Globalisation/International Business

- **Globalisation**
  - Recent Progression
    - Value of world exports tripled between 1980 and 2000.
    - Foreign investment grew x20
  - Motives
    - Cultural
  - Pros & Cons
    - **Cost**
- **International Business** - business activities that involve the transfer of resources, goods, services knowledge, skills or information across national boundaries
  - Factors → International vs Domestic Business
    - Environmental Dynamics
      - Currency, inflation, interest rates, accounting practices, cultures, social customs, laws, political stability
    - Operational Nature
      - Communication, coordination, motivation, differences in organizational principles and management philosophies
  - Motives 4 expansion
    - **Economic** Motive
      - Increase return through higher revenues and/or lower costs.
      - Enables the company to benefit from the differences in:
        - Costs of labours
        - Natural resources
        - Differences in regulatory treatment
    - **Strategic** Motive
      - Capitalise on resources or capabilities already developed at home
      - Be the first mover in a target foreign market
      - Benefit from vertical integration involving different countries
      - Follow the company's major customers abroad
    - **Market** Motive
      - Offensive- seize market opportunities in foreign countries through trade or investment.
      - Defensive- to protect and hold a firm's market power or position in the face of threats from domestic rivalry or changes in government policy.
        - Asset Acquisition Motivation - When 1 MNC agrees to purchase the assets (e.g. property, buildings, and equipment) of a second corporation (TATA --> Land Rover --> helps them go international quicker)

– All companies have 2 pressures:
  - Making a profit --> financial objective
  - Making a profit and being a good/ethical company at the same time

Resource-Based View → IBM

- Resource-Based View - how individual firms differ from each other within an industry and can outperform the industry average consistently/significantly.
        - Analysing/identifying a firm's strategic advantages based on its combination of assets/skills/capabilities/intangibles
    - Features of Competitive Advantage:
        - Superior quality, efficiency, innovation, and customer service
    - Core Competencies - KBFs that orgs can do as well as or better than any other org in the world
    - **Implication for Strategy:**
        - Why do firms differ? – Resource heterogeneity → every firm is unique in its bundle of resources/capabilities
        - How do firms behave? –how they take advantage of their strengths embodied in resources/capabilities + overcome their weaknesses.
        - What determines the scope of the firm? – firm is determined by performance of different value-adding activities relative to rivals.
- **VRIO Framework** (**V**alue, **R**arity, **I**mitability and **O**rganisational) - matrix analysis of resources/capabilities of a firm + the difficulty of their replication
    - 2 Key Assumptions → sustainable competitive adv.
        - **Resource heterogeneity** - Each firm has a unique combo of resources /capabilities such that no 2 firms are twins
        - **Resource immobility** - Resources/capabilities unique to one firm cannot easily migrate to competing firms.
    - Question of Value
        - Only value-adding resources can lead to competitive advantage, whereas non-value-adding capabilities may lead to competitive disadvantage.
        - The search for valuable resources/capabilities is a never-ending challenge.
    - Question of Rarity
        - Valuable common resources and capabilities can lead to competitive parity but no advantage
        - Valuable rare resources and capabilities can provide, at best, temporary competitive advantage.
    - Question of Imitability
        - Valuable and rare resources and capabilities are a source of competitive advantage only if competitors have a difficult time imitating them
        - Imitation of intangible resources (knowledge, managerial talents, and organizational culture) is much more difficult.
    - Question of Organization
        - How is a firm organized to develop and leverage the full potential of its resources and capabilities?
- Resources + Capabilities
    - Tangible
        - **Financial -** Ability to generate internal funds
        - **Physical -** Plants/offices/equipment & access to raw materials/distribution channels
        - **Technological -** Patents/Trademarks/Copyright
        - **Organisational -** Formal planning, command, and control systems
    - Intangible
        - **Human** - Knowledge/trust/managerial talent

        - **Innovation** - Supportive atmosphere for new ideas/R&D
        - **Reputational** - Perception of product reliability/durability/ quality
            - Reputation = a socially responsible corporate citizen

- **IBM → VRIO Framework**
    - **Value**
        - Intangible innovative (R&D and organisational change) and human capabilities (trust, global leadership, knowledge) + tangible organisational resources (planning, command, control systems)
        - Success: invention of automated teller machine (ATM), hard drive, floppy disk etc. Most successful IT firms.
    - **Rarity**: <u>1993 Crisis</u>
        - Company nearly turned over → lack of execution (important for strategy)
        - IBM Business leadership Model → Lou Gerstner dynamically reshaped business → success
        - *strategic insight* (strategic intent, marketplace insight, innovation focus, and business design) designed to systematically identify opportunities
    - **Imitability**: Other great technical companies (Nokia, Xerox, Philips, and Polaroid) failed to leverage the intellectual capital IBM had to reshape business model in a rapidly evolutionary industry.
    - **Organisation:**
        - IBM Business leadership model:
        - *strategic execution* (alignment of people, structure, culture, and process) designed to seize opportunities by ensuring that every strategic initiative also had an associated plan for execution.
    - *Success*: Sales of $100 billion + ranked as 2nd largest publicly traded company worldwide behind Apple (2011).

Institution → Pharmaceutical Companies

- **Institutions** (rules and norms that define social behaviour)
    - "Regulatory, normative and cognitive structures (pillars) provide stability and meaning to social behaviour" (Scott, 1995)
        - <u>Regulatory</u>: Coercive power of the government through rules/regulation
        - <u>Normative</u>: Values/beliefs/norms of other relevant organizations
        - <u>Cognitive</u>: Internalized and taken for granted values/beliefs that guide firm behaviour
    - Organizations conform to these pillars to gain legitimacy + obtain support from external environment
    - <u>What do institutions do?</u>
        - Institutions affect the strategy of firms by reducing uncertainty + signalling conduct as acceptable or not → constrains the range of acceptable actions.
        - Uncertainty can → transactions costs (costs associated w economic transactions/costs of doing business)
    - Informal Institutions
        - Constraints on socially sanctioned norms of behaviour → 'unwritten' rules
        - Professional norms do not have the force of law but are obeyed by those in a profession.
            - E.g. physicians, professors, lawyers, accountants → if they don't follow the 'rules' of their profession, reputation is ruined

- *If formal constraints fail, informal constraints play a larger role in reducing uncertainty* → important during institutional transitions
  - "Transition economies"- a subset of EEs e.g. China, Russia, Poland (from communism → capitalism)
  - Importance of *guanxi* and *blat* during China + Russia's recent institutional transitions
    - **Guanxi** → Chinese term → "networks" or "connections" that open doors for new business and facilitate deals. A person who has a lot of guanxi will be in a better position to generate business than someone who lacks it.
    - **Blat** → Russian colloquial → practices are associated with sociability, i.e. the use of personal contacts or networks, but also serve an instrumental purpose of gaining influence or accessing limited resources, or pulling strings for a favour.

- Formal Institutions
  - Expensive legal/regulatory framework of courts, police, lawyers, regulators, etc. that enforce laws/regulations to facilitate the widening of markets
  - Benefits of formal institutions:
    - Bring distant parties (strangers) together.
    - Foster rule-based transactions that attract new players into a global economy → economic expansion and growth
- *Institutions directly impact a firm's formulation and implementation of strategy*
- Core Principles of Institution-Based View
  - **1)** Managers and firms rationally pursue their interests and make strategic choices within institutional constraints
    - Lax enforcement of, patents {exclusive rights to manufacture}, copyrights {right to decide who can publish or disperse intellectual good e.g. music} and trademarks. {e.g Levi's}
  - Without stable institutional frameworks transaction costs may be high →investment is severely limited without an effective system of property rights

– Pharmaceutical Industry → Strong vs Weak Formal Institutions
  - Pharmaceutical Industry events the most into R&D out of any industry
    - Europe + US benefit from strong protection laws + abundant investment capital
    - Takes 12-15 years + >$1bill in R&D to successfully bring new drug to market
    - 3/10 new + approved compounds successfully recover R&D costs
    - As such, firms must charge high enough prices to recover their losses + profit
  - Intellectual Property (IP)- Protection property rights is a key objective o legal system
    - IP is weak in developing countries → India has weak IP protection → discouragement of R&D + innovation
  - India's Pharmaceutical Corruption
    - India = large history of counterfeit medication through violated drug patents of foreign pharmaceutical firms

        - Illicit laboratories in India infringed on drug patents + engaged in a selling free-for-all in Indian market
        - Reversed engineered patented compounds of developed companies, sold pirated generics at drastically lower prices
    - Counterfeit Drug Busts
        - China Company- supplied 1mill fake OneTouch Test Strips (4 diabetes) to hundreds of pharmacies in Canada, US , etc.
        - Niger- 2500 people died after receiving fake meningitis vaccines
        - Counterfeit drug sales = $500 bill. Annually
        - CHINA- 200,000 ppl die annually from counterfeit medicine
- **Big Pharma** (includes Merck, Eli Lilly, Bristol-Myers, and Pfizer of the United States; GlaxoSmithKline (GSK) and Wellcome of Britain; and Hoffman La Roche, Ciba Geigy, Novartis, and Sandoz of Switzerland)
    - Relentless drive for (R&D) → typically ranks the most profitable industry in the world.
- US government helps make sure that Big Pharma reap huge profits.
    - Food and Drug Administration (FDA) significantly heighten the entry barriers → extremely stringent drug approval requirements
    - Allows only "big pharmas" to compete → cheaper drugs aren't allowed to be imported
    - Due to institutional effect, Americans often pay double what Canadians + Europeans pay for the *same* drugs → Americans spending approximately $240 billion a year on drugs, more than Britain, Canada, France, Germany, Italy, and Japan *combined*.
- Firms argue that their wellspring of innova- tion will run dry if their patents are not protected by government

International Entry Strategy I & II → Volkswagen & General Motors

- **Going Abroad**
    - Positives (SEE GLOBALISATION)
    - Negatives
        - *Liability of Foreignness* (LOF)- inherent disadvantage foreign firms experience in host countries because of their non-native status.
        - Liability occurs in 2 dimensions:
            - Differences in formal/informal institutions in different countries (e.g., regulatory, language, and cultural differences).
            - Failure to recognize these rules may cost foreign firms.
            - Customers formally/informally discriminate against foreign firms
    - *NOTE – most firms **overestimate** why they should go abroad and **underestimate** why they shouldn't go abroad.*
        - Prematurely venturing overseas could be detrimental 4 smaller firms w a small margin for error
    - Success Factors → overcoming LOF (See Globalisation Pro's)
    - Determining firm internationalisation
- **Where - Location Choice**
    - Factors determining [**where** to enter] (country + location w/in country):
        - Cost/Tax Factors - transportation, wage, availability of land, construction cost, materials cost, financing costs, tax rates, etc.
        - Demand Factors - market size/growth, customer presence, local comp.

        - Strategic Factors - Investment infrastructure, industrial concentration, supply/distribution linkages, workforce productivity
        - Regulatory/Eco. Factors - Industrial policies, FDI policies, availability of economic zones
        - Socio-political Factors - political risk/instability, cultural barriers, local practices, government efficiency and corruption, pollution control
            - Not only must ^ factors be considered → strategic objectives, global integration, and market orientation objectives must also be met
            - Strategic Objectives – growth & competitive factors
            - Integration Factors – access to trading blocs + integrated ecos.
            - Market Orientation – if primary target markets are available @ host location
    - Distances
        - Cultural Distance
            - difference between 2 cultures along identifiable dimensions (e.g. power distance)
        - Institutional Distance
            - (Dis)similarity between regulatory/normative/cognitive institutions of 2 countries
            - Colony-coloniser links boost trade by 900%
    - Location-specific advantage
        - Enter a location that has the most of your target market/matches your positioning strategy (e.g. top-down) → Tier 1 buyers → Tier 1 city
        - Clustering of eco. activities (agglomeration) – industry related.
            - Knowledge spillover among closely located firms that attempt to hire individuals from competitors.
            - Regional skilled labour force available to work for different firms.
            - Regional pool of specialized suppliers and buyers
    - Strategic Goals & Locations
        - Natural resource seeking → oil - middle east/Russia | bananas - Caribbean
        - Market Seeking → seafood – Japan | soft drinks - Mexico
        - Efficiency Seeking (Ecos of Scale) → manufacturing – China | IT - India
        - Innovation Seeking → financial services – London/NY | chemicals – Germany
- [**When**] International Entry timing
        - IMPORTANT - determines the risks & potential returns from investment.
    - Early Movers…
        - Advantages - market power, more pre-emptive opportunities, and strategic advantages over late movers.
        - Disadvantages – environmental/operational risks from host government, underdeveloped investment laws/regulations, protectionism, shortages of workers, uncertain foreign exchange, unstable market structures.
- [**What**] Internationalising Functions
    - Infrastructure → R&D
    - Logistics → Components / final assembly
    - HR → marketing and service
- [**How**] Entry Mode Selection
        - Can be trade related/transfer related/FDI related

- Trade-related:
  - Countertrade
  - Subcontracting
  - **Export** – Only available choice for small/new firms wanting to go overseas → easy access → minimum investment
    - Direct: Ecos of Scale, better control over distribution
    - Indirect: Concentration of resources on production, no need to handle export processes
- Transfer-related
  - BOT
  - **Franchising** – arrangement with franchisor allowing franchisee to operate an enterprise using its trademark/logo etc. in return for a fee
    - Common in fast-food & hotel/motel industries
    - Minor adjustments for the local market → results in highly profitable IB
  - **Licensing** – Agreement allowing 1 party to use IP in exchange for payment to other party
    - By licensing a firm already 'there' → avoid entry costs
    - Small firm that lacks financial/managerial resources
    - Spend very little on R&D
  - Leasing
- FDI-related:
  - Umbrella Company
  - **Wholly owned subsidiary** – overseas operation totally owned/controlled by an MNC
    - Managerial efficiency is better w/out outside partners
    - Host countries r concerned MNC will drive out local firms
    - Most MNCs opt for a merger, alliance, or JV rather than WOS
  - **JV** – agreement between 2+ partners from different countries owning a buss.
    - Improvement of efficiency, access to knowledge, political factors

– **Volkswagen & General Motors → First Mover vs Late Mover**
- Volkswagen – Early Mover
  - Volkswagen (VW), a first mover to China, has dominated the passenger car market through their proactive approach, despite potential risks.
  - 1984: VW entered a 50/50 JV with Shanghai Automotive Industrial Corporation (SAIC) to produce the Santana model → distinguished itself as China's first mass-produced modern passenger car.
    - Success: VW established a solid market position, enjoying significant first mover advantages (market share - > 70% for passenger cars
- Competition
  - However, by the late 1990s, the market became a more competitive buyer's market → VW's passenger car market share in China dropped to 39% (2004).
- GM – Late Mover/Follower

- 1995: GM signed a 50/50 JV agreement with SAIC in China → constructed a greenfield plant in Shanghai → produced 100,000 sedans per year → produced two Buick models modified for China.
  - **Success**: GMs superior global branding remained present in transition to China → didn't have to spend $4,000 per vehicle in incentives to lure new buyers → made $437 million in profits in 2003, selling just 386,000 cars.
- Future: GM operated six JVs and two wholly owned foreign enterprises in China → positioning of #1 in the Chinese automobile market over VW (2005)

- Conclusions
  - First mover holds potential for competitive advantage in some cases but not in others
  - Being a fast follower can sometimes yield as good a result as being a first mover