# International Business Strategy

How can you best extend your knowledge of how multinational enterprises (MNEs) function? What does globalization mean for today's managers? How do students turn the messages from the academic literature into effective business strategies within an MNE?

This practical textbook shows how the key concepts from the business strategy literature can be applied to MNE management.

- MBA and Master's students will gain the practical knowledge and skills needed to succeed as effective managers in multinational companies through a critical study of mainstream strategy models and the analysis of forty-five key journal articles.
- More than twenty 'half-length' case studies from leading firms including Dell, Nike, Honda, IKEA and Danone show globalization in practice.
- Identifies seven central themes from the literature for successful global strategies and unifies them into a clear framework that can be applied to real businesses worldwide.

Alain Verbeke is Visiting Chair in Strategy and International Business at the Rotterdam School of Management, Erasmus University, Rotterdam, and an Academic Associate of the Centre for International Business and Management, Judge Business School, University of Cambridge. He holds the McCaig Research Chair in Management at the Haskayne School of Business, University of Calgary, and was previously the Director of the MBA programme at the Solvay Business School, University of Brussels (VUB).

# International Business Strategy

## Rethinking the Foundations of Global Corporate Success

ALAIN VERBEKE

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To my wonderful spouse Juliet and my children,
Raymond-Laurent, Mary-Claire and Sophie-Charlotte

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# Case studies

# About the author

Dr Alain Verbeke is Editor of the ***Journal of International Business Studies*** (Area Multinational Enterprise Theory and International Strategy) and an elected Fellow of the Academy of International Business. He is associated with the Centre for International Business and Management, Judge Business School, University of Cambridge (UK), and is Visiting Chair in International Business at the Rotterdam School of Management, Erasmus University Rotterdam (The Netherlands).

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Dr Verbeke has consulted widely for a variety of firms and public agencies, evaluating large-scale, strategic investment projects and restructuring programmes. His research and advisory work has involved numerous large multinational enterprises from Europe, North America and Asia. He has particular expertise in the linkages between multinational enterprise corporate headquarters and foreign affiliates.

# Foreword

Too many international business strategy textbooks slavishly adhere to mainstream conceptual models. The publication of those models in prestigious practitioner journals such as the *Harvard Business Review* seems to shelter them from scholarly criticism. The problem is that the policy recommendations derived from these models, while sometimes insightful, are all too often based on implicit and restrictive assumptions. They are frequently oversimplified and seldom based on a rigorous analytical framework that assesses the opportunity costs of following the recommended paths, that is the costs of foregoing alternative strategies.

In this textbook of unusual depth and scope, Alain Verbeke provides a critical reassessment of Theodore Levitt's famous edicts on global marketing, Michael Porter's diamond, Prahalad and Hamel's core competence, Bartlett and Ghoshal's transnational solution, and many other conceptual models that have until now been treated as almost sacrosanct. These mainstream views are not analyzed in isolation, but systematically within the context of a simple but insightful conceptual framework, which synthesizes several decades of scholarly research on multinational enterprise strategy.

In addition to solid conceptual foundations, this book provides a rich empirical background. Every concept is illustrated with examples drawn from actual managerial practice. The tight link between theory and practice makes for a powerful intellectual toolkit which can be directly used by senior managers as they weigh alternative global strategies.

As a scholar engaged in the comparative institutional analysis of multinational enterprises, I am struck by the ad hoc quality of much of the advice offered to senior managers. Too often such advice makes short shrift of the considerable body of theoretical insights and empirical evidence that has been amassed by international business researchers over the last decades. Not so with this book which shows, once again, that 'nothing is more practical than a good theory'.

**Jean-François Hennart**
*Fellow of the Academy of International Business*
*Professor of International Management*
*Tilburg University, The Netherlands*

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Charles Backman, Nathan Greidanus and Jeff Huebner provided fine research assistance. Intellectual exchanges with Markus Nordberg, Christos Pitelis, Bob Schulz, Paul Beamish, John Cantwell, Shih-Fen Chen, Anthony Goerzen, Ans Kolk, Sarianna Lundan, Anoop Madhok, Hemant Merchant, Peter Sherer, Steven Tallman, Ilan Vertinsky, Bernard Wolf, Bernard Yeung and George Yip helped me refine various components of the manuscript. Brad Abernethy edited the entire volume and greatly improved its language and style. Teri Bryant performed the last edit; her pedagogical insights helped to clarify and improve the text even further.

With pride, I acknowledge my former student and friend, Wenlong Yuan, whose assistance in writing the cases has been invaluable. He co-drafted all twenty-three cases in the book, and provided substantive comments on the manuscript throughout the writing process.

With abiding gratitude, I acknowledge my colleagues in international business, whose ideas have inspired the concepts developed throughout the text. First, my friend and mentor, Alan Rugman, with whom I have worked for more



 

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than twenty years. Second, John Dunning, Peter Buckley, Mark Casson, Jean-François Hennart, Julian Birkinshaw and the late Sumantra Ghoshal, whose brilliant conceptual ideas have greatly influenced my own thinking and writing on international business strategy. Third, my senior colleagues, Jean Boddewyn, Lorraine Eden, Arie Lewin, Klaus Macharzina and Daniel Van Den Bulcke, from whom I have learned much about collegiality, inclusion and institution building in the field of international business.

I should also like to acknowledge the hundreds of senior managers from around the globe who shared with me their insight and dreams of international growth for the companies they cherish.

Finally, I thank my wife and our children for their patient support. In particular, I am grateful to Sophie-Charlotte for her eager solidarity. Throughout this process, she sat shoulder to shoulder with me watching *Dora, the Explorer*. Embarked on separate adventures, we happily travelled together.

*Calgary, July 2008*



 

# Abbreviations

| | |
|---|---|
| 3M | Minnesota Mining and Manufacturing Company |
| A&C | Automation and control |
| AAFLI | Asian-American Free Labor Institute |
| AAU | American Asiatic Underwriters |
| ACLA | Acer Computec Latinoamerica |
| AIG | American International Group |
| ASA | alliance-specific advantages |
| ATM | automated teller machines |
| BEF | brightness enhancement film |
| BP | best position, best practice, and best performance |
| BP | British Petroleum |
| BPI | Beauté Prestige International |
| BSN | Boussois-Souchon-Neuvesel |
| C&C | computers and communications |
| CD | compact disk |
| CEO | chief executive officer |
| CMD | Committee of managing directors |
| CMR | California Management Review |
| CNPC | China National Petroleum Company |
| CSR | corporate social responsibility |
| CT | corporate technology |
| CTO | chief technology officer |
| CVCC | controlled vortex combustion chamber |
| DEC | Digital Equipment Corporation |
| DGC | Data General Corp. |
| EBC | European business centre |
| EDC | European distribution centres |
| EDLP | every-day low price |
| EMS | electronics manufacturing service |
| ERP | enterprise resource planning |
| EU | European Union |
| FDI | foreign direct investment |
| FMS | flexible manufacturing systems |

## List of abbreviations

| | |
|---|---|
| FSA | firm-specific advantage |
| GDP | gross domestic product |
| GE | General Electric |
| GM | General Motors |
| GMS | global manufacturing system |
| GNPOC | Greater Nile Petroleum Operating Company |
| H&C | Harrisons & Crosfields |
| HAM | Honda of America manufacturing |
| HBR | *Harvard Business Review* |
| HP | Hewlett-Packard |
| HPs | high potentials |
| HRH | His Royal Highness |
| HTML | hyper text mock-up language |
| HTTP | hyper text transfer protocol |
| I&C | information and communication |
| IBM | International Business Machines |
| ICJ | International Court of Justice |
| ICT | information communication technology |
| IE | Instrumentation Engineering, Inc. |
| IKEA | a major company manufacturing and selling furniture |
| IPR | intellectual property rights |
| JIT | just in time |
| JV | joint venture |
| KFC | Kentucky Fried Chicken |
| LA | location advantages |
| LB | location-bound |
| LCD | liquid crystal display |
| LNG | liquefied natural gas |
| LSID | Lake Stevens Instrument Division |
| Ltd | Limited |
| LVMH | Moët Hennessy Louis Vuitton |
| M&A | mergers and acquisitions |
| MBA | Master of Business Administration |
| MCM | multi-chip module |
| MIT | Massachusetts Institute of Technology |
| MNE | multinational enterprise |
| NAFTA | North-American Free Trade Agreement |
| NAO | North American operations |
| NCR | National Cash Register |
| NDG | Nippon Data General Corporation |
| NEC | Nippon Electric Company |
| NIOC | National Iranian Oil Company |

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| | |
|---|---|
| NLB | non-location-bound |
| NMC | Nippon Mini Computer Corporation |
| NPPC | Nestlé Purina PetCare |
| NUMMI | New United Motor Manufacturing Inc. |
| NYSE | New York Stock Exchange |
| OEM | original equipment manufacturing |
| OMR | organizational management review |
| P&G | Procter & Gamble |
| PCB | printed circuit boards |
| PCBA | printed circuit board assembly |
| PICC | People's Insurance Company of China |
| PTH | pin-through-hole |
| R&D | research and development |
| RTU | remote terminal unit |
| SAPREF | Shell African Petroleum Refinery |
| SBC | Sony Broadcast Limited |
| SBU | Strategic Business Unit |
| SCGP | Shell coal gasification process |
| SCR | Siemens Corporate Research |
| SISL | Siemens Information Systems Limited |
| SMI | Societa Metallurgica Italiana |
| SMR | *Sloan Management Review* |
| SMT | surface mount technology |
| SONAM | Sony Corporation of America |
| SOSA | Sony Overseas S.A. |
| SPDC | Shell Petroleum Development Company |
| SRI | Stanford Research Institute |
| SSA | subsidiary-specific advantages |
| SUV | Sport utility vehicle |
| TKS | time-keeping system |
| TPS | Toyota production system |
| TQM | total quality management |
| TSX | Toronto Stock Exchange |
| UK | United Kingdom |
| UNCTAD | United Nations Conference on Trade and Development |
| UNCTC | United Nations Centre on Transnational Corporations |
| US | United States |
| VLSI | very large scale integration |
| VTE | vocational training and education |
| VUB | University of Brussels |

(Compiled by: Charles A. Backman)

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# WALKTHROUGH

## Chapter 1

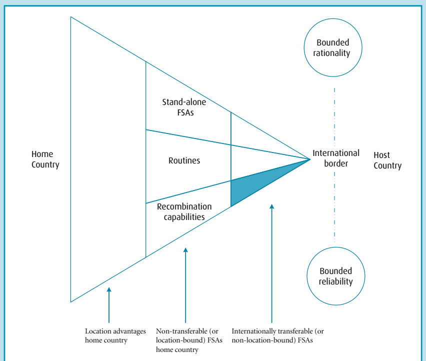
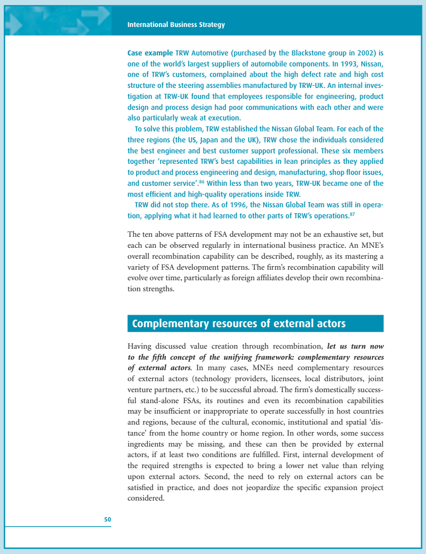



**Figure 1.1** Core concepts

*International Business Strategy* presents, interprets and critiques 45 seminal articles from the *Harvard Business Review*, *Sloan Management Review* and *California Management Review*. It synthesizes the practical knowledge contained in these articles into a unifying framework of seven key concepts for successful global business. These concepts are analysed in detail in Chapter 1.

## Case examples



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**Case example** TRW Automotive (purchased by the Blackstone group in 2002) is one of the world's largest suppliers of automobile components. In 1993, Nissan, one of TRW's customers, complained about the high defect rate and high cost structure of the steering assemblies manufactured by TRW-UK. An internal investigation at TRW-UK found that employees responsible for engineering, product design and process design had poor communications with each other and were also particularly weak at execution.

To solve this problem, TRW established the Nissan Global Team. For each of the three regions (the US, Japan and the UK), TRW chose the individuals considered the best engineer and best customer support professional. These six members together 'represented TRW's best capabilities in lean principles as they applied to product and process engineering and design, manufacturing, shop floor issues, and customer service'.[86] Within less than two years, TRW-UK became one of the most efficient and high-quality operations inside TRW.

TRW did not stop there. As of 1996, the Nissan Global Team was still in operation, applying what it had learned to other parts of TRW's operations.[87]

The ten above patterns of FSA development may not be an exhaustive set, but each can be observed regularly in international business practice. An MNE's overall recombination capability can be described, roughly, as its mastering a variety of FSA development patterns. The firm's recombination capability will evolve over time, particularly as foreign affiliates develop their own recombination strengths.

**Complementary resources of external actors**

Having discussed value creation through recombination, ***let us turn now to the fifth concept of the unifying framework: complementary resources of external actors***. In many cases, MNEs need complementary resources of external actors (technology providers, licensees, local distributors, joint venture partners, etc.) to be successful abroad. The firm's domestically successful stand-alone FSAs, its routines and even its recombination capabilities may be insufficient or inappropriate to operate successfully in host countries and regions, because of the cultural, economic, institutional and spatial 'distance' from the home country or home region. In other words, some success ingredients may be missing, and these can then be provided by external actors, if at least two conditions are fulfilled. First, internal development of the required strengths is expected to bring a lower net value than relying upon external actors. Second, the need to rely on external actors can be satisfied in practice, and does not jeopardize the specific expansion project considered.

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Chapter 1 includes a wide range of short case examples featuring high-profile multinational firms. The case examples illustrate aspects of each of the seven key concepts of successful business strategy in practice.

## Critical analysis

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technological knowledge, tax rate differentials among countries, etc. Internal MNE markets can overcome such imperfections, since senior managers set the transfer prices themselves, in the best interest of the firm as a whole, through administrative fiat. The internal MNE market also lets all domestic and foreign investment projects be evaluated using a single cost of capital, and this internal market, run by a centralized financial management function, acts as a 'proxy' for an external, internationally integrated capital market.

Importantly, Rugman argues against the suggestions of some finance scholars that economic exposure should drive strategic decisions such as plant location. For Rugman, financial transactions should not dominate 'real-world' transactions: 'The exposure of MNEs to foreign exchange risk is not a problem in itself . . . Instead, the MNE should determine its long-run profit maximization strategy by producing and selling in optimal locations. Its economic decisions should include exchange risk as only one element in the location decision.'[12]

CRITICAL ANALYSIS

Lessard and Lightstone's analysis should be considered not simply as the study of one specific, functional area in international business. Rather, it sheds additional light on the nature of location advantages: any configuration of location advantages, whether in input or output markets, carries risks, in this case the risk of unexpected exchange rate fluctuations affecting future cash flows. In response, MNEs should aim to develop, as an FSA, a central routine that integrates economic-exposure information into the capital budgeting evaluation of large investment projects. This is especially relevant in the context of large-scale foreign expansion. The development of this type of FSA reflects Pattern I in this book's framework (see Figure 8.2). However, especially for large subsidiaries, it may be useful to combine this internationally transferable knowledge with local capabilities in the particular affiliates, following Pattern III. Obviously, especially in the absence of a central economic-exposure policy, one would also expect Pattern IV to occur, whereby individual affiliates learn how to protect themselves against the hazards of economic exposure.

This last pattern allows us to identify a first limitation of Lessard and Lightstone's story line, namely the suggestion that operations managers not responsible for setting economic-exposure policy should not be held accountable for performance differentials resulting from such exposure. The problem is that many large MNE subsidiaries, operating without strict firm-wide economic-exposure policies or guidelines, have substantial autonomy in their supply chain management processes and targeting of markets – actions which create economic exposure. Chapters 5, 6 and 7 addressed precisely this issue of strategic leader-type subsidiaries benefiting from substantial autonomy and in some cases developing their own knowledge bases. Why should the managers of such subsidiaries be exempted from the risks resulting from economic exposure? How is this

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A rigorous and in-depth analysis of articles drawn from the leading practitioner journals. Their content is fully explored in terms of the key concepts in international business strategy, as well as recent real-world examples.

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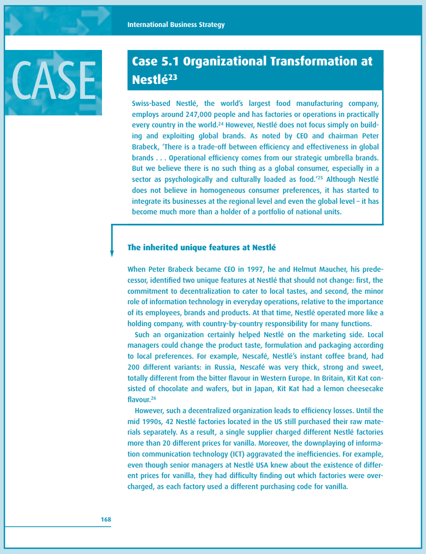
# WALKTHROUGH

Twenty-three 'half-length' case studies are spread throughout the text to relate the concepts discussed to real-life examples in global business. These provide up-to-date coverage of leading firms and offer valuable material for independent or classroom study.



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CASE

Case 5.1 Organizational Transformation at Nestlé[23]

Swiss-based Nestlé, the world's largest food manufacturing company, employs around 247,000 people and has factories or operations in practically every country in the world.[24] However, Nestlé does not focus simply on building and exploiting global brands. As noted by CEO and chairman Peter Brabeck, 'There is a trade-off between efficiency and effectiveness in global brands . . . Operational efficiency comes from our strategic umbrella brands. But we believe there is no such thing as a global consumer, especially in a sector as psychologically and culturally loaded as food.'[25] Although Nestlé does not believe in homogeneous consumer preferences, it has started to integrate its businesses at the regional level and even the global level – it has become much more than a holder of a portfolio of national units.

The inherited unique features at Nestlé

When Peter Brabeck became CEO in 1997, he and Helmut Maucher, his predecessor, identified two unique features at Nestlé that should not change: first, the commitment to decentralization to cater to local tastes, and second, the minor role of information technology in everyday operations, relative to the importance of its employees, brands and products. At that time, Nestlé operated more like a holding company, with country-by-country responsibility for many functions.

Such an organization certainly helped Nestlé on the marketing side. Local managers could change the product taste, formulation and packaging according to local preferences. For example, Nescafé, Nestlé's instant coffee brand, had 200 different variants: in Russia, Nescafé was very thick, strong and sweet, totally different from the bitter flavour in Western Europe. In Britain, Kit Kat consisted of chocolate and wafers, but in Japan, Kit Kat had a lemon cheesecake flavour.[26]

However, such a decentralized organization leads to efficiency losses. Until the mid 1990s, 42 Nestlé factories located in the US still purchased their raw materials separately. As a result, a single supplier charged different Nestlé factories more than 20 different prices for vanilla. Moreover, the downplaying of information communication technology (ICT) aggravated the inefficiencies. For example, even though senior managers at Nestlé USA knew about the existence of different prices for vanilla, they had difficulty finding out which factories were overcharged, as each factory used a different purchasing code for vanilla.

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## Case studies

Questions at the end of each case study test and reinforce the reader's knowledge and understanding of the main ideas discussed in the case.

Conceptual foundations

QUESTIONS:

1. What was Four Seasons' distinct resource base, including elements of its administrative heritage, that provided internationally transferrable FSAs?
2. Which value-added activities in which foreign location(s) permitted Four Seasons to exploit and augment its distinct resource base to the fullest?
3. What were the expected costs and difficulties Four Seasons faced when transferring this distinct resource base?
4. What specific resource recombination (associated with each alternative foreign entry and operating mode) was required so as to make the proposed international value-added activities successful?
5. Did Four Seasons have the required resource recombination capability in-house?
6. What were the costs and benefits of using complementary resources of external actors to fill resource gaps?
7. What were the main bounded rationality and bounded reliability problems Four Seasons faced when extending the geographic scope of the firm's activities, given the changed boundaries of the firm, the changed linkages with outside stakeholders and the changes in its internal functioning?

Implications of international business strategy for MNE performance

MNE managers can answer the seven questions above at various levels: the level of a single expansion project, the level of a divisional/business unit's growth strategy or the level of the firm's overall international business strategy. In order to answer those seven questions, managers must reflect on the MNE's strengths (relative to rival companies) and its ability to match its distinct resource base with the challenges and opportunities found in the international environment, thereby creating value and satisfying shareholder needs.

The question then arises whether an international expansion programme is likely to improve MNE performance. A vast international business literature attempts to answer the question whether international expansion and the related increase of international diversification (e.g., the share of foreign investment to total investment, foreign sales to total sales or foreign production to total production) is likely to have positive effects on the MNE's return and risk. The answer is: it depends on several factors.

First, at the project level, the MNE should compare the expected net present value per invested monetary unit in foreign expansion with that of domestic expansion, taking into account a variety of risk factors. MNEs should undertake

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## Case questions

## Web materials

**For students:**

- Links to articles in *Fortune*, *FT*, etc., with cases that can be applied to the framework developed in the book. This set will be updated and will grow over time.
- Links to useful databases and other electronic sources of useful information relevant to international business strategy.

**For lecturers:**

- The answers to the case study questions (password protected).
- Downloadable PowerPoint slides for every chapter and all figures.



 