In a world characterised by fast-moving developments in business and industry and elsewhere, internationalisation is a pervasive phenomenon. So are digitalisation of business and the increasing trend of reaching out to partners in cooperative relationships. All these are the issues that come to the fore in the case of an organisation such as Ranbaxy that we highlighted at the beginning of this chapter. Internationalisation and digitalisation are glamorous strategic options in many ways. Organisations adopt them many a times because it is the in-thing to do. Yet, there are myriad challenges and pitfalls. It requires a high level of business acumen to succeed. Cooperation is seen as a viable option to competition in today's business world. In fact, the three strategies of internationalisation, cooperation and digitalisation have much in common and support each other as strategic alternatives. This chapter will discuss many of these issues and more.

6.1 INTERNATIONALISATION STRATEGIES

International strategies are a type of expansion strategies that require organisations to market their products or services beyond the domestic or national market. For doing so, an organisation would have to assess the international environment, evaluate its own capabilities and devise strategies to enter foreign markets. There are several entry options that an organisation can choose from, as we will see shortly, ranging from exporting to setting up wholly-owned subsidiaries. Then the organisation would have to implement the strategies and monitor and control its foreign operations. In this manner, international strategies require a different strategic perspective than strategies that are formulated for and implemented in, the national context. Let us begin by looking at the larger context in which the international strategies operate.

Context for Internationalisation Strategies

International trade and investment have grown dramatically since the end of World War II. There have been several factors that account for this growth. The major factors are the technological developments reducing the transportation costs, improvement in communication technology enabling better contact between trading and investing nations and the policy-induced trade liberalisation leading to lowering of barriers to international trade and investment. The tariff rates on trade have fallen and restrictions on cross-border investments have eased considerably, creating a global environment conducive to increase in international trade and investment.

The two trends of lowering of trade and investment barriers between nations and the easing of regulations governing trade and investment have led to intensification of globalisation of production and markets.[2] Globalisation has emerged as a potent force owing to global integration—the intensification of economic linkages among nations—and the internationalisation of markets, trade, finance, technology, labour, communication, transportation and the economic institutions.[3]

The globalisation of production and markets has a profound impact on the corporate strategies of organisations. Taking advantage of lower tariff barriers and ease of cross-border investing, organisations can disperse production at locations where they can reap economic advantages. Similarly, organisations can market their products and services across borders owing to the ease of transportation and communication.

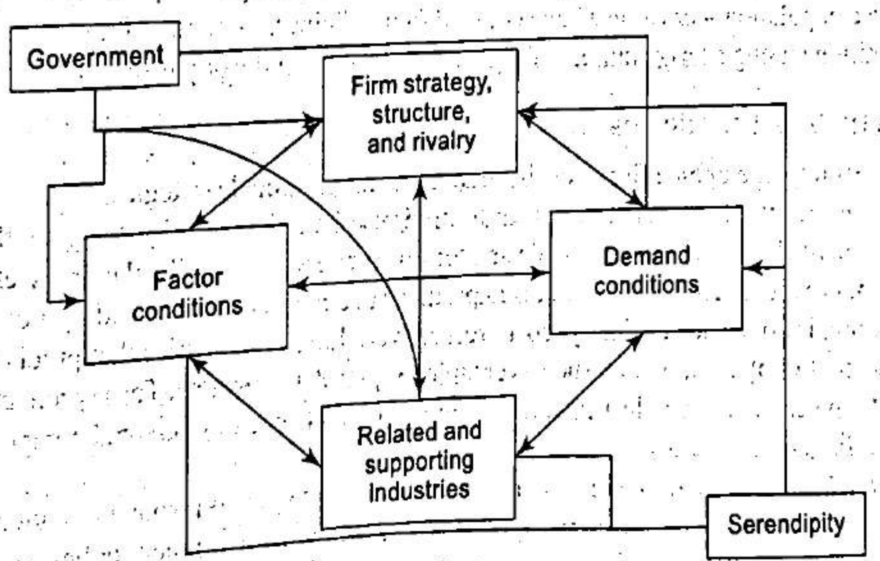
International economic dynamics accompanied by geopolitical changes, over the past several years, particularly since the oil crisis of 1973, have changed the paradigms of international business. In the context of a changing international environment, nations need to identify the industries and businesses that their firms need to focus upon to gain a competitive edge. We see next a model that seeks to explain why some nations may possess competitive advantage in particular industries and how firms in that nation endeavour to utilise that advantage.

Porter's Model of Competitive Advantage of Nations

Porter, in *The Competitive Advantage of Nations*, has extended his idea of the competitive advantage of firms to the analysis of competitive advantage of nations,[4] later extended in his 1998 book on competition.[5] In his opinion, four national characteristics create an environment that is conducive to creating globally competitive firms in particular industries. These four national characteristics are also interrelated as shown in Exhibit 6.1, in the form of a diagram popularly known as the Porter's diamond. The four factors are called the diamond determinants.

1. *Factor conditions* The special factors or inputs of production such as natural resources, raw materials, labour, etc., that a nation is especially endowed with.
2. *Demand conditions* The nature and size of the buyer's needs in the domestic market.
3. *Related and supporting industries* The existence of related and supporting industries to the ones in which a nation excels.
4. *Firm strategy, structure and rivalry* The conditions in the nation determining how firms are created, organised and managed and the nature of domestic competition.

Exhibit 6.1 The Porter's diamond



Source: Adapted from M.E. Porter, 'The Competitive Advantage of Nations', *Harvard Business Review*, March-April 1990, p. 77.

Based on an analysis of these four sets of factors, a country can determine the industry or industry niche in which a cluster of companies that are globally competitive can be developed. But doing so is a task that requires concerted and coordinated action on the part of the national governments and the business firms. Government plays a significant role in impacting these four factors. Chance or serendipity may also play a role sometimes, which may help to explain why a nation or geographical area with no apparent strength came to be associated with a fortuitous industrial concentration.

The diamond of competitive advantage can be viewed as instrumental to the creation of localised knowledge clusters, usually restricted to particular industries, which arise from the linkages among specific factor conditions, demand conditions, related and supporting industries and a particular configuration of firm strategies, structure and rivalry. The framework of Porter's diamond has in some cases been useful in explaining why internationally successful industries from a particular nation became globally competitive. This has largely been an outcome of favorable local diamond determinants. This has happened, for instance, in the case of the automobile industry in the U.S., leather industry in Italy or watch industry in Switzerland.

Porter defines a cluster as 'a geographically proximate group of interconnected companies and associated institutions in a particular field, linked by commonalities and complementarities'.[6] Here, it is fundamentally, conditions external to the individual firm that drive cluster functioning while many forces and actors influence the ultimate success of a cluster. These conditions may include specialised and advanced production factors, sophisticated demand, cooperative linkages with firms in related and supporting industries and intense domestic rivalry. The idea of clusters helps to explain, for instance, why are there so many factories making leather products at Agra and Kolkata or why safety matches units are concentrated at Kovilpatti and Sivakasi.

The remarkable growth of the Indian IT industry or the Indian pharmaceuticals industry can be partly understood and explained by the help of the Porter's competitive advantage model. The IT industry relied on the technical skills available at lower cost, high demand created by domestic companies offering software services to foreign firms and looking for outsourcing, existence of semiconductor and other supporting industries to manufacture computer hardware and the presence of IT clusters at many cities and the stiff competition that Indian computer companies experienced all through the 1990s. The Indian pharmaceuticals industry got a tremendous boost all through the 1970s and 80s through the protectionist policies of the government, large population—creating a huge demand for medicines, existence of upstream supplier industries and competition among a large number of big and small firms in the organised and unorganised sector.

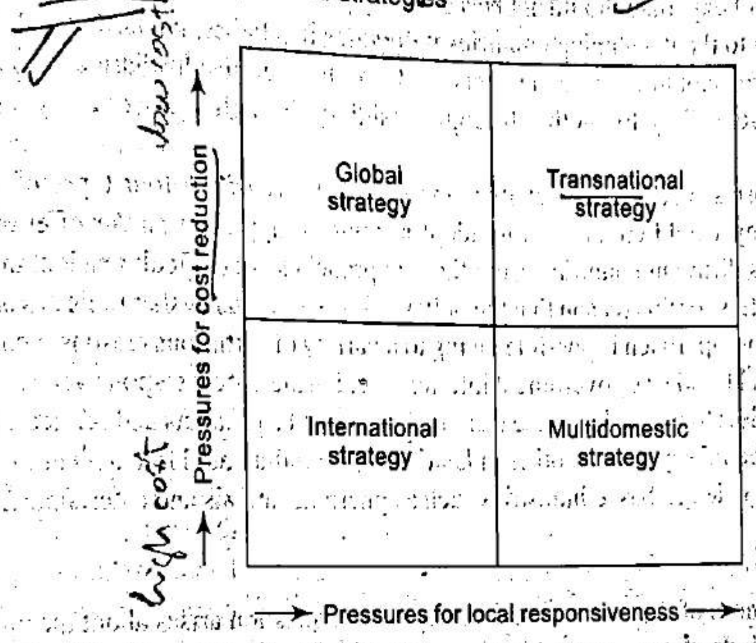
Types of International Strategies

Two sets of factors impinge upon a firm's decision to adopt international strategies:

- *Cost pressures* denote the demand on a firm to minimise its unit costs. By doing so, the firm tries to derive full benefits from economies of scale and location economies. Ideally, the firm seeks a single low-cost location, producing globally standardised products and marketing them widely around the world to achieve economies of scale. Typically, cost pressures are high in industries that produce products that have characteristics of a commodity such as chemicals, petroleum or steel. These products serve universal needs. Some category of industrial and consumer products such as personal computers or cameras too have similar characteristics.
- *Pressures for local responsiveness* make a firm tailor its strategies to respond to national-level differences in terms of variables like customer preferences and tastes, government policies or business practices. In doing so, the firm customises its products and services to the requirements of the individual country-market it is serving. A whole range of products and services like cars, clothes, food, entertainment or insurance face pressures for local responsiveness and firms have to tailor them to the requirements of individual country-markets.

Often the pressure for cost reduction and the pressure for local responsiveness act in a contradictory manner—minimising unit costs may not be possible when products and services have to be differentiated across countries.[7] The juxtaposition of these two factors, as shown in Exhibit 6.2, leads to four types of international strategies.

Exhibit 6.2 Four types of international strategies



Source: Based on C.A. Bartlett & S. Ghoshal, *Managing Across Borders*, Boston, M.A., Harvard Business School Press, 1989.

According to Bartlett and Ghoshal, there are four types of international strategies: international strategy, multidomestic strategy, global strategy and transnational strategy.[8]

- Firms adopt an *international strategy* when they create value by transferring products and services to foreign markets where these products and services are not available. This is a simple strategy in the sense that an international firm, by maintaining a tight control over its overseas operations, offers standardised products and services in different countries, with little or no differentiation.
- Firms adopt a *multidomestic strategy* when they try to achieve a high level of local responsiveness by matching their products and service offerings to the national conditions operating in the countries they operate in. In this case, the multidomestic firm attempts to extensively customise their products and services according to the local conditions operating in the different countries. Obviously, this leads to a high-cost structure as functions such as research and development, production and marketing have to be duplicated.
- Firms adopt a *global strategy* when they rely on a low-cost approach based on reaping the benefits of experience-curve effects and location economies and offering standardised products and services across different countries. The global firm tries to intensively focus on a low-cost structure by leveraging their expertise in providing certain products and services and concentrating the production of these standardised products and services at a few favourable locations around the world. These products and services are offered in an undifferentiated manner in all countries the global firm operates in, usually at competitive prices.

- Firms adopt a *transnational strategy* when they adopt a combined approach of low-cost and high local responsiveness simultaneously, for their products and services. Dealing with these two often contradictory objectives is a difficult proposition and calls for a creative approach to managing the production and marketing of products and services. Bartlett and Ghoshal make a strong case for adopting the transnational strategy as they opine that this is possibly the only viable strategy in a competitive world. They feel that the flow of expertise should not be a one-way process from the transnational firm situated in a developed country to the developing countries it operates in. Rather, as Bartlett and Ghoshal suggest, a transnational firm should transfer the expertise from its foreign subsidiaries to its headquarters and from one foreign subsidiary to another foreign subsidiary through a process they term as global learning.

As you will note, Indian firms would find it challenging to adopt any of the four types of international strategies. For doing so, they would either need to adopt a low-cost approach and/or offer differentiated products and services across different countries. Both these approaches are difficult to adopt in the absence of the capabilities required. It is for this reason that the only world-class industry that India has is of software development. Here, a low-cost approach is possible owing to a variety of fortuitous reasons such as low cost, widely available expertise in IT and less government interference. Further, local responsiveness is not necessary in the case of software development due to the technical nature of IT products and services. Following a similar line of thought, one could say that the other industries where India could find a niche are the service industries, in general and knowledge-based industries such as pharmaceuticals and entertainment.

International Entry Modes

When a firm adopts one or more of the international strategies, the question arises about the mode of entry that the firm should adopt. Mode of entry means the manner in which the firm would commence its international operations. There are several entry modes, each with their own set of advantages and disadvantages. A firm would have to decide which mode suits its circumstances best before it could be adopted.

Root presents a three-part classification of entry modes, under which we could place the different entry modes mentioned by various authors.[9]

1. Export Entry Modes Under these modes, the firm produces in the home country and markets in the overseas markets.

(a) *Direct exports* do not involve home-country intermediaries and marketing is done either through a direct agent/distributor or through a direct branch/subsidiary in the overseas markets.

(b) *Indirect exports* involve intermediaries in the home country, who are responsible for exporting the firm's products.

2. Contractual Entry Modes These modes are non-equity associations between an international company and a company or any other legal entity in the overseas markets.

(a) *Licensing* is an arrangement where the international company transfers knowledge, technology, patent, etc. for a limited period of time, to an overseas entity, in return for some form of payment, usually a royalty payment.

(b) *Franchising* involves the right to use a business format, usually a brand name, in the overseas market, in return for the franchiser receiving some form of payment.

(c) Other forms of contractual arrangements such as *technical agreements* (for technology transfers), *service contracts* (for technical support or expertise provision), *contract manufacturing, production sharing, turnkey operations, build-operate-transfer (BOT) arrangements*, etc.

3. Investment Entry Modes These modes involve ownership of production units in the overseas market, based on some form of equity investment or direct foreign investment.

(a) *Joint venture and strategic alliances* involve a cooperative partnership between two or more firms, with financial interests as the basis of cooperation. (These entry options have been discussed earlier under the heading of cooperative strategies.)

(b) *Independent ventures or wholly-owned subsidiaries* are modes in which the parent international company holds 100 per cent equity and is in full control. Such facilities may be created either through a new venture known as greenfield venture or acquired through takeover strategies.

A firm contemplating entry into international markets has to weigh several factors before choosing one or more types of the entry modes. Normally, exporting and licensing are the easier initial options as these involve a lower level of commitment and hence, lower risk. Strategic alliances have proved to be a popular entry mode due to its several advantages such as facilitated entry into foreign markets, sharing the risks and costs of entry or using complementary skills and assets with strategic partners. But for a stronger presence, joint ventures or wholly-owned subsidiaries are required.

Born-global Firms Traditional theories in internationalisation strategy explain the process of firm internationalisation as gradual, where firms start as exporters and progressively move on the life-cycle trajectory to use strategic alliances and joint ventures and finally, to the stage of having wholly-owned subsidiaries. Accelerated internationalisation in recent times has seen firms jumping the queue to adopt a stage further on the life cycle. In this context, the *born-global firms* are 'business organisation that, from or near their founding, seek superior international performance from the application of knowledge-based resources to the sale of outputs in multiple countries.'[10] The born-global firms tend to be smaller firms formed by proactive entrepreneurs. This phenomenon is quite common among Indian expatriates. Typically, the born-global firms offer products and services that involve a substantial value added, often due to significant processes or technology breakthroughs. The born-global firm owner adopts a global focus from the outset and embarks on a rapid and dedicated internationalisation. In recent times, we observe the emergence of such firms that can possibly be explained by the ongoing trends such as advances in information and communication technologies, the increasing role of niche markets and the growth of global networks. All of these help in facilitating the development of mutually beneficial relationships with international partners.

Several foreign firms in India have taken the route of exports, followed by strategic alliances and joint ventures. With the liberalisation of government policies, reduction of stringency for foreign investments and the promulgation of the Foreign Exchange Management Act, the entry of international firms has increased. The Indian firms have also shed their inhibitions and, for reasons described earlier in this subsection, started moving beyond the national boundaries. The Indian software industry has also seen the emergence of born-global firms owing to a fortuitous juxtaposition of Indian entrepreneurs, expatriates and venture capitalists. An example is of the non-profit organisation, The Indus Entrepreneurs, founded in 1992 in Silicon Valley by a group of entrepreneurs, corporate executives and professionals with roots in the Indus region.[11] The Indian diasporas have made a significant contribution to the development of born-global firms. For instance, thousands of Indian IT professionals in the Silicon Valley in the U.S. have formed effective linkages to create IT services companies, several of which are born-global firms.[12]

Strategic Decisions in Internationalisation

There are three strategic decisions related to the international entry modes: which international markets to enter, when to enter those markets and on what scale.[13] We look at each of these strategic decisions.

Which International Markets to Enter? There are innumerable markets around the world, in more than 200 countries. Each of these markets has a different profile in terms of benefits, costs and risk. Clearly then, a firm contemplating internationalisation has to carefully assess the expected benefits of entering a market, the costs that are liable and the risks that are likely to be faced. A rational assessment of international market opportunities would call for a systematic analysis of the benefits, costs and risk of market entry and profiling of countries by assigning them ranking in terms of their attractiveness and long-term profit potential. But such a rational assessment might not really be adopted in practice. Entry into international market may occur as a logical outcome of the organic growth of a firm or just by happenstance.

The Indian pharmaceuticals industry has made impressive forays into the international markets in different ways. A research study into the phenomenon of internationalisation of the Indian pharmaceuticals industry offers an interesting insight by pointing out that more than 50 large and small Indian companies adopted internationalisation strategies during the decade 1990-2000. The international markets in which these companies entered are situated in the developing countries (55.2%), developed countries (37.5%) and the Central and Eastern European countries (7.3%).[14]

Timing of Entry into International Markets Having decided which international markets to enter, the next strategic decision is about the timing of entry. By timing of entry is meant whether the international entry is made earlier than other international companies or later than them. There are several first-mover advantages associated with an early entry, like that of registering presence by building the brand name, build up demand, sales revenue and market share and create entry barriers for other companies. But there are some disadvantages of being a first-mover as well, like that of facing greater risks and incurring pioneering costs.

Scale of Entry into International Markets The final strategic decision related to international entry is that of the scale of entry. By scale of entry is meant entry on a small scale with little commitment in terms of resources or a large-scale entry with significant commitments. A small-scale entry has the advantages of testing the waters before the final plunge is taken and the possibility of a reversal of the strategic decision if the entry turns out to be unprofitable. Large-scale entry has the advantages of impacting the local competition significantly in favour of the company and creating a major presence.

Advantages and Disadvantages of Expansion through Internationalisation

International strategies offer an attractive strategic alternative for expansion by firms and carries with it rewards in the form of lower costs, increased sales and higher profits. There are ample opportunities for economies of scale and learning. Above all, it offers what we could say, a glamorous option for expansion strategies and a promise of above-average returns. Some of the major advantages of international strategies are as below.

- *Realising economies of scale* By expanding sales volume through international expansion, firms can realise cost economies from economies of scale.
- *Realising economies of scope* Firms develop valuable competencies and skills when they operate in home markets and implement particular business models. When these competencies and skills are stretched by firms to operate in global markets and their business models are replicated, economies of scope can be realised.
- *Expansion and extension of markets* Economies of scale and scope enable firms to expand their markets from local to global markets, in a two-way beneficial relationship where the expanded markets enable the firms to realise lower costs and attain economies of scale.
- *Realising location economies* In the beginning of this chapter, we mentioned the Porter's model of national competitive advantage. There we saw how some countries are endowed with natural resources that provide them a national competitive advantage. This advantage can be utilised by firms to produce at lower cost or to use their low-cost advantage to provide differentiation or do both.

- *Access to resources overseas* By expanding internationally, firms gain access to resources overseas that they do not get when they operate in domestic markets only. Such resources can be natural, financial or human resources.

The advantages of internationalisation can only be achieved, however, by assuming a certain number of additional costs, like infrastructure costs and informational costs which are barely visible at a superficial level.[15] The latter costs have been most clearly demonstrated in the studies on the choice of organisational structure in the internationalisation process.[16] Such information costs tend to decline substantially with the accumulation of international experience. Many studies have therefore focused on the initial entry choices because they represent a critical learning phase.[17]

Overall, international strategies offer an attractive strategic alternative to firms. Yet, the cost of failures can be great. It is generally recommended that managers should be eager to pursue new international opportunities, but should be wary of over-expanding or overextending their firms, particularly geographically.[18] The disadvantages of international strategies lie in factors such as:

- *Higher risks* International expansion often entails a higher risk as compared to a situation where a firm operates only domestically. These risks are related to uncertainty in the economic and political environments of the host countries.
- *Difficulty in managing cultural diversity* International firms face challenges of managing cultural diversity within and outside. Within, they have to manage employees who come from different cultural backgrounds. Outside, they serve markets that may be very different culturally, from their own domestic markets.
- *High bureaucratic costs* Operating internationally requires an extensive coordination between the home office and the foreign operations and subsidiaries. These result in higher bureaucratic costs of coordination and communication.
- *Higher distribution costs* When a firm operates internationally and in order to utilise its home advantages, does not set up manufacturing facilities abroad, then supplying products might entail higher distribution costs. Even when manufacturing facilities are established in countries where markets for the firm exist, the differences in distribution channels might require higher costs to operate.
- *Trade barriers* Despite liberalisation of trade between countries, substantial trade barriers in the form of tariffs, pricing restrictions, differing standards or local content requirements exist.