INTERNATIONAL BUSINESS STRATEGY - REASONS AND FORMS OF EXPANSION INTO FOREIGN MARKETS

Katarzyna Twarowska
Maria Curie-Skłodowska University, Poland
katarzyna-twarowska@wp.pl

Magdalena Kąkol
Maria Curie-Skłodowska University, Poland
mkakol@hektor.umcs.lublin.pl

Abstract:
During the last half of the twentieth century, many barriers to international trade fell and a wave of firms began pursuing global strategies to gain a competitive advantage. However, some industries benefit more from globalization than do others, and some nations have a comparative advantage over other nations in certain industries. To create a successful global strategy, managers first must understand the nature of global industries and the dynamics of global competition.

The paper presents the problem of international business strategy. First, the authors define a concept of international strategy and gives some reasons why do companies go international and how they do it (entry strategy). The paper includes the case study of international strategy used by IKEA and attempts to explain when firms should standardize or adopt their products to foreign market. After that, the authors show some examples of joint venture and international alliances.

Keywords: international strategy, management, collaboration, strategic alliances, management

1. INTERNATIONAL STRATEGY AND GLOBAL STRATEGY - WHAT IS THE DIFFERENCE?

An international strategy means that internationally scattered subsidiaries act independently and operate as if they were local companies, with minimum coordination from the parent company.

Global strategy leads to a wide variety of business strategies, and a high level of adaptation to the local business environment. The challenge here is to develop one single strategy that can be applied throughout the world while at the same time maintaining the flexibility to adapt that strategy to the local business environment when necessary (Yip G. 2002). A global strategy involves a carefully crafted single strategy for the entire network of subsidiaries and partners, encompassing many countries simultaneously and leveraging synergies across many countries.

What differences are there between the global strategy and international strategy? There are three key differences.

The first relates to the degree of involvement and coordination from the centre. Coordination of strategic activities is the extent to which a firm's strategic activities in different country locations are planned and executed interdependently on a global scale to exploit the synergies that exist across different countries. An international strategy does not require strong coordination from the centre. A global strategy, on the other hand, requires significant coordination between the activities of the centre and those of subsidiaries.

The second difference relates to the degree of product standardization and responsiveness to local business environment. Product standardization is the degree to which a product, service, or process is standardized across countries. An international strategy assumes that the subsidiary should respond to local business needs unless there is a good reason for not doing so. In contrast, the global strategy assumes that the centre should standardize its operations and products in all the different countries, unless there is a compelling reason for not doing so (Zou S., Cavusgil S.T. 2002).

The third difference has to do with strategy integration and competitive moves. 'Integration' and 'competitive move' refer to the extent to which a firm's competitive moves in major markets are interdependent. For example, a multinational firm subsidizes operations or subsidiaries in countries where the market is growing with resources gained from other subsidiaries where the market is declining, or responds to competitive moves by rivals in one market by counter-attacking in others. The international strategy gives subsidiaries the independence to plan and execute competitive moves independently—that is, competitive moves are based solely on the analysis of local rivals . In contrast, the global strategy plans and executes competitive battles on a global scale. Firms adopting a global strategy, however, compete as a collection of a globally integrated single firms. An international strategy treats competition in each country on a 'stand-alone basis', while a global strategy takes 'an integrated approach' across different countries (Yip G. 2002).

2. WHY DO COMPANIES GO INTERNATIONAL?

Companies go international for a variety of reasons but the typical goal is company growth or expansion. When a company hires international employees or searches for new markets abroad, an international strategy can help diversify and expand a business.

Economic globalization is the process during which businesses rapidly expand their markets to include global clients. Such expansion is possible in part because technological breakthroughs throughout the 20th century rendered global communication easier. Air travel and email networks mean it is possible to manage a business from a remote location. Now businesses often have the option of going global, they assess a range of considerations before beginning such expansion.

Overseas operations are often attractive to executives seeking to reduce their budgets in order to increase profit. For example, it is possible to cut business overhead costs in countries with relatively deflated currencies and lower costs of living. U.S.-based businesses can further reduce overhead by operating in countries that have free trade arrangements with the United States. It is often cheaper to employ a workforce in these countries since the cost of living is lower. When companies experience financial crises, executives sometimes attempt to save what remains of the company by reformulating the budget and moving overseas (Elmuti D., Kathawala Y. 2001).

Expanded markets entice many executives into going global. William Edwards of All Business explains that going global can reduce a company's reliance on local and national markets. That is, downturns in consumer demand at home are offset by upturns in consumer demand in international markets. Larger markets also mean the potential for greater profit, so companies go global to seek new business opportunities and even to expand the range of goods and services that they offer. Sometimes businesses expand to under-exploited regions to gain market dominance before an industry competitor expands into the region (Retrieved from http://www.ehow.com/list_7581425_reasons-companies-go-global.html).

Change is an ever present facet of business development. Businesses transfer ownership, for example, and end up reformulating their entire business structures. Companies hire outside consultants to advise restructuring during financial crises. Sometimes the fact that businesses go global is the product of the inevitable ebb and flow of commerce. An overseas buyer may transfer operations to the home country. The majority of an industry's business may shift overseas, making global expansion all the more desirable. Competition may develop in regions such that it is unwise for your company not to follow.

3. HOW DO FIRMS GO INTERNATIONAL? – ENTRY STRATEGIES

Foreign market entry strategies differ in degree of risk they present, the control and commitment of resources they require and the return on investment they promise. There are two major types of entry modes:
1) non-equity mode, which includes export and contractual agreements,
2) equity mode, which includes joint venture and wholly owned subsidiaries.

The market-entry technique that offers the lowest level of risk and the least market control is export and import. The highest risk, but also the highest market control and expected return on investment are connected with direct investments that can be made as an acquisition (sometimes called Brownfield) and Greenfield investments (Terpstra V., Sarathy R. 2001).

3.1. Exporting and importing

The first and the most common strategy to be an international company is: import and export of goods, materials and services. Exporting is the process of selling goods or services produced in one country to other countries. There are two types of exporting: direct and indirect. Indirect export means that products are carried abroad by other agents and the firm doesn’t have special activity connected with international market, because the sale abroad is treated like the domestic one. For these reasons it is difficult to say that it is an internationalization strategy. In the case of direct exporting, the firm becomes directly involved in marketing its products in foreign markets.

3.2. Licensing

Licensing is another way to enter a foreign market with a limited degree of risk. The international licensing firm gives the licensee patent rights, trademark rights, copyrights or know-how on products and processes. In return, the licensee will: produce the licensor’s products, market these products in his assigned territory and pay the licensor fees and royalties usually related to the sales volume of the products. This type of agreement is generally welcomed by foreign public authorities because it brings technology into the country.

3.3. Franchising

Franchising is similar to licensing except that the franchising organisation tends to be more directly involved in the development and control of the marketing programme.

The franchising system can be defined as a system in which semi-independent business owners (franchisees) pay fees and royalties to a parent company (franchiser) in return for the right to become identified with its trademark, to sell its products or services, and often to use its business format and system.

Compared to licensing, franchising agreements tends to be longer and the franchisor offers a broader package of rights and resources which usually includes: equipments, managerial systems, operation manual, initial trainings, site approval and all the support necessary for the franchisee to run its business in the same way it is done by the franchisor. In addition to that, while a licensing agreement involves things such as intellectual property, trade secrets and others in franchising it is limited to trademarks and operating know-how of the business.
Advantages of the international franchising mode are as follows:

- low political risk
- low cost
- allows simultaneous expansion into different regions of the world
- well selected partners bring financial investment as well as managerial capabilities to the operation.

There are also disadvantages of the international franchising mode:

- franchisees may turn into future competitors
- demand of franchisees may be scarce when starting to franchise a company, which can lead to making agreements with the wrong candidates
- a wrong franchisee may ruin the company's name and reputation in the market
- comparing to other modes such as exporting and even licensing, international franchising requires a greater financial investment to attract prospects and support and manage franchisees.

3.4. Joint Ventures

Foreign joint ventures have much in common with licensing. The major difference is that in joint ventures, the international firm has an equity position and a management voice in the foreign firm. A partnership between host- and home-country firms is formed, usually resulting in the creation of a third firm (Byrne S., Popoff L. 2008).

This type of agreement gives the international firm better control over operations and also access to local market knowledge. The international firm has access to the network of relationships of the franchisee and is less exposed to the risk expropriation thanks to the partnership with the local firm (Geringer J.M., Hebert L. 1989).

This type of agreement is very popular in international management. Its popularity stems from the fact that it permits the avoidance of control problems of the other types of foreign market entry strategies. In addition, the presence of the local firm facilitates the integration of the international firm in a foreign environment (Killing J.P. 1982).

3.5. Strategic alliances

A strategic alliance is a term used to describe a variety of cooperative agreements between different firms, such as shared research, formal joint ventures, or minority equity participation (Campbell E., Reuer J.J. 2001). The modern form of strategic alliances is becoming increasingly popular and has three distinguishing characteristics:

- they are usually between firms in high - industrialized nations
- the focus is often on creating new products and technologies rather than distributing existing ones
- they are often only created for short term durations.

Technology exchange - this is a major objective for many strategic alliances. The reason for this is that technological innovations are based on interdisciplinary advances and it is difficult for a single firm to possess the necessary resources or capabilities to conduct its own effective R&D efforts. This is also supported by shorter product life cycles and the need for many companies to stay competitive through innovation (Jagersma P.K. 2005).

The greatest disadvantage of strategic alliances is the risk of competitive collaboration - some strategic alliances involve firms that are in fierce competition outside the specific scope of the alliance. This creates the risk that one or both partners will try to use the alliance to create an advantage over the other (Grant R.M., Baden – Fuller Ch. 2004).

3.6. Direct investments

In this arrangement, the international firm makes a direct investment in a production unit in a foreign market. It is the greatest commitment since there is a 100% ownership. There are two primary ways for direct investments: firms can make a direct acquisition in the host market or they can develop its own facilities from the ground up and this form is called Greenfield investment. Acquisition has become a popular mode of entering foreign markets mainly due to its quick access. Acquisition is lower risk than Greenfield investment because the outcomes of an acquisition can be estimated more easily and precisely. Greenfield investment is the establishment of a new wholly owned subsidiary. It is often complex and potentially costly, but it is able to full control to the firm and has the most potential to provide above average return. Greenfield investment is high risk due to the costs of establishing a new business in a new country. This entry strategy takes much time due to the need of establishing new operations, distribution networks, and the necessity to learn and implement appropriate marketing strategies to compete with rivals in a new market.

Foreign market entry strategies are numerous and imply a varying degree of risk and of commitment from an international firm. In general, the implementation of an international development strategy is a process achieved in several steps. Indirect exporting is often used as the starting point; if the results are satisfactory, more committing agreements are made by associating local firms.

4. IKEA'S INTERNATIONALIZATION STRATEGY - ADAPTATION AND STANDARDISATION PROBLEM

The furniture industry is an example of an industry that did not lend itself to globalization before the 1960s. The reasons for that are its features. Furniture has a huge volume compared to its value, relatively high transport costs and is easily damaged in shipping. Government trade barriers also were unfavorable. But IKEA – company established in the 1940s in a small village in Sweden, has become one of the world's leading retailers of home furnishings. In 2002 it was ranked 44th out of the top 100 brands by Interbrand, topping other known brands such as Pepsi. In 2002, it had more than 160 stores in 30 countries. How did IKEA achieve it? The IKEA business idea is: '*We shall offer a wide range of well-designed, functional home furnishing products at prices so low that as many people as possible will be able to afford them*.' By the early 1960s the Swedish market was saturated and IKEA decided to expand its business formula outside Sweden. They noted: '*Sweden is a very small country. It's pretty logical: in a country like this, if you have a very strong and successful business, you're bound to go international at some point. The reason is simple—you cannot grow any more*' (Retrieved from http://www.ikea.com). IKEA's internationalization strategy in Scandinavian countries and the rest of Europe has not paid significant attention to local tastes and preferences in the different European countries. Only necessary changes were allowed, to keep costs under control and IKEA's low responsiveness to local needs strategy seems to work well in Europe (Kling K., Gofeman I. 2003).

The first challenge came in 1985 when IKEA entered the US market and faced several problems there. The root of most of these problems was the company's lack of attention to local needs and wants. US customers preferred large furniture kits and household items. As a result of initial poor performance in the US market, IKEA's management realized that a standardized product strategy should be flexible enough to respond to local markets. In the early 1990s IKEA redesigned its strategy and adapted its products to the US market. Thanks to it IKEA's sales in the US increased significant and by 2002 the US market accounted for 19% of IKEA's revenue. As the case study illustrates, in several industries firms with effective strategy do not have to change their core strategy significantly when they move beyond their home market. IKEA does not significantly change its corporate strategy and operations to adapt to local markets unless there is a compelling reason for doing so. IKEA's strategy in the US during the 1980s demonstrates that even the most successful formula in the home market can fail if multinational companies do not respond effectively to local business realities (Carnegy H. 1995).

5. EXAMPLES. WHY DO WE NEED COLLABORATION?

This section shows an example of international alliance and collaboration between companies from one sector. In the 1960s US companies, particularly Boeing and McDonnell-Douglas, had become the dominant players in the increasingly capital-intensive airplane industry. The smaller European manufacturers competed with one another as well as with their international rivals, but the lack of capital and production scale did not allow them to compete effectively against their US counterparts in building big, modern passenger jets. By the end of the 1960s, the Europeans' combined share of the global aircraft market had decreased to just 10%. Then, in 1970, four of the leading European manufacturers – from France, Germany, Spain and the UK – did something radical. They decided to collaborate rather than compete. They formed the joint venture Airbus, pooling their resources to design, produce and sell jet aircraft (Slywotzky A., Hoban Ch. 2007).

The collaboration did not just provide temporary life support for the aircraft makers, it has allowed them to develop themselves. Although Airbus's first customers were European airlines, the venture began penetrating the American market by 1980. European aircraft manufacturing survived and Airbus had become the only rival to Boeing.

Why form a cross-border alliance? Do we need to collaborate to compete? According to the survey, cross-border alliances are appropriate for four broad purposes (many cross-border alliances involve multiple objectives):

1. To combine partner resources to develop new businesses or reduce investment. Typical examples include new business start-ups with parents contributing specific complementary capabilities that constitute the basis for a new business. For instance, ten leading drug companies, including Smith Kline Beecham, created a $ 45 million joint research consortium to study variations in human DNA. Airbus was a joint venture between French, German, British and Spanish manufacturers that eventually became a single company. Each national partner has specialized in one bit of aircraft manufacturing. The French became experts in aircraft electronics and cockpit design, the British became world leaders in wing manufacturing, the Germans concentrated on making fuselages and the Spanish focused on aircraft tails. Separate ventures or parent-to-parent collaboration? One of the most important decisions is whether to establish a separate equity venture or to establish a direct parent-to-parent alliance. Cross-border ventures are appropriate when: it is possible to establish a stand-alone business with dedicated resources provided by all parents. A high degree of integration of specific parent resources is required to achieve goals and it is desirable to create loyalty to a new business distinct from the parents because their interests might otherwise prevent the success of a collaboration (Kale P, Singh H. 2009). Toshiba and Motorola, for example, created a semiconductor manufacturing alliance, even though the two parents compete in downstream product areas. Direct parent-to-parent collaboration (often including licensing or long-term contractual agreements) is appropriate when assets or resources are best kept in separate parent organizations. Parent interests are competitive close parent control is required, and success cannot be measured in terms of performance measures that apply to stand-alone businesses (for instance, the main purpose is to learn).
2. To eliminate risks. During the past few years, Renault, General Motors and DaimlerChrysler have bought stakes in Nissan, Fuji Heavy Industries (which makes Subaru brand cars), and Mitsubishi Motors, respectively. The idea is that a stake in a Japanese carmaker, with a network of factories and dealerships in Asia, is a less risky way to expand into the world's fastest-growing automotive market than a full merger. Pilkington, the UK glass manufacturer, has joint ventures with Saint-Gobain of France, one of its fiercest rivals, in Brazil. The two companies take turns to build glass-making plants. Each side manages its own plants but they share the profits. Building a glass plant is hugely expensive. Through their cross-border joint ventures, they reduce the risk of having too much capacity for the local market.
3. To learn. Learning may entail improving skills through working with a partner or gaining access to countries. Turner Broadcasting, which is part of Time Warner, has completed a deal with Philips, a Dutch electronics company, where Philips will get the right to name a new sports arena that TBS is building in Atlanta. But TBS's main motive is to find out more about European consumers and about the digital communications hardware that is Philips's stock-in-trade. British Rover improved its manufacturing through the Honda alliance. GM learned about quality control, work teams, flexible assembly lines from Suzuki and from Nummi (i.e. the GM/Toyota global alliance), then transferred these capabilities to Saturn. Mazda has helped

Ford to improve its emissions testing – critically important as global regulations tighten. Ford has also gained access to Japanese manufacturing practices, including kaizen (constant improvement). Having watched several of its peers make expensive mistakes trying to buy stores or go it alone, Britain's Tesco wanted to penetrate South Korean markets without making the same mistakes. It formed an alliance with Samsung and began many joint ventures in the 1990s with foreign firms because they couldn't do a cross-border acquisition.

4. To change the name of the competitive game. To manage industry rivalry, Star Alliance, which includes Lufthansa and United Airlines, began as a series of loose arrangements to share codes and direct passengers to partners' flights; now it is beginning to look more like a quasi-merger, with shared executive lounges and pooled maintenance facilities (Slywotzky A., Hoban Ch. 2007).

6. SUMMARY

In the international competitive environment, the ability to develop a transnational organizational capability is the key factor that can help the firm adapt to the changes in the dynamic environment. As the fast rate of globalization renders the traditional ways of doing business irrelevant, it is vital for managers to have a global mindset to be effective. Globalization of business has led to the emergence of global strategic management. A combination of strategic management and international business will result in strategies for global cooperation. However, there are obstacles to progress along the way. The problems caused by these obstacles can be solved by cooperative ventures based on mutual advantages of the parties involved. Proper effective communication will be a key element for global strategies because what is proper and effective in one culture may be ineffective and improper in another. Marketing products globally is complex and difficult because of several factors including: International Strategic Alliances, coordination and control of international marketing, communication, regional trade blocks, and choice of global strategy. The firm with the choice of an effective global strategy that takes into consideration its strengths and weaknesses in the face of the opportunities and threats in the environment, will survive.

REFERENCE LIST

1. Burdon S., Chelliah J., Bhalla A. (2009). Structuring enduring strategic alliances: the case of Shell Australia and Transfield Services, *Journal of Business Strategy, 30*(4), 42-51.
2. Byrne S., Popoff L. (2008). *International Joint Ventures Handbook*, Baker & McKenzie.
3. Campbell E., Reuer J.J. (2001), *International Alliance Negotiations: Legal Issues for General Managers*, Indiana University Kelley School of Business, Business Horizons Copyright.
4. Carnegy H. 1995. *Struggle to save the soul of IKEA*, Financial Times (27 March 1995).
5. Elmuti D., Kathawala Y. (2001). *An overview of strategic alliances*, Management Decision 39/3 205-217, MCB University Press.
6. Geringer J.M., Hebert L. (1989). Control and Performance of International Joint Ventures, *Journal of International Business Studies, 20*(2), 235-254.
7. Grant R.M., Baden – Fuller Ch. (2004,1 January), *A Knowledge Accessing Theory of Strategic Alliances*, Journal of Management Studies 41: 0022-2380.
8. Jagersma P.K. (2005), Cross – border alliances: advice from the executive suite, *Journal of Business Strategy,2*(1), 41-50.
9. Kale P, Singh H. (2009), *Managing Strategic Alliances: What Do We Know Now, and Where Do We Go From Here?, Perspectives*, Academy of Management.
10. Killing J.P. (1982, May – June). *How to Make a Global Joint Venture Work*, Harvard Business Review, No. 82310.
11. Kling K., Gofeman I. (2003). *Ikea CEO Anders Dahlving on international growth and Ikea's unique corporate culture and brand identity*, Academy of Management Executive.
12. Slywotzky A., Hoban Ch. (2007), Stop competing yourself to death: strategic collaboration among rivals, *Journal of Business Strategy, 28*(3), 45-55.
Retrieved from http://www.emeraldinsight.com/journals.htm?articleid=1603609&show=html
13. Terpstra V., Sarathy R. (2001). *International Marketing*, 8th edn., Chicago Il, Dryden Press.
14. Yip G. (2002). *Total Global Strategy*, London Prentice-Hall.
15. Zou G., Cavusgil S.T. (2002). The GMS: a broad conceptualization of global marketing strategy and its effect on firm performance, *Journal of Marketing, 66*, pp. 40-57.