

Growth Strategies of Multinational Companies

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Abstract

The turbulent start of the new century has brought new challenges for firms, industries and countries. This paper investigates business and growth strategies of multinational companies. The main objective is to identify whether a company's performance is determined by its growth strategy or not. The purposes for the research are: to understand what kind of business models and strategies global companies pursue, what growth strategies global companies pursue and if there is a link between a company's growth strategy and its profitability. Least but not last, the findings are reviewed on their transferability to all industries. The findings regarding the business models and growth strategies pursued are that all of them are based on Porter's generic strategies as well as internationalization and diversification but there is no specific preference given to any of the strategic elements.

Keywords: strategies; growth; competitiveness; multinational companies; global

JEL Classification: M20, M29

Introduction

The goals for this research are to investigate if there is a connection between a company's growth strategy and its profitability and to identify if the findings can be generalized to other industries.

To achieve the above described goals, the paper starts with the theoretical background of this research. It is presented a description of Strategic Management and its framework to define, plan and implement a company's strategic as well as assess its performance. Strategic Management Michael Porter's models on competitive strategy and competitive advantage are introduced and discussed further. Even if the models have been introduced in the 1980's they are still amongst the most popular ones used to decide on a company's strategy in today's economic environment. The information presented in the paper provides the theoretical background to understand and assess a company's competitive, growth and internationalization strategy.

Various sources of information that were found related and important are used in this paper. The secondary data collection for this paper was obtained through the Internet from different sources, such as market analysis, press articles, journals and reports, and printed information, such as books.

The 21st century seems to have begun with events indicative of the turbulence, challenges and opportunities ahead. Survival and success in such turbulent environment increasingly depend on competitiveness. Competitiveness has been described by many researchers as a

multidimensional and relative concept. The significance of different criteria of competitiveness changes with time and context. Theories and frameworks must be flexible enough to integrate the change with key strategic management processes if their utility is sustained in practice.

Competitiveness

Competitiveness is a multidimensional concept. It can be looked at from three different levels: country, industry, and firm level. Competitiveness originated from the Latin word, *competer*, which means “involvement in a business rivalry for markets”. It has become common to describe economic strength of an entity with respect to its competitors in the global market economy in which foods, services, people, skills, and ideas move freely across geographical borders (Murths, 1998).

Firm level competitiveness can be defined as the ability of firm to design, produce and/or market products superior to those offered by competitors, considering the price and non-price qualities (D'Cruz, 1992).

Competitiveness processes are those processes, which help identify the importance and current performance of core processes such as strategic management processes, human resources processes, operations management processes and technology management processes.

Firm-level competitiveness is of great interest among practitioners. Porter says “it is the firms, not nations, which compete in international markets”, (Porter, 1998). The environmental factors are more or less uniform for all competing firms. Research shows that 36 per cent of the variance in profitability could be attributed to the firms' characteristics and actions (McGahan, 1999). Other pro-firm views (Bartlett and Ghoshal, 1989; Prahalad and Doz, and 1987; Prahalad and Hamel, 1990) focus on individual firm and their strategies for global operations, and resource positions to identify the real sources of their competitiveness (Table 1).

Table 1. Studies of Firms' Performance

Contributor	Key Findings
McGahan (1999)	36 per cent of the variance in profitability could be attributed to the firms' characteristics and actions
Rumelt (1991)	Corporate—parent explains 1–2 per cent Industry membership explains 9–16 per cent Business unit effect explains 41–46 per cent in business unit performance
McGahan & Porter (1997)	Corporate—Parent explains 4.33 per cent Industry 18.68 per cent
Schmalensee (1985)	Corporate—parent effect is negligible Industry membership explains 20 per cent of firm's total performance Business unit effect is significant
Wemerfelt&Montgomery (1988)	Industry membership explains 12.3–20 per cent depending on controls
Roquebert et al (1996)	Industry explains 10 per cent variance in business unit performance

Source: adapted from Brush (1999) and McGahan (1999)

Competitiveness involves “a combination of assets and processes, where assets are inherited (natural resources) or created (infrastructure) and processes transform assets to achieve economic gains from sales to customers” (DC, 2001). Some authors view competitiveness with the competency approach. They emphasise the role of factors internal to the firms such as firm strategy, structures, competencies, capabilities to innovate, and other tangible and intangible resources for their competitive success (Bartlett and Ghoshal, 1989; Doz and Prahalad, 1987; Hamel and Prahalad, 1989, 1990). This view is particularly among the resource-based approach towards competitiveness (Prahalad and Hamel, 1990; Grant, 1991; Barney 2001, 1991; Peteraf,

1993; Ulrich, 1993). Ability to develop and deploy capabilities and talents far more effectively than competitors can help in achieving world-class competitiveness (Smith, 1995).

Strategic Management

In today's competitive business environments companies presents their plans on how to sustain their business operations, their competitive advantage and increase their profitability using the concept of strategic management. The benefits of strategic management have already been pointed out in the 1960's when Alfred Chandler mapped out that "structure follows strategy", meaning that a long-term perspective and formulated strategy provides a company structure, focus, alignment and direction. In other researchers' opinion, such as Carpenter and Sanders (2007), strategic management is a "... process by which a firm incorporates the tools and frameworks for developing and implementing a strategy"(p.7). A comprehensive summary of strategic management definition is formulated by Lamb (1984): "Strategic management is an ongoing process that evaluates and controls the business and the industries in which the company is involved; assesses its competitors and sets goals and strategies to meet all existing and potential competitors; and then reassesses each strategy annually or quarterly to determine how it has been implemented and whether it has succeeded or needs replacement by a new strategy to meet changed circumstances, new technology, new competitors, a new economic environment, a new social, financial or political environment".

When entering on a market and develop a strategy each company is interested in understanding what kind of competition and market conditions are and if it is an attractive step. As response to this demand Porter developed his competitive analysis in using the framework of five forces shaping industries, markets and competition. Industry attractiveness in this model is considered as the overall profitability of the industry. The five forces impact collectively the profitability through their effects on price, costs and investment requirements. The more impact they have the less attractive the industry gets and vice versa. The five forces shaping an industry are the *threat of new entrants*, the *threat of substitute products or services*, the *bargaining power of suppliers*, the *bargaining power of buyers* and the *intensity of competitive rivalry*. According to Porter's Five Forces Model one of the tools pointed out in the strategy development process is a competitive analysis. When applying this model a company can assess whether it is profitable to enter a new industry or market and what business conditions have to be expected. Porter's five forces are interrelated and developments in one force have an impact on the remaining forces. The figure below illustrates the interrelation and summarizes the elements discussed before.



Fig. 1. The Five Forces of the Competitive Analysis and their interrelation

Source: M.E.Porter, The Five Competitive Forces that Shape Strategy, *Harvard Business Review*

Porter's Generic Strategies

This model was introduced by Porter in 1980 with the publication of his book “Competitive Strategy”. The purpose of the strategic positioning model and its generic strategies is to establish, sustain and grow a company’s competitive advantage over its competition. Together with the competitive analysis model, the market positioning and competitive advantage model and the value chain model Porter provides a comprehensive strategic approach for a company to sustain and maximize its profitability.

The concept of competitive advantage was introduced by Porter in 1985 and describes competitive advantage as an attribute that “...grows fundamentally from the value a firm is able to create... Value is what buyers are willing to pay, and superior value stems from offering lower prices than competitors for equivalent benefits or providing unique benefits that more than offset higher prices.” (Porter, 1985, p.3)

Competitive advantage describes therefore the situation when a company is able to deliver the same benefits as its competitors but at a lower cost or to deliver benefits that exceed those of competing products (QuickMBA 1999-2010) as well as the company’s ability to create value in a way that its competitors cannot (Carpenter and Saunders, 2007, p.19). In his work, Porter (Competitive Advantage, 1985) argues that from a strategic perspective, a company’s strengths to create this value are either in the category cost advantage or differentiation. Both strengths can be applied strategically in a broad or narrow scope, creating three generic strategies: cost leadership, differentiation and focus. These strategies are independent from a company, market or industry and therefore generic. Using the generic strategies a company can prepare the framework for its strategy implementation on the level of its strategic business units.

The Strategic Positioning Model (Carpenter and Saunders, 2007, p. 127) visualizes the merging of the categories and scope into the following two-by-two matrix shown in Figure 2:

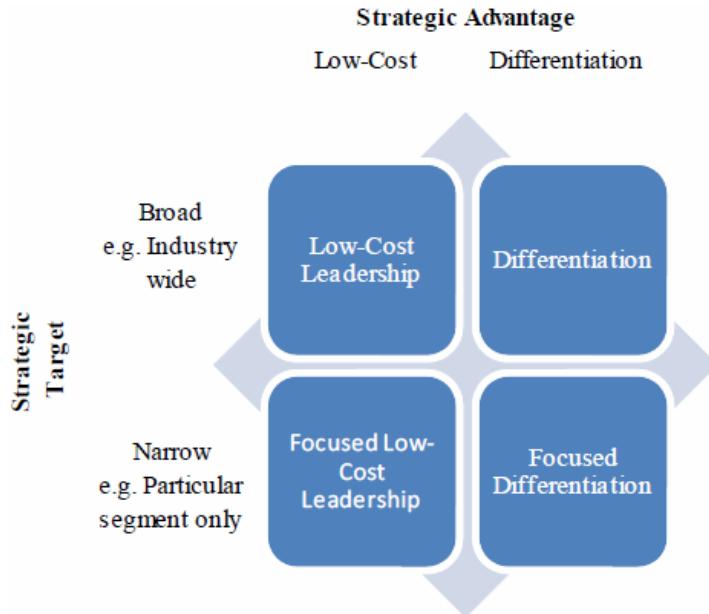


Fig. 2. The Strategic Positioning Model

Source: Carpenter and Sanders (2007), p.127

The cost leadership strategy uses the lower production unit price as strategic key element to gain bigger market share or higher profits as the competition and probably driving some competitors out of the market (Carpenter and Sanders 2007, p. 128). The cost leadership strategy's key competitive advantage is the lower price in comparison or the lowest price in the entire market and therefore appealing to cost-conscious or price-sensitive industries and consumers. In reference to the competitive analysis in these markets the buyers have significant power to bargain prices, it is easy for them to switch between manufacturers and the products are very alike. The products serve basic needs and consumers all use them in a similar way, like e.g. a tooth brush and the market size is large. To achieve and sustain the cost leadership companies pursue strategies to cut down costs to a minimum through e.g. spreading fixed cost over a large product volume to benefit from the economies of scale. Furthermore, production costs are cut down producing more and more standardized products and the outsourcing of e.g. overhead activities. In addition to the companies peruse a maximum integration of their value chain to sustain low costs. Companies pursuing cost leadership have to be a step ahead of their competition to sustain the profitable cost gap and not only predict changes in customer behaviour or substitute products, but also the impact of technology breakthroughs and value chain developments to their business and keep pricing aggressive but not cutting down their own profit.

The strategy of focus can be combined with the cost leadership or differentiation strategy and applies both strategies core ideas to a narrow market segment. Focused cost leadership describes the ability of a company to offer a product to a niche group of customers or niche market at the lowest price in the market. For example Ryan Air is focusing on extremely cost sensitive commercial travellers by offering flights at the lowest prices in the niche market. Focused differentiation describes unique products offered to a niche market and target group. In this case the products get extremely rare, unique, custom-made or specialized, that their position is in a high end niche market. Luxury products or technically very sophisticated products are positioned under the use of this strategy, e.g. luxury cars like Maserati or Austin Martin.

The four strategies, cost leadership, differentiation, focused cost leadership and focused differentiation, are commonly used in today's strategic management and have been adapted to

the changes since their introduction in the 1980's. According to David (2009, p.193), e.g. it is possible to differentiate the generic strategies not only into four but into five detailed types of strategic positions. David takes the two-to-two matrix discussed above and diversifies the strategies cost leadership and focus into two sub-strategies using the focal points low cost and best value. The two-to-three matrix shown below in Figure 3 describes 5 types of generic positioning strategies.

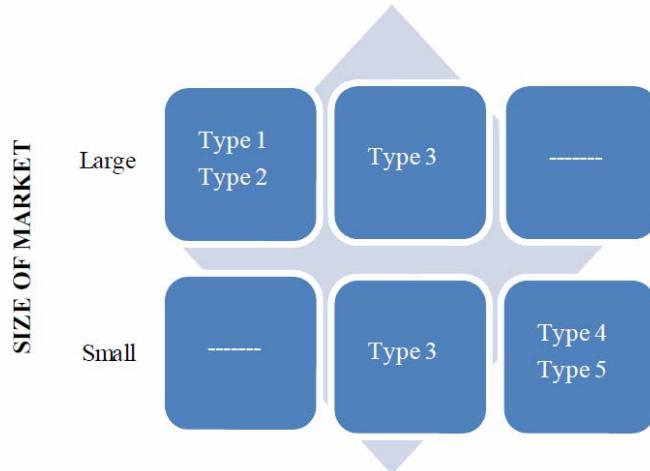


Fig. 3. Porter's Five Generic Strategies according to David

Source: David (2009), p.193

The core activity for cost leadership in this matrix is identical to the one discussed before. The company aims to cut down production cost to a minimum and sell to cost conscious or price sensitive buyers. Type 1 describes cost leadership under the key requirement low cost. Under the requirement low cost the company aims to sell its products or services at the lowest price in the market to a large group of buyers. These products require streamlined product features, large sales volumes in other terms mass production and economy of scale conditions to achieve profitability. In a Type 1 shaped market aggressive pricing and price wars are constantly present, since the target buyers are heavily price sensitive. Type 2 describes cost leadership under the key requirement best value. In this position the company is aiming to secure the lowest price in combination with the best value. The target buyers here are cost conscious buyers, comparing all available products on the market according to the price paid and perceived value received. Product or service prices are still produced at the lowest cost but probably sold at the level of competition to benefit from a higher margin. (David 2009, p. 194) Type 3 describes differentiation in the sense discussed before. The company aims at a competitive advantage through a unique product or service feature. The more complex and resources consuming the features duplication is, the more sustainable the competitive advantage is. The successful implementation allows the company to charge a higher price on its product or service and benefit from customer loyalty. In large markets differentiation can be achieved through a rather streamlined product combined with enhanced product design, warranty and customer service. In smaller markets products can be more complex, probably customized and choice of material, design, personal customer service etc. lead to the desired competitive advantage. (David 2009, p. 195) Type 4 describes focus under the key requirement low cost in small or niche markets. The company identifies a profitable and growing niche market and is able to sell its product or service at the lowest price on the market. The difference to the cost leadership in large markets is found in the nature of the product or service. The product or service is very buyer specific and requires the company to specialize and focus on the requirements and features. They are not available on a large scale or produced in mass production. Insurance companies for example may focus on a specific type of insurances e.g. for

self-employed people or singles and have the competitive advantage over its competition through its specialization and customer focused offers at lower prices. Type 5 describes focus under the key requirement best value. The type 5 niche markets are as small and specific as the ones discussed before, but best value indicates that price is no longer a decision maker in this strategic concept. (David 2099, p. 196) The value and perceived value of the product or service bought are deal makers for the buyers. Buyers have very specific and individual requirements to be met and are willing to pay the higher or high price charged. Products and services are in many sophisticated and unique and probably the purchase will only be done once like e.g. engagement rings.

Growth Strategies

When a firm seeks to grow, it is also a strategic question whether to diversify or internationalize to sustain its business operations. A firm may diversify if current product lines do not match growth potential, or if current operations are not profitable. There are two basic diversification strategies, concentric/ related and conglomerate/ unrelated (Hunger and Wheelen, 2009, 2003, 2001). Related diversification occurs when a firm enters into strategic business area (SBAs) by adding products or services, which are related to the existing core SBA. The goal of related diversification is to achieve strategic fit, which allows a firm to achieve synergy. Synergy is the ability of two or more businesses to generate more profits together than they could separately. Hunger and Wheelen (2009) has stated that, this strategy may be appropriate if a firm has a strong competitive position but current industry attractiveness is low. Related diversification can be classified by the direction of diversification, vertical integration (backward and forward) and horizontal integration.

Firms that operate in global industries must compete on worldwide basis if they are to succeed. This is because their strategic positions in specific markets are affected strongly by their overall global positions (Kotler et al., 2005). The fundamental reasons for firms to go international can be seen in proactive and reactive motives. Proactive motive represents stimuli to attempt strategy changes, which based on the firm's interesting in exploiting unique competences and/or market possibilities. Such strategy changes (Hollensen, 2007; Deresky, 2005, p. 223-225) are: to fulfil a firm's growth and profit ambitions, the desire, drive and enthusiasm of management towards internationalization, a firm produce products or services that are unique or technologically advanced in a specialized field, foreign market opportunities or market information which distinguish a firm from its competitors, resource access and cost savings enhance a firm to control over raw materials/ other resources and lower transportation, economics of scale, and tax benefits which may also play a major motivating role. It may allow a firm to sell its products at a lower cost in foreign markets or to accumulate a higher profit.

Conclusions

The hyper-competitive era in the last few decades has created the need for an explicit management of competitiveness. The literature review identifies that the firm level has received the maximum attention among the three levels.

Firm growth is related to economic expansion due to the processes taking place within the firm (Penrose, E.T, 1959). The more firms grow, the more resources they can access, thus firm growth is considered as a path dependent process (Akpinar, 2009). The resource-based view considers a firm's own set of resources and capabilities as the driver of growth and states that a firm predicts the growth strategies based on its resources and competencies (Otto & Low 1998). A firm's strategy is at its best continuously reviewed to be able to act, react and adapt to the movements in a company's business environment and sustain its competitive advantage. Diversification and internationalization are the two major types of growth vectors, and are

alternative routes for expanding a company's portfolio in terms of growth. Growth also improves the effectiveness of the company. Larger companies have a number of advantages over smaller companies such as economies of scale resulting from marketing or production synergies. The company may pursue one or both types of growth strategies or the company may prefer diversification over internationalization except the firm's objectives cannot be met through diversification. The reason is because internationalization is much more difficult, risky and costly than diversification.

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