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INTRODUCTION

The focus is on the firm itself and, in particular, on the actions managers can take to compete more effectively as an international business.
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Value Creation

• The more value customers place on the firm’s products, the higher the price the firm can charge for those products.

• The value created by a firm is measured by the difference between $V$ (the price that the firm can charge for that product given competitive pressures) and $C$ (the costs of producing that product).

Do you agree?
Firms can increase their profits:

• by adding value to a product so that customers are willing to pay more for it
• by lowering the costs

There are two basic strategies for improving a firm’s profitability:

• a differentiation strategy
• a low cost strategy
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Strategic Positioning

A central tenet of the basic strategy paradigm is that in order to maximize its long run return on invested capital, a firm must:

• Pick a position on the efficiency frontier that is viable in the sense that there is enough demand to support that choice
• Configure its internal operations so that they support that position
• Make sure that the firm has the right organization structure in place to execute its strategy
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Operations: The Firm as a Value Chain

- The firm can be thought of a value chain composed of a series of distinct value creation activities, including production, marketing, materials management, R&D, human resources, information systems, and the firm infrastructure.

- These value creation activities can be categorized as primary activities and support activities.
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Organization: The Implementation of Strategy

The term organization architecture can be used to refer to the totality of a firm’s organization, including formal organizational structure, control systems and incentives, organizational culture, processes, and people.
In Sum: Strategic Fit

In sum, for a firm to attain superior performance and earn a high return on capital, its strategy must make sense given market conditions. It must sustains and fosters the organization culture.
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GLOBAL EXPANSION, PROFITABILITY, AND PROFIT GROWTH

Firms that operate internationally are able to:

• Expand the market for their domestic product offerings by selling those products in international markets

• Realize location economies by dispersing individual value creation activities to locations around the globe where they can be performed most efficiently and effectively

• Realize greater cost economies from experience effects by serving an expanded global market from a central location, thereby reducing the costs of value creation

• Earn a greater return by leveraging any valuable skills developed in foreign operations and transferring them to other entities within the firm’s global network of operations
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Location Economies

• Firms can benefit by basing each value creation activity at that location where economic, political, and cultural conditions, including relative factor costs, are most conducive to the performance of that activity.

• Firms that pursue such as strategy can realize location economies (the economies that arise from performing a value creation activity in the optimal location for that activity, wherever in the world that might be).
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Creating a Global Web

- By taking advantage of location economies in different parts of the world, multinational firms create a **global web** of value creation activities.

- Under this strategy, different stages of the value chain are dispersed to those locations around the globe where perceived value is maximized or where the costs of value creation are minimized.
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Some Caveats

• Introducing transportation costs and trade barriers complicates this picture

• Political risks must be assessed when making location decisions
Firms that compete in the global marketplace typically face two types of competitive pressures:

- pressures for cost reductions
- pressures to be locally responsive

These pressures place conflicting demands on the firm.
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Pressures for Cost Reductions

Pressures for cost reductions are greatest:

• in industries producing commodity type products that fill **universal needs** (needs that exist when the tastes and preferences of consumers in different nations are similar if not identical) where price is the main competitive weapon
• when major competitors are based in low cost locations
• where there is persistent excess capacity
• where consumers are powerful and face low switching costs
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Firms facing pressures for cost reductions:

• must try to lower the costs of value creation by mass-producing a standard product at the optimal locations worldwide
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Pressures for Local Responsiveness

Pressures for local responsiveness arise from:

- differences in consumer tastes and preferences
- differences in traditional practices and infrastructure
- differences in distribution channels
- host government demands
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Pressures for cost reductions and pressures to be locally responsive
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CHOOSING A STRATEGY

Firms use four basic strategies to compete in the international environment:

• global standardization
• localization
• transnational
• international
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Global Standardization Strategy

• A global standardization strategy focuses on increasing profitability and profit growth by reaping the cost reductions that come from economies of scale, learning effects, and location economies
• The strategic goal is to pursue a low-cost strategy on a global scale
• This strategy makes sense when there are strong pressures for cost reductions and demands for local responsiveness are minimal
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Localization Strategy

• A localization strategy focuses on increasing profitability by customizing the firm’s goods or services so that they provide a good match to tastes and preferences in different national markets.

• Localization is most appropriate when there are substantial differences across nations with regard to consumer tastes and preferences, and where cost pressures are not too intense.
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Transnational Strategy

A *transnational strategy* tries to simultaneously:

- achieve low costs through location economies, economies of scale, and learning effects
- differentiate the product offering across geographic markets to account for local differences
- foster a multidirectional flow of skills between different subsidiaries in the firm’s global network of operations

A transnational strategy makes sense when cost pressures are intense, and simultaneously, so are pressures for local responsiveness.
International Strategy

• An international strategy involves taking products first produced for the domestic market and then selling them internationally with only minimal local customization.

• When there are low cost pressures and low pressures for local responsiveness, an international strategy is appropriate.
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The Evolution of Strategy

• An international strategy may not be viable in the long term
• To survive, firms may need to shift to a global standardization strategy or a transnational strategy in advance of competitors
• Similarly, localization may give a firm a competitive edge, but if the firm is simultaneously facing aggressive competitors, the company will also have to reduce its cost structures, and the only way to do that may be to shift toward a transnational strategy
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As competitors emerge these strategies become less viable.

PRESSION FOR COST REDUCTION

HIGH

GLOBAL STANDARDIZATION STRATEGY

INTERNATIONAL STRATEGY

LOW

PRESSION FOR LOCAL RESPONSIVENESS

LOW

HIGH

TRANSNATIONAL STRATEGY

LOCALIZATION STRATEGY

As competitors emerge these strategies become less viable.