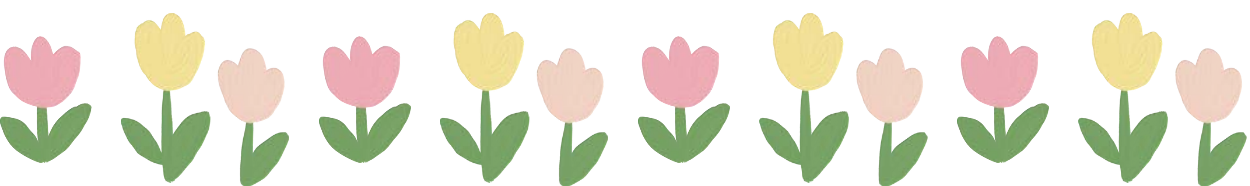
chapter four

Entry and Expansion



Non-Equity Modes of Entry

Low Investment & Risk

Non-equity modes (e.g., exporting or licensing) need less money and have lower risk, but the company depends on local partners.

Less Control, More Flexibility

These modes give less control over business operations but allow more flexibility to adapt or exit the market easily.

EXPORTING

DEFINITION

Selling goods or services produced in one country to customers in another country. It's a common method for businesses to expand globally by entering foreign markets.

EXPORT METHODS AND EXPANSION STRATEGIES

Direct vs. Indirect Exporting

Direct exporting involves selling products directly to foreign customers, while indirect exporting uses intermediaries (e.g., agents or export companies).

Other Expansion Strategies

Businesses can use Licensing/Franchising (allowing foreign partners to use their IP or business model) or set up Wholly Owned Subsidiaries/Joint Ventures to have more control over their foreign operations.

Advantages

1. Market Expansion & Revenue Diversification:
Exporting allows access to new international markets, helping to increase customer reach and diversify revenue sources.

2. Cost Efficiency & Economies of Scale:
By increasing production volumes, exporting can lower per-unit costs and improve profitability.

3. Risk Diversification & Brand Growth:
Expanding globally spreads business risks across different markets and enhances the company's global brand visibility.

DISAdvantages

1. Market Research and Logistics:
Conduct thorough market research to understand local conditions, and ensure efficient logistics and distribution for smooth delivery to international customers.

2. Legal Compliance and Financial Management:

Ensure adherence to export regulations, tariffs, and intellectual property laws while managing currency fluctuations and securing profitability in global transactions.

3. Risk Management:

Mitigate risks related to political instability, economic volatility, supply chain disruptions, and legal challenges to protect the business in foreign markets.

TURNKEY PROJECTS

COMPLETE SOLUTION

Turnkey projects involve the contractor managing all aspects of design, construction, and installation, delivering a fully operational facility to the company.

SINGLE POINT OF CONTACT

The company works with one contractor who oversees the entire project, simplifying communication and coordination across all stages of development.

Advantages

Time and Cost Efficiency:

Contractors handle all aspects of the project, reducing management overhead and speeding up timelines for the company.

Risk Transfer:

The contractor assumes responsibility for risks related to design, construction, and integration, protecting the company from potential project challenges.

Expertise and Focus on Core Business:

Companies benefit from the contractor's specialized knowledge and skills while focusing on their core business operations without being involved in day-to-day project management.

DISAdvantages

Contractual Clarity:

Clear contracts are vital to define the project scope, deliverables, timelines, and responsibilities, ensuring mutual understanding and expectations.

Quality Assurance & Compliance:

Ensuring the project meets agreed-upon quality standards while adhering to local laws, regulations, and permits is crucial for project success.

Communication & Coordination:

Effective communication and coordination among the company, contractor, and subcontractors are essential to ensure smooth project execution and resolve any issues promptly.

Licensing

Intellectual Property Rights & Financial Terms

Licensing involves granting the rights to use intellectual property (such as patents, trademarks, or technology) in exchange for royalties or fees.

Quality Control & Legal Compliance

The agreement specifies the licensee's obligations regarding product quality and marketing while ensuring adherence to local laws and regulations in the licensee's market.

Advantages

1. Market Expansion: Licensing helps companies enter new markets using local partners.
2. Revenue Generation: Licensors earn royalties and fees without big investment.
3. Risk Sharing: Risks are shared with the licensee, who handles operations.

DISAdvantages

1. Loss of Control: Licensors may have limited influence, affecting quality and brand reputation.
2. IP Protection: Protecting intellectual property (IP) rights in different markets to avoid violations.
3. Contractual Risks: Managing complex contracts, including disputes and termination terms.

FRANCHISING

Definition

A strategy where a franchisor allows a franchisee to operate under its established brand and business model in a foreign market.

Franchisor-Franchisee Relationship & Fees

The franchise agreement outlines the terms, fees (initial and royalties), and the responsibilities of both parties.

Advantages

Rapid Expansion

Franchising enables quick market entry by utilizing local entrepreneurs' capital and knowledge, allowing for faster growth.

Risk Sharing

Franchisees bear much of the operational and financial risk.

Brand Consistency

Franchisors ensure uniformity in branding, customer experience, and operational standards across all franchise locations.

DISAdvantages

Legal and Regulatory Compliance

Franchisors must ensure they meet varying legal requirements.

Cultural and Market Adaptation

Franchisors must balance global brand consistency with local market needs, adapting to cultural preferences and consumer behavior.

Communication and Management

Effective communication, training, and ongoing support are essential for maintaining franchisee satisfaction and efficient operations across international locations.

Contract Manufacturing

1 Outsourcing Production

Contract manufacturing allows a company (client) to outsource the production of its goods to a third-party manufacturer.

2 Cost and Efficiency

This arrangement provides cost savings through economies of scale, lower labor costs, and specialized manufacturing capabilities.

ADVANTAGES

A. Cost Savings: Lower production costs and access to specialized manufacturing.

B. Focus on What You Do Best: Outsource manufacturing so you can focus on product and marketing.

C. Flexibility: Easily adjust production levels without big investments.

DISADVANTAGES

A. Quality Control: Ensure products meet quality standards across all manufacturing locations.

B Protecting Intellectual Property: Safeguard exclusive designs and technology shared with manufacturers.

C Supply Chain Management: Manage logistics, shipping, and customs to avoid delays and risks.

Management Contract

1 Scope of Services and Performance

A management contract allows a contractor to provide managerial and operational expertise, with performance measured through KPIs like profitability, cost reduction, and customer satisfaction.

2 Risk, Responsibility, and Communication

The contractor manages daily operations while the client retains ultimate business risks, with clear reporting and communication channels ensuring alignment and transparency.

3 Example

In a management contract with a hotel in Kuala Lumpur, the management contractor may handle operations, marketing, and staffing, with performance measured through customer satisfaction scores and revenue growth.

ADVANTAGES

A Access to Expertise: The company gains specialized knowledge and experience from the contractor without the need for extensive recruitment or training efforts.

B Cost Efficiency: Management contracts offer a more affordable alternative to building a permanent management team, especially for short-term or international projects.

C Flexibility: The company can focus on its core business while outsourcing non-essential operations or challenges to experienced professionals.

DISADVANTAGES

A Cultural and Regulatory Differences: Managing international operations requires navigating local laws, regulations, and cultural norms to ensure compliance and effective management.

B Contractual Clarity: Well-defined contracts are crucial to outline roles, responsibilities, and performance expectations, preventing potential misunderstandings or legal disputes.

C Dependency Risks: Relying heavily on external management may reduce the client's internal capabilities and strategic flexibility over time.

Equity Modes of Entry

1 Full Control & Ownership

The parent company has full ownership and control over operations, allowing for better adaptability and decision-making in the foreign market.

2 Higher Investment & Long-Term Commitment

Equity modes require substantial financial investment and a long-term commitment to establish a strong market presence, but they carry higher risks.

Wholly Owned SUBSIDIARY

OWNERSHIP AND CONTROL 1

A wholly owned subsidiary is 100% owned by the parent company, granting it full control over operations, management, and strategic decisions without the need for external partners or investors.

2 PURPOSE AND STRUCTURE

It operates as a separate legal entity under the laws of the host country, often established to expand into foreign markets, retain control over intellectual property, and ensure consistent business practices across locations.

ADVANTAGES

1 FULL CONTROL:

The parent company has complete control over the subsidiary's operations, ensuring consistency in processes and brand strategy.

2 FLEXIBILITY:

The subsidiary can adapt to local market needs and regulations, offering more freedom to respond quickly.

3 GLOBAL INTEGRATION:

It helps integrate operations and technologies across markets, improving efficiency and synergy within the company.

DIS ADVANTAGES

1 HIGH COSTS:

Setting up and maintaining a wholly owned subsidiary involves significant expenses, including initial setup, ongoing operations, and compliance with local laws.

2 INCREASED RISK:

It carries higher financial and operational risks, especially with market volatility and political instability.

3 COMPLEXITY:

Managing legal, regulatory, and cultural challenges in the host country, as well as local relationships, adds complexity to operations.

Joint Venture (JV)

1 Shared Ownership and Risks

A joint venture involves two or more companies sharing ownership, resources, and risks in a collaborative business initiative.

2 Strategic Collaboration

JVs help partners leverage each other's strengths to achieve common goals, such as market entry or technology development, while reducing international business risks.

Advantages

1 Shared Resources:

Access to capital, technology, skills, and market knowledge.

2 Risk Sharing:

Spread financial and operational risks between partners.

3 Market Access:

Entry into new markets or expansion of existing market presence.

DISAdvantages

1 Cultural Differences:

Managing diverse organizational cultures and business practices.

2 Conflict Resolution:

Potential disagreements over decision-making, strategy, or resource allocation.

3 Complex Governance:

Establishing clear roles, responsibilities, and governance structures.

Strategic Alliances

1 Purpose and Benefits

Strategic alliances help partners enter new markets, share risks, exchange technologies, and pool resources to reduce costs and enhance competitiveness.

2 Types of Alliances

Strategic alliances can take various forms, including joint ventures, equity alliances, non-equity alliances (e.g., licensing or franchising), and cross-border mergers or acquisitions.

ADVANTAGES

1. Access to New Markets: Partners can enter new markets more swiftly and effectively by leveraging local market knowledge and distribution networks.
2. Shared Resources: Pooling of financial, technological, and human resources to achieve economies of scale and scope.
3. Risk Management: Spreading risks associated with market volatility, regulatory changes, and geopolitical uncertainties.

DISADVANTAGES

1. Cultural Differences: Managing cultural diversity and ensuring alignment of organizational values, norms, and practices.
2. Coordination and Control: Balancing autonomy and control over decision-making processes, operational strategies, and resource allocation.
3. Intellectual Property Protection: Ensuring protection of proprietary technologies, patents, and intellectual assets shared between partners.

Non-Equity Modes of Entry

1 Exporting

Selling goods or services produced in one country to customers in another without establishing a physical presence.

2 Turnkey Projects

A company completes and hands over a fully operational facility or project to a foreign client without retaining ownership or long-term involvement.

3 Licensing

Granting a foreign company the right to use intellectual property, like patents, trademarks, or technology, in exchange for royalties or fees.

4 Franchising

Allowing a foreign company to operate a business using the franchisor's brand, business model, and support systems in exchange for fees and royalties.

5 Management Contracts

Providing managerial expertise and operational services to a foreign business without taking ownership of the business.

6 Contract Manufacturing

A company contracts a foreign manufacturer to produce its products according to specified quality standards and design.

Equity Mode of Entry

1 Joint Ventures

A partnership where two or more companies create a new business entity together, sharing ownership, risks, and rewards.

2 Wholly Owned Subsidiaries

A company fully owns and controls a subsidiary in a foreign market, either through acquisition or by setting up a new operation (new venture investment).

3 Strategic Alliance

A strategic alliance is a partnership where two or more companies collaborate to achieve shared goals, such as pooling resources or expertise, while maintaining their independence.