

INTERNATIONAL BUSINESS STRATEGY

SECOND EDITION

ALAIN VERBEKE

CAMBRIDGE

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International Business Strategy

Verbeke provides a new perspective on international business strategy by combining analytical rigour and true managerial insight on the functioning of large multinational enterprises (MNEs). With unique commentary on forty-eight seminal articles published in the *Harvard Business Review*, *Sloan Management Review* and *California Management Review* over the past three decades, Verbeke shows how these can be applied to real businesses engaged in international expansion programmes, especially as they venture into high-distance markets. The second edition has been thoroughly updated and features greater coverage of emerging markets with a new chapter and seven new cases. Suited for advanced undergraduates and graduate courses, students will benefit from updated case studies and improved learning features including 'management takeaways', key lessons that can be applied to MNEs and a wide range of online resources.

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Sjoerd Beugelsdijk, Professor of International Business, University of Groningen, The Netherlands

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‘Being the first of its kind, this insightful textbook not only describes the main academic insights relevant to international business strategy, but also rigorously scrutinizes and reinterprets them using an overarching yet simple framework composed of country, firm, and individual-level concepts. By taking this reflective and integrative approach, Verbeke offers an unprecedented learning experience to both students and practitioners by greatly enhancing their understanding of successful international strategy formulation and implementation.’

Arjen Slangen, Associate Professor of International Business, Rotterdam

International Business Strategy

Rethinking the Foundations of Global Corporate Success

Second Edition

Alain Verbeke



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About the author

Dr Alain Verbeke is an Elected Fellow of the Academy of International Business and former Editor of the *Journal of International Business Studies* (Area Multinational Enterprise Theory and International Strategy). He is an Academic Associate of the Centre for International Business and Management, Judge Business School, University of Cambridge (UK).

Dr Verbeke holds the McCaig Research Chair in Management at the Haskayne School of Business, University of Calgary (Canada). He was previously the Director of the MBA programme, Solvay Business School, University of Brussels (VUB, Belgium). He has also been a Visiting Professor at Dalhousie University (Canada), the University of Toronto (Canada) and the Université Catholique de Louvain (Belgium), as well as an Associate Fellow of Templeton College, University of Oxford (UK).

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 analysed 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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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 twenty-five years. Second, the late 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 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.

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

Calgary

Abbreviations

3M

Minnesota Mining and Manufacturing Company

AB

Anheuser Busch

A&C

Automation and control

AAFLI

Asian-American Free Labor Institute

AAU

American Asiatic Underwriters

ACLA

Acer Computec Latino America

AIA

American International Assurance

AIG

American International Group

Ambev

Companhia de bebidas das Américas

APEAL

Automotive performance, execution and layout

ARIS

Architecture of integrated information systems

ASAs

Alliance-specific advantages

ATM

Automated teller machines

BEF

Brightness enhancement film

BFW

Bayerische Flugzeugwerke

BLMC

British Leyland Motor Corporation

BMW

Bayerische Motoren Werke

BP

Best position, best practice, and best performance

BP

British Petroleum

BPI

Beauté Prestige International

BRIC

Brazil, Russia, India and China

BSN

Boussois-Souchon-Neuvesel

C&C

Computers and communications

CAD

Computer-aided design

CAM

Computer-aided manufacturing

CCC

China customer centre

CD

Compact disk

CEO

Chief executive officer

CMD

Committee of Managing Directors

CMR

California Management Review

CNOOC

China National Offshore Oil Corporation

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.

DM

Deutsche Mark

EBC

European business centre

EDC

European distribution centres

EDLP

Every day low price

EMNEs

Emerging economy multinational enterprises

EMS

Electronics manufacturing service

ERP

Enterprise resource planning

FAA

Federal Aviation Administration

FDI

Foreign direct investment

FLA

Fair Labor Association

FMS

Flexible manufacturing systems

FSA

Firm-specific advantage

GCI

Global competitiveness index

GDP

Gross domestic product

GE

General Electric

GM

General Motors

GMS

Global manufacturing system

GNPOC

Greater Nile Petroleum Operating Company

GOS

Government of Sudan

GTF

Global technology fields

H&C

Harrisons & Crosfields

HAM

Honda of America manufacturing

HBR

Harvard Business Review

HBS

Harvard Business School

HP

Hewlett-Packard

HPs

High potentials

HR

Human resources

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.

IPO
Initial public offering

IPR
Intellectual property rights

IT
Information technology

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

LVMH
Moët Hennessy Louis Vuitton

M&As

Mergers and acquisitions

MBA

Master of Business Administration

MCM

Multi-chip module

MFA

Multifiber Arrangement

MIC

Market information centre

MIT

Massachusetts Institute of Technology

MNE

Multinational enterprise

NAFTA

North-American Free Trade Agreement

NAO

North American operations

NASDAQ

National Association of Securities Dealers Automated Quotations

NCR

National Cash Register

NDG

Nippon Data General Corporation

NEC

Nippon Electric Company

NGO

Non-governmental organization

NIOC

National Iranian Oil Company

NLB

Non-location-bound

NMC

Nippon Mini Computer Corporation

NPPC

Nestlé Purina PetCare

NUMMI

New United Motor Manufacturing Inc.

NYSE

New York Stock Exchange

ODM

Original design manufacturing

OEM

Original equipment manufacturing

OMR

Organizational and management review

P&G

Procter & Gamble

PC

Personal computer

PCB

Printed circuit boards

PCBA

Printed circuit board assemblies

PICC

People's Insurance Company of China

PTH

Pin-through-hole

R&D

Research and development

RMB

Renminbi

RTUs

Remote terminal units

SAPREF

Shell African Petroleum Refinery

SBC

Sony Broadcast Limited

SBU
Strategic business unit

SCGP
Shell coal gasification process

SCR
Siemens Corporate Research

SINOPEC
China Petroleum and Chemical Corporation

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

SPLM
Sudanese People's Liberation Movement

SRI
Stanford Research Institute

SSAs
Subsidiary-specific advantages

SSI
Strategic sourcing initiative

SUV
Sport utility vehicle

TBT
Technical barriers to trade

TCS

Tata Consultancy Services

TKS

Time-keeping system

TPS

Toyota production system

TQM

Total quality management

TSX

Toronto Stock Exchange

TTB

Technology-to-business

UNCTAD

United Nations Conference on Trade and Development

UNCTC

United Nations Centre on Transnational Corporations

VET

Vocational education and training

VLSI

Very large scale integration

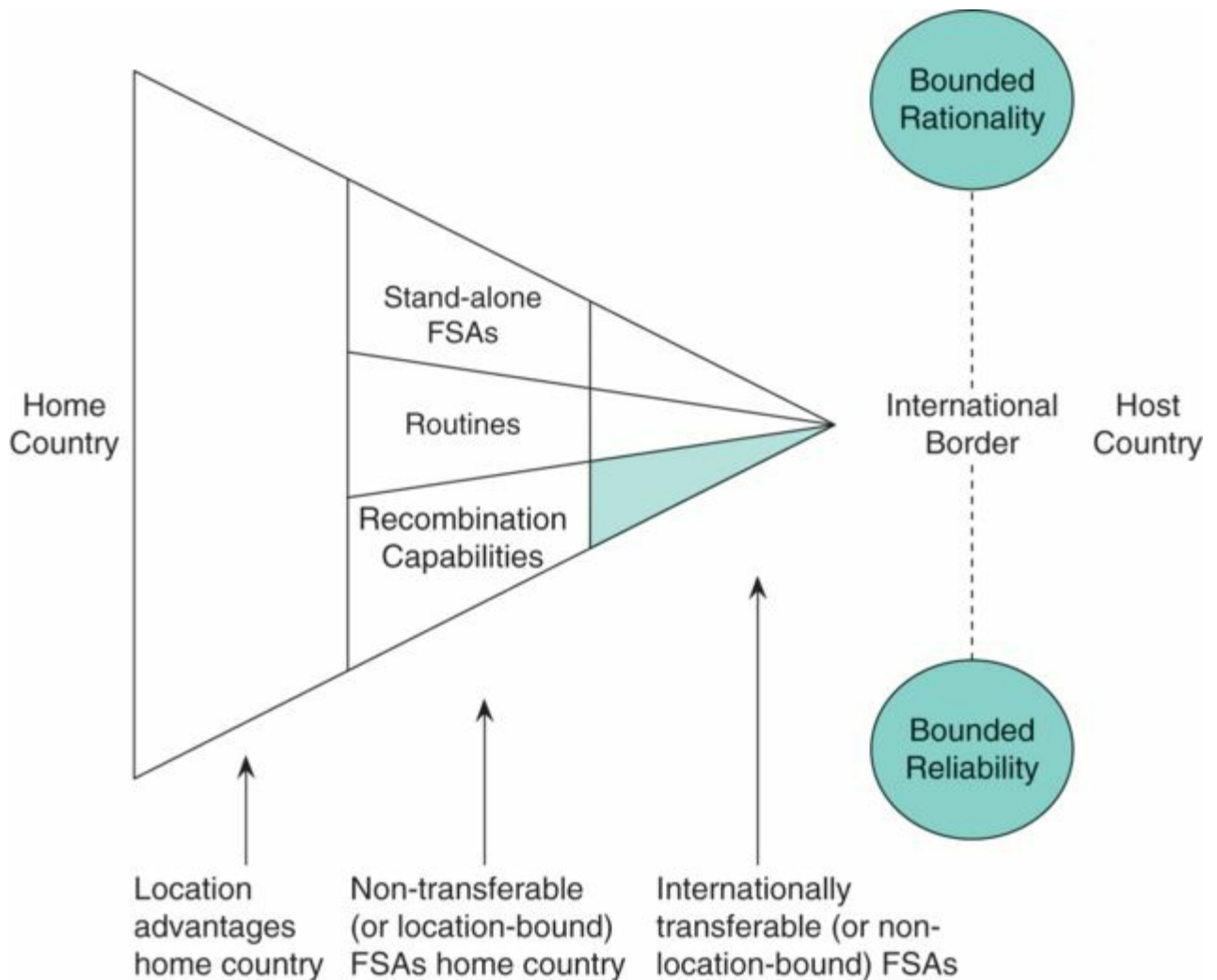
VUB

University of Brussels

(Compiled by: Charles A. Backman)

Walkthrough

Chapter 1



The triangular shape in the model represents the pyramidal nature of the firm's advantages: on the broad base of the location advantages (LAs) of its home country (left) it builds a smaller subset of FSAs that are location-bound (LB; middle), and then a still smaller subset that are non-location-bound (NLB; right). Bounded rationality and bounded reliability influence the ability of these non-location-bound FSAs to be transferred across the international border to the host country.

International Business Strategy presents, interprets and critiques 48 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

Case examples

In 1996, Kao was Japan's largest consumer goods company, with a quarter of the shampoo market, three quarters of the bleach market and half of the laundry detergent market.

One of the main reasons for Kao's dominant domestic position was its control of a comprehensive distribution system within Japan. Kao owned Hansha, a wholesale distributor, which distributed only Kao's products. As a result, Kao was able to supply small shops easily and also prevent outsiders from entering the market. Moreover, Hansha allowed Kao to gain privileged information on consumers' shopping habits. However, "[I]n Europe and America Kao has failed to build the comprehensive distribution system that it has in Japan".²⁹ In 1996, around 20 per cent of Kao's sales came from overseas markets; by 2011, the percentage of foreign sales had risen to nearly 30 per cent, in ascending order of proportion from North America, Europe and Asia/Oceania. Kao has not been able to replicate fully its domestic success abroad.³⁰

Case example

The immobility of domestic networks has also brought tremendous challenges to many foreign retail banks in Japan, such as Citibank (now Citigroup). Despite its leading position in the US retail banking industry and a large network of branches in the US, Citibank found it difficult to access Japanese customers when it decided to target individual consumers in 1984. It took Citi-Japan a full ten years to break into the Japanese market. According to Citibank, "[R]etail banking . . . is like the petrol-station business: you've

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.

Management insights

Management insights

Applying the concepts developed in Chapter 1, we see that Prahalad and Hamel's notion of core competencies is largely equivalent to the higher-order FSA concept, with a strong focus on routines and recombination capabilities. Recombination capabilities are especially critical for Prahalad and Hamel, but, as they correctly point out, these can be difficult to define exactly or to deconstruct. These FSAs are also affected by the administrative infrastructure or heritage that has evolved over the life of the company. However, the key ingredients are similar to the ones described in Chapter 1: an *entrepreneurial attitude* of senior corporate-level managers and competence carriers, critical to identifying and pursuing new *market opportunities* and to uncovering *resources that are not yet fully utilized* and can be deployed in other markets, and an *organizational ability to meld extant and new resources* in novel ways.

In terms of the patterns of FSA development discussed in Chapter 1, the authors paradoxically focus largely on Pattern I (see Figure 1.7 in Chapter 1), with core competencies typically developed in the home country (guided by corporate-level senior management) and then diffused to the rest of the firm. Here, the firm has been very effective in recombination at home, across product lines and units, but there is little need for further recombination abroad. The authors assume that North American and European firms are less effective than Asian companies in implementing Pattern I. As the authors see it, internationally transferable FSAs are typically developed in the home country, but their exploitation is, unfortunately, usually bounded to one unit, rather than shared across the company. The authors advocate that North American and European firms shift their strategic focus to align with that of Japanese MNEs, but observe that North American and European firms are hampered by an administrative heritage of 'bounded innovation'. Bounded innovation

means that innovation activities and resulting resource recombinations are guided by decentralized unit goals rather than corporate goals, and innovation outcomes remain within the unit, rather than being deployed throughout the firm. The authors also criticize the presence of imprisoned resources, whereby the different units fully control specific individuals and technologies underlying core competencies. The authors thereby point to extensive bounded rationality problems in Western firms, since corporate-level senior management lacks the insight to engage in corrective action.

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.

Case studies

Case 1.1 Honda's 'answers' to the seven basic questions in international strategy formation

For the Japanese car manufacturer Honda, the domestic and international environments in the early 1970s brought tremendous challenges to its export strategy, previously based on mass production in Japan. Honda wanted to develop extensive international production capabilities in overseas markets, especially the US market. However, Honda doubted its foreign facilities could attain the quality level characteristic of its Japanese-built cars. Furthermore, Honda also wondered whether its foreign manufacturing facilities could achieve Japanese cost levels.

The environment in the early 1970s

Internationally, Honda faced three major environmental changes in the early 1970s: the rising value of the yen against the US dollar, new US regulations of tailpipe emissions and the first oil crisis. Although the rising yen threatened Honda's traditional export strategy, the other two changes – together with the success of its small, fuel-efficient Civic model in Japan and the US – provided a window of opportunity for Honda to expand in the US.

Specifically, the rising value of the yen in 1971 increased the costs of exporting cars to the US, Honda's largest overseas market. The first oil crisis of 1973 negatively affected Honda's domestic operations, as rising oil prices significantly increased Honda's manufacturing costs. At the same time, however, the public demanded more fuel-efficient cars to reduce the costs brought by the roaring oil prices.

In 1970, the US Congress passed the Clean Air Act, imposing stricter requirements on tailpipe emissions. However, the US automakers had not been able to reach a consensus regarding the appropriate technology to meet such requirements. Both the first oil crisis and the Clean Air Act pushed the demand for fuel-efficient cars, which became the market niche US automakers had not been able to occupy. Clearly, Honda viewed the US regulations as a welcome opportunity for it to catch up, as reflected in the words of Honda's President Soichiro Honda: "(T)his allows latecomers like us to line up at the same starting line as our rivals".¹⁰⁷

In 1972, Honda brought to the Japanese market its Civic model with the CVCC (Controlled Vortex Combustion Chamber) engine, which met the US emissions standards. The CVCC engine permitted the regulated burning of a very lean mixture without the catalytic converter or exhaust-gas recirculation required by most other engines. In Japan, the Civic model won the Car of the Year Award for three consecutive years as of 1973; in the US, it beat all other competitors in a fuel-economy test for four consecutive years as of 1974.

Thirty '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.

Case questions

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?

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.

Web materials

ents:

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.