

Strategic Management for Competitive Advantage
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Lecture 22
Complexities and Challenges of Competing in Global Markets - I

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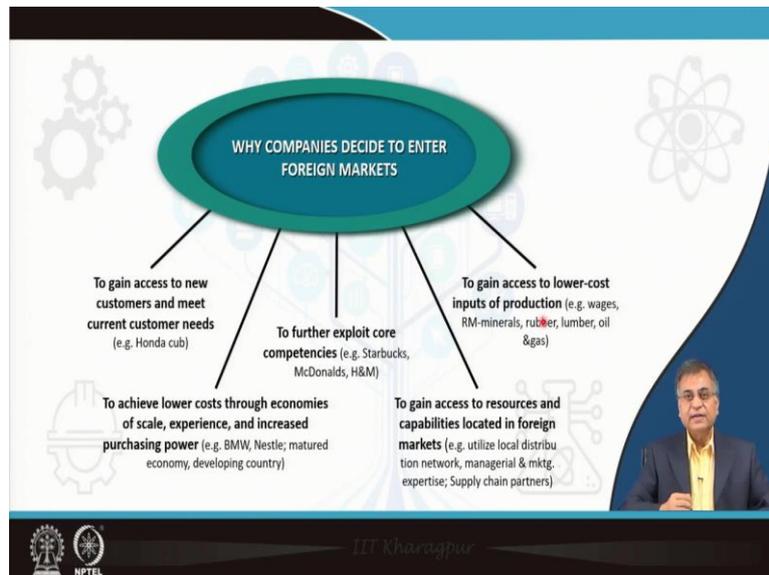
Welcome to the course Strategic Management for Competitive Advantage. In the last class, we covered operating and financial analysis, display matrices and portfolio analysis. Today, we will be covering a new chapter; this is called International Strategies for Competing in Global Markets. So, for the first lecture, we talk about the complexities and challenges of competing in global markets.

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In this lecture, we will cover the concepts and reasons for companies to enter into a foreign market. Then challenges and complexities are involved in international business. Lastly, we will discuss home-country industry advantages and Porter's national diamond model. This is a very interesting chapter, so we will go one by one.

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So, the first question comes, why do companies decide to enter foreign markets? Usually, the companies who are very competent, who have a strong domestic market, generally try to venture into the overseas market, what are the motives? What are the drivers that the companies go for, and what are the reasons the companies go for the overseas market? So, these are the five main reasons we will discuss one by one. These are five major reasons why companies decide to enter a foreign market.

The first is to gain access to new customers and meet current customer needs, what does it mean? Suppose you are operating in one country, so you are very strong in that soon you will find that you got saturated, your demand got saturated with that, that populations of the country. So, what do you need? You need a new market for your growth, particularly when the country is small, suppose say European countries, and they are small-small countries.

So, their local demand is fulfilled very fast, then for their survival what they have to do. They had to go beyond their country, so other European countries, and then maybe they will go further. So anyway, we will talk more about it a bit later. But you have to meet the needs of new customers, and also you have to satisfy the need of the existing customers also. Take the classic case of Honda 50 CC motorcycle, Honda 50 CC motorcycle, it is called Honda cub,

the Japanese company produced it first in the 1970s. So, after a few years, the demand got saturated in Japan, it was a huge success in Japan.

So, what did they do? So, if it is within Japan, it will be a declining stage. So, they went overseas, they went to many countries, say developing economies, developing markets, like India, Bangladesh, China, then Latin America, then even in the East European countries, so they went for it and by these 50 years has gone by from 1970, it is over 50 years.

But this Honda cub is still going strong, its demand is still very strong, even today. So, this is the need for which they are going overseas, and they are meeting the new customers, and the demand is going very strong or even after 50 years. That is one of the main reasons for venturing outside the domestic or the home country. Then other reasons for it are to achieve lower costs through economies of scale, experience, increased purchasing power of the people, and take advantage of the increased purchasing power of the population. I will discuss it one by one.

So, many companies go for the production of many products. Their design, their production, and their marketing take huge investments and huge costs. So, to get the economies of scale those companies need to go beyond their country so that their product sales, much more to get the volume advantage and the economies of scale advantage. Take the case of BMW or Nestle. BMW says that products that can be bought by a certain population, certain income groups of people and those income groups of people will not be found in many developing countries say India or Bangladesh or Latin American countries like Brazil and Argentina. You will not find many there, but you will find many of these populations of that income level in the USA, in some European countries, in Germany and all.

So, out of necessity, BMW has to explore beyond the national boundaries, they have to go to the USA, Germany and all the countries. BMW is from Germany and other European countries where the purchasing power is there, and the desired income group is there. So, they had to go out to get the economies of scale, get out the experience and increase purchasing power, these all are related.

On the other hand, if you see the economy cars like there are many Sedans and other economic cars and their growth rates are much faster in developing countries like China, India, in Brazil as compared to the matured countries - whose economies are matured like Denmark, like many of the European countries. There the sales volume, the growth will not

be much, but in India, China and all, this economic car group's demand is much more than that. So, this purchasing power is also related to the demographic population. It also matters that the companies go for the overseas market.

Then another reason is to exploit core competencies further. Let us take the case of McDonald's, KFC, and Starbucks, they have the core competencies, and other companies cannot take their things away. If they remain within their home country, they cannot exploit their core competencies for that to exploit the core competencies and to take competitive advantage they have to go out, they have to go overseas which is why they go for the global market.

Similarly, H&M is an online trading company, and they have tremendous exposure with popularity in 23 countries. Then that is on online purchases, and with that, they are capitalizing and paving the way for physical stores in those 23 countries. So, this is another reason for venturing outside the home country and venturing into foreign countries for businesses.

Then another reason for entering a foreign market is to gain access to resources and capabilities located in foreign markets. Some companies go for the overseas market to utilize the local distribution network, these countries or these companies may not have that complementary strength like distribution channel, distribution network or managerial or marketing expertise. They may not have all these. Therefore, they come to another country to gain, to supplement their deficiencies so that they become more robust.

Take the case of that distribution channels in India in many companies say ITC or the Hindustan Lever and all, are very strong. Even when Coca-Cola came, we had products in Indian soft drinks like Thumbs-Up, Mazaa and many other brands. They had a good distribution channel, so Coca-Cola and all they collaborated with them to gain those distribution channels.

Similarly, many foreign companies have come and collaborated with say Tata's, Tata Hitachi and many joint ventures there like Tata McGraw Hill, so to gain the managerial and marketing expertise of the home country of the foreign country. So, they take this route to come over the overseas market.

Again, there are supply chain partners. If you have considered big automobile companies, they try to open a new plant in a foreign country, what happens to their supply chain

providers? There are big suppliers for automotive components, they also give the majority of the supply to the parent automobile company. So, they also come to the foreign country and open a shop to do their businesses, their factory is there so that their products can be supplied to the automobile companies.

So, these other supply chain partners also move like Walmart. Walmart has a New Rubbermaid Company; they supply most of the homemade products and all. So, when Walmart goes to a new country, they also try to go to that country to supply things to Walmart. This is how the supply chain partners move in to gain access to resources and capabilities in foreign.

Lastly, to gain access to lower-cost inputs of production, as you know, why do companies go to foreign countries? To get the advantage of the low cost of production and which can be done where the labor costs are low. That is why you will find in developed countries that the cost of Labor's very high, but the developing countries it is very low, that is why you will find most of the factories in the world are in China because of the low wages, low input cost, like the materials and all costs, are also low. So, they take advantage of that, and the company try to open a shop there.

Another is the raw materials, cheap raw materials like in the oil and gas industry, those are specifically in some areas. So, for the products of oil, say refineries, petrochemicals and the different products, it will be cheaper if you make it there, the country where or the location where it is produced, so not in another country.

Similarly, for the rubber, lumber, minerals, and forestry products, inputs costs of raw material will be cheaper if you produce there instead of transporting all this to say 1000's miles away and producing. So that is why the companies come to the source of the supply, and it will be cheaper there to produce or so, you open up your plant there, or if you don't open, you give a contract of manufacturing with the local companies, so, that you have a contract to get those manufacturing products with a cost advantage. So, these are the main reasons why companies decide to enter foreign markets.

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The slide is titled "Why competing across national borders makes strategy-making more complex". It lists five reasons, each with a blue arrow pointing to the right. A small inset video of a speaker is visible in the bottom right corner of the slide area.

1. Different countries with different home-country advantages in different industries (e.g., Chile, Japan)
2. Location-based value chain advantages for certain countries (e.g. China for mfg., India/Ireland for call centers, S.Korea for R&D)
3. Differences in government policies, tax rates, and economic conditions (e.g. Ireland, UAE- Dubai)
4. Currency exchange rate risks
5. Differences in buyer tastes and preferences for products and services (e.g. buyer's preference: washing m/c in France and other European countries; appliances in HK & Taiwan; Novelty ice cream flavor; electrical devices in US and European countries; RH/LH driving car)

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Next, we are discussing how competing across national borders makes strategy-making more complex. Actually, when you go to the international market when you go for overseas market, it is a challenging job because you are dealing in a different environment, dealing with a different culture, and dealing with different countries' value systems. So, the decision-making is also not only a challenge, the complexities involved are far deeper.

So, there are five major reasons why in overseas markets, making strategy becomes very complex. These five reasons are these. First is - different countries have different home country advantages for different industries. I will discuss this first. Then we will be going for the others. What are the others? Location-based value chain advantage for some countries, the certain country gets the location-based advantage, and we will be talking about this.

Then there are differences in government policies, tax rates and economic conditions. Then for the overseas business, another main point is currency exchange rate risk, the fluctuations of currency can have a huge impact on your profitability, and then the difference in buyer tastes and preferences for products and services in different countries. So, these are the major reasons why strategy-making is complex for foreign international business.

So, let us talk about the first one in this lecture as part of this lecture. Different countries with different home country advantages in different industries, what does it mean? Suppose you take the case of some countries that are endowed with natural resources, so they have certain advantages over those particular industries or group of industries. Suppose take the case of

Chile, Chile is endowed with forestry, fishing, then copper mining, then paper and pulp, then wine. So, they are endowed with those natural resources and all. So, any industry of this type will flourish and will have an advantage in cost and competitive advantage over the other companies and other countries in these areas.

Now, take the case of Japan. Japan does not have much of natural resources, but what do they have? They developed themselves what is called homegrown capabilities, one is endowed with natural resources, and the other is homegrown capabilities. There are many factors, and I will be coming to those later. Which industries Japan is very competent in? Consumer electronics, automobiles, semiconductors, then speciality steel and steel products, because they have grown with those due to various reasons and all those reasons, we will be discussing bit later, what are the reasons, why they have grown, their talents and all those areas. So, we will be discussing these in more detail.

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If you look at this diagram, we will be talking about the rest part of this lecture with this diagram, this is the home country's advantages. Different countries have different home country advantages for a different or a particular type of industry. Why should you go for overseas operations? These are four factors. This is called Porter's national diamond model; this Professor Michael Porter has empirically found these four factors that influence whether the company should go for overseas competitions or not. These four factors are demand conditions, then factor conditions, then related and supportive industries and farm strategy, structure and rivalry. These entire four-factor has to be favorable, then you get the home country advantage, and you should go for the overseas market or the global market.

So, what is demand conditions? Demand conditions as Michael Porter have stated it is the growth of your home market, the growth of the size of your market and the growth rate of the market or the growth of the population, and buyers' tastes, the preference of that buyers, all these matters. What do certain demographic populations and income levels determine? That determines your home market growth rate and growth size.

Suppose you have the income level to buy a BMW. If there are a sizable number of people in the country, then only you will go for those BMWs. You have seen in USA and Germany, the number of those income level people are higher, so the BMW goes to the USA and all, not to Brazil or India. They will come with economic cars in India or Brazil or developing countries, so these are the demand conditions.

And what is the primary driver for this demand? For this home country's demand, the primary driver comes from the innovations and quality of the product, you have to improve, you have to be innovative and improve the quality of the product and then only you can get the competitive advantage in the overseas market. Say, take, for example, Switzerland, Switzerland's preeminence in watches, the Rolex watch and all you will find.

Why they are so preeminent in watches? That is because the Swedish people are obsessed with time and punctuality and that is their national characteristic, that is why they had innovation and quality for the watches, and it is just an outcome of that. So, their competitive advantage grew from there, and they went for the global stage where they got the competitive advantage because of quality and the high precision signal there.

Similarly, Japan's dominance in cameras, what is the driver for these? The driver is the national characteristic of Japan. The people of Japan are amateurs, their hobby is taking photography, group photography, family photography, and outside photography and that is their hobby, has culminated in their love for the camera. Not only that, the national characteristic of Japan is that people are very adaptive to innovation, the cameras are coming with higher and higher innovation, and they will adapt very fast. That is why Japan's dominance in cameras and all those consumer electronics you will find.

Then similarly, the National characteristics of Germans, Germans, we know a dominance in automobiles, high-end speedy cars if you see, the Audi, BMW, Mercedes, then Porsche, Volkswagen, all are German descent, why it is so? They are German national characteristics, one is they are very quality conscious, quality engineering and their love for high-speed

driving. So, that is why you will find that national characteristics and all that were the driver that gave them the competitive advantage to conquer the rest of the world. These are the demand conditions, and if in your home country the demand conditions are strong, that will be a driver for going into the global market.

Then another thing is the factor conditions, what are the factor conditions? This means the factor of production, what are the inputs productions, these are like availability of the raw materials, availability of the labour, availability of the materials, all these inputs and not only the availability, its quality, quality of the products, quality of the labour, skilled labourer or not, these are also equally important.

And relative prices of these inputs like if the cost is favourable, then only you will get a competitive advantage that is why the cost cheap labour, cheap materials and all. China and all are dominating because these factor conditions are more favourable to China and all than the developed countries. Another factor condition is infrastructure and distribution channel. Infrastructure means what the industry requires. That your communications, your transportations, your banking systems all have to be also upgraded, so that you take good advantage of that, so this is infrastructure.

Another is the distribution channel. Like if you have a distribution channel very extensive you get a competitive advantage. Take the case of India. In India's distribution channel we have say urban areas, semi-urban areas, rural areas and deep rural areas, the HLL, the ITC and all many companies having this deep distribution channel. In fact, India has 3 million which is 30 lakhs retailers. The dealer network and retailer's network are there, so it is a very good reason for the extensive distribution channel.

China makes many things locally with these materials, goes to the locals, and is distributed from there. So, these are the call factor condition. Porter Michael Porter has given some very good examples, these factor conditions can be homegrown, he has given the example of homegrown factor conditions and not you endowed with natural resources.

Take the case of Hollywood. Hollywood's preeminence in what? Preeminence in the film industry and related to the film industry and related all those activities. Why it is so? Because nearby, there are two Film Institute, one is UCLA, University of California Los Angeles and the other University of Southern California, these two Film Institute's produce very skilled technical staff, they produce all designers, then the film producers, then the cameraman and

all entire gamut. So, that is why Hollywood gets a competitive advantage, and for that, it has grown, that is the homegrown competitive advantage, that is a factor condition.

Similarly, if you take the case of the Japan Post where Japan has a constraint on raw materials, and it was not there. So, they had to import the raw material, they had to import everything. So, what did they do? They had to develop substitutes for this product, and so they had to look for that. There is a low defect in their product, their product is having high quality with low defect, they develop the substitute, and they have grown up the skills nearby themselves. That is the homegrown scale and miniaturization of the product. Therefore, they have excelled in all these; these are the homegrown conditions, factor conditions they have developed.

Similarly, Italy, if you have seen Italy's labour laws, are very restrictive. So, that forces them to go for automation that is why Italy has excelled in automation and in many industries, so these are the called factor conditions. Then again, another factor is - related to and supporting industries, what is this? This is, say you get national competitive strength, a country can get national competitive strength if their industries are in a cluster, the similar industry in the same area, same cluster, they get a national competitive strength, Michael porter has found it empirically.

Take the case of Silicon Valley; Silicon Valley is a cluster of what? There are semiconductor industries, there are computer industries- hardware, there are software companies, and there are venture capital. So, they are the clusters of that, and within this cluster, there are many companies, so they get that cross-fertilization, and the knowledge goes within that cluster, high degree of knowledge transfer takes place, and they get more enriched, and so, this gives them that competitive advantage.

Similarly, if you see Denmark, Denmark is the capital of wind power in the world; they are the leading wind power in the world. They have clusters of areas where they manufacture the wind turbines; they manufacture the machinery for the wind farm and deliver them throughout the world. They also manufacture wind farm equipment, and these are in the cluster within the cluster the knowledge transfer goes on very fast and the competitive advantage increases.

And another is if you see Italy, Italy has that Ferrari, Maserati, then your Ducati motorcycles and many others, their supplier are housed in one cluster that is called engine technological

district. So, what happens there? These big automobile components suppliers are very close to these companies, like this Ferrari, Maserati, and Ducati, where they can take innovative works and innovations. So, the knowledge moves to and fro very fast and they do collaborative things, and within these clusters, it grows very faster. So, these are the related and supporting industries. These also help you to be in the proximity of suppliers and end users and complementary industries. You must produce complementary industries there, and that is why you will find Toyota and all big automobile companies, they are in clusters with their suppliers and all in a very close range in clusters and that gives you the competitive advantages, so this is one.

In addition, the last factor is the firm strategy, structure and rivalry the different country has different style of management and organizations and the degree of local rivalry between different organizations have different. Say, in some countries, you will find the strategic alliances are very successful like Asian countries or Latin American countries, strategic alliances are mostly successful because their culture is based on trust and cooperation - these are the two things we value it.

So, the Asian countries, and Latin American countries, are common - cooperation and trust. So, strategic alliances are successful here. But if you see the American companies, the US companies, they are more of that individualism, is more influential on that individualism and all that, that is why strategic alliances are not that successful in the US, this is because of different types of management, different culture, organizations culture.

Similarly, home competitions are another potential factor for getting a competitive advantage for going overseas. Like, take the case of Japan versus Europe. In Japan, what happens, they have fierce competition within the home country in most of the industries. Like if you see automobiles, steel, or office equipment, and consumer electronics, there are at least five-six major producers, and their competition is cutthroat competition. That is why they have to innovate to get competitive advantages, they had to be efficient, and they had too innovative. So, that razor-sharp competitive advantage they carry overseas, they go overseas, and this competitiveness helps them to succeed.

In contrast, if you see the European countries, you will find that in high-tech industries there are very few European countries that have excelled because European governments and all do not encourage that competition rather, they prefer one national champion. So, these are some of the reasons for the firm strategy structure and rivalry. So, Porter says if in the home

country, all these four factors are favourable, then you can go for the competitive global market, and you will be set successful in that.

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The Diamond Framework

Answers important questions about competing on an international basis by:

- Predicting where new foreign entrants are likely to come from and their strengths
- Highlighting foreign market opportunities where rivals are weakest
- Identifying the location-based advantages of conducting certain value chain activities of the firm in a particular country

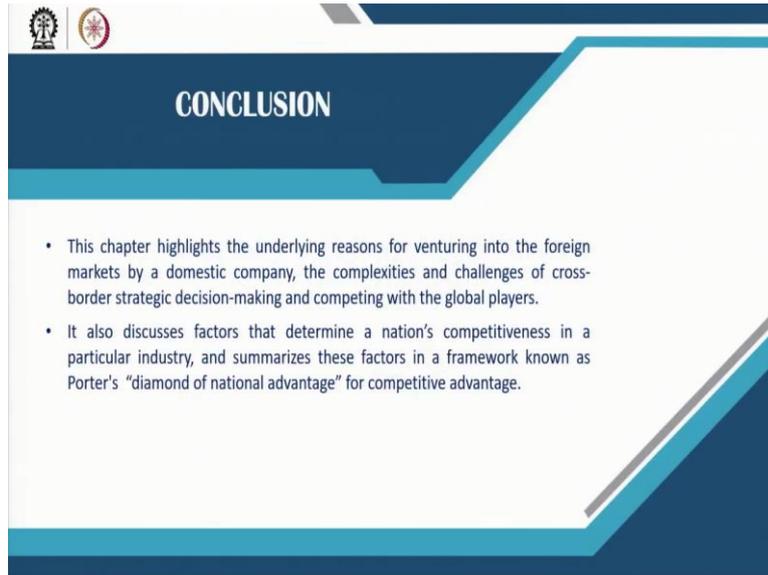
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Now, this diamond framework answers important questions about competing on an international basis. What does it say? This answers one is with this diamond framework managers or a strategist can predict where the new entrants are likely to come from and what the strengths of those companies are. These will allow you to see the foreign firms that will invade your home country through these areas; you can predict where you are weak. So, what are those countries and what are their strengths that it helps you to know?

Then also it highlights the foreign market opportunities. Now, we can, with this diamond network framework, also identify where the opportunities in the foreign market are and where the rivals are weakest. So, you can attack in those areas, you can go for those foreign markets and these also help you to find it out.

Then also it helps you to identify the location-based advantages and conduct certain value chain activities of the firm in a particular country. I will talk more about this point in the next lecture. So, I will not elaborate on this now. The diamond framework gives you these points that managers or strategists can know with the diamond framework of Michel Porter.

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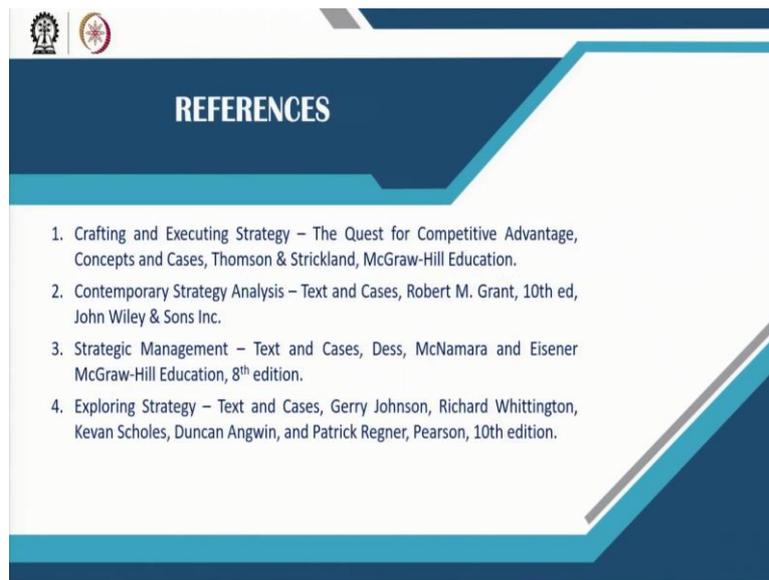


The slide features a dark blue header with the word "CONCLUSION" in white. Below the header, there are two bullet points. The slide is decorated with blue and white geometric shapes, including a large white triangle on the right side and a blue triangle at the bottom right.

- This chapter highlights the underlying reasons for venturing into the foreign markets by a domestic company, the complexities and challenges of cross-border strategic decision-making and competing with the global players.
- It also discusses factors that determine a nation's competitiveness in a particular industry, and summarizes these factors in a framework known as Porter's "diamond of national advantage" for competitive advantage.

Now, to sum up, today's lecture. So, what have we learned? We have discussed here what are the underlying reasons for venturing into foreign markets by a domestic company. We have also learned about the complexities and challenges of cross-border strategic decision-making and competing with global players. In addition, we have discussed the factors (four factors) that determine a nation's competitiveness in a particular industry and summarized these factors in a framework, which is known as Porter's diamond framework for the national advantage that will give you the competitive advantage.

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These are some of the references you can go through to enhance your knowledge further. Lastly, thank you very much for attending.