4 How Do Companies Go Global: Choices and Issues between Entry Strategies

Introduction

For hundreds of years trade flows have created international markets for domestic goods. The Silk Route created great wealth for those who were willing to travel it. For some in our survey, their organizations had been operating internationally for almost 250 years. In more recent years industrialists understood the importance of expansion into new markets, and researchers have increasingly studied how companies formed their global footprint. The path to internationalization will be explored in this chapter.

Theories to internationalization

There are numerous theories as to how companies expand their global footprint. These include the staged approach, the network approach, the born global approach, and the early strategic internationalizer. This research found another type of internationalizer, the opportunistic internationalizer.

The most famous and well-accepted approach for global expansion is the staged approach, also known as the Uppsala Theory, as it originated from the University of Uppsala in Sweden. Johanson and Vahlne found that when organizations initially ventured across borders, they gravitated toward those with similar cultural characteristics especially languages, a connection they call "cultural distance" (1977). So, for example, British internationalizers would venture first into the United States or a former British colony, a French organization may move into Belgium, and a Spanish company into South America. Similarly, they might also pick a neighboring country in which to invest that gives them a "proximity comfort" in their expansion so they can utilize existing systems for organizational support. There is a logic in seeking out those markets with a common language and shorter "culture distance": business can be conducted in both countries' native tongues, documentation need not be translated, and there tends to be more similarities of national culture and most likely legal systems, which in turn should lead to a faster learning curve especially surrounding the local market differences.

The Uppsala Theory suggests that organizations set up operations on a gradually increasing basis starting off with exports, agents, a sales subsidiary, and ultimately a production facility, the idea being that it commits more resources as it becomes increasingly familiar with the local market conditions, thereby creating a slower and more methodical path to internationalization (ibid.). Thus, globalizers only expand as fast as their knowledge and understanding of foreign markets will allow them, thereby reducing their "liability of foreignness" (Zaheer, 2002).

There are certainly numerous examples of how organizations have expanded initially on the basis of shorter culture distance even if they did so through acquisition. Almost 90 percent of Spain's outward investment has targeted either fellow European countries or Spanish colonies in Latin America (Sudekum, 2010). For example, when examining the mega deal activity of Telefonica Moviles Espana's expansion outside of Spain, they initially moved via acquisition into Latin America (see Table 4.1) with five mega deals in four years spanning four Spanish-speaking countries.

Recently, however, firms are increasingly finding alternative routes to internationalization that do not follow the Uppsala path due to rapidly moving industries as well as the transformational changes discussed in Chapter 2. Recent changes have created a greater willingness and more opportunities to expand rapidly into regions that share no cultural, legal, or linguistic similarities with the organization's host nation.

A second approach to internationalization, the network theory, puts forth that overseas expansion follows the internationalizing organization's relationships. These relationships can include "formal and informal relationships, alliances with other firms at any stage of the value chain of activities (suppliers, customers and intermediaries) and membership of professional organisations" (Hynes, 2010, p. 90). These networks provide market intelligence and compensate for a lack of "on-the-ground" knowledge. So in order to succeed, the internationalizer must maintain and manage these ongoing relationships to ensure a timely and accurate flow of information.

Table 4.1 Telefonica Movile Espana's mega deal acquisition history

Year	Target	Target's country of origin	Amount paid
2001	Telefonica de Argentina	Argentina	\$1.6 billion
2004	Telefonica Movil de Chile	Chile	\$1.3 billion
2004	BellSouth Columbia	Columbia	\$1.05 billion
2004	Telcel Celular	Venezuela	\$1.2 billion
2005	BellSouth Latin America	Argentina	\$1.5 billion

Source: Thompson Financial.

They must also be willing to relinquish some control over their organizational processes in order to facilitate overseas expansion in the form of alliances or trusting the market intelligence of their network partners (Oviatt and McDougall, 2005). Both the staged and network approaches rely on organizations taking a slower approach to internationalization as they slowly bridge cultural and market differences between their home and foreign markets.

Related to this is the "piggyback approach" in which an internationalizing organization leverages its existing client relationship as they follow the client into a new geography. Once there and established with the existing client and cash flow, the internationalizer can work on establishing its presence further vis-à-vis local customers. One service provider said, "You want to set up wherever your clients are and broadly speaking all clients want to go to emerging markets so we need to be in the emerging markets." The approach can also leverage an internal corporate relationship such as one division providing contacts and relationships for another in order for them to access the region. While research in this approach has focused primarily on banks, this research found that the same concept appears to be relevant for all the service providers interviewed (Qian and Delios, 2008). These companies do not follow a set pattern but instead appear to be more network-driven in their expansion. Not only did all but one bank interviewed use this approach but so did both other service providers and specialist manufacturers. Several of the larger manufacturers also used this approach leveraging the local knowledge and contacts held by their divisional brethren.

The third theory, the "born global," is based on the premise that there are a number of firms that are global from almost the instant they are created, in many cases relying on the international aspect for their very existence (Autio, Sapienza, and Almeida, 2000; Callaway, 2008). Born globals share some similarities. They often rely on new technology such as the Internet to give them a wide geographic reach in a relatively short period of time (Freeman, 2001). In addition, their product offering may be relatively standardized and as such not require a significant adaptation to be sold across a variety of markets thereby facilitating a homogeneity in approach (Callaway, 2006). Finally, they may need to gain a global scope at an early stage of development in order to gain a first-mover advantage—a jump on the competition—and therefore survive once the market becomes more competitive (McDougall and Oviatt, 2000).

The fourth type of internationalizer is discussed more in depth in Chapter 9, that of the early strategic internationalizer. It is an organization that makes the conscientious choice that overall success is predicated by a move into international markets at a very early stage of development. It is not a born global in that the business is not inherently international but instead a decision taken by management. One example of this internationalization route is Nidec, the Japanese manufacturer that entered several foreign markets within a year of their founding. It is discussed in more detail in Case 9.1 of Chapter 9.

This research has found a fifth type of internationalizer—the "opportunistic globalizer"—whose management understands its needs to capitalize on economies of scale in as many markets as possible. Its product offering is relatively homogenous, often commodity based, and benefits from local production through heavy transportation costs. Examples could be commodity items such as steel, cement, or agriculture. They globalize in no set pattern but instead, expand into regions as suitable acquisition targets or joint venture arrangements become available.

An excellent example of an "opportunistic globalizer" is the world's largest steel manufacturer and Indian giant, Mittal. The company, now known as ArcelorMittal SA following their $33 billion acquisition of French/Spanish/Belgian/Luxembourgian steel giant Arcelor in 2006, have grown in the past 20 years via acquisition into a truly global entity. It is clear when examining the expansion path of Mittal and the target countries of origin that there is no systematic progression of cultural distance in their internationalization. As seen in Table 4.2, Mittal's acquisitions have been in culturally diverse locations suggesting that they have expanded based on opportunistic availability of targets overlaid upon the constraints of internal resources (funding, management time, and expertise). In addition to their acquisitions, ArcelorMittal also has shareholdings in companies in Morocco, Canada, Brazil, China, Canada, and Poland.

The survey participants are well beyond the beginnings of internationalization, but looking back at their roots indicate a variety of approaches to internationalization. Several companies have mirrored the Uppsala approach, including Santander, Cadbury Schweppes, Centrica, and JBS. The approach is also demonstrated by the world's largest generic pharmaceutical company Teva's expansion into Japan (see Case 4.1). They formed a small joint venture

Table 4.2 ArcelorMittal's overseas expansion, 1992–2012

Year	Target country of origin
1992	Mexico
1994	Canada
1995	Kazakhstan, Germany
1997	Germany
1998	US
1999	France
2001	Russia, Algeria
2003	Czech Republic
2004	Bosnia, Macedonia, Poland, South Africa
2005	US, Ukraine, Canada
2006	Mexico
2007	France/Belgium/Spain/Luxemburg (acquisition of Arcelor meant a change in name to ArcelorMittal SA)
2007	Austria, Argentina, UK, Uruguay, France, Brazil
2008	US, Brazil, Russia, Venezuela

Source: ArcelorMittal website.

that built their market knowledge prior to a more substantial acquisition. As discussed before, Nidec is an early stage internationalizer who went global within 12 months of their founding much to their advantage. There are several who at this stage of development would be considered opportunistic internationalizers, including BP and Lafarge. They are both represented in cases: BP in Chapter 6 and Lafarge in Chapter 7.

Method of foreign direct investment

One of the most significant topics of globalization is the choice of FDI; extensive analysis has been undertaken investigating the best options for entering any market. Globalizers are faced with the options of whether one acquire, grow organically, or form a strategic alliance. If it is the latter, what kind of alliance—equity based such as a joint venture or a nonequity mode such as a licensing agreement. The options are endless. Literally hundreds of correlations have been found indicating that companies with certain characteristics are more likely to favor certain entry modes with varied rates of success, such as CEO experience (Hermann and Datta, 2006), industry type and maturity (Couturier and Sola, 2010), and desired speed of entry (ibid.).

When entering a foreign market, there are several considerations one must consider that could impact the form of entry most likely to bring success. The key issues that were seen as being critical to the survey's participants were being in control, speed, local market knowledge, and resource requirements. In addition, other research has found that both external and internal issues can impact successful entry choice. They include external issues such as government regulations, corruption, and competitors, and the internal issue of intellectual property rights and managing other intangibles. These will be discussed in turn.

Four issues in entry-mode choices for survey participants

Control

The level of operational and organization control is probably the first decision one makes when going overseas. Control over the assets is seen as a significant factor when considering mode of entry. Both greenfield investment and acquisitions allow for the organization to retain full legal, operational, and financial control over the venture. But the two share some significant differences; acquisitions allow for immediate cash flow and market access and create potential synergy enhancements between the acquirer and target (Tekin-Koru, 2009). Acquisitions also bring with them the risk of a failed implementation or poor target choice. Greenfields offer the opportunity for transferal of a unique firm competency into a new market (ibid.). This is the approach that Arc International took into its Chinese greenfield investment—taking its cutting-edge manufacturing technology and implementing it in a new market (see Case 10.2 in Chapter 10). Research has found that newly internationalizing firms who want control will use acquisition rather than greenfield investment while more experienced globalizers tend to use greenfield investment (Couturier and Sola, 2010). In either choice, "the price of control means a greater commitment of resources, reduces the firm's ability to change partners if they are not performing well and generally reduces flexibility" (Datta, Musteen, and Hermann, 2009, p. 931). One survey participant said, "We generally like control. We will give up equity if we are required to in order to operate in that market, but we consider it the price of doing business there. What we won't do is give up control." Control is an issue that is revisited in Chapter 6.

Control and ownership are two different things. Ownership is the breakdown of share ownership in the entity—it is wholly owned either as a greenfield investment or where shares are fully acquired or it is owned jointly in some way by two or more parties. Control is different. Control is who dictates the organization's ongoing operational and managerial practices on a day-to-day basis. It is very common in joint ventures for one party to have operational control while not having full ownership or sometimes even majority ownership of the entity. In most circumstances, however, organizations must cede some control, usually with both parties bringing some assets into the organization. In the developing world, the globalizer often brings capital, brand and marketing expertise, and technology while the local partner provides employees, market knowledge, political connections, and sometimes a locally known brand. Management responsibilities are often split between the two parties. Interestingly, in the developing world, who controls the HR function is often a source of contention. Globalizers are interested in efficiently staffed organizations while the indigenous government is very often interested in fuller employment. If the joint venture partner happens to have close state connections or shareholding, there is an increased pressure to seek fuller employment at the cost of profit, thus potentially creating a mismatch of objectives. One survey participant commented about his joint venture partner that is an emerging world local municipality, "They said 'why don't you give us the HR part of your business?' and we said, 'Never.' They are interested in having as many employees as they can, they chose the employees and we know what we need in our business. So we would never give them that." Interestingly, Indonesia requires that the HR manager of any foreign investment be an Indonesian national (World Bank Report, 2010). Not surprisingly, previous research has found that globalizers who want a greater level of control prefer to use acquisition as their mode of entry over other means of foreign investment (Bogan and Just, 2009).

Joint ventures bear heightened risks as an entry choice in terms of control. Having legal control does not necessarily guarantee actual control as seen in the Danone case (Chapter 10). Having an agent means giving up the vast

majority of control with the hopes that the agent properly and professionally represents the product or products accurately and honestly. While this is the lowest-cost option, it is also the least-control option available to a globalizer. To mitigate this risk, some globalizers set up a representative office to monitor their agent's performance to ensure compliance to their wishes and maximize performance. While this seems cost intensive, there is an opportunity cost by having a poor agent, while a representative office simultaneously allows for the globalizer to gain valuable market knowledge.

While almost all the participants were forced to use a variety of mechanisms to gain entry into the wide variety of markets in which they operated, almost all showed a distinct favorite mode whether it be acquisition, greenfield investment, or joint venture, most of which centered around control. Seventy percent of participants favored a wholly owned overseas operation either organically grown or acquired. And even of those who used joint ventures almost to a person preferred to have operational control. One participant said, "We generally don't enter into joint ventures. We only consider a joint venture if there is a clear path to either full control or a complete exit." Control will be further discussed when analyzing success factors in joint ventures in the following chapter.

Speed

When survey participants were asked the most important consideration in entering a market, it wasn't control as anticipated, it was speed, with almost one-quarter of participants indicating it was the main reason for using acquisition to enter the market. How quickly one can effectively enter the market is dictated in part by the method of market investment. Buying either partially or fully into an existing operation certainly is the fastest option of entry mode. Many of the survey participants were willing to acquire an existing business rather than grow one organically knowing there was a significant cost premium and risk during acquisition implementation in order to save time.

While research suggests it can take between six and ten years for an organic growth business to become cash positive in the emerging world, acquisitions generally generate revenue from the time of purchase (Woodward and Wang, 2005). It is worth noting with acquisition, however, that while acquisitions are generating cash flow from day one, it can take up to a year to clear regulators and purchase a local business as a foreigner in some jurisdictions and industries (ibid.). Joint ventures cover a wide spectrum and can vary quite dramatically in how quickly one delivers to the market. Nonequity modes of investment are the same depending on the nature of the strategic alliance.

One commented:

> Acquisition is a much faster and quicker method of doing it than setting up everything from scratch, but there is a trade-off in terms of uniformity and getting everything done the right way right from the beginning. But it's speed versus uniformity that seems to be the big trade-off with buying versus joint ventures or organic growth.

Roughly half of globalizers were willing to give up some control to gain quicker access to the markets by entering into joint ventures. One participant said, "Personally I prefer organic growth. But there were time constraints—competitors were entering the market quickly, and we needed to do something in response."

There was a small but significant number of respondents, however, who said speed was not an issue. They were willing to get to know the new market and after doing so make a decision on how best to enter the market on a larger scale. This longer-term perspective was seen most readily in emerging markets and family-owned businesses. A representative of one company that used this approach said, "I think we were in Turkey for about ten years by ourselves before we entered into a partnership with someone else. Same in Nigeria—we operated on a much smaller scale before we bought our target."

This perspective is also seen in Case 4.1 in this chapter with Teva. While they did enter Japan with a very small joint venture, the purpose of the joint venture was to give them better market intelligence in order to facilitate deciding how best to proceed in the future when they invested on a larger scale. They ultimately acquired Japan's third largest generic pharmaceutical company.

Local market awareness

According to our participants, the greatest perceived benefit of having a local partner is the immediate access to the subtleties of the local market, culture, and political structure. As seen in China (Chapter 10) this knowledge is paramount especially in emerging world markets and when one is operating with a long "culture distance" to one's home market. One participant commented:

> If you don't know the territory, if you don't know the market, if you haven't got distribution, then really aligning the product with the market is one of the big risks. What you don't do is simply export one central view all over the world, which may not be appropriate. You have to strike a balance between having a core understanding of what you want the business to do, but a regional flexibility to acknowledge the local circumstances in how it is run there.

One participant who has done dozens of complex joint ventures throughout the world commented, "We have lots and lots of different joint venture structures, and they are actually my preferred way of doing business often because it allows you to bring together that local expertise and international experience."

In some cases, having a local partner is the only way one can invest in a foreign market. Choosing the appropriate partner does present risks. One only has to remember the dozens of horror stories of failed joint ventures that collapsed due to incompatible partner objectives or strategy. One participant commented about his most recent joint venture:

> We have struggled with the partnership. Sometimes there's an imbalance in the priorities and objectives of both sides ... there are huge differences in personalities and styles of our joint ventures—right or wrong they operate differently. If it is going to crash, it is because the partners didn't, couldn't, work together.

When operating alone in a foreign market, four perspectives were seen as working well. One was buying a local company that provided the local intelligence and market knowledge. The other was to establish a presence in the local market and build up local knowledge and in time use this knowledge to pursue an appropriate entry mode whether it be through acquisition, greenfield investment, or partnering with a suitable candidate. One participant said, "We set up an office in the country and get to know it on a very small scale. Once we have the 'lie of the land' so to speak, we have a better idea of how best to tackle the market." The third choice was to enter the market with a greenfield investment either through a piggyback approach or directly using unique technologies and recruit a local management workforce with market knowledge. The final method was to partner with a local firm and keep a presence there. One participant said, "We have been more successful in having a small local presence—local relationships, local presence, history, references make all the difference in the world. I mean, versus someone traveling to a country once every month or so." All three proved successful and will be discussed in Chapter 8.

The optimal result for globalizers was the combination of a global presence and local feel that "acts" like a local company but with the products, systems, processes, and branding of the global group behind it. Many participants commented on this, both globalizers from the emerging and developed worlds. An example of this is seen in Lafarge's Indian operations discussed in Chapter 7—the Indian company feels like a local company but behind it stands the power and structure of a huge global player.

One participant commented:

> The country needs to see the company as a local company and not as a multinational company coming in. One needs to shift the center of gravity. This is more than gaining control.

Another said:

> We have both local and international competitors, and so to compete against the international companies we only employ locals and say we are local. At the same time we are bigger than any local players. Against the locals, we can bring best international practices when it comes to our wholesale business and when it comes to retail we have international products. So when it comes to it, we give the local company an international flavor and the international company a local flavor so we play the game of best practice. We keep it local with best international practice at a local level.

This ability to be global and feel local proved to be a key success factor in ensuring acceptance in the local market regardless of the mode of entry.

Resource allocation

The amount of resources necessary for FDI varies depending on the type of organization and entry. An agency agreement requires up front time but less ongoing financial investment. Joint ventures vary widely with the establishment of a manufacturing operation requiring significant management time not only in finding the right joint venture partner but also in setting up the operations all without the influx of revenue. The same is true of greenfield investment. But it is a misconception to believe that greenfield investment and joint ventures are the only modes of entry involving a significant up-front outlay without the benefits of cash flow. An acquisition requires significant management time in finding the right target as well as the up-front and ongoing implementation time and costs. At least there is a purchase of cash flow to help alleviate some of the financial burden albeit usually at a premium.

Having the correct internal resources is also an issue for market-entry choices. The organization may not have the skills and competencies in-house to proceed as a greenfield investor at that stage of their development or for that specific market—whether it be management skills, languages, or local market knowledge. In these cases, the ability to "go greenfield" is greatly impeded without buying this knowledge via the locally hired workforce. Those organizations with fewer financial resources tend to partner rather than own outright an overseas operation, as the pooling of resources is the least expensive and most efficient option for entering a new market all the while sharing financial risk (Couturier and Sola, 2010). If an organization is lacking in one or more business aspects necessary for success in that market, it will tend to partner with another firm that provides that skill. It is more effective than acquiring when there is only a limited resource that is lacking—in those cases acquisition would bring a greater duplication of resources.

This is seen in Case 4.1, Teva, the world's 12th largest pharmaceutical company, who early on in their organizational growth had to pursue joint ventures to compensate for a lack of requisite resources when internationalizing. As they grew, they developed the skills internally and moved more heavily toward acquisition-based expansion. Coming full circle, they are now partnering again in high-cost ventures such as biotechnology development in order to share risk and costs.

Several of those interviewed commented that the amount of management time necessary to complete an acquisition is significant regardless of the transaction's size, thus they only pursue deals of a certain threshold. One Japanese participant said, "Although M&A is always one of the options of business expansion, we believe that if M&A projects are not over a certain size, the management resources required would not match expected benefits." Another participant commented, "We tended to actually decrease in number because we try to buy bigger acquisitions than smaller ones in the last few years, and I think that's the trend simply because we're an $18 billion corporation these days. And trying to move the needle just doesn't happen with $1 million acquisitions." Yet another commented:

> I am not a fan of small deals and it is not just difficulty, it's the chances of success. When you buy a small deal, a lot has to "go right" for it to grow into something important. I mean whether the deal is a $100 million company or a $5 million company, the due diligence is typically not too different; we go through the same process. Sometimes the business is so small that it doesn't survive the "bear hug" in the integration phase.

Acquisitions were not the only entry mode seen in this light—another participant made the same comparison with joint venture partnerships, saying:

> It's very hard for me, in my mind, to think about JVs with small companies … it's going to be the same amount of work, the same kind of over-communication and managing expectations [as with a big company]. So I think JVs are one end of complexity on an extreme complexity, time consuming. I would rather just acquire a company and then decide what to do with it.

Additional issues to consider in entry-mode choices

As mentioned previously, research has found there are several issues one should consider before deciding on a mode of market entry in order to optimize success in addition to those outlined by the survey participants. These include openness of the market to foreign ownership, corruption, level of market competition, market risks, managing intellectual property rights, and intangible resources.

Openness of market to inward investment

There has been a general liberalization of world markets over the past decade with more countries allowing controlling interest in joint ventures, wholly owned subsidiaries, and the ability to acquire outright indigenous organizations (UNCTAD, 2010). Indeed a large portion of FDI can be attributed to the privatization and liberalization of formerly closed markets such as China, the former Eastern Bloc, and South America. There are, however, a considerable number of major markets that still do not allow foreign firms to invest outright in all industries. In fact, almost 90 percent of the world's economies restrict outright foreign ownership in some domestic industries; those most heavily protected include electricity, transportation, and telecommunications/media (World Bank Report, 2010). Some of the countries restricting foreign ownership include Canada, Indonesia, Japan, Malaysia, Russia, France, China, Mexico, the Philippines, and Thailand with the latter four being among the worst offenders (ibid.). Many protect certain industries under a banner of "national security" as seen in China (ibid.). In these circumstances, FDI can't be wholly owned; therefore, if one wants to operate in these countries in certain industries, some form of collaboration with a local partner must take place.

Other geographies are so complex they make local operation almost impossible to the outsider. Brazil was cited repeatedly by survey participants during this research as being the most baffling of locations in which to conduct business—it is riddled with difficulty in establishing a foreign entity (on average half a year to establish a foreign-owned subsidiary), restrictions on nationality of board membership and executives, and tight restrictions on foreign companies' abilities to operate across all sectors (World Bank Report, 2010). One participant lamented:

> I think the biggest issue in Brazil is around the tax laws. Effectively you can be selling a product, the same product, and be selling to three or four different states within Brazil and you'll pay different taxes. And it can vary depending upon how you shipped it and all sorts of things. And it's not just one tax; it's three or four different taxes. So you'll have a tax where you're coming from this state and going to State B so that's one tax. If you're coming from State C to State B it's different tax. If the product changes slightly, it's different. Is it packaged; is it not packaged, tax changes. It is very difficult to function.

Another participant added about doing business in Italy: "Italy, that's the only country, by the way, I've never made an acquisition. I mean, every time I try to buy something in Italy it's got to the third set of books and every time I walked away and said okay I'm just waiting for the fourth set. I can't cope with this." In these cases, joint venture with a local partner who understands how to conduct business is sometimes the easiest approach.

The inability to operate globally on a free basis was noted by several of the participants both as a risk and a challenge. Several of those interviewed operate in sectors heavily regulated where ownership is restricted, including BT, Cargill, BAe, and Tele2. They felt the frustration of being unable to operate in many jurisdictions especially when foreign entities were able to enter their home markets freely. One participant commented, "We recently paid about $1 billion to increase its ownership stake in its listed Indian operations from 55 percent to 75 percent. When the Indian authorities saw this,

they changed the law to not allow foreigners to own more than a 75 percent stake in Indian companies."

Corruption

Corruption is seen as the abuse of public power for private benefit (Uhlenbruck et al., 2006) and is more prevalent in the developing regions of the world (Hellman et al., 2000). Researchers differentiate between pervasiveness and arbitrariness of corruption (Uhlenbruck et al., 2006). Pervasiveness is the likelihood that one will encounter corruption while operating on a daily basis while arbitrariness refers to how corruption varies in terms of reoccurrence and severity. Interestingly, while pervasive corruption may actually cost the organization more in real terms due to its widespread occurrence, arbitrary corruption has been found to be more damaging due to the capricious nature, as the former is seen more as an ongoing "tax" and can be controlled to some extent (ibid.).

Corruption systematically has been linked to lower levels of direct foreign investment and is causing globalizers to eschew those forms of investment that would require interaction with corrupt regimes (ibid.). Thus research has found the preferred mode of foreign investment in these circumstances is through nonequity investment, or in some cases the use of a joint venture partner rather than via a wholly owned subsidiary (ibid.).

Managing the expectations of alliance partners was considered a key challenge when operating in more traditionally corrupt parts of the world. Russia and Africa were considered the most corrupt environments in which the globalizers operated. The unyielding stance of adherence to the Foreign Corrupt Practices Act (FCPA) and its guidelines by globalizers was seen to dramatically slow down the process of expansion, but in the long run gave great transparency to the expected behavior of globalizers operating in those regions and helped in managing parties' expectations. One participant when grappling with the issue of corruption commented in hindsight:

> You get payments sometimes in places where they consider them quite normal not contravening any rules and regulations and we look at them and go, "Hmmm ... that may be alright here but under the bright lights of a [Western] ray doesn't quite stand up." They think they're behaving—it's like you're asking people we drive on the left-hand side of the road and they've been driving on the right-hand side of the road and you say, "Sorry you guys, we're all going to go on the left side of the road now. Well, there's nothing wrong with driving on the right-hand side of the road, it's just not what we do." And, that's tough. So you'll have to readjust and obviously explain and obviously get that ingrained into the culture of the company as it goes forward.

Alignment in terms of corporate governance was certainly a key finding for joint venture success especially in terms of partner objectives and ways of doing business that is discussed in Chapter 6.

Existing competition in the market

Existing local competition was seen to promote acquisitions as opposed to either greenfield investment or joint ventures. This is for three reasons. Firstly, with more competition, there is a great opportunity to find an attractive acquisition target that strategically fits the incoming acquirer. Secondly, in markets where there is a greater competition for scarce resources, acquisition doesn't heighten resource-seeking behavior as does greenfield investment. Finally, acquisition keeps the level of competition stable by not adding another competitor as would occur with organic growth. One participant commented about why his organization bought a competitor in the region, "We bought [the target] so we would eliminate a competitor that was starting to become threatening in the region, which was seen as very attractive to us."

Conversely, when the market is in its infancy and still growing, there is not a lot of choice in terms of acquisition targets, making acquisition, again, less attractive. In these cases, organic growth is seen as the best alternative. In many cases, time to market is seen as less important as the market is growing and the globalizer can afford to enter with a greenfield site.

Greater-risk markets

In those markets perceived as being higher risk due to political instability, market turbulence, government interference, or rapid technological change, joint venture is seen as being the preferred option (Couturier and Sola, 2010). Research has found that globalizers are less likely to invest via acquisition in those countries that carry significant "hazard risks" when compared to the globalizer's country of origin (Tsang and Yip, 2007). Instead they opt for a joint-venture arrangement in which the risk and rewards are shared. The same was found in service-based organizations; in those who perceived a high level of uncertainty and risk in the market, there was a greater likelihood of pursuing joint venture instead of either greenfield investment or acquisition (ibid.). This is logical—as service businesses possess less tangible assets that can be sold if necessary, the less risky option is to collaborate and share the spoils.

Intellectual property rights and other intangible assets

Intellectual property rights are a key constraint for overseas expansion in those jurisdictions without developed legal safeguards. Research has found that those organizations whose core products are intellectual property based are more likely to wholly own any FDI either via organic growth or acquisition in a new market rather than partner with a domestic business (Slangen and Hennart, 2008).

The same perception is held for other intangible assets held by the globalizer. If the organization holds key intangibles such as innovation- or technology-based assets, they are less likely to want to risk local partnering where they don't have full ownership control (ibid.). An example is research and development—those acquisitions with intense research and development are more likely to buy into a local market rather than partner.

Ironically, as will be seen in Chapter 10, advanced technology and knowledge transfer are the top reasons for wanting to partner with an incoming globalizer given by emerging market partners—others being strong marketing and brand management (Shenkar and Li, 1999). Local emerging world partners seek to learn from their globalizing partners both in innovation management and marketing, two areas they perceive themselves as weaker and from which they feel they can learn from globalizing firms.

Research has found that if an organization has a strong corporate culture or perceives itself as having distinct core competencies, it is more likely to want control when operating abroad. Thus, it is more likely to choose a wholly owned option, either greenfield investment or acquisition. This was seen in the survey participant JBS whose management attributes their acquisition success to implementing their streamlined, simple processes combined with their informal culture within their targets. They prefer wholly owned investments and choose acquisition for its speed over greenfield investment. Their acquisition of Swift is profiled in Case 9.2 of Chapter 9.

Thus the different modes of entry bring with them different strengths and weaknesses, which in turn differ for each organization. Over two-thirds of the organizations interviewed preferred one mode of entry above others with joint ventures clearly being the least preferred option. One participant commented, "It depends on the circumstances, we've done all [types of market entries]. If we're buying an existing business to bolt onto our own organization because it brings certain benefits, then we'll buy 100 percent. If we're starting something new or extending something into a new country, we would prefer a joint venture." Very few, however, had the luxury of only using one means especially as they operated in parts of the world where full ownership is not allowed.

The risks associated with the various entry modes are outlined in Table 4.3. While these are generalizations, they give some indication of the various risks associated with each entry-mode issue. Some operating environments may have increased levels of risk while others lower depending on the circumstances. The importance of each entry-mode issue will also differ between organizations and situation. For example, SAP will find resource allocation in terms of technology and intellectual property protection vitally important; for them outright control in the form of greenfield investment or possibly acquisition is likely to be preferable to joint ventures. Uniqlo (Fast Retailing) may find lower-cost sourcing or local market awareness more important in the specificity of fashion for that region; thus a joint venture or strategic alliance may be a better option. In any case, the choice of entry mode is the first major decision one takes when deciding to enter the market, and as such it creates a unique path.

Table 4.3 Issues of market entry and the risk spectrum

Spectrum of risk / Entry-mode issues	Low	Low/Medium	Medium/High	High
Speed	**Acquisition** Existing revenue stream and access to market	**Buying into ongoing joint venture** Existing revenue stream and time to market subject to modifications	**Joint venture with initial set up** Delays if no ongoing operations but faster than greenfield because of market knowledge	**Greenfield investment** Significant delay in set up and revenue generation
Control	**Greenfield investment or acquisition** Control is held by the internationalizer	**Joint venture** Control shared between partners in varying degrees and is higher if it does not include operational control	**Minority stake/control joint venture** Relinquishing operational control or a minority stakeholding in a joint venture	**Strategic alliance** Control is given to a third party to represent the internationalizer in the market
Local awareness (culture, market, political)	**Strategic alliance, joint venture, and acquisition** The local partner provides local insights; however, local knowledge is needed to pick the right partner/acquisition target in the first place			**Greenfield investment** The internationalizer must acquire cultural, market, and political knowledge or can buy it in through strategic hiring of key personnel
Resource allocation	**Strategic alliance** The local partner supplies the bulk of resources	**Minority stake/control joint venture** The local partner provides the bulk of resources, including management; internationalizer often provides technology	**Joint venture** Resource requirements are shared between the partners	**Greenfield investment and acquisition** Greenfield investment requires significant ongoing investment over a longer time frame. Acquisitions require financial investment and management time up front

(continued)

Table 4.3 Continued

Entry-mode issues \ Spectrum of risk	Low	Low/Medium	Medium/High	High
Risk (political, managerial, and economic)	**Strategic alliance** The local partner takes on the vast bulk of the risk but still at the risk of poor partner choice	**Minority stake/control joint venture** The local partner and internationalizer share the risk but still at the risk of poor partner choice	**Joint venture** While the partners share the risk, there is still the risk of poor partner choice, and if there is imported manufacturing, there is redeployment of fixed resources if there is a difficult problem **Acquisition** Has known revenue stream, supply chain, and labor costs, but post-acquisition implementation risks and poor target-choice risks	**Greenfield investment** Significant risks about impact of increased capacity, revenue timings and amounts, supply chain and workforce management

Source: Adapted from Hermann and Datta (2006).

Conclusion

The route to internationalization has changed significantly since its study as an academic subject began 40 years ago. Originally organizations were thought to internationalize along lines that were familiar to them: culture, proximity, language, or through networks of connections to avoid the liability of foreignness. Rapid world changes have meant this is not necessarily the case any more with organizations now being born global and opportunistic globalizers and as such not following traditional approaches. Five areas are seen to be fundamental when making the decision of how to enter the local market: speed, control, resource allocation, local awareness, and risk evaluation. From these, the globalizer can judge which approach is optimal for the situation. The various modes of entry are discussed in the following chapters.

Case 4.1 Teva Pharmaceuticals

Teva, the world's largest producer of generic pharmaceuticals, are the most global organization in the survey with 96 percent of their sales coming from outside their native Israel. They pursued global growth originally through joint venture, moving to acquisitions, and now they use a combination of the two. Their original venturing came out of necessity. Shlomo Yanai, former CEO of Teva, explained Teva's expansion and their initial use of joint ventures,

> Historically, when we were small we found that the core element of the business, which we needed and we didn't have, would take us a long time or was going to be very expensive. Then we would co-venture with companies to complement what we missed. For example, if we had a product but we didn't have the go-to-market assets, then we joint venture with a company that had these capabilities.

Once Teva grew their capabilities, they pursued less joint ventures and more acquisitions. Lately, however, they have begun using joint ventures again to share risks or development costs, which, in pharmaceuticals, can be very high. They have also returned to using joint ventures to provide complementary skills. Yanai continued,

> We pursue joint ventures when we think that there is some expertise or excellence that we don't have and it's much better to save time and to join forces together with that excellent or competent company in order to get a better result than doing it by ourselves. For example, we joined together with Procter & Gamble when we found that in a certain part of our business we needed branding power.

Teva have used joint ventures as a way to reduce risk when entering a market. One example is their market entry into Japan. At the time, Japan was the second largest pharmaceutical market in the world with only a 17 percent penetration of generic products; hence it was a highly attractive market for Teva. Due

to the difficulty in entering Japan as a foreign entity, Teva entered the market via a small joint venture. Yanai continued,

> We first did small joint venture [in Japan] because we said we needed a local partner to help us understand this market ... and for the next three years together we actually studied the Japanese generics market, and we did even a small acquisition just to test the waters. Only after three years when we really felt we understood [the Japanese market], and of course the opportunity showed up, we went for the major move and we acquired a company at the level of $1 billion.

Teva bought Taiyo, Japan's third largest generic pharmaceutical company in May 2011. In addition, Teva bought out their joint venture partner and merged that operation into Taiyo thereby creating a commanding position in the Japanese generic pharmaceutical market.

This case demonstrates two points. The first is using different FDI methods in order to best implement a corporate strategy. In the beginning, Teva used joint ventures to "borrow" the competencies of other organizations because they simply didn't have the resources internally. When they had sufficient resources to acquire targets, they used them successfully capturing technology, innovation, and market share. Today they continue to collaborate with other market-leading organizations when appropriate instead of bolstering their own competing resources internally. Rather they use those resources for other strategic opportunities. In some cases they do this to reduce risk and capital expenditure.

Secondly, Teva used joint venture as a means of learning about a very foreign market rather than entering blindly and buying without adequate market and cultural understanding. They entered Japan in a very limited fashion as they got to know its unique features and characteristics before ultimately pursuing a substantial acquisition. This supports one of the key success factors of the survey participants: those who have entered markets most successfully have done so with full knowledge of the local market.

5 Nonequity Modes of Investment

Introduction

There is no wider or more ambiguous subject in this book than the strategic alliance. Strategic alliances are the catch-all phrase used to suggest a long-term working relationship between two separate organizations. Outsourcing, long-term supplier relationships, licensing agreements, and agency agreements all fall under the heading of nonequity alliances—the organizations hold no equity in the other partners but can influence their actions. They differ from joint ventures and minority equity stakes that are the most common forms of equity alliances. Nonequity alliances are discussed in this chapter as is research on alliances that doesn't differentiate between alliance types.

General strategic alliance research

In research, there is often little differentiation between types of strategic alliances as many share the same similarities. Because of this, research on strategic alliances often fails to differentiate between the levels of collaboration or mutual reliance and characterizes them as the same. This oversimplifies the relationships and overriding factors that influence the success of the various types of alliances.

Strategic alliances, including both contractual and collaborative alliances (discussed later in this chapter), are the mainstay of emerging markets, accounting for over half of market entries into Latin America, Asia, and even Eastern Europe (Adarkar et al., 1997). There has been an explosion of strategic alliance activity in the past 20 years (Gulati, 2007) as markets have opened up for inward investment. Research has found that the world's top 500 global businesses have on average 60 *major* strategic alliances in addition to countless less strategic relationships (Dyer, Kale, and Singh, 2004).

Yet strategic alliance performance has been, at best, mixed. Some organizations have been able to parlay their alliances into financial success such as HP and Oracle who, because of repeated alliance value creation, realize share price gains simply upon the announcement of another alliance