MSL 686
Strategic Leadership
Belhaven University

Unit 7

- International Strategy

Introduction to Unit 7

- Unit 7 examines opportunities facing firms as they seek to develop technological innovation and exploit core competencies by diversifying into global markets. A business that plans to operate globally must formulate a successful strategy to take advantage of these global opportunities. Furthermore, to mold their firms into truly global companies, managers must develop global mind-sets.

Unit 7 Topics

1. Incentives that influence international strategy
2. Three basic benefits from international strategy
3. Determinants of national advantage
4. Three international corporate-level strategies
5. Environmental trends affecting international strategies
6. Five modes for international markets
7. Two major risks of using international strategies
8. Strategic competitiveness outcomes
9. Two important issues for international strategies

Unit 7 Objectives

- Understand International Strategy
- Understand Incentives to use international strategy
  - New market expansion extends product life cycle
  - Gain access to materials and resources
  - Integration of operations on a global scale
  - Better use of rapidly developing technologies
  - International markets yield potential new opportunities

Biblical Foundation Unit 7

- 1 Corinthians 14:40—planning decently and in order
- Proverbs 15:22, 27, 31 & 33—using advisers for planning
- Nehemiah 1-5—Long-range planning
- Psalm 146: 3-4—putting your trust in God
- Luke 14:31-32—planning for battle

Biblical Foundation, cont.

- 1 Corinthians 16:5-6, 8-9 Effective leader’s planning
- Luke 14:28-30 Planning for a project
- Isiah 32:7-8 Liberals and plans
- Proverbs 19:21-22 Man’s planning and God’s will
- Proverbs 24:1& 27 Preparing plans

Identifying International Opportunities

- 1. A firm introduces an innovation (new product) in its domestic market.
- 2. Product demand develops in other countries and exports are provided from domestic operations.
- 3. As demand increases, foreign rivals produce the product; then firms justify investing in production abroad.

Identifying International Opportunities, cont.

- 4. As products become standardized, firms relocate production to low-cost countries.
- Some firms implement an international strategy to secure critical resources, such as petroleum reserves (for the oil industry), bauxite (for the manufacture of aluminum), or rubber (for tire manufacturing).

Identifying International Opportunities, cont.

- Increased Market Size
  - Domestic market may lack the size to support efficient scale manufacturing facilities.
- Economies of Scale (or Learning)
  - Expanding size or scope of markets helps to achieve economies of scale in manufacturing as well as marketing, R&D or distribution.
  - Can spread costs over a larger sales base and increase profit per unit

Identifying International Opportunities, cont.

- By expanding the size and scope of their markets, firms may be able to achieve economies of scale in manufacturing (and in other operations, such as marketing, research and development, and distribution) by standardizing products across national borders and spreading fixed costs over a larger sales base.

Identifying International Opportunities, cont.

- Firms may also be able to exploit core competencies in international markets through resource and knowledge sharing between units across country borders. This sharing generates synergy, which helps the firm produce higher-quality goods or services at lower cost. In addition, working across international markets provides the firm with new learning opportunities.

Identifying International Opportunities, cont.

- Location Advantages
  - Low cost markets aid in developing competitive advantage by providing access to:
    - raw materials
    - transportation
    - lower costs for labor
    - key customers
    - energy

International Strategies

- International strategies available to firms are business-level and corporate-level.
- Business-level strategy choices are generic, extending our earlier discussion of cost leadership, differentiation, focus, and integrated cost leadership/differentiation strategies.

International Strategies, cont.

- Corporate-level strategies are dependent on the complexity and scope of product and geographic diversification, and these include multi-domestic, global, and transnational (hybrid) strategies.
- In an international business-level strategy, the home country of operation is often the most important source of competitive advantage.

International Strategies, cont.

- The resources and capabilities established in the home country frequently allow the firm to pursue the strategy into markets located in other countries.
- As a firm continues its growth into multiple international locations, research indicates that the country of origin diminishes in importance as the dominant factor.

International Strategies, cont.

- Four interrelated national or regional factors contribute to the competitive advantage of firms competing in global industries.
- Factor conditions or the factors of production
- Demand conditions
- Related and supporting industries
- Firm strategy, structure, and rivalry

International Strategies, cont.

- Perhaps the most basic factor in the model, ***factor conditions*** or ***factors of production***, refers to the inputs necessary to compete in any industry. These include labor, land, natural resources, capital, and infrastructure (such as highway, postal, and communications systems).

International Strategies, cont.

These factors can be subdivided into four categories:

- 1. Basic factors, such as labor and natural resources
- 2. Advanced factors, including digital communications systems and highly educated work forces

International Strategies, cont.

- 3. Generalized factors (required by all industries), such as highway systems and a supply of capital
- 4. Specialized factors that are most valuable in specific uses (e.g., skilled personnel employed at a port who specialize in the handling of bulk chemicals)

International Strategies, cont.

- The second factor that determines national advantage is ***demand conditions***, which are characterized by the nature and size of buyers’ needs in the home market for the industry’s products or services. The size of the segment can create demand sufficient to justify the construction of scale-efficient facilities.

International Strategies, cont.

- ***Related and supporting industries*** are the third factor of the national advantage model. National firms may be able to develop competitive advantage when industries that provide either materials or components or that support the activities of the primary industry are present.

International Strategies, cont.

- Growth in certain industries is fostered by the fourth factor—***firm strategy, structure, and rivalry***. In Italy, there are strong industries in sports cars, fashion apparel, and furniture.
- In the United States, there is competition among computer manufacturers and software producers.

International Strategies, cont.

- The type of corporate strategy selected will have an impact on the selection and implementation of the business-level strategies.
  - Some strategies provide individual country units with the flexibility to choose their own strategies.
  - Other strategies dictate business-level strategies from the home office and coordinate resource sharing across units.

International Strategies, cont.

There are three types of international corporate level strategies:

- 1. International Corporate-Level Strategies
- 2. Multi-domestic strategy.
- 3. Global strategy (transnational strategy).

A firm should choose its international corporate-level strategy based on the need for both local responsiveness **and** for global integration.

International Strategies, cont.

- When the need for global integration is high and there is little need for local market responsiveness, the firm should adopt a *global strategy*.
- When the need for global integration is low, but there is great need for local market responsiveness, the firm should adopt a *multi-domestic strategy*.

International Strategies, cont.

- When there is a great need for both global integration and local market responsiveness, the firm should adopt a *transnational strategy*.

International Strategies, cont.

The use of **multi-domestic strategies**:

- Usually expands the firm's local market share because the firm can pay attention to the needs of local buyers
- Results in more uncertainty for the corporation as a whole, because of the differences across markets and thus the different strategies employed by local country units

International Strategies, cont.

Multi-domestic strategies, cont.

- Does not allow for the achievement of economies of scale and can be more costly
- Decentralizes a firm's strategic and operating decisions to the business units operating in each country

International Strategies, cont.

- A ***global strategy*** is one where standardized products are offered across country markets and competitive strategy is dictated by the home office. The global strategy:
  - Assumes strategic business units operating in each country are interdependent
  - Attempts to achieve integration across business and national markets, as directed by the home office
  - Coordination across national borders

International Strategies, cont.

- Emphasizes economies of scale
- Offers greater opportunities to use innovations developed by the firm
- May lack responsiveness to local markets. Is difficult to manage because of the need to coordinate strategies and operating decisions across borders
- Requires resource-sharing and an emphasis on coordination across national borders

International Strategies, cont.

- A ***transnational strategy*** is a corporate strategy that seeks to achieve both global efficiency and local (national market) responsiveness.
- It is difficult to achieve because of requirements for both strong central control and coordination to achieve efficiency **and** local flexibility and decentralization to achieve local responsiveness.

International Strategies, cont.

- A transnational strategy mandates building a shared vision and individual commitment through an integrated network to produce a core competence that would result in strategic competitiveness.
- Effective implementation of a transnational strategy often produces higher performance than does implementation of either the multi-domestic or global international corporate-level strategies

Environmental Trends

Implementing a transnational strategy is difficult; however, firms are challenged to do so because of these facts:

- There is an increased emphasis on local requirements, e.g., customization to meet government regulations within particular countries or to fit customer tastes and preferences.

Environmental Trends, cont.

- Most multinational firms desire coordination and sharing of resources across country markets to hold down costs.
- Some products and industries may be more suited than others for standardization across country borders.

Environmental Trends, cont.

- Liability of Foreignness
  - Legitimate concerns about the relative attractiveness of global strategies
  - Global strategies not as prevalent as once thought
  - Difficulty in implementing global strategies
- Regionalization
  - Focusing on particular region(s) rather than on global markets
  - Better understanding of the cultures, legal and social norms

Environmental Trends, cont.

Exporting

- A common—but not necessarily the least costly or most profitable—form of international expansion is for firms to export products from the home country to other markets.
- Exporters have no need to establish operations in other countries.

Environmental Trends, cont.

- Exporters must establish channels of distribution and outlets for their goods, usually by developing contractual relationships with firms in the host country to distribute and sell products.
- However, exporting also has disadvantages:
  - Exporters may have to pay high transportation costs.

Environmental Trends, cont.

- Tariffs may be charged on products imported to the host country.
- Exporters have less control over the marketing and distribution of their products.
- Because of the potentially significant transportation costs and the usually greater similarity of geographic neighbors, firms often export mostly to countries that are closest to its facilities.

Environmental Trends, cont.

- Small businesses are the most likely to use exporting. One of the largest problems with which small businesses must deal is currency exchange rates, a challenge for which only large businesses are likely to have specialists.

Environmental Trends, cont.

Licensing

- Through licensing, a firm authorizes a foreign firm to manufacture and sell its products in a foreign market.
- The licensing firm (licensor) generally is paid a royalty payment on every unit that is produced and sold.
- The licensee invests in manufacturing and paying marketing/distribution costs.

Environmental Trends, cont.

- Licensing is the least costly (and potentially the least risky) form of international expansion because the licensor does not have to make capital investments in the host countries.
- Licensing is a way to expand returns based on previous innovations, even if product life cycles are short.

Environmental Trends, cont.

The potential disadvantages of licensing:

- The licensing firm has little control over manufacture and distribution of its products. Licensing offers the least revenue potential as profits must be shared between licensor and licensee.
- The licensee can learn the firm's technology and, upon license expiration, may create a competing product.

Environmental Trends, cont.

Strategic alliances enable firms to:

- Share the risks and resources required to enter international markets
- Facilitate the development of new core competencies that yield strategic competitiveness

Environmental Trends, cont.

- Most strategic alliances represent ventures between a foreign partner (that provides access to new products and new technology) and a host country partner (that has knowledge of competitive conditions, legal and social norms, and cultural idiosyncrasies that enable the foreign partner to successfully manufacture or develop and market a competitive product or service in the host country market).

Environmental Trends, cont.

Several factors may cause a relationship to sour. Trust between the partners is critical:

- The initial condition of the relationship
- The negotiation process to arrive at an agreement
- Partner interactions
- External events
- The country cultures involved in the alliance or joint venture

Environmental Trends, cont.

Acquisitions

- Cross-border acquisitions have been increasing significantly. Cross-border acquisitions have comprised more than 45 percent of all global acquisitions.
- Acquisitions can provide quick access to a new market. Acquisitions may provide the fastest and largest initial international expansion of any of the alternatives.

Environmental Trends, cont.

International acquisitions also can be quite expensive (because of debt financing) and require difficult and complex negotiations:

- The same disadvantages as domestic acquisitions
- The great expense that often requires debt financing

Environmental Trends, cont.

- The exceedingly complex international negotiations for acquisitions—only about 20 percent of the cross-border bids made lead to a completed acquisition, compared to 40 percent for domestic acquisitions
- Different corporate cultures
- The challenges of merging the new firm into the acquiring firm, which often are more complex than with domestic acquisitions

Environmental Trends, cont.

- Firms that choose to establish new, wholly owned subsidiaries are undertaking a ***greenfield venture***.
- Advantages of a wholly owned subsidiary:
  - Achieving maximum control over the venture
  - Being potentially the most profitable alternative (if successful)
  - Maintaining control over the technology, marketing, and distribution of its products

Environmental Trends, cont.

Establishing a new wholly owned subsidiary is risky for two reasons:

- Has the highest costs of all entry alternatives since a firm must build new manufacturing facilities, establish distribution networks, and learn and implement marketing strategies.
- May have to acquire expertise relevant to the new market, often having to hire host country nationals (in many cases from competitors) and/or costly consultants.

Environmental Trends, cont.

Dynamics of Mode of Entry

- The choice of a market entry strategy is determined by a number of factors. However, initial market development strategies generally are selected to establish a firm's products in the new market.
- *Exporting* does not require foreign manufacturing expertise; it only requires an investment in distribution.

Environmental Trends, cont.

- *Licensing* also can facilitate direct market entry by enabling the firm to learn the technologies required to improve its products in order to achieve success in international markets or to facilitate direct entry.
- *Strategic alliances* are also popular because the firm forms a partnership with a firm that is already established in the new target market and reduces risks by sharing costs with the partner.

Environmental Trends, cont.

- If intellectual property rights in an emerging economy are not well protected, the number of firms in the industry is growing fast, and the need for global integration is high, entry modes such as joint ventures or wholly owned subsidiary are preferred.

Environmental Trends, cont.

The entry mode decision should be based on the following conditions:

- The industry’s competitive conditions
- The target country’s situation
- Government policies
- The firm’s unique set of resources, capabilities, and core competencies

Risks in the International Environment

- Political and economic risks complicate the management of international diversification. One reason is that these risks result in competitive conditions that may differ significantly from what was expected.
- ***Political risks*** are those related to instability in national governments and to war, civil or international.

Risks in the International Environment, cont.

- National government instability creates multiple potential problems: Economic risks come up as governments react to a variety of events, reflected in uncertainty in terms of:
- Economic risks and uncertainty created by government regulation
- Existence of many, possibly conflicting, legal authorities or corruption
- The potential nationalization of private assets

Risks in the International Environment, cont.

- **Economic risks** are interdependent with political risks; however, some economic risks are specific to international diversification. For example, differences and fluctuations in the value of the different currencies are a primary concern to internationally diversified firms.

Risks in the International Environment, cont.

- For US firms, the value of international assets, liabilities, and earnings are affected by the value of the dollar relative to other currencies (e.g., as the dollar value increases, the value of foreign assets decreases).
- The value of the dollar may make US firms' exports uncompetitive in international markets because of price differentials (and, in turn make imports from other countries more attractive to US customers).

Strategic Competitive Outcomes

- Based on the advantages discussed earlier, international diversification should be positively related to firm performance. Research has shown that, as international diversification increases, firms’ returns decrease and then increase as firms learn to manage international expansion.

Strategic Competitive Outcomes, cont.

- There are several reasons for the positive relationship between international diversification and performance.
- Potential advantages from economies of scale and experience
- Location advantages
- Increased market size
- The potential to stabilize returns

Strategic Competitive Outcomes, cont.

- Developing new technology is critical to strategic competitiveness. In fact, Porter indicates that a **nation's** competitiveness depends on the innovativeness of its industries and that **firms** achieve strategic competitiveness in international markets through innovation.

Strategic Competitive Outcomes, cont.

- One of the advantages of international expansion is having larger potential markets. Larger markets allow firms to achieve greater returns on innovation, which yields lower R&D-related risk. Thus, international diversification provides firms with incentives to innovate.

Strategic Competitive Outcomes, cont.

- Cultural diversity enable a firm to compete more effectively in international markets.
- Culturally diverse management teams have a greater knowledge of international markets.
- An in-depth understanding of diverse markets facilitates inter-firm cooperation, the use of strategically relevant, long-term criteria to evaluate managerial and business unit performance, and improved innovation and performance.

The Challenge of International Strategies

- Managers of internationally diversified firms face a number of complex challenges.
- Firms face multiple risks from being in several countries.
- Firms can grow only so large before they become unmanageable.
- The costs of managing large diversified firms may outweigh the benefits of diversification.
- Global markets are highly competitive.

The Challenge of International Strategies, cont.

- Firms must understand and effectively deal with multiple cultural environments.
- Systems and processes must exist to manage shifts in the relative values of multiple currencies.
- Firms must scan the environment to be prepared for potential government instability.

The Challenge of International Strategies, cont.

- There are limits to the advantages of international diversification.
- Greater geographic dispersion across country borders increases the costs of coordination between units and the distribution of products.
- Trade barriers, logistical costs, cultural diversity, and other differences by country greatly complicate the implementation of an international diversification strategy.

The Challenge of International Strategies, cont.

- Institutional and cultural factors can present strong barriers to the transfer of a firm’s competitive advantages from one country to another.
- Marketing programs often have to be redesigned and new distribution networks established when firms expand into new countries.

The Challenge of International Strategies, cont.

- Firms may encounter different labor costs and capital charges.
- In general, it is difficult to effectively implement, manage, and control a firm’s international operations.

Unit 7 Recap

- Explained incentives that can influence firms to use an international strategy
- Identified three basic benefits firms achieve by successfully implementing an international strategy
- Explored the determinants of national advantage as the basis for international business-level strategies
- Described the three international corporate-level strategies

Unit 7 Recap, cont.

- Discussed environmental trends affecting the choice of international strategies, particularly international corporate-level strategies
- Explained the five modes firms use to enter international markets
- Discussed the two major risks of using international strategies

Unit 7 Recap, cont.

- Discussed the strategic competitiveness outcomes associated with international strategies particularly with an international diversification strategy
- Explained two important issues firms should have knowledge about when using international strategies

What's next?

- Complete reading assignments
- Complete writing assignments
- Answer discussion questions
- Complete unit quiz

References

Hitt, M., Ireland, R., & Hoskisson, R. (2017). *Strategic Management Competitiveness and Globalization 2015-2017.* Boston, MA: Cengage

Image References

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