gaining confidence and moving outside their domestic markets, investing internationally to become global players in their own right. Mega acquisitions that were once the domain of the developed world are now occurring throughout the emerging world, with an increasing number of EWGs participating, fueled by deregulation and relaxation of markets. It is a trend set to continue.

3 The Risks, Challenges, and Benefits of Being Global

Introduction

The organizations studied in this research are atypical of most businesses as they include some of the largest multinationals in the world. But even they began as purely domestic businesses at one point. This research began by trying to understand the mindset of the globalizers and the risks, benefits, and challenges they see when venturing overseas. From this the foundation is laid for understanding what choices they made when entering foreign markets and how they did it, whether it be through alliances, acquisitions, or greenfield growth.

How do participants see their businesses in a global context

The research began by asking participants how they viewed their organization—as a domestic, regional, or global player. Only a handful (7 percent) saw themselves as domestic players with international operations accounting for typically less than 15 percent of total turnover. A significant minority (32 percent) saw themselves as regional players. Of these regional players, one-quarter aspired to be global players in due course and stated that their longer-term strategy was to move from being regional players into the global scene. One Japanese participant commented, "Until now we have been a regionally based company centered in Asia, but our mid- to long-term target is to be the industry sector global leader and a truly global company." Those who didn't aspire to becoming global were pursuing greater saturation in their chosen region, preferring to become a "dominant regional" rather than try to compete on multiple fronts. In this way, they demonstrated "mini global" characteristics: that is, they concentrated their efforts in their specific industries and specialized in that region. That is not to say they didn't operate outside of that region, but that any external operations were designed to help promote growth within that geography. Standard Bank,

Bank of Nigeria, Lonrho, Santander, Evertec, and Tele2 all stated that their longer-term strategy was to remain a regional player and become increasingly dominant in that region. One regional player commented, "We recognize what we know and what we don't know, our in-house expertise. Our brand name is about [our region] so we are going to stay there." Several companies that had a more diverse product offering stated that they operated in specific markets or that they offered a hybrid approach. ITW, United Technologies, Centrica, British Aerospace, all operated in set "home markets" many centered on the Anglo-American axis. One participant whose company operates in 24 countries throughout the world commented, "To this day we are not a global company; we describe ourselves as international. To me global means you really are literally everywhere and there aren't many companies like that; consumer goods probably, oil, but not typical companies like us. We would describe ourselves as an expanding international company."

The global businesses had several key characteristics. Firstly they saw that while their customers had different product demands, the products they offered could be tailored to meet those demands with few wholesale changes. In many cases they could take a product being offered in one geography and roll it out in another with little change to the actual product itself, to their marketing platform or channels of distribution. Companies such as BP, Amcor, JBS, and Lafarge all deal in what is generally a commodity, which means it is universally marketable. Those interviewed also felt that there was a benefit in being global especially in terms of information sharing, cost savings, and intra-market management. Secondly, some companies such as BAT, BT, JTI, and Cargill had products that required little tailoring for the local market thereby making global expansion easier. Finally, global organizations held some kind of advantage that was replicable across borders; in most cases, it was superior technology. Companies such as IMAX, Arc International, Schaeffler, Hitachi, Sony, BAe, ABB, and Nidec held a technological advantage that could be transferred from one geography to another. Others such as Fast Retailing had a brand and style that could be translated into differing markets while Ford, SAP, and Experian held a unique product offering, which with tailoring could be applied to differing markets.

Thus, it seems there is a rational progression from being a domestic organization to internationalizing some if not all business aspects that may lead to becoming a "dominant regional" on the way to becoming a true globalizer in search of new markets. This growth pattern has undoubtedly been fueled by the economic turmoil of the past five years culminating in the dichotomy of growth between the developed and developing world seen since 2007 (UNCTAD, 2011). When speaking to the participants it is, without doubt, a leading cause of globalization and the recent move into the developing world. As one participant put it, "Everybody's going to look to the East for growth in the coming years. Well, I think it's fairly clear—you already see it at a political level, that the G7 has been replaced by the G20, so that the emerging markets are claiming their seat at the table." Another added:

> You see, here it's the uncertainty in the world economy and it makes the people uncomfortable. European growth is going to be less than what everyone thought five years ago and so you have large pieces of the world growing in low, low single digits and then you see the US, which is expected at 2 or 3 percent. Then you see Asia, in theory, still on a very high trajectory—that is, whether it's 8 percent, 9 percent, or 10 percent, whatever the growth projections are, they are fairly significant. You see the disparity and you see a lot of risk.

There was seen a tension between the enormous market size with growth stagnation in the developed world and the emerging world's smaller and immature markets exhibiting double-digit growth. And with them came additional perceived risks. As one participant said, "If you fail in the United States or Europe, it is not because of the markets." At this point, the high-growth, higher-risk markets are winning in the eyes of globalizers—over 80 percent of participants said their focus was on the emerging markets over the next five years.

Key risks

Respondents were asked what were the key risks and challenges associated with going global. These were numerous and fell roughly into five key categories: political, economic/financial, market, people, and internal intangibles management. No respondents had a simple answer to this question—all foresaw that the risks and challenges were complicated, numerous, and interrelated.

Political

Political risks and challenges included:

- ▷ Regulatory risks.
- ▷ Nationalism, including favoritism to state-owned or local companies.
- ▷ Government instability and the risk of nationalization.
- ▷ Corruption or the inability to operate fairly with local competition when not being corrupt.

These risks were especially notable when entering the emerging world, although nationalism was seen as a key issue still in Europe. One respondent said, "For us I really think the two biggest challenges when going overseas are regulatory and nationalism—they are the two things that must stand out." Related to nationalism was the perception of local bias against

foreign companies, which was seen quite acutely especially when operating in China and India. One European said of operating in a regulated industry outside their home territory, "The biggest issue we have in operating [in that territory] is dealing with the fervent nationalism that puts us at an automatic disadvantage." The frustration of having to compete with state-owned enterprises was apparent as indigenous competitors or those in partnership with Chinese or Indian companies were given preferential treatment over those considered "outsiders." One participant commented:

> They're not making it easy. Formally they say you will be treated in the same way as a domestic [company], but you cannot ignore that a country organization of a large international [player] will always be smaller than one who has India as his home country. After China not much can surprise you. I must say the only thing that surprises me here [in China] is the government is playing quite a large role awarding licenses. So, it's not only up to the [regulators] but also the different ministerial departments [which] also have to clear it—there you always come into more political arguments. Let's say bilateral relationships, treaties, as opposed to being judged on your own merits.

Furthermore, two participants lamented that due to Chinese "strategic industry" restrictions, they weren't even allowed to operate in their core businesses in that country. One said, "China is a very attractive market for us, but sadly, we can't participate in it as the government has declared it off limits."

Political stability and changes in legislation was also seen as a risk for operating throughout the world. Political stability was seen especially in the emerging world where there hung the potential threat of regime change or nationalization of assets. One participant commented, "One of the benefits of being throughout the region is that we are less reliant on one country or one government in case it goes haywire. You only have to look at Northern Africa and the Middle East for that." Changes in legislation were also seen to be a risk when operating in Europe. One participant lamented that the change in European Union legislation had almost overnight cost his organization dearly. Another emerging market globalizer commented about European law, "It is so bureaucratic, half of it doesn't make sense—it is hard to see how it could get more complicated."

Government corruption was, not surprisingly, seen as a key problem for operating in developing parts of the world, and was especially noted in Africa and Russia. It is discussed more fully in Chapter 4. One participant, who operated in many emerging market economies commented,

> It takes a brave government official to try to bribe [one of our employees]. Take for instance bribery. Having our employee say to the person, "Sorry, I'm not gonna do that but let me just phone the [country's] president up and ask him if he thinks it's okay," is quite compelling although it is quite worrying when the president turns around and says, "Yeah, 'course it's okay!" But you know, that is one of the risks of doing business in [that part of the world] and you will always find it being pushed in your face; you have to just be careful. It's actually surprisingly easy to take the high ground so to speak, if you do things the right way ... you get a reputation for doing things the right way. And if they play by the rules they can make money as well. So that takes longer. I'm sure we could have [got our last operating license] done it in a tenth of that time if we'd been willing to make a payment to someone but we don't do that, so we just stuck it out and kept on filling the forms in and saying, "Are we ready yet? Are we ready yet?" And when she said, "No," "Okay then," and you just keep going. But that is a risk and I think it's a risk for any business that doesn't really understand [the region]. And that's where some of the businesses wanting to do business there see that as being a challenges barrier.

Economic

Economic risks and challenges discussed were:

- ▷ Cost fluctuations, including rising labor costs in low-cost manufacturing sites and keeping control of diverse cost structures.
- ▷ Availability of reliable suppliers.
- ▷ Economic slow down, lack of market growth, or stagnation.
- ▷ Scarcity of good acquisition targets.

Overwhelmingly (80 percent) of participants answered that their growth plans were focusing investment on the developing world, as it was possible to achieve much higher growth rates than in the developed world. Interestingly, emerging world companies also were focusing on their developing world counterparts, but also indicated that if developed world opportunities arose they would be pursued as well. While Brazil was seen as a country of interest, the high costs of labor, energy, and transportation were seen as particular challenges.

Related to the aforementioned closed market issue, six participants discussed the challenges of trying to quickly enter a market through acquisition and being unable to do so either because of government restrictions (e.g. India) or because there were simply not enough suitable targets. This could be related to the markets being too immature, too fragmented, have insufficient ways to value businesses in that arena, or there was simply a scarcity of targets large enough to be appealing to these globalizers. One Japanese participant said, "In Japan, hostile takeovers are difficult, but forward-looking M&A cannot be easily implemented. There are usually only but a few good existing businesses in the emerging countries. Therefore, we believe that good projects tend to be found in the West [US and Europe]." Another commented, "Acquisitions all require the same basic amount of management time and resources in sourcing and implementing them. In the developing world there are just simply not enough choices of size to be

interesting to us—we want scale." Still, one further added, "M&A is slow in terms of a source of growth at the moment, but probably more because of scarcity of good targets."

Social or market based

Social- or market-based considerations include:

- ▷ Lack of deep market or customer knowledge.
- ▷ Lack of local understanding: culture of the country, partner- or target-selection risk.
- ▷ Product differentiation.

The risk and challenge most mentioned by participants was that relating to social or market issues (56 percent). This primarily was based around an inability to gather true and deep knowledge about new markets, their customers, product preferences, competitors, and cultural differences that exist between the globalizer and the new market. Respondents throughout the world's regions mentioned this as a serious challenge when embarking on globalization. An example is seen in a story told by one participant, a native Spanish speaker, as he talked about his experiences as an American, trying to sell in Latin America:

> In Latin America, you know, you can talk over the phone but only after they meet you. Face-to-face relationships seem to mean so much more—face-to-face and trust and references. So it is a lot more relationship based than may be in other places. I remember going to Columbia just when I joined the company and it was our first meeting with this potential customer, and we were there for three hours and no one was talking about business. They were, like, making jokes, and I was so out of place because, you know, I just came from the US, right? I just flew seven hours here, and we are still not talking about what we are going to accomplish. We have a little bit of the "PowerPoint" culture, you know in the US—people like to have some type of structure to follow and PowerPoint helps people have some kind of structure to the discussion. And this is not like that at all here.

How globalizers dealt with this lack of knowledge, however, differed. As will be discussed later, some partnered with a local firm that had local market knowledge while others acquired a local firm. This raises the corollary question of knowing which is the right firm with whom to partner or buy, which was also a point raised by participants. To avoid this, a small but significant number of participants took a longer-term perspective and established a local presence to understand the local markets more fully before doing anything. Still others used their networks and time to learn as much as they could before committing significant resources. This approach will be discussed more fully in Chapter 5.

People management

People management issues were more apparent as a challenge than a risk with 44 percent of respondents indicating this was an ongoing matter. The most commonly indicated HR risk was attracting and retaining the right employees, especially local senior managers, in emerging markets. "The local markets are so competitive right now, it is hard to find good managers who have both technical and language skills. Those we do have know how valuable they are and switch jobs [easily]." Employee engagement and the ability to get new employees to understand and embrace the company's corporate culture were also seen as issues to several of the study participants. One participant explained:

> Talent is the essence of this overseas expansion. They need to be able to move across boundaries and borders; understand people, cultures; and build a local organization. It is not always easy to find these kinds of people. We grow talent so we look for employees who fit the business culture first not those who are "well connected," in fact we are wary of people who are well connected politically and rather would hire people who have a business fit and then build trust—and trust takes a long time.

Senior- and middle-management retention was a major concern especially in the developing world where talented multilingual managers were able to command a salary premium. One European company operating in China told of being unable to find a middle manager for their Shanghai operation for a salary of US$120,000 per year plus a car. He said:

> The key point will be at a certain point in time whether there is enough labor, qualified labor, in China for these managerial challenges. Because just paying $120,000 and you have somebody who speaks English well but he hasn't got the skills. You don't want to do it.

In addition, managing global HR practices and talent across the organization as a whole was seen as a critical challenge especially for Japanese companies participating in the research. All but one indicated that attracting and retaining senior management was a challenge. As a group, though, those interviewed understood this and were proactively addressing it through a variety of means, including locating their headquarters in more central locations, actively seeking out a diverse managerial workforce, promoting the non-Japanese into high-visibility roles, and extensive managerial and cultural awareness training.

Others included how to manage human talent across the organization as a whole, ensuring the correct skills were being deployed at the right locations. Still others included how to measure HR talent and improve HR systems to meet the wide range of skills needed and possessed by the organization at any one time. Increasingly global businesses are requiring an

ever increasingly international managerial workforce. Some manage this by proactively moving their workforce throughout their global operations—it is expensive but does create a "world citizen" who is culturally adept in the end. As one participant phrased it:

> We want diversity and train our people to give them a different experience by which you make sure that everybody has a very diverse experience when they grow in [our company]. Now, we also take executives from the countries that we operate and move them to other locations. We are going to move our people as much as we can, in order to give them the most varied experiences within [the company]. It's the way to disseminate the best practice, to mix cultures, and to make sure that we benefit from diversity.

Intangibles management

The aforementioned challenges are not altogether surprising when dealing with the complexities of a transnational business. Perhaps what were more interesting were the intra-organizational coordination challenges that participants discussed. They included:

- Managing intellectual property risk.
- Striking the balance between centralization and decentralization in management and information.
- Sharing of knowledge, human resources, innovation, research and development, and capital across the organization as a whole.
- Making priorities in capital expenditure.
- Ensuring clients were being serviced consistently well all over the world.

Not surprisingly managing technology and intellectual property (IP) rights in parts of the world that have immature or ineffectual legal protection was seen as a major ongoing challenge for some organizations especially those whose key product offerings were in that sector. One participant whose company held proprietary technology said, "R&D is centralized [at our headquarters] because here again it is language. Also I would have never put it in China because everyone would have it, maybe in ten or 20 years!" Another said:

> What concerns me the most is really the IP laws and how that affects the economic position quite honestly. If the IP is protected, I still think Europe and the United States will still have a major, major role in terms of economic position even if China does overtake us both; but, you know what, to me it becomes who is really the innovator and the technology driver. But, you know, I am a little bit worried about some of the technology protection and piracy issues ... which could significantly minimize Europe's and US' position even if they are the technology innovator.

Several participants spoke of the inherent difficulties of how one managed a transnational company of this size and complexity. Not only were the obvious choices of coordinating managers and human capital around the world ensuring the proper skills were held in the needed locations, but issues such as how to ensure knowledge and innovation management were also fully exploited.

In addition, the difficulty in how to prioritize capital expenditure was seen as a major challenge as was the corporate sharing of capital among operating units. Another participant raised the issue of the inherent tension between how far one centralizes information and operations knowing that the further the operations are centralized the more global coordination one can achieve. But in doing so one potentially loses touch with the individual market nuances that were seen as a major challenge previously and critical to country-specific success. One participant commented:

> Striking a balance between centralization and decentralization in terms of the uniformity of the brand and the degree of localization in each market is a major challenge as is how to share knowledge of each country with each other. We aim to maximize thoroughness of global policies with local implementation.

Another participant said:

> I think [balancing global versus local] is the biggest challenge because you know the constant balance you're trying to strike is how much you allow local management determine "broader policy" and how much you impose central thinking in the interests of economy of scale. And I think that's the constant balance you have to strike. But if you give up on local knowledge then I think you run the risk of doing all the wrong things without really understanding the local position.

The two issues that the survey participants indicated were the most pressing were control and universality of product. If one takes those as the two parameters, certain modes of entry are preferable when entering new markets (see Diagram 3.1). If the globalizer desires absolute control, then the options available are only acquisition or greenfield investment. If the product requires a fair degree of modification, then acquisition is the most sensible route to market—the globalizer can ensure the product is tailored for the local market and customers' needs. If there is universality to the product that means it is able to enter the market quite quickly—that is, if it is a commodity or relatively homogenous product—then greenfield investment is suitable.

If the globalizer does not require outright control or does not want to spend the resources in order to obtain it, a partnering option is more appropriate. If the product does require modification for the local market, then working with a local joint venture partner is probably the best option. They will already understand the local market and may have existing channels of distribution and customers in place for the product. In those cases in which

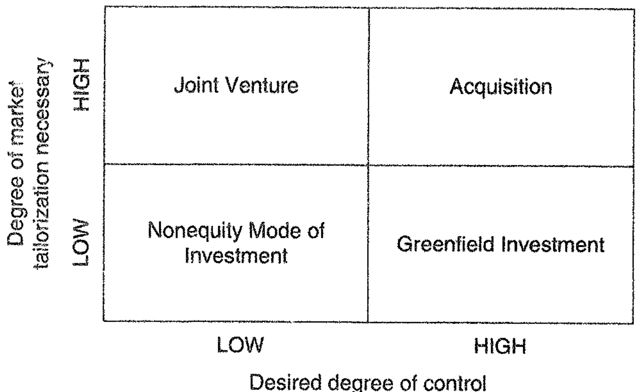

Diagram 3.1 **Entry-mode choice and its relation to market tailorization and control required**

the product being offered is more universal, it is possible to enter into one or more nonequity modes of investment in order to develop long-term relationships. These could include licensing or an agency agreement.

So why go global?

Bearing in mind the significant risks and challenges highlighted when going global, respondents were asked what benefits they saw in global expansion. The answers fell into several categories: the opportunity for global growth and entry into new markets, the diversification of geographic risk, access to more diverse human resources, ability to serve global customers more effectively, and finally market perceptions.

Market entry

Without a doubt the overwhelming benefit of going global was seen to be the ability to enter new markets and thereby expand one's top-line growth. This was seen especially by Anglo-Saxon and European companies that were expanding into the developing world in reaction to the recent economic downturn impacting North America and Europe. The reverse was also seen by emerging world globalizers who were entering mature markets in search of market share and more stable markets.

Risk reduction

Related to top-line growth was the desire to reduce cash flow and market risk by operating in a diverse array of markets. Previously organizations indicated they were able to reduce cyclical and market risk by industrial diversification; now geographic diversification was seen as being a preferable alternative (Chen and Findlay, 2003). One participant said:

> You are part of a global market but there are regional differences and, therefore, [internationalization] gives us some balance in the business, which we would never have otherwise. It is not just economic but regulatory balance and also sovereign risk. So to be in multiple countries, have optionality for investment; for governments to realize we have optionality is part of the rationale for being in more than one place.

Others concurred, acknowledging that the risks of operating in a high-growth market comes with higher risks that can be tempered by lower-risk markets such as Europe and the US, which at the moment are not yielding robust positive growth. The inherent tension of operating in a high-risk/high-growth market is balanced by operating in more stable economies. One participant said:

> One of our shareholders said we should sell our assets in the US and concentrate on the developing world, and I said they are stupid. The emerging world is dangerous. And we are still not that well protected, there are so many risks. The Chinese could just nationalize everything, and you just lose what you have created and that will never happen in the US or never in Europe. So you need to keep business in these countries.

Acquisition of human resources

A small but significant number of respondents rated the ability to attract diverse human resources as being a key reason for global expansion. Interestingly, all those who responded as this being a key benefit were Japanese companies. Survey participants understood that in order to further expand globally employees needed to have a global mindset that went beyond a cultural setting. In addition, there was an acknowledgment that marketing to a global audience required a multiculturally diverse management team. One participant, JTI, indicated that a main objective of internationalization was to enhance the globalization of their organization. To facilitate this they established their international division headquarters in Switzerland and radically diversified their executive board of directors. It has lead to a board of 17 people consisting of 12 different nationalities, making it one of the most diverse boards of any major company in the world.

Ability to better serve global customers

Every participant interviewed whose organization's main focus was service provision indicated the ability to better serve their global customers as a

key reason for global expansion. In essence they had no choice in order to remain competitive. As their customers increased their global footprint, the service providers needed to follow suit. As one service provider commented, "The more integrated and global our customers are the more integrated and global we have to be—a global business model requires a global presence." In many ways following customer expansion makes a service-providing organization's transnational expansion much easier if one is planning on greenfield investment. With an existing customer base, the service provider has instant revenue stream and legitimacy in the new market. One commented, "Multinational corporation customers help—they want to deal with us all over the world so we can follow key customers [into a new market] and that helps us with the initial set-up volumes."

Market perceptions

One of the great arguments for corporate diversification was to reduce risk related to operating in a specific geography; risk was seen to be spread across a variety of industries. The financial markets still desire a reduction of risk, but instead of rewarding industrial diversification, they are now rewarding those organizations that are able to achieve that risk reduction through global diversification. Indeed they should; research has found that international firms outperform their purely domestic counterparts (Hitt, Hoskisson, and Ireland, 1994).

One example is the cinema industry. As seen in Table 3.1, Cinemark has less than 60 percent of the screen capacity of Regal yet their market capitalization is over 30 percent larger. Cinemark, however, have operations in 14 countries throughout Latin and South America, as well as their US operations giving them access to high-growth markets such as Mexico and Brazil. The comparison of IMAX with their proprietorial technology may not be exactly applicable; even so, IMAX have one-eighth the number of screens of Regal yet their market capitalization is almost two-thirds of Regal's value. IMAX's wide geographic exposure especially in high-growth markets such as China gives them investor preference. As IMAX's Greg Foster put it, "Why China, Brazil, Russia? Wall Street loves global. You have to be relevant and global is relevant. And by the way, the Street will give you credit for having that as a strategic objective versus actually literally making it happen."

Thus, global is seen as attractive, relevant, and above all else inevitable in certain industries that are perceived as being capable of internationalization. In those cases, companies are penalized if they *don't* go international. As we have seen *why* one goes global differs from *how* they accomplish this. Organizations can choose a myriad of options in the pursuit of globalization such as acquisition, joint venture, and greenfield growth in order to achieve the organizational objectives. And these differ depending on a host of factors, including region, size of transaction, and skills held by the various organizations.

Table 3.1 Market perceptions of publicly quoted cinema chains as of December 1, 2012

Company	Country of origin	Number of screens/and theaters	Number of countries in which it operates	Market capitalization
Regal Entertainment	USA	6,550 screens	USA	2.27 billion
Cinemark	USA	3,825 screens	USA and 13 others	3.06 billion
IMAX	USA	583 screens	USA and 47 others	1.40 billion

Conclusion

There are a variety of risk factors that globalizers must contend with in their overseas expansion that can be generalized as being economic, political, social, people-based, and intangibles management. The irony is that globalizers often venture out to secure those exact resources that can cause risk in the first place such as more diversified management, new product and technology, and the mitigation of political and economic risk. The overwhelming reason for venturing abroad has changed from lower-cost manufacturing locations to domestic market penetration due to the opening of markets. The methods for expansion are discussed in the next chapters beginning with market-entry modes.