

# International Management

## What is International Management?

Firm Strategy and Organization in cross-border business: Where do we do what and how?

- Strategy (what) looks at how to : Create } Value  
 Capture }  
 Deliver }
- Organization (how) requires understanding and expanding of organizational capabilities
- International management adds the dynamics of location (where)

## Firms motivations for going international

- Classic: Exploit firm-specific CA (resource/markets/labor seeking)
- Emerging: Building/ Expanding a firm's CA (Technology, Experience, Competitive strategy, Geographic diversification/risk reduction)

## Benefits of internationalization:

- Efficiency: Global economics of scale, Comparative advantage of location
- Knowledge Leverage: Use people and ideas globally, create knowledge via multinational scope
- Responsiveness: To customers and stakeholders

## Levels of analysis; issues and frameworks:

Level of analysis	Issues	Location specific Frameworks	General Strategy Frameworks
Industry	<ul style="list-style-type: none"> <li>• What is the <u>relevant industry (in terms of geographic space) for benchmarking?</u> For competitive analysis?</li> <li>• Is globalization an <u>imperative, an opportunity, or a trap</u> in my industry?</li> <li>• What changes will intensify the <u>degree of global competition</u> in my industry?</li> </ul>	<ul style="list-style-type: none"> <li>• Forces for Globalization and Local Responsiveness (I-R grid)</li> <li>• Yip (1995)</li> </ul>	Industry attractiveness (Porter's five forces)  Firm's strength in the industry (growth/share, strengths and weaknesses relative to other firms, core competencies)
Location	<ul style="list-style-type: none"> <li>• Do firms based in a particular country have an advantage/disadvantage in my industry?</li> <li>• What competitive advantages can my firm gain by locating particular activities in particular countries</li> </ul>	<ul style="list-style-type: none"> <li>• Dynamics of location-specific advantages (Porter's diamond)</li> </ul>	
Firm	<ul style="list-style-type: none"> <li>• Which activities do we place where</li> <li>• How do we balance global integration with local responsiveness</li> <li>• Why do firms internationalize and how they do it</li> <li>• Modes of internationalization</li> </ul>	<ul style="list-style-type: none"> <li>• Value chain configuration</li> <li>• Integration-responsiveness by activity</li> <li>• Leveraging locations (virtual diamond)</li> <li>• Models of the MNC</li> <li>• Modes of expanding abroad</li> </ul>	Value chain Resource based view Capabilities
Individual	<ul style="list-style-type: none"> <li>• What skills, networks are critical to success in specific roles</li> <li>• How can these skills, networks be developed</li> </ul>	<ul style="list-style-type: none"> <li>• Location-specific skills and knowledge</li> <li>• Border-crossing skills and knowledge</li> </ul>	

## Organization of cross-border firms

Must understand what capabilities give a competitive advantage and how these depend on (home and host) location. Levers we have to consider: Formal organization, Coordination processes, Internal markets/rules, Rewards/incentives, IT networks, Shared experience...(Are my company's capabilities Relevant, Appropriable, Transferable?)

## Industry Level Frameworks

### Forces for Globalization and Local Responsiveness (I-R grid) by C.K. Prahalad and Yves Doz

- Pressures for integration
  - Pressures for Global *Operational* Integration:
    - Technology intensity, scale economies
    - Pressures for cost reduction
    - Homogenous needs/tastes
  - Pressures for Global *Strategic* Integration:
    - Importance of multinational customers
    - Importance of multinational competitors
    - Investment intensity
- Pressures for local responsiveness
  - Differences in customer needs/tastes
  - Differences in distribution systems
  - Needs for substitutes (regulations)
  - Market structure (fragmented vs. concentrated market)
  - Host government requirements

When we look at this framework we have to consider how these pressures differ for

- How do these pressure differ for
- Lead regions, countries
- Large, semiautonomous countries
- ROW

Remember, the IR grid:

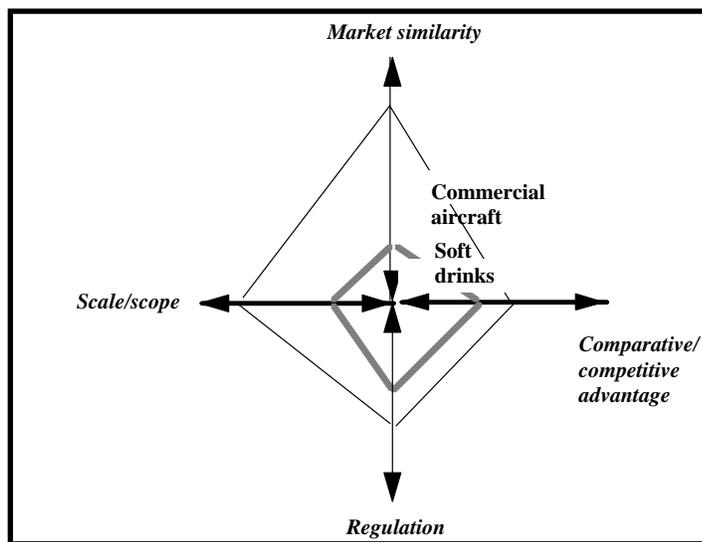
- Is not only a tool for discovering the orientation of the business for strategy making, but also for determining the most appropriate form of organization to achieve the strategy desired.
- Is useful to assess the pattern and speed of change in a firms positioning over time
- Helps managers assess opportunities and threats in the industry due among others to changes in underlying cost structure of the industry, political pressures, shift in competitive focus of customers, opportunities for resegmentation, ability to change the rules of the game.
- All measurements are relative!!!

Once we have analyzed the business as a whole, it is important that we examine how/if IR pressures have affected functions within business differently. (See below)

### Degree of global competition in an industry - Yip (1995)

Yip's "radar" maps four dimensions that determine the level of global competition in an industry:

- The upper vertical dimension in this "radar" chart refers to **market conditions**, whether the market is effectively one or several geographically defined segments because of similarities/differences in tastes, requirements, channels, etc.
- The left horizontal dimension refers to various sources of *increasing returns to scale* in the *production process*.
- The right horizontal scale refers to the **comparative and/or competitive advantages of particular locations**.
- The lower vertical dimension refers to **regulatory interventions** that limit the geographic scope of the industry such as tariffs and non-tariff barriers to trade and limits on cross-border investment.



*Example.* The figure below maps the globalization drivers for two industries -- commercial aircraft and soft. Commercial aircraft is global by virtue of market integration and very large-scale economies and knowledge advantages. Soft drinks are much lower on all these dimensions, but Coca-Cola dominates as a global player through its mastery of advertising, rapid transfer of knowledge among operating units, and financial strength. Local players also exist, although typically with very different strategies (e.g., me-too products, little advertising, lower price).

## Location level Frameworks

### The competitive advantage of nations (Porter–1990)

While it typically is applied to countries, it also applies to industrial regions that are smaller than countries, and to some extent to economic zones that are larger than nations

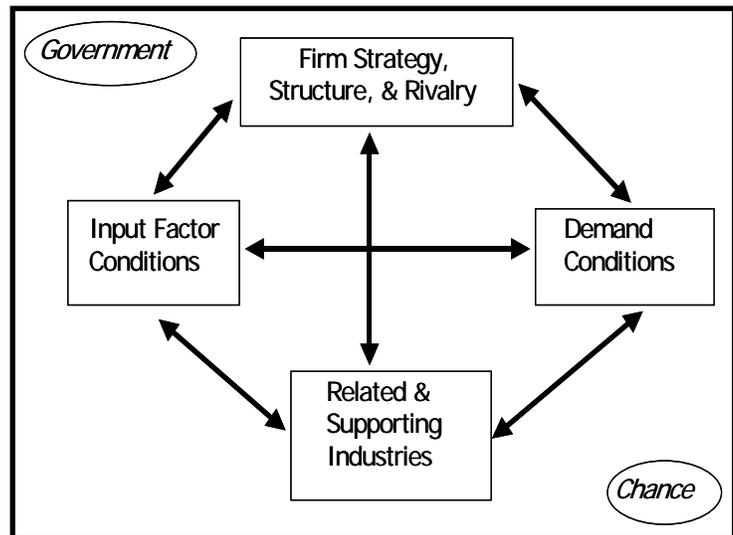
#### Some definitions:

- A nation's industry is considered **internationally successful** if it possessed competitive advantage relative to the best worldwide competitors
- **Competitive Advantage** is defined as: substantial and sustained exports to a wide array of other nations and/or significant outbound of foreign investment based on skills and assets in home country. Only sustainable through continuous upgrades that imply:
  - Global approach to strategy
  - Making its existing advantage obsolete
- **Innovation is the key to competitive advantage** (new technologies or new processes)
- **Home base**: if the firm is locally owned or managed autonomously (although owned by foreigners)
- Industries dependent on **natural resources are discarded** for the study: they say these companies are not the backbone of advanced economies and are better explained by classical theory

**The diamond** : A nation's competitiveness –based on constant innovation- lies on four broad attributes:

- Factor conditions: A nation does not inherit but creates the most important factors of production (skilled labor, scientific base).
  - Innovation depends on the rate –rather than stock- and efficiency of creation, upgrade and deployment of these resources
  - These factors have to be highly specialized to the industry's particular needs

- Demand conditions: CA arises if home demand gives firms a clearer of earlier picture of buyer's needs. The more demanding and sophisticated the home demand, the better. Importance of demand constraints due to local values and circumstances
- Related and supporting industries: Presence in the nation of related and supporting industries that are internationally competitive. Relevant dimensions of related industries: cost-effectiveness, parts innovation and upgrading, short lines of communication
- Firm strategy, structure and rivalry: CA arises from a combination of management practices and organizational modes favored in the country and sources of CA in the industry. Consider issues like company goals, management compensation... Strong local rivals are a stimulus to innovate. Emphasized if local concentration.



Diamond as a system : The effect of one element of the diamond depends on the state of the others.. Of specific importance for the dynamism are domestic rivalry and geographic concentration (clusters of competitive industries) → appearance of networks.

The role of Government: The proper role is considered to be both a catalyst and a challenger for innovation. Except in extreme cases indirect rather than direct role. Main tasks: promote rivalry, encourage change and specialize in factor creation.

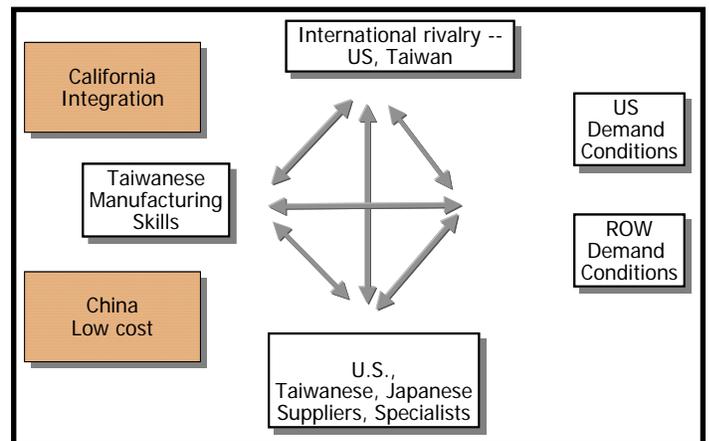
Conclusion: Locate the home base to support competitive advantage

Criticisms to this framework:

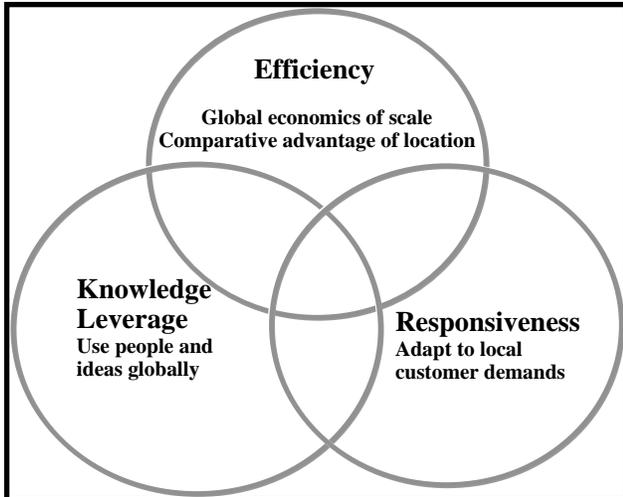
- How do you get to create your diamond? No theory for how to go there. Just analysis.
- Existence of virtual diamonds. Not everything has to be at home.
- Clusters may cross borders (existence of double diamonds)
- You don't need to locate all activities in the hot spot. You only need them where they create value.

Stretching the Diamond / Virtual diamond

As was clear in the Shimano and Acer cases, some home country diamonds are incomplete and firms have to "stretch" one or more dimensions of their diamond in order to innovate and be able to compete at international level. Note that a virtual diamond forcefully implies some level of global integration between the core and the "stretched" parts of the diamond. (Ex, in Shimano, the "big ear" wouldn't be of much use if it wasn't properly integrated with –at least- product design at home)



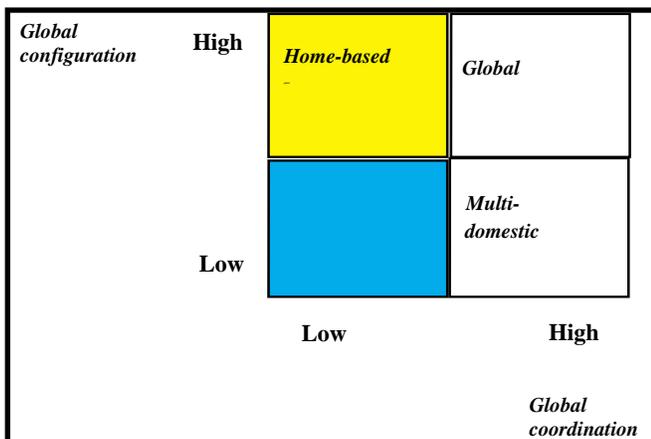
## Firm level frameworks



### Why do firms internationalize? Bartlett and Ghoshal (1989)

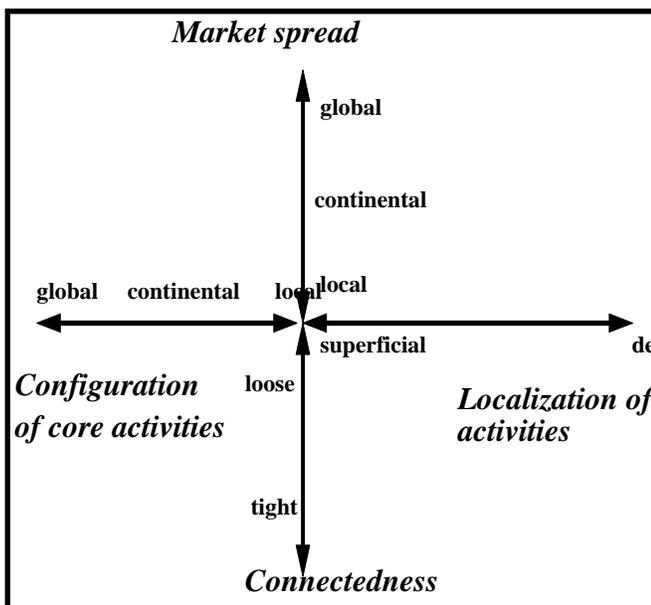
There are three main "leverage points" that can be gained from internationalization.

A key element of their argument is that different organization forms are particularly well adapted to one or another of these dimensions of performance, but that addressing all three is extremely difficult. The traditional European multinational, they argue, was extremely good at responding to varying needs, while the Japanese firm of the 1980s did extremely well in terms of efficiency.



### International Configuration/Coordination: Porter (1987)

Porter (1987) provides a useful two dimensional framework in which he categorizes internationalization as involving configuration --where and at what scale are primary activities conducted--, and coordination --to what extent and how are activities coordinated, knowledge shared, etc.

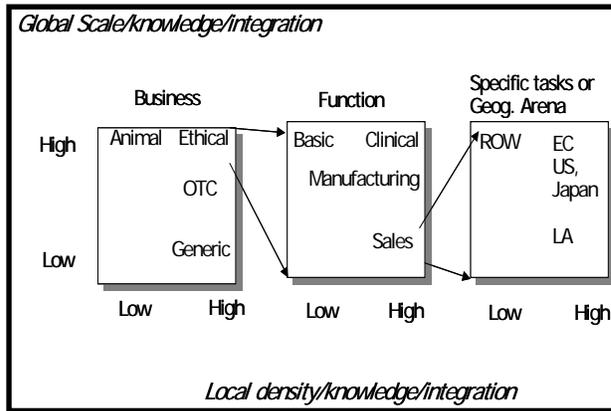


### Mapping the global reach of the firm (Lessard)

- Market spread refers to the geographic scope of the firm's sales, ranging from local, through regional or continental, to global
- Configuration of core activities refers to the geographic focus of key activities, whether they are locally focused, continentally focused, or globally focused.
- Connectedness refers both to coordination in the traditional sense and to sharing, joint development of know-how
- Localization refers to the degree to which responsiveness to and/or embeddedness in various local environments. It involves much more than just tailoring products to the market. It is useful to think of at least five levels, ranging from the most superficial to the deepest:

- 1) sufficiently localized **not to offend**
- 2) sufficiently localized to **sell** home based products and services effectively
- 3) sufficiently localized to **adapt** home based products and services to local environment,
- 4) sufficiently localized to **develop** internationally products based on local conditions
- 5) sufficiently localized to **influence the rules** of the game in local environments.

**Integration-responsiveness by activity (I-R grid) by C.K. Prahalad and Yves Doz**

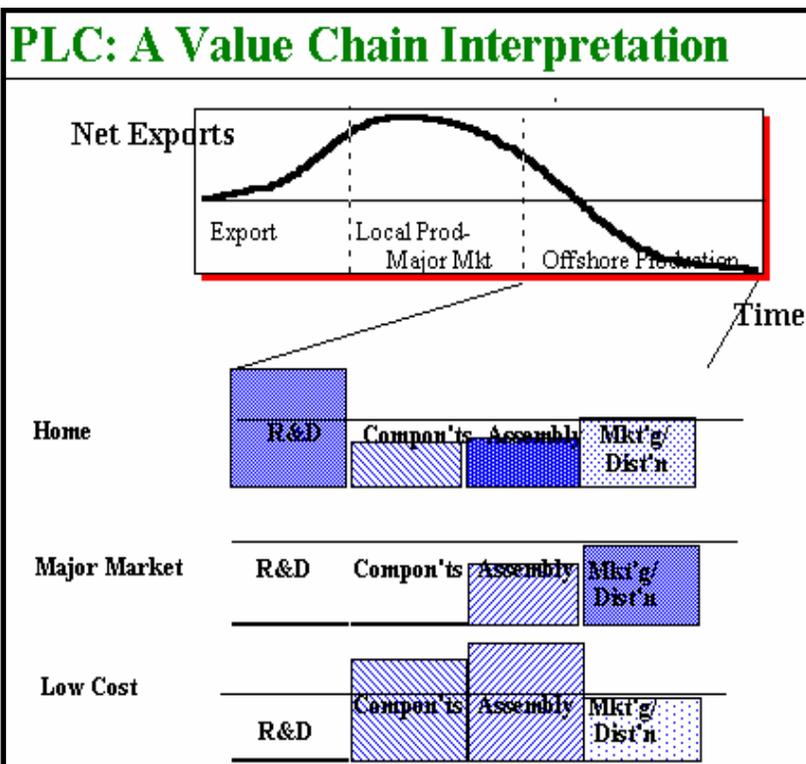


It is important to bear in mind that the degree of globalization is dependent not only on the specific industry, but also on the industry segment we consider, specific task, geographical arena and even product life cycle stage (see PLC framework for the latter).

**Product Life Cycle Model (1966, Ray Vernon, extended to value chain by Lessard)**

According to this model there are 3 stages in a firm's internationalization process:

- Internationalization begins with sales to similar (high income) countries
- Production (typically local for local) moves to major countries that represent major markets.
- Production moves to offshore platforms



**Stage I**

- process driven largely by home market co-location
- R&D close to market, production close to R&D, etc. Closely coupled system
- quality of linkages, feedback outweigh factor costs

**Stage II**

- process driven by host market co-location
- assembly, marketing pulled to foreign markets by transport, tariffs, co-location,
- manufacturing gains cost improvements via scale, learning, automation

**Stage III**

- location crucial
- assembly (labor) costs now a large proportion of total, technologies maturing, co-location less relevant

Relevance of this framework:

- Emphasizes market similarities, leadership and not just factor costs
- Gives central role to experience, learning by doing
- Allows for adjustment costs that may be both objective and subjective.

Criticisms:

While the PLC theory came to be widely accepted as a theory of the migration of industries across locations over time, Vernon himself recognized that its validity as a model of the evolution of the MNC was challenged by the changes in U.S. MNCs in the ensuing decade. By the late 1970s, many of America's leading MNCs had well-established networks of production around the world, and were increasingly likely to introduce new products simultaneously in several markets, rather than beginning at home and rolling out the product internationally over time. Reasons: closing of the income and labor cost gaps between the U.S. and the other developed countries; another reason was the speed at which increasingly capable local companies could emulate (often through reverse engineering) new products

### The Learning Model (Johanson & Vahlne, 1977: 24).

Swedish firms (in the 1970s) often developed their international operations in small steps, rather than by making large foreign production investments at single points in time". The process was incremental in two ways:

- in terms of the level of involvement (the mode),  
Exporting through an agent → sales subsidiary → manufacturing subsidiary
- in terms of locations  
Gradual increase in "psychic distance" of locations, involving the degree of difference from the home country in terms of language, education, business practices, culture, and industrial development. 1<sup>st</sup> Neighboring countries → region → continent → global

### Models of the Multinational (Bartlett and Ghoshal (1989))

**Definitions:**

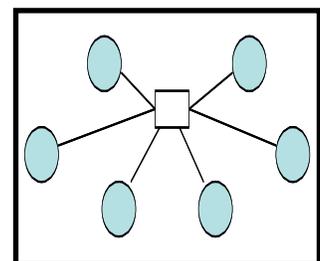
**MNC:** a firm with operations outside its original ("home") country

**Subsidiary:** MNC-owned operation/unit in a foreign country -- *recently less hierarchical language preferred ("affiliate", "local unit" etc.)* Each subsidiary subject to local company law (taxation, reporting, etc.)

**Classic MNC models**

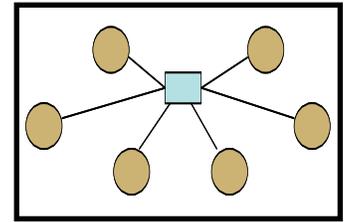
#### **The Classic "Multi-domestic" MNC: European model**

- Expanded when trade barriers were high, entire value chain in each country
- Strategy: high local responsiveness, "insider" within country
- Structure: portfolio of relatively independent national companies, linked by top mgr. sent out from HQ, little cross-unit linking
- Weak center, strong subsidiaries highly responsive to local stakeholders
- Subsidiaries strongly "local" in orientation & culture
- Pattern of innovation: local for local



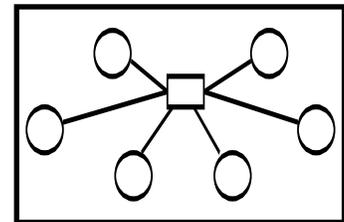
## The “Modified Multi-domestic”: U.S. model

- Characteristic of U.S. firms expanding abroad during global reconstruction after WW II, when U.S. was world’s lead market
- Strategy: CA based on leadership in technology & marketing expertise developed in advanced home market, local responsiveness on production & distribution
- Structure: national companies with most of value chain except new product development
- Controlled by formalized systems (reporting systems, performance measurement, etc.) -- impersonal control
- Strong managerial culture, extensive home country training of local mgrs
- Pattern of innovation: central for local adaptation



## The “Global” MNC: Japanese MNCs

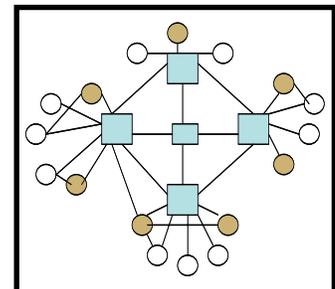
- Emerged when trade barriers & costs of transportation falling (late 1960s on)
- Strategy: globally standardized product/service, produced to global scale - scale economies
- Structure: low value-adding local units tightly controlled from home, strong cross-border functional linkages
- Power & decision-making tightly held at the center; dense communications networks between subs and home through expatriate managers
- Weak local identity, efforts to export home company identity and culture Pattern of innovation: central for global



## Newer MNC models

### The Model of the 1980s: The Transnational

- Emerged in mid-1980s - era of “Triad strategies”, high levels of cross-border M&A, falling communications costs, new IT
- Strategy: simultaneously seeking efficiency and scale economies, local responsiveness, cross-border learning
- Structure: integrated network of interdependent subsidiaries, linked directly to each other in wide



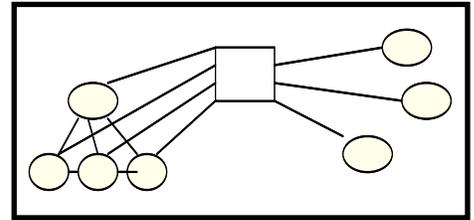
*Roles in the Transnational Model*

- array of relationships
- Power dispersed in the network, linked to strategic importance of location & org'l capabilities
- Efforts to build strong emergent shared company culture and strong local insider identity
- Pattern of innovation: leveraging local innovations throughout the network, linking innovation centers in multiple units for joint knowledge creation

<i>Strategic Importance of the Environment</i>	H	Black Hole	Strategic Leader
	L	Implementer	Contributor
		L	H
<i>Level of capabilities in local unit</i>			

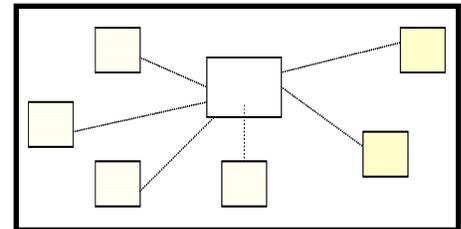
## The Home-based MNC

- Often next stage of development of global company
- Key functions still concentrated at home, especially innovation; growing dispersion of value-adding activities to production platforms
- Strategy: pursue scale economies and efficiencies through product & production platforms, increase local responsiveness capability, reduce concentration risk
- Structure: high value adding activities in home country operations and small number of key subsidiaries (guided from home), often key subsidiaries manage regional networks of subsidiaries; specialized subsidiaries
- Power concentrated primarily at home, secondarily in key subs; strong expatriate network
- Strong parent company culture
- Pattern of innovation: central for global

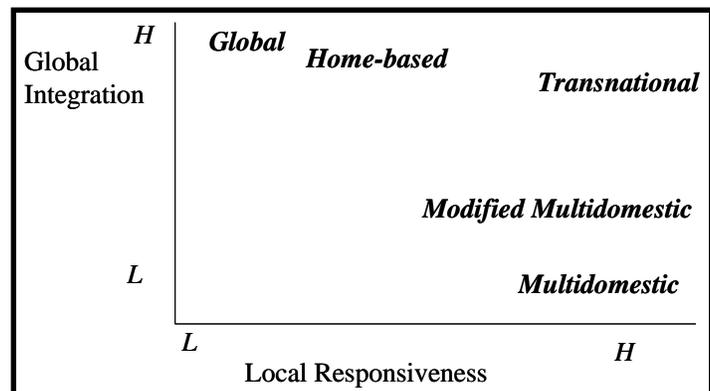


## Model for the future? The Virtual MNC

- Emerges as costs of cross-border communication and coordination have fallen, value of flexibility has increased
- Strategy: expand markets & tap location advantages without investment through alliances
- Structure: concentrate operations in home country, build strong networks to companies outside home base
- Power in network depends on relative capabilities, scale
- Pattern of innovation: central for network

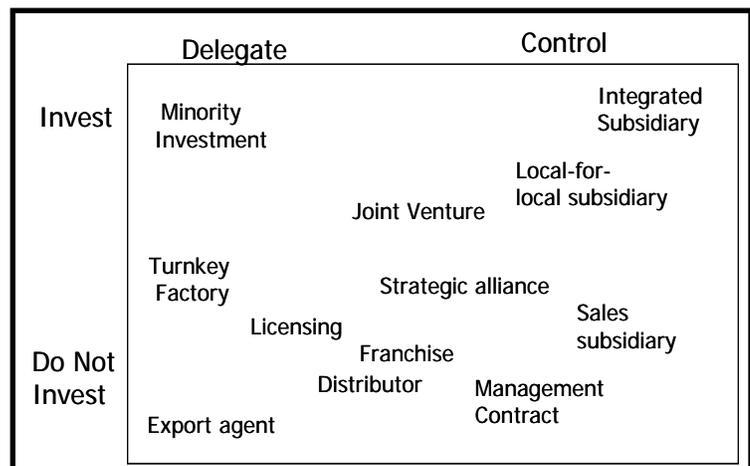


## Mapping the MNC models in the I-R grid



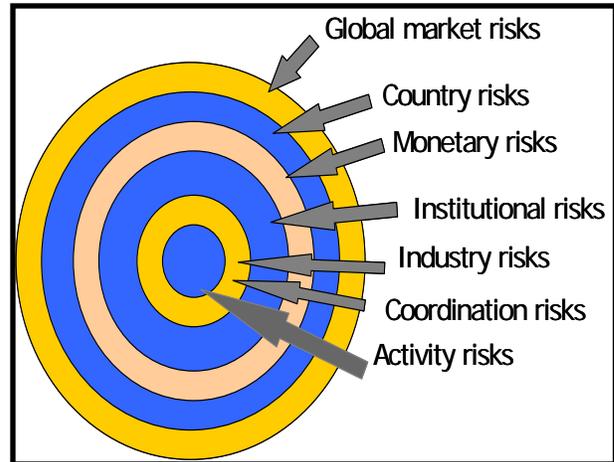
## Modes of Internationalization

Firms use a vast array of alternatives to internationalize their operations. Some are better fitted than others to serve the objectives of the international ventures of the firms. As an example, see the graph below. During the course we have seen in some more detail two of these modes: Mergers & Acquisitions and Strategic Alliances (Joint Ventures would be a third major mode but we have not seen it in detail)



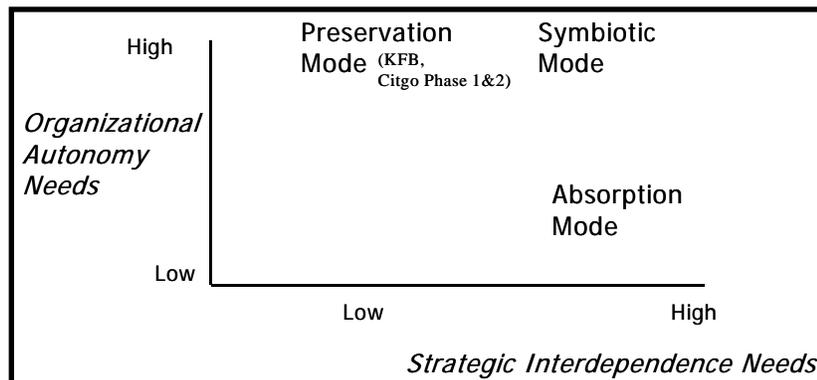
## Mergers, Acquisitions, and Alliances

- Key **pre-acquisition** challenges are: getting the structure (complementary positions, competencies, comparative advantages in dealing with risk and price)
  - Risk analysis framework (Don Lessard)
    - See graph
  - International projects risk management (Miller, Lessard)
    - Understand risk
    - Transfer/Hedge
    - Diversify/pool
    - Create options/flexibility
    - Transform risk drivers/mitigate
    - Embrace residual risks



- Key **post-acquisition** challenge is **integration**: given that cross-border integration is costly, in what activities will international **consolidation, integration, coordination, or knowledge sharing** add the most value? (assess location factors, industry factors, firm-level competitive advantage)
  - Critical points for successful cross-border Integrations (Philippe Haspeslagh)
    - Manage by phases:
      - Immediate actions to signal intent, benefits, need for change
      - Medium-term actions to develop synergies
      - Long-term actions for strategic growth
    - Focus on key issues – not all issues are equally important
    - Have respect for your acquisition and show it
    - Emphasize local management; resist upward delegation (erodes local capabilities)
    - Be willing to learn and adapt
    - Ongoing and visible involvement of top management is critical
    - Choose the right people

However, not all integration processes have the same needs and, therefore, can take different forms:



However, as M&As have increased in number and value, criticism has arisen (Ghemawat, Ghadar (2000))

- Challenge to the view that industries are consolidating – over 40-year period, consolidation has fallen in most industries
- Alternatives to mega-mergers:
  - Focus (“stay home”, focus on internal expansion)
  - Alliances
  - “Pick up the pieces” – buy spun-off

## Alliances

Alliances are defined as cooperative relationships in which independent partners combine resources, assets, etc to improve their overall competitiveness. Alliances are non-equity transfer relationships.

### **Dimensions of alliances (Hamel-Prahalad-Doz 1989)**

It is important that each partner considers before entering in the alliance what is:

- Its strategic intent (Capture-Exit or Leverage)
- The level of receptivity of its organization
- The level of transparency of supplied know-how

### **However, alliances sometimes fail. The usual reasons for failure are:**

- Mismatch of strategic objective
  - One partner views alliance as a substitute for developing its own capabilities
  - Other partner views the alliance as a means to develop capabilities
- Mismatch in transparency of know how
  - One partner contributes codified, transparent capabilities
  - Other partner contributes tacit knowledge
- Mismatch of learning capabilities
  - One partner has low absorptive capacity
  - Other partner has high learning or absorptive capacity

## Individual level frameworks

### **Issues:**

What skills, networks are critical to success in specific roles  
How can these skills, networks be developed

### **Frameworks:**

**Location-specific** skills and knowledge, networks:

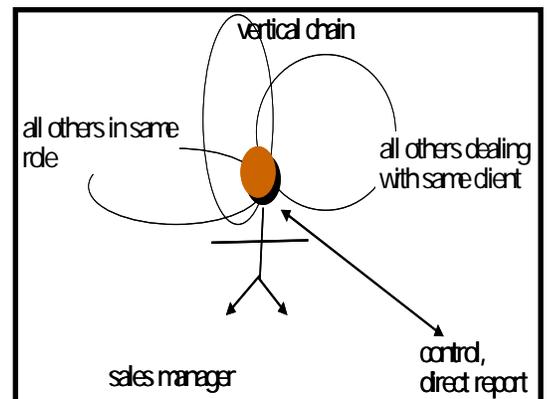
- Knowledge of business culture of a specific industry in a specific country
- Networking skills within country

**Border-crossing** skills and knowledge:

- Knowledge of how to learn quickly in new contexts
- Knowledge of how capabilities are distributed across locations, networks across those locations
- Knowledge/skills in linking complementary capabilities
- Common sense re which must be standard, which can vary

### **Systems for developing global managers:**

- Recruitment – positive discrimination for international experience, interests
- Cross-border experience (short-term visits, short-term transfers, long-term postings)
- Training (training programs rotated around locations, including participants from multiple locations and roles)
- Career development: Rotation across positions, recognizing and building on personal networks (e.g. the engineer who understands a particular foreign customer and has networks into customer's organization gets formal responsibility for relationship)



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