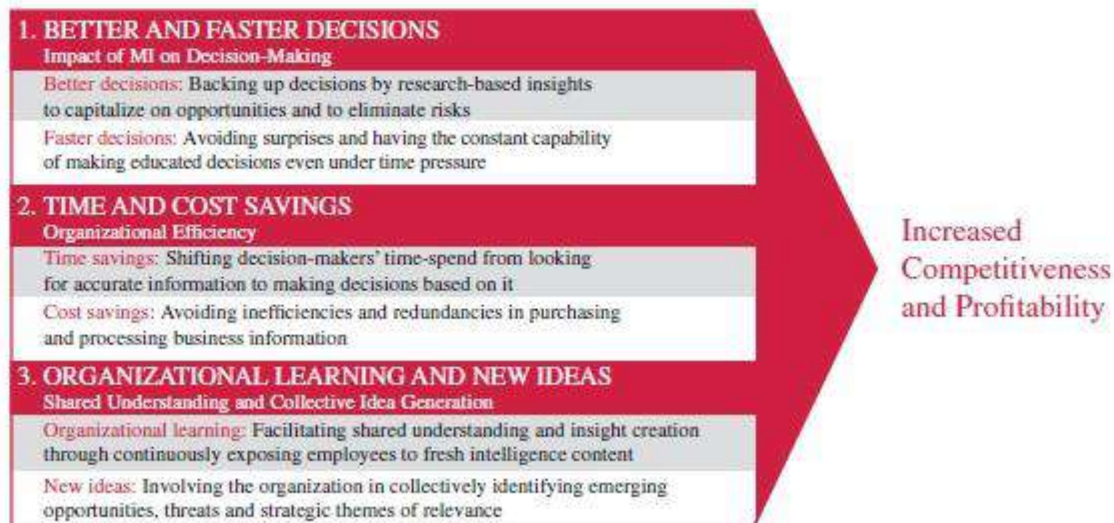


Figure Benefits of a systematic MI program

Impact: Better and Faster Decision-Making

What the corporate MI program yields as a result should be demonstrated by the organization's competitive success in its operating environment. The intelligence activity should be able to continuously produce deliverables that respond to true information needs and provide such valuable business support that timely and educated decisions are being made as a result.

In its eventual impact on decision-making, the financial worth of a well-organized MI program may be enormous, yet it is hard if not impossible to point out and quantify exactly which MI efforts contributed to which successful decisions and by how much. These benefits are therefore considered qualitative in nature.

Even though it is often hard to put a finger on exactly how big an impact MI efforts have had on the quality of a single decision, it is safe to say that an organized MI program improves the average quality of decisions made. When decision topics regularly go through a systematic process of research and analysis, the resulting decisions will be based on solidly grounded insights into aspects covering anything from the anticipated competitive response to compliance with the governing laws. Over time, this tradition makes an intelligent organization, and business literature continuously brings us success stories of how such organizations have survived even critical periods of transition.

However insightful and well grounded the decisions in an organization are, sometimes they are just made too late. One of the characteristics of an organization where the intelligence program is deeply rooted is the capability to react fast, that is, an ability to reach decisions quickly while its slower peers may still only be digesting the original surprise. The speedy process of course should not compromise the quality of the related analysis; again a reason to have an intelligence infrastructure in place that can handle rapidly emerging topics for research and analysis.

Efficiency: Time and Cost Savings

The impact of an MI program on decision-making is of course the primary justification for its existence. However, regardless of what its eventual impact is, in today's corporate world it is safe to assume that almost every organization gathers and disseminates business information somehow, which brings us to the efficiency perspective: if time and resources will be put into collecting and analyzing information in any case, it makes a big difference whether this process is organized and cost-efficient or not. While the impact

of MI on the quality of decision-making is hard to quantify, the efficiency of an intelligence program can be quite accurately measured in both time and money.
Accurate information is needed to back up decisions, and without a systematically organized intelligence program, decision-makers repeatedly find themselves in situations where they have to dig for missing pieces of information. Over time, this collective search by executives becomes very expensive for the company, and organizing the MI program therefore yields measurable benefits in the form of liberating decision-makers from searching for to actually using information. The related cost savings can be derived from the amount of expensive hours that executives save by always having the information they need at their fingertips when they need it.
Another form of very measurable benefits of MI is cost savings through optimizing the purchases and processing of information. A large organization easily spends millions of euros or dollars annually on different forms of business information, and several people may be analyzing the same topics internally without knowing of each other's efforts. If this activity is not centrally coordinated, overlaps are hard to avoid, and it may be that no one knows exactly how many budgets are being tapped into at different levels of the organization. Coordinating the purchases and processing of information therefore helps the organization to control the overall MI budget, to negotiate better deals with consultants and information vendors, and to eliminate redundancies.

Organizational Learning and New Ideas
Finally, the third category of MI benefits highlights the role of MI in facilitating the development of a shared understanding in the organization about its operating environment and in that way involving a large part of the organization in generating valuable new ideas.
Organizational learning and collective idea generation contribute to the eventual impact of MI on decision-making, but refer more to the process of constantly having potentially relevant topics or decision-making on the radar than to the actual decision-making itself. Having many years experience on the ground also contributes to the company's ability to implement decisions rapidly, as the organization, being collectively aware of the developments in its business environment, is prepared for and even expects swift reactions from the decision-makers.

Key Success Factors of World Class Market Intelligence
Six Key Success Factors of Market Intelligence Development

MI development efforts need to be seen as parts of a systematic initiative to build and maintain an intelligence program, as opposed to addressing the KSFs in isolation from each other.

Intelligence Scope refers to defining the very purpose of the intelligence program, the user groups, and timeframe (past – present – future) of the intelligence activities, and the specific topics of which the user groups will need information on a regular basis. Topics under the intelligence scope typically include, e.g. customers, competitors, suppliers, trends, and geographical market areas.
Intelligence Process refers to the gathering, analysis, and reporting of information to its user groups. The intelligence process should always be anchored to the existing corporate processes, such as strategic planning, marketing and sales, innovation, and product management, as well as supply chain management.
Intelligence Deliverables are the concrete output of the intelligence process. Deliverables may be tangible content products such as analysis reports, profiles, or market signals monitoring, or they can be interactive workshops and briefings. Deliverables may also include software tools designed to enable self-service usage of MI.

Intelligence Tools by we refer mainly to dedicated intelligence software tools that help keep the intelligence process together by serving as a searchable database of structured and relevant information. Also, intelligence tools help to automate routines of processing data into intelligence and regularly delivering the intelligence output to its users. Intelligence tools may also include templates and analysis techniques.

Intelligence Organization refers to the resources that combined make the intelligence process happen. Appointing someone as the owner of the corporate intelligence activity typically is the starting point of forming an intelligence organization, but the person needs both internal and external networks to support their work: internal network of intelligence users and contributors from different parts of the organization, as well as an external network of information sources that may include outsourcing partners, databases, industry consultants, research report providers, and so forth.

Intelligence Culture keeps the entire intelligence program alive, and it obviously cannot be sourced externally. The most important element in building an intelligence culture is senior management's genuine support of the activity. Other important building blocks are demonstrated benefits of the activity as well as internal training and marketing efforts.

Table 1 The World Class MI Roadmap

Description	Informal MI "Firefighters"	Basic MI "Beginners"	Intermediate MI "Coordinators"	Advanced MI "Directors"	World Class MI "Futurists"
Intelligence Scope	No Specific focus has been determined. Ad hoc needs drive the scope.	Limited scope, seeking quick wins. Focus typically on competitors or customers only.	Wide scope with the attempt to cover the current operating environment comprehensively.	Analytical deep dives about specific topics complement the comprehensive monitoring of the operating environment.	Broad, deep and future-oriented scope that also covers topics outside of the immediately relevant operating environment.
Intelligence Process	Reactive ad hoc process puts out fires as they emerge. Uncoordinated purchases of information.	Needs analysis made. Establishing info collection from secondary external sources. Little or no analysis involved in the process.	Secondary info sourcing complemented by well established primary info collection and analysis.	Advanced market monitoring and analysis processes established. Targeted communication of output to specific business processes and decision points.	Intelligence process deeply rooted in both global and local levels of the organization. MI fully integrated with key business processes; two-way communication.
Intelligence Deliverables	Ad hoc deliverables quickly put together from scratch.	Regular newsletters and profiles complement ad hoc deliverables.	Systematic market monitoring and analysis reports emerge as new, structured MI output.	Two-way communication is increased in both production and utilization of MI output. Highly analytical deliverables.	High degree of future orientation and collaborative insight creation in producing and delivering the MI output.
Intelligence Tools	Email and shared folders as the primary means for sharing and archiving information.	Corporate intranet is emerging as a central storage for intelligence output.	Web-based MI portal established that provides access to structured MI output. Users receive email alerts about new info in the system.	Sophisticated channeling of both internally and externally produced MI content to the MI portal. Multiple access interfaces to the portal in use.	Seamless integration of the MI portal to other relevant IT tools. Lively collaboration of users through the MI portal.
Intelligence Organization	No resources specifically dedicated to MI. Individuals conducting MI activities on a non-structured basis.	One person appointed as responsible for MI. Increasing coordination of MI work in the company. Loose relationships with external info providers.	A fully dedicated person manages MI and coordinates activities. Centralized, internally or externally resourced info collection and analysis capabilities exist.	Advanced analytical and consultative skills in the intelligence team. MI network with dedicated resources in business units for collecting local market info. Non-core MI activities outsourced.	MI team has reached the status of trusted advisors to management. Internal MI network collaborating actively. Internal MI organization smoothly integrated with the outsourced resources.
Intelligence Culture	No shared understanding exists of the role and benefits of systematic MI operations.	Some awareness exists of MI, but the organizational culture overall is still neutral towards MI.	MI awareness in a moderate level. Sharing of info is encouraged through internal training and marketing of MI.	MI awareness is high and people participate actively in producing MI content. Top management voices its continuous support to MI efforts.	A strong MI mindset is reflected in the way people are curious towards the operating environment and co-create insights about it.

Intelligence Scope

The first step is to reach a stage where there's at least some sort of focus in the intelligence activity rather than only putting out fires as they emerge. Most companies concentrate on first understanding their customers and competitors better, and this immediate focus may often carry over as the most important focus area throughout the intelligence development effort.

Also, at first the intelligence program may only be serving one **group** of users in the organization instead of several. Indeed with limited resources it is wise to rather first concentrate the efforts on narrow areas where good results can realistically be expected than trying to serve too many user groups for any of them to see any true impact from the activity.

Over time, the scope of an average intelligence program tends to deepen, i.e. the analytical and consultative delivery capability of the intelligence program increases, and so will the usefulness of the deliverables for strategic decision-making purposes. Finally, an increasing emphasis will be placed on future-orientation, i.e. in addition to producing highly analytical output on a wide range of topics – and probably for a wide user base – the intelligence program will be able to drive discussions about the future strategic choices that the organization has, going forward.

Breadth of Scope:

Once the primary user groups of the intelligence program have been defined, their intelligence needs should be addressed. These needs will fall under two categories: the topics on which information is needed, and the *format* in which the output should be delivered.

Depth of Scope: Ensuring that the intelligence program can deliver actionable insights that will have an impact on business rather than just gathering and further disseminating information.

Business needs of the primary target groups of the intelligence program will drive the analytical and consultative efforts towards topic areas where insightful intelligence output should serve as decision-making support. On the other hand, if in conjunction with the intelligence topics set up a continuous market screening system has already been established to monitor the entire operating environment of the company, the system may also raise topics to the agenda that call for further analytical processing: opportunities and threats may arise from the business environment that would go unnoticed without systematic market screening. As a result, companies start adding depth to their intelligence output. Profiles, analysis reports, briefings, and workshops will emerge as intelligence deliverables on selected topics of interest.

Adding depth to the scope of the intelligence program may also happen in parallel with adding breadth, i.e., expanding its user base.

Intelligence Process

The intelligence process is a cyclical flow of events that is kicked off with a needs analysis about a topic that should be looked into for decision-making purposes.

Information will subsequently be collected from secondary and/or primary sources, and it will be analyzed and reported to decision-makers for them to use it and give feedback on the project.

Intelligence professionals will process any assignment through the same phased cycle, yet roughly speaking there are two types of approach to doing it, depending on the goals set in the needs analysis:

Rapid response research where speed is important, hence there's little time for conducting analysis and producing comprehensive reports.

Strategic analysis where being thorough and producing polished and detailed reports is more important than speed.

Being world class in intelligence process:

Decision points in key business processes have been identified and matched with regular intelligence deliverables.

A world class intelligence process starts with a world class needs analysis, i.e. anticipating and verifying the upcoming decision-making needs.
The information collection phase is “industrialized”, allowing time and resources for conducting primary intelligence and hence adding insight to readily available secondary information.
The majority of time and resources is spent on analysing information and drawing conclusions and making interpretations.
The delivery of the resulting intelligence content is personalized and followed up.
The intelligence team has adopted a mindset of continuous improvement.

Intelligence Tools - Collecting, Storing, and Communicating Intelligence

Most central tool in running a world class intelligence program is an intelligence portal; software that has been designed to support the intelligence activity both at the production end and in accessing and contributing to the deliverables. Hence, we will limit the focus in this chapter to intelligence portals only.
An intelligence portal provides a single user interface to screened and organized information content from both external and internal sources. Companies around the world are using a wide range of IT solutions for the general purpose of managing and processing business information; however, the best intelligence portals have been specifically designed and developed to support the requirements of the corporate intelligence process, and the eventual configuration of the software typically follows each company’s own intelligence process flow. An intelligence portal usually nests in the organization’s intranet and is hosted either in the company’s own IT infrastructure or by an external service provider.

Figure Screen shots of an intelligence portal, the Intelligence Plaza®

An intelligence portal is one of the most tangible elements of an intelligence program. As such, it serves as a natural centrepiece of an MI program, even though people are doing most of the value-adding intelligence work.

Unlike the intelligence process or culture, or other abstract concepts associated with intelligence activities such as needs analyses and workshops, an intelligence portal has a concrete look and feel, and this makes it a great marketing vehicle for the intelligence deliverables and indeed the entire MI program.

There is an established market for commercial software applications to support the specific requirements of MI processes. However, the advanced functionalities nowadays included in the corporate intranet platforms such as SharePoint have encouraged some companies to build up home-grown solutions. Experience shows, however, that commercial applications are still in demand: new possibilities offered by SharePoint have not turned MI professionals into application developers, nor have they made the IT professionals better at understanding MI processes. As a result, a market niche for SharePoint MI software applications is emerging.

Useful **features** and aspects to consider when implementing an intelligence portal include:

Content management

Data sourcing and input features

Security

Dissemination

Self-service access

Collaboration

Being world class in intelligence tools:

All relevant intelligence content is stored in one searchable database.

Personalized email alerts of market developments and new relevant content are being sent to the MI users on a regular basis.

The functionalities support all phases in the intelligence process.

The functionalities facilitate the sharing of field intelligence, networking, and co-creation of intelligence deliverables through an engaging user experience comparable to the existing social media applications.

The functionalities enable integration of intelligence content to various user interfaces (mobile, SharePoint, etc.) and business processes.

Designing a Global Strategy

A ***global strategy*** is the way a company defines its long-term objectives for the world market; selects its value proposition for the world market; builds, integrates and co-ordinates its business system to gain and sustain a global competitive advantage and puts in place an organisation to manage its operations worldwide.

Framework For Global Strategy

A global strategy is made up of **four** major components

Global ambition Stating the relative importance of region and countries for a company

Global positioning Choice of countries, customer segments and value proposition

Global business system Investments in resources, assets, and competences to create a global value chain and global capabilities through alliances and acquisitions

Global organisation Global structure, processes, co-ordination and HRM.

The global strategic ambition expresses the role a company wants to play in the world marketplace and how it views the future distribution of its sales and assets in the key regional clusters of the world. One can identify **five** types of **role:**

- Global player
- Regional player
- Regional dominant global player
- Global exporter
- Global operator.

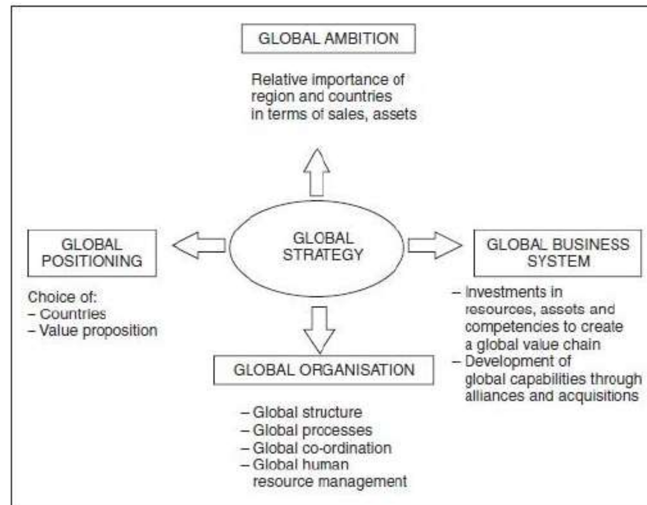


Figure Global strategy framework

A company whose ambition is to be a **Global player** aspires to establish a *sustainable competitive position in the key markets of the world* and to build an integrated business system of designs spread over those key markets. SONY would qualify for such a description of its role, as would Unilever, Ericsson, Nokia, Alcatel, Motorola, Shell, Xerox, Canon, Procter & Gamble and Citibank.

A **Regional player** defines its role as to capture a *strong competitive advantage in one of the key regions of the world* – North America, Europe or Asia – and to be a marginal or relatively weak competitor in the other parts. Peugeot or Fiat in automobiles, NEC or Barclays would be examples of such an ambition.

A **Regional dominant global player** is a company whose role is more than a regional player but it is not yet selling across the *key markets of the world*.

A **Global exporter** is company whose role is to *sell across the key markets of the world* products manufactured or services operated in its home country and who builds foreign operations only to support the export drive. The major aerospace or defence companies like Boeing, Airbus and Raytheon can be classified into this category despite the fact that they have some supporting assets (maintenance, sales offices, etc.) outside their home region.

A **Global operator** is a company that procures a large fraction of its product components in factories3 located outside its base market and which concentrates its sales in its *domestic market*. In such a case the ambition would hardly qualify as a global: however, many managerial issues of integration and co-ordination of activities, both in-house factories or long-term subcontracting, would be quite similar to those that a global company would have to face.

Entry strategies

Entry strategy concerns three aspects:
Entry *objectives* (*why*)
Timing of entry (*when*)
Mode of entry (*how*).

Entry objectives:

Market development objectives are to enter a market because of:
– Size and growth opportunity – depends on income and population of a country
– Criticality of countries – there are key countries in which a presence is needed for global long-term competitiveness owing to size or quality of customer base
Resource access objectives – extracting key resource such as natural or human resources which contribute to competitive advantage
Learning objectives – gains in knowledge/competence in countries where industry is state-of-the-art
Co-ordination objectives – regional co-ordination of activities owing to favourable location and infrastructure advantages.

Entering A Country Through Wholly Owned Subsidiaries

This entry mode is the one that gives the most control over operations, but also involves the highest mobilisation of resources and competencies and bears the highest risks. Creating a subsidiary in a country calls for the following requirements:

- Assuming that a proper country attractiveness and risk analysis has been done prior to the investment, one needs first to familiarise oneself with the *legal, institutional, commercial* and *relational* environment. It is one thing to have analysed the market and competition for decision-making, it is another thing to master the nitty-gritty of a full greenfield investment or an acquisition. This is the role of the *feasibility study* that analyses the various aspects of an investment dealing with real estate, construction, project management, sourcing, recruitment, incorporation, registrations, financing, fiscal and legal matters. Feasibility studies should be supported by a full financial plan projecting future cash flow calculations and financial needs. Feasibility studies as well as project management can be contracted out to locally-based consultants or engineering firms, but the overall control and responsibility falls upon the foreign investor.
- Managing a construction project in a foreign country involves a series of practical and sometimes difficult impediments, such as the norms and standards of construction, the professionalism of local contractors and their commercial practices, the availability of supplies, customs clearance of imported materials and components, the behaviour and attitude of project workforces and the local bureaucratic hassles. When an investor is investing in a greenfield operation for the first time in a country, it is advisable that they should rely on a *locally-based project manager*.
- A further impediment of a greenfield operation is the need for *recruitment, training* and *management* of a local workforce and the capacity of expatriate personnel to get quickly culturally acquainted and able to *transfer technology*. This determines the timing and the cost of the investment that will ultimately affect the overall profitability and cash flow of the project.
- On the positive side, a greenfield wholly-owned investment gives the investor full control over operations and access to the *full profitability* of the investment. Sometimes the feeling of 'full control' may be illusory if the company has sent expatriates with a superficial knowledge of the country and a lack of cultural understanding. In such case, expatriate top managers will be isolated in an ivory tower and local personnel manages the operations their own way, hiding themselves behind apparent obedience and respect.

On the financial front, a wholly owned investment demands that foreign investors bear the full risk of *equity and debt financing*, sometimes facilitated by export credit insurance granted by the home country government or insurance community.
(a) **Advantages** – gives most control over operations, low technological leakage
(b) **Disadvantages** – requires the highest mobilisation of resources and competencies; highest risk; high up-front investment; slow entry

Entering a Country through acquisitions

Overall, the advantage of acquisitions as an entry mode is the immediate availability of resources, assets and competencies that saves time for the foreign investor. Another advantage is the access provided to a market of resources when the competitive arena is already well occupied, and the window of opportunity is closed. On the less positive side, acquisitions in foreign environments demand cross-cultural integration skills that may not be the prime talent of investors. Acquisitions of local firms by foreigners can also be seen in certain case as an intrusion that bruises national pride. Finally, acquisitions are often made with high acquisition premiums that make this mode of entry more costly than other alternatives.
(a) **Advantages** – immediate availability of resources, assets, and competencies enables access to market when window of opportunity is closed; high market penetration; high control of market; low technological leakage
(b) **Disadvantages** – requires cross-cultural integration skills which acquiring company may not possess; some nationalities may view acquisition by foreigners unfavourably; costly, as often associated with high acquisition premiums; high political risk exposure

Entering a country through Joint Ventures

A joint venture is an ambiguous concept since it embraces several forms of partnership. We shall consider joint ventures as *equity participations in separate legal entities* in which two or more partners invest tangible and intangible capital. Some countries, like China, have set up the concept of 'contractual joint ventures that are a hybrid form of equity and project partnership agreement, but these are relatively limited and in practice the implications of their management are very similar to equity joint ventures. In emerging markets, joint ventures have been the main form of foreign direct investment (FDI). In 1996, in Korea, joint ventures represented around 77 per cent of all FDI, 72 per cent in China, 52 per cent in Latin America and 54 per cent in Eastern Europe.

(a) **Advantages** – quick entry; medium to high market penetration
(b) **Disadvantages –** medium to high technological leakage; high managerial complexity
(c) Partner selection – depends on a combination of legal requirements and internal capabilities the firm possesses
(d) Partners categories:
(i) Sleeping
(ii) Complementing
(iii) Investor
(iv) 'Teaching'
(v) Acquisition
(e) Partner types – each has their own advantages and disadvantages:
(i) Supplier
(ii) Customer/distributor
(iii) Competitor

(iv) Diversifier
(v) Investor
(vi) Government
(f) Partner evaluation – uses the same criteria used in assessing alliance partner: strategic fit, capability fit, cultural fit and organisational fit
(g) Management:
(i) Staffing – foreign managers should possess political and cultural skills; local staff should ideally be loyal to the joint venture, not to the local partner
(ii) Control – can be obtained through shareholding ownership or responsibility over operational functions
(h) Termination renewal:
(i) Termination – potential problems are the '*Death Valley*' *issue* (development of a vicious cycle in which partners' communications are shut off) and *joint venture decay* (drop of mutual interest and loss of impetus for further collaboration)
(ii) Failures/problems – absence of strategic vision; 'believing without seeing'; failure to understand local partner's strategic logic; haste in negotiation; insufficiently prepared staff or lack of organisational support
(iii) Renewal – revitalise the joint venture by increasing range or broadening scope of its activities

Licensing agreements are contractual arrangements by which a company (the *licensor*) transfers to another company (the *licensee*) its product and/or process technology with the right to exploit it commercially. The brand name of the licensor may or may not be part of the licensing agreement. The licensor receives financial compensation in the form of royalties and an up-front lump sum payment. Royalties can be calculated as a percentage of sales or as a fixed amount per unit sold. In addition to the transfer of technology, the licensor may send its engineers to help in technology transfer and functioning. It may also receive some form of technological fees. Finally, within a licensing agreement, a licensor can contractually force the licensee to buy intermediate products or components. In that case, the licensor gets the benefits and profits associated with those sales. The benefits of licences are the low commitment in term of personnel and capital involved. It is an economic way to enter a market. However, the disadvantages are manifold. First, there is a risk of *technological appropriation* by the licensee, who may become a future competitor. This has been the case in the past with Framatome of France, who licensed in the technology of high-pressure nuclear reactors from Westinghouse and which progressively became more advanced and more competitive than the licensor. Another risk involves *quality control*. Particularly when the licence includes the brand name of the licensor, if the licensee is not quality conscious, it may ruin the name of the licensee. The main strategic disadvantage of licensing is that the licensors are very distant from the market and have no control over the company's destiny in the licensee country.

Franchises are another form of indirect contractual arrangement through which the franchiser grants the franchisee the right to use its name and receive a financial compensation similar to the licensing agreement (fixed plus royalties). The franchiser generally forces the franchisee to adopt a certain number of operating policies so that it can maintain a standard level of quality associated with its brand name. **Examples** of international franchises can be found in the hospitality industry (Hilton, Accor), beverages (Coca-Cola bottling), fast food (McDonald's) and distribution (Benetton, Gap).
(a) **Advantages** – economic (low commitment of personnel and capital); low political risk exposure
(b) **Disadvantages** – risk of technological appropriation by licensee who may become future competitor; damage to brand name if licensee is not quality conscious; licensor's lack of control over licence destiny in the licensee country

Entering a Country through Local Agents and Distributors

The appointment of a local agent or distributor is probably the most frequent mode of entry for the thousands of SMEs who want to reach international markets. For the most established large multinational enterprises, this is also a means to reach countries that are either risky, or whose size does not justify a major investment. It can also be an economic way to test markets without committing too many resources up front. The distinction between an agent and a distributor is that the latter carries out the logistical tasks of stocking, transporting and billing, while the former is simply a salesperson and an order-taker. In emerging markets one can often find three categories of agents and distributors: domestic companies (most often medium-sized firms or large multi-business family conglomerates), government monopolies in planned economies or large international trading companies like Jardine Matheson, the East Asiatic Company, Diethelm or Swire in the Asia Pacific region.

The main **advantage of distribution agreements** is that they require a limited amount of resources from the global firm; the main disadvantages are the lack of contact with the market and the conflict of interest that can emerge when sales reach a certain level. The economic reason for this conflict is caused by the fact that distributors are generally remunerated by a commission as a percentage of sales. When sales grow, the total commission may reach a point where it is bigger than the fixed costs required to set up a wholly-owned marketing subsidiary. The multinational firms then try to get rid of the local distributor, as it has seen in Europe with the Japanese car-makers who have progressively replaced their distributors by their own organisation in major countries. Knowing this, the local distributor may be tempted to fail to push sales when it is obvious that a substitution point is approaching. Instead of fighting a lost cause, international distributors have often adopted a strategy of becoming ‘partners’ rather that pure distributors and raising the value added of their services to both customers and principals in order to raise ‘switching costs’. However, when the country becomes a significant portion of the turnover and becomes ‘key’, the global firm will generally turn to another, more direct mode of entry.

Advantages:

(i) Economic (low resource commitment)
(ii) Possible quick entry
(iii) Low political risk exposure
(iv) Low technological leakage

Disadvantages:

(i) Lack of contact with market
(ii) Conflict of interest when the sales reach certain level

Entering Country through Representatives, Procurement or a Technical Office

The representative office is another very frequent entry mode, considered as a steppingstone or a ‘beachhead’. In China, Russia, Vietnam and newly opened countries this type of entry consists of sending an expatriate manager (sometime using a locally recruited person) to collect information, establish contacts, organise direct sales, lobby for licences, negotiate distribution or joint venture agreements and recruit local personnel. This entry mode is frugal in resource consumption and beneficial in competencies-building, but it reaches its limit when it comes to actually running a business. It fits corporations that are selling big projects (railways systems, airport, defence contracts, turnkey plants) at the pre-bidding phase. In these cases, representative offices complement and control the local agents who are lobbying for information and access to decision-makers. Technical or procurement offices are another form of entry. Technical offices are most relevant when the country is a source of technological innovation and a presence can give access to useful contacts and information. Procurement or purchasing offices are most appropriate for large retailers or big commodity buyers who set up an office in order to be close to suppliers, to negotiate contracts and to control

their execution. Some companies specialise in buying for third parties and are used by firms which do not want to commit resources to establishing their own office.

(a) Representative office

(i) **Advantages** – Frugal in resource consumption; beneficial in competence building; appropriate when corporations are selling big projects at the pre-bidding phase; low political risk exposure; low technological leakage

(ii) **Disadvantages** – Slow entry; low market penetration; low control of market

(b) Technical or procurement offices:

(i) Useful when country is source of technological innovation and company presence give access to useful contacts and information

(ii) Procurement offices most appropriate for large retailers or big commodity buyers who want to be close to suppliers and control contract execution

Unit 5
Globalization, Innovation, and Sustainability

Challenges to Strategic Management

A business corporation could be successful by focusing only on making and selling goods and services within its national boundaries. International considerations were minimal. Profits earned from exporting products to foreign lands were considered frosting on the cake, but not really essential to corporate success. During the 1960s, for example, most U.S. companies organized themselves around a number of product divisions that made and sold goods only in the United States. All manufacturing and sales outside the United States were typically managed through one international division. An international assignment was usually considered a message that the person was no longer promotable and should be looking for another job.

For a very long time, many established companies viewed innovation as the domain of the new entrant. The efficiencies that came with size were considered to be the competitive advantage of the large organization. That view has been soundly defeated during the past 30 years. The ability to create unique value and grow an organization organically requires innovation skills. A strategic management approach suggests that if an organization stands still, it will be run over by the competition. What was extraordinary last year is the standard expectation of customers this year. We have watched many large corporations succumb to the lack of innovation in their organization. Sears was the dominant retailer in the United States for more 70 years. Today, it is struggling to find an approach that will give it a competitive advantage. IBM was a company that dominated mainframe computing and was fortunate enough to find a visionary CEO when the mainframe market was crushed by the advent of the PC. That CEO (Louis V. Gerstner, Jr.) transformed the organization with innovation that was cultural, structural, and painful for the company employees. Innovation is rarely easy, and it is almost never painless. Nonetheless, it is a core element of successful strategic management.

Similarly, until the later part of the 20th century, a business firm could be very successful without considering sustainable business practices. Companies dumped their waste products in nearby streams or lakes and freely polluted the air with smoke containing noxious gases. Responding to complaints, governments eventually passed laws restricting the freedom to pollute the environment. Lawsuits forced companies to stop old practices. Nevertheless, until the dawn of the 21st century, most executives considered pollution abatement measures to be a cost of business that should be either minimized or avoided. Rather than clean up a polluting manufacturing site, they often closed the plant and moved manufacturing offshore to a developing nation with fewer environmental restrictions. Similarly, the issues of recycling and refurbishing, as well as a company's responsibility to both the local inhabitants and the environment where it operated, were not considered appropriate business approaches, because it was felt these concerns did not help maximize shareholder value. In those days, the word *sustainability* was used to describe competitive advantage, not the environment.

Today, the term used to describe a business's sustainability is the triple bottom line. This phrase was first used by John Elkington in 1994 to suggest that companies prepare three different bottom lines in their annual report.

1. Traditional Profit/Loss
2. People Account – The social responsibility of the organization
3. Planet Account – The environmental responsibility of the organization

Impact of Globalization

Today, everything has changed. **Globalization,** the integrated internationalization of markets and corporations, has changed the way modern corporations do business. As Thomas Friedman points out in *The World Is Flat*, jobs, knowledge, and capital are now able to move across borders with far greater speed and far less friction than was possible only a few years ago.

For example, the interconnected nature of the global financial community meant that the mortgage lending problems of U.S. banks led to a global financial crisis that started in 2008 and impacted economies for years. The worldwide availability of the Internet and supply chain logistical improvements, such as containerized shipping, mean that companies can now locate anywhere and work with multiple partners to serve any market. For companies seeking a low-cost approach, the internationalization of business has been a new avenue for competitive advantage. Nike and Reebok manufacture their athletic shoes in various countries throughout Asia for sale on every continent. Many other companies in North America and Western Europe are outsourcing their manufacturing, software development, or customer service to companies in China, Eastern Europe, or India. English language proficiency, lower wages in India, and large pools of talented software programmers now enable IBM to employ an estimated 100,000 people in its global delivery centers in Bangalore, Delhi, or Kolkata to serve the needs of clients in Atlanta, Munich, or Melbourne.19 Instead of using one international division to manage everything outside the home country, large corporations are now using matrix structures in which product units are interwoven with country or regional units. Today, international assignments are considered key for anyone interested in reaching top management.

As more industries become global, strategic management is becoming an increasingly important way to keep track of international developments and position a company for long term competitive advantage. For example, General Electric moved a major research and development lab for its medical systems division from Japan to China to learn more about developing new products for developing economies. Microsoft's largest research center outside Redmond, Washington, is in Beijing. The formation of regional trade associations and agreements, such as the European Union, NAFTA, Mercosur, Andean Community, CAFTA, and ASEAN, is changing how international business is being conducted. See the Global Issue feature to learn how regional trade associations are forcing corporations to establish a manufacturing presence wherever they wish to market goods or else face significant tariffs. These associations have led to the increasing harmonization of standards so that products can more easily be sold and moved across national boundaries. International considerations have led to the strategic alliance between British Airways and American Airlines and to the acquisition of the Anheuser-Busch Companies by the Belgium company InBev, creating AB InBev, among others.

Impact of Innovation

Innovation, as the term is used in business, is meant to describe new products, services, methods and organizational approaches that allow the business to achieve extraordinary returns. Innovation has become such an important part of business that *Bloomberg Businessweek* has a weekly section of articles on the topic. A 2012 survey of more than 160 CEOs in the United States administered by consulting group PWC found that CEOs expected the following areas of change in their innovation portfolios:

- New Business Models—56%
- New Products/Services—72%
- Significant Changes to Existing Products/Services—57%
- Cost Reductions for Existing Processes—6%

Innovation is the machine that generates business opportunities in the market; however, it is the implementation of potential innovations that truly drives businesses to be remarkable. While there is a value in being a first mover, there is also a tremendous value in being a second or third mover with the right implementation. PC tablets had been developed and even sold almost two decades before the iPad stormed

the market. Many people forget that Apple released the Newton tablet back in 1992. Not only was the timing not right, but the product was not promoted in a way that consumers felt a compelling need to buy one. Many elements have to come together for an innovation to bring long-term success to a company.

Impact of Sustainability

Sustainability refers to the use of business practices to manage the triple bottom line as was discussed earlier. That triple bottom line involves (1) the management of traditional profit/loss; (2) the management of the company's social responsibility; and (3) the management of its environmental responsibility.

The company has a relatively obvious long-term responsibility to the shareholders of the organization. That means that the company has to be able to thrive despite changes in the industry, society, and the physical environment. This is the focus of much of this textbook and the focus of strategy in business.

The company that pursues a sustainable approach to business has a responsibility to its employees, its customers, and the community in which it operates. Companies that have embraced sustainable practices have seen dramatic increases in risk mitigation and innovation, and an overall feeling of corporate social responsibility. A 2010 research study out of the University of Notre Dame found that employees at companies who focused on business sustainability report higher levels of engagement, high-quality connections, and more creative involvement.22 In fact, a Gallop research study found that these engaged organizations had 3.9 times the earnings per share (EPS) growth rates when compared to organizations with lower engagement in the same industry.

The company also has a responsibility to treat the environment well. This is usually defined as trying to achieve (or approach) zero impact on the environment. Recycling, increased use of renewable resources, reduction of waste, and refitting buildings to reduce their impact on the environment, among many other techniques, are included in this element of the triple bottom line. The most recognized worldwide standard for environmental efficiency is the ISO 14001 designation. It is not a set of standards, but a framework of activities aimed at effective environmental management.

South American countries are also working to harmonize their trading relationships with each other and to form trade associations. The establishment of the **Mercosur** (**Mercosul** in Portuguese) free-trade area among Argentina, Brazil, Uruguay, and Venezuela means that a manufacturing presence within these countries is becoming essential to avoid tariffs for nonmember countries. Paraguay was an original member but is currently suspended following the hasty impeachment of its President Fernando Lugo. The **Andean Community** (Comunidad Andina de Naciones) is a free-trade alliance composed of Columbia, Ecuador, Peru, and Bolivia. On May 23, 2008, the **Union of South American Nations** was formed to unite the two existing free-trade areas with a secretariat in Ecuador and a parliament in Bolivia. It consists of 12 South American countries.

In 2004, the five Central American countries of El Salvador, Guatemala, Honduras, Nicaragua, and Costa Rica, plus the United States, signed the **Central American Free Trade Agreement (CAFTA).** The Dominican Republic joined soon thereafter. Previously, Central American textile manufacturers had to pay import duties of 18%–28% to sell their clothes in the United States unless they bought their raw material from U.S. companies. Under CAFTA, members can buy raw material from anywhere, and their exports are duty free. In addition, CAFTA eliminated import duties on 80% of U.S. goods exported to the region, with theremaining tariffs being phased out over 10 years.

The **Association of Southeast Asian Nations (ASEAN)**—composed of Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Vietnam—is in the process of linking its members into a borderless economic zone by 2020. Tariffs had been significantly reduced among member countries by 2008 and a new agreement is expected by early 2013. Increasingly referred to as

ASEAN+3, ASEAN now includes China, Japan, and South Korea in its annual summit meetings. The ASEAN nations negotiated linkage of the ASEAN Free Trade Area (AFTA) with the existing free-trade area of Australia and New Zealand. With the EU extending eastward and NAFTA extending southward to someday connect with CAFTAand the Union of South American Nations, pressure is building on the independent Asian nations to join ASEAN.

Porter and Reinhardt warn that “in addition to understanding its emissions costs, every firm needs to evaluate its vulnerability to climate-related effects such as regional shifts in the availability of energy and water, the reliability of infrastructures and supply chains, and the prevalence of infectious diseases.” Swiss Re, the world’s second-largest reinsurer, estimated that the overall economic costs of climate catastrophes related to climate change threatens to double to US$150 billion per year by 2014. The insurance industry’s share of this loss would be US$30–$40 billion annually. Although global warming remains a controversial topic, the best argument in favor of working toward environmental sustainability is a variation of Pascal’s Wager on the existence of God.

Theories of Organizational Adaptation

Globalization, innovation, and sustainability present real challenges to the strategic management of businesses. How can any one company keep track of all the changing technological, economic, political–legal, and sociocultural trends around the world in order to make the necessary adjustments? This is not an easy task. Various theories have been proposed to account for how organizations obtain fit with their environment and how these approaches have been used to varying degrees by researchers trying to understand firm performance. The theory of **population ecology** suggests that once an organization is successfully established in a particular environmental niche, it is unable to adapt to changing conditions. Inertia prevents the organization from changing in any significant manner. The company is thus replaced (is bought out or goes bankrupt) by other organizations more suited to the new environment. Although it is a popular theory in sociology, research fails to support the arguments of population ecology. **Institution theory,** in contrast, proposes that organizations can and do adapt to changing conditions by imitating other successful organizations. To its credit, many examples can be found of companies that have adapted to changing circumstances by imitating an admired firm’s strategies and management techniques. The theory does not, however, explain how or by whom successful new strategies are developed in the first place. The **strategic choice perspective** goes one step further by proposing that not only do organizations adapt to a changing environment, but they also have the opportunity and power to reshape their environment. This perspective is supported by research indicating that the decisions of a firm’s management have at least as great an impact on firm performance as overall industry factors.30 Because of its emphasis on managers making rational strategic decisions, the strategic choice perspective is the dominant one taken in strategic management. Its argument that adaptation is a dynamic process fits with the view of **organizational learning theory,** which says that an organization adjusts defensively to a changing environment and uses knowledge offensively to improve the fit between itself and its environment. This perspective expands the strategic choice perspective to include people at all levels becoming involved in providing input into trategic decisions.

In agreement with the concepts of organizational learning theory, an increasing number of companies are realizing that they must shift from a vertically organized, topdown type of organization to a more horizontally managed, interactive organization. They are attempting to adapt more quickly to changing conditions by becoming “learning organizations.”

Creating a Learning Organization

Strategic management has now evolved to the point that its primary value is in helping an organization operate successfully in a dynamic, complex environment. To be competitive in dynamic environments, corporations are becoming less bureaucratic and more flexible. In stable environments such as those that existed in years past, a competitive strategy simply involved defining a competitive position and then defending it. As it takes less and less time for one product or technology to replace another, companies are finding that there is no such thing as a permanent competitive advantage. Many agree with Richard D'Aveni, who says in his book *Hypercompetition* that any sustainable competitive advantage lies not in doggedly following a centrally managed five-year plan but in stringing together a series of strategic short-term thrusts (as Apple does by cutting into the sales of its own offerings with periodic introductions of new products). This means that corporations must develop *strategic flexibility*—the ability to shift from one dominant strategy to another Strategic flexibility demands a long-term commitment to the development and nurturing of critical resources. It also demands that the company become a **learning organization**— an organization skilled at creating, acquiring, and transferring knowledge and at modifying its behavior to reflect new knowledge and insights. Organizational learning is a critical component of competitiveness in a dynamic environment. It is particularly important to innovation and new product development.34 Siemens, a major electronics company, created a global knowledge-sharing network, called ShareNet, in order to quickly spread information technology throughout the firm. Based on its experience with ShareNet, Siemens established People ShareNet, a system that serves as a virtual expert marketplace for facilitating the creation of cross-cultural teams composed of members with specific knowledge and competencies. Learning organizations are skilled at four main activities:

Solving problems systematically

- Experimenting with new approaches
- Learning from their own experiences and past history as well as from the experiences of others
- Transferring knowledge quickly and efficiently throughout the organization

Business historian Alfred Chandler proposes that high-technology industries are defined by "paths of learning" in which organizational strengths derive from learned capabilities. According to Chandler, companies spring from an individual entrepreneur's knowledge, which then evolves into organizational knowledge. This organizational knowledge is composed of three basic strengths: technical skills, mainly in research; functional knowledge, such as production and marketing; and managerial expertise. This knowledge leads to new businesses where the company can succeed and creates an entry barrier to new competitors. Chandler points out that once a corporation has built its learning base to the point where it has become a core company in its industry, entrepreneurial startups are rarely able to successfully enter. Thus, organizational knowledge becomes a competitive advantage that is difficult to understand and imitate. Strategic management is essential for learning organizations to avoid stagnation through continuous self-examination and experimentation. People at all levels, not just top management, participate in strategic management—helping to scan the environment for critical information, suggesting changes to strategies and programs to take advantage of environmental shifts, and working with others to continuously improve work methods, procedures, and evaluation techniques. The Toyota production system is famous for empowering employees to improve. If an employee spots a problem on the line, he/she pulls the andon cord, which immediately starts a speedy diagnosis. The line continues if the problem can be solved within one minute. If not, the production line is shut down until the problem is solved. At Toyota, they learn from their mistakes as much as they learn from their successes. Improvements are sent to all factories worldwide.

Organizations that are willing to experiment and are able to learn from their experiences are more successful than those that are not. This was seen in a study of U.S. manufacturers of diagnostic imaging equipment, the most successful firms were those that improved products sold in the United States by incorporating some of

what they had learned from their manufacturing and sales experiences in other nations. The less successful firms used the foreign operations primarily as sales outlets, not as important sources of technical knowledge. Research also reveals that multidivisional corporations that establish ways to transfer knowledge across divisions are more innovative than other diversified corporations that do not.

Environmental Scanning

Environmental scanning is the monitoring, evaluating, and disseminating of information from the external and internal environments to key people within the corporation. Its purpose is to identify **strategic factors**—those external and internal elements that will assist in the analysis in deciding the strategic decisions of the corporation. The simplest way to conduct environmental scanning is through **SWOT analysis.** SWOT is an acronym used to describe the particular **S**trengths, **W**eaknesses, **O**pportunities, and **T**hreats that are strategic factors for a specific company. The **external environment** consists of variables (**O**pportunities and **T**hreats) that are outside the organization and not typically within the short-run control of top management. These variables form the context within which the corporation exists. **Figure** depicts key environmental variables. They may be general forces and trends within the natural or societal environments or specific factors that operate within an organization's specific task environment—often called its *industry*. used to describe the particular **S**trengths, **W**eaknesses, **O**pportunities, and **T**hreats that are strategic factors for a specific company. The **external environment** consists of variables (**O**pportunities and **T**hreats) that are outside the organization and not typically within the short-run control of top management. These variables form the context within which the corporation exists. **Figure** depicts key environmental variables. They may be general forces and trends within the natural or societal environments or specific factors that operate within an organization's specific task environment—often called its *industry*. The **internal environment** of a corporation consists of variables (**S**trengths and **W**eaknesses) that are within the organization itself and are not usually within the short-run control of top management. These variables form the context in which work is done. They include the corporation's structure, culture, and resources. Key strengths form a set of core competencies that the corporation can use to gain competitive advantage. While strategic management is fundamentally concerned with strengths, weaknesses, opportunities, and threats, the methods to analyze each has developed substantially in the past two decades. No longer do we simply list the SWOT variables and have employees try to populate the quadrants. Each of the four is rich with processes and techniques that will allow for a robust and sophisticated understanding of the company.

Strategy Formulation

Strategy formulation is the process of investigation, analysis, and decision making that provides the company with the criteria for attaining a competitive advantage. It includes defining the competitive advantages of the business (Strategy), crafting the corporate mission, specifying achievable objectives, and setting policy guidelines. An organization's **mission** is the purpose or reason for the organization's existence. It announces what the company is providing to society—either a service such as consulting or a product such as automobiles. A well-conceived mission statement defines the fundamental, unique purpose that sets a company apart from other firms of its type and identifies the scope or domain of the company's operations in terms of products (including services) offered. Research reveals that firms with mission statements containing explicit descriptions of customers served and technologies used have significantly higher growth than firms without such statements. A mission statement may also include the firm's values and philosophy about how it does business and treats its employees; however, that is usually better kept as a separate document. It can put into words not only what the company is now but what it wants to become—management's strategic vision of the firm's future. The mission statement promotes a sense of shared expectations in employees and communicates a public image to important stakeholder groups in the

company's task environment. Some people like to consider vision and mission as two different concepts: Mission describes what the organization is now; **vision** describes what the organization would like to become. We prefer to combine these ideas into a single mission statement. A classic example is that etched in bronze at Newport News Shipbuilding, unchanged since its founding in 1886:

We shall build good ships here—at a profit if we can—at a loss if we must—but always good ships.

A mission may be defined narrowly or broadly in scope. An example of a *broad* mission statement is that used by many corporations: "Serve the best interests of shareowners, customers, and employees." A broadly defined mission statement such as this keeps the company from restricting itself to one field or product line, but it fails to clearly identify either what it makes or which products/markets it plans to emphasize. Because this broad statement is so general, a *narrow* mission statement, such as the preceding example by Newport News Shipbuilding, is significantly more useful. A narrow mission very clearly states the organization's primary business and will limit the scope of the firm's activities in terms of the product or service offered, the technology used, and probably the market served.

Objectives: Listing Expected Results

Objectives are the end results of planned activity. They should be stated as *action verbs* and tell what is to be accomplished by when and quantified if possible. The achievement of corporate objectives should result in the fulfillment of a corporation's mission. In effect, this is what society gives back to the corporation when the corporation does a good job of fulfilling its mission. Coca-Cola has set the standard of a focused, international company. In their new Vision 2020 plan, they have laid out specific objectives including reducing the overall carbon footprint of their business operations by 15% by 2020, as compared to the 2007 baseline, and reducing the impact of their packaging by maximizing their use of renewable, reusable, and recyclable resources to recover the equivalent of 100% of their packaging. This type of focus has made Coca-Cola a perennial member of the Fortune 500, one of the Fortune 50 Most Admired Companies, one of Barron's Most Respected Companies in the World and a Diversity, Inc. Top 50 company. Over the past 10 years they have raised their dividend an average of 9.8% per year and the company's earnings per share have jumped 11.3% per year over the past 5 years.46

The term *goal* is often used interchangeably with the term objective. In this book, we prefer to differentiate the two terms. In contrast to an objective, we consider a *goal* as an open-ended statement of what one wants to accomplish, with no quantification of what is to be achieved and no time criteria for completion. For example, a simple statement of "increased profitability" is thus a goal, not an objective, because it does not state how much profit the firm wants to make the next year. A good objective should be action-oriented and begin with the word *to*. An example of an objective is "to increase the firm's profitability in 2014 by 10% over 2013."

Some of the areas in which a corporation might establish its goals and objectives are:

- Profitability (net profits)
- Efficiency (low costs, etc.)
- Growth (increase in total assets, sales, etc.)
- Shareholder wealth (dividends plus stock price appreciation)
- Utilization of resources (ROE or ROI)
- Reputation (being considered a "top" firm)
- Contributions to employees (employment security, wages, diversity)
- Contributions to society (taxes paid, participation in charities, providing a needed product or service)
- Market leadership (market share)
- Technological leadership (innovations, creativity)
- Survival (avoiding bankruptcy)
- Personal needs of top management (using the firm for personal purposes, such as providing jobs for relatives)

Strategy: Defining the Competitive Advantages

An organization must examine the external environment in order to determine who constitutes the perfect customer for the business as it exists today, who the most direct competitors are for that customer, what the company does that is necessary to compete and what the company does that truly sets it apart from its competitors. These elements can be rephrased into the strengths of the business, the understanding of its weaknesses relative to its competitors, what opportunities would be most prudent, and what threats might affect the business's primary competitive advantages.

A **strategy** of a corporation forms a comprehensive master approach that states how the corporation will achieve its mission and objectives. It maximizes competitive advantage and minimizes competitive disadvantage. Pfizer, the giant drug company has embraced the need for this type of approach. Faced with the rapid fall-off of its biggest blockbuster drugs (patents expiring), Pfizer was faced with the question of how to generate the R&D to create new drugs. Historically, the company had relied upon its cadre of scientists, but this changed in the past few years. Pfizer plans to have 50 drug development projects running with university research centers by 2015. They opened their first one in 2010. This is the crucial new ground from which they hope to replace such blockbusters as Lipitor, which expects to see sales drop by more than 80% (from US$12 billion in 2012) when the patent expired. The typical business firm usually considers three types of strategy: corporate, business, and functional.

1. **Corporate strategy** describes a company's overall direction in terms of its general attitude toward growth and the management of its various businesses and product lines. Corporate strategies typically fit within the three main categories of stability, growth, and retrenchment.

2. **Business strategy** usually occurs at the business unit or product level, and it emphasizes improvement of the competitive position of a corporation's products or services in the specific industry or market segment served by that business unit. Business strategies may fit within the two overall categories: *competitive* and *cooperative* strategies. For example, Staples, the U.S. office supply store chain, has used a competitive strategy to differentiate its retail stores from its competitors by adding services to its stores, such as copying, UPS shipping, and hiring mobile technicians who can fix computers and install networks. British Airways has followed a cooperative strategy by forming an alliance with American Airlines in order to provide global s ervice. Cooperative strategy may thus be used to provide a competitive advantage. Intel, a manufacturer of computer microprocessors, uses its alliance (cooperative strategy) with Microsoft to differentiate itself (competitive strategy) from AMD, its primary competitor.

3. **Functional strategy** is the approach taken by a functional area to achieve corporate and business unit objectives and strategies by maximizing resource productivity. It is concerned with developing and nurturing a distinctive competence to provide a company or business unit with a competitive advantage. Examples of research and development(R&D) functional strategies are technological followership (imitation of the products of other companies) and technological leadership (pioneering an innovation). For years, Magic Chef had been a successful appliance maker by spending little on R&D but by quickly imitating the innovations of other competitors. This helped the company keep its costs lower than those of its competitors and consequently to compete with lower prices. In terms of marketing functional strategies, Procter & Gamble (P&G) is a master of marketing "pull"—the process of spending huge amounts on advertising in order to create customer demand. This supports P&G's competitive strategy of differentiating its products from those of its competitors.

Business firms use all three types of strategy simultaneously. A **hierarchy of strategy** is a grouping of strategy types by level in the organization. Hierarchy of strategy is a nesting of one strategy within another so that they complement and support one another. (See **Figure 1–4.**) Functional strategies support business strategies, which, in turn, support the corporate strategy(ies).

Policies: Setting Guidelines

A **policy** is a broad guideline for decision making that links the formulation of a strategy with its implementation. Companies use policies to make sure that employees throughout the firm make decisions and take actions that support the corporation's mission, objectives, and strategies. For example, when Cisco decided on a strategy of growth through acquisitions, it established a policy to consider only companies with no more than 75 employees, 75% of whom were engineers.48 Consider the following company policies:

- **3M:** 3M says researchers should spend 15% of their time working on something other than their primary project. (This supports 3M's strong product development strategy.)
- **Google:** Google's health care plan includes their onsite medical staff. Any employee who feels ill at work can make an appointment with the doctor at the Googleplex. This supportsthe Google HRM functional strategy to support its employees.
- **General Electric:** GE must be number one or two wherever it competes. (This supports GE's objective to be number one in market capitalization.)
- **Starbucks:** All Starbucks employees are offered a Total Pay Package that includes a 401(k) savings plan, stock options, and an employee stock purchase plan. This goes a long way toward their goal of having every employee feel like a partner in the business.
- **Ryanair:** Ryanair charges for everything a passenger might want or need on a flight. The only thing you get with your ticket is the right to a seat on the plane (and that seat depends upon how fast you can run to the plane).