Entry Strategy / Modes of Entry into International business

Before deciding on the mode of entry, any firm contemplating foreign expansion must first struggle with the issue of which foreign markets to enter and the timing and sale of entry.

ENTRY MODES

Once a firm decides to enter a foreign market, the question arises as to the best mode of entry. When pursuing international business, a co. can choose from a number of operating modes.

- EXPORTING

Exporting is the selling of goods in one's own country for use or resale in other countries. More cos. are involved in exporting than in any other international mode. Many manufacturing firms begin their global expansion as exporters and only later switch to another mode for serving a foreign market
Merchandise export/ visible trade: Trade in goods / tangible products such as clothing, computers and raw materials.
Service exports /invisible trade: Trade in services / intangible products such as banking, travel and accounting activities.

- *Tourism and transportation*: International tourism and transportation are important sources of revenue for airlines, shipping cos., travel agencies and hotels. Some economies depend heavily on revenue from these sectors. E.g, in Bahamas, earnings from foreign tourism are more important than export of goods. In recent years, the US has earned more form foreign tourism than its exports of agricultural goods.
- *Performance of services*: Services like banking, insurance, engineering, management services etc. bring earnings to the cos. in the form of fees. E.g., on an international level, cos. pay fees for engineering services that are often handled through **turnkey operations** (construction of facilities that are transferred to the owner when they are ready to begin operating). Cos. also pay fees for management contracts- arrangements in which one co. provides personnel to perform general or specialized management functions for another co.

(In countries like Japan, there are international trading houses which transact enormous volume of business. The Export Houses, Trading Houses, Star Trading Houses and Super Star Trading Houses of India are merchant exporters – they buy and resell goods. They are comparatively small in size compared to the giant trading houses of Japan.)

Often, cos. Begin as **passive exporters**, where the effort can be as little as treating and filling overseas orders like domestic orders. A co. gets an order over its website or while showing its goods at a trade fair and just treats the foreign customer the same as any other customer. Alternatively, an MNC can put more resources into exporting using, for example, a dedicated export department or division or an international sales force.

such case rather than transferring a physical product, an MNC can transfer an intangible know-how through a license.

b. Distance: Exporting long distances, specially with products that are heavy or perishable, can significantly add to costs. So, where transportation costs can make a product prohibitively expensive in a target county market, licensing the tech. to local producers is a good option.

3. *Nature of the company*: Where the co. lacks adequate financial, technical or managerial resources to export or invest directly in foreign operations, licensing can be an attractive entry strategy.

Franchising

It is a specialized form of licensing where a firm in one country (the franchisor) authorizes a firm in a second country (the franchisee) to utilize its operating systems as well as its brand names, trademarks and logos in return for a royalty payment. (The franchisor assists on a continuing basis in the operation of business – e.g. by providing components, management services and technology). The franchisor licenses to the franchisee the use of a whole business model.

Franchising is a method of doing business wherein a **franchisor** licenses trademarks and tried and proven methods of doing business to a **franchisee** in exchange for a recurring payment, and usually a percentage piece of gross sales or gross profits as well as the annual fees. Various tangibles and intangibles such as national or international advertising, training, and other support services are commonly made available by the franchisor, and may indeed be required by the franchisor.

Advantages:

- ***Quick start*** - Franchising offers franchisees the advantage of starting up a new business quickly based on a proven trademark and formula of doing business, as opposed to having to build a new business and brand from scratch
- ***Expansion*** - After their brand and formula are carefully designed and properly executed, franchisors are able to expand rapidly across countries and continents, and can earn profits commensurate with their contribution to those societies.
- ***Training*** - Franchisors often offer franchisees significant training, which is not available for free to individuals starting up their own business.
- ***Consistency*** - For some consumers, having franchises offer a consistent product or service makes life easier. They know what to expect when entering a franchised establishment.

Disadvantages:

- ***Control*** - For franchisees, the main disadvantage of franchising is a loss of control. While they gain the use of a system, trademarks, assistance, training, and marketing, the franchisee is required to follow the system and get approval for changes from the franchisor. For these reasons, franchisees and entrepreneurs are very different.
- ***Price*** - It can be expensive. Because of standards set by the franchisor, the franchisee often has no choice as to signage, shop fitting, uniforms etc. and may not be allowed to

source less expensive alternatives. Added to that is the franchise fee and ongoing royalties and advertising contributions. The franchisee may also be contractually bound to spend money on upgrading or alterations as demanded by the franchisor from time to time.

- ***Conflicts*** - Another problem is that the franchisor/franchisee relationship can easily cause conflict if either side is incompetent (or not acting in good faith). For example, an incompetent franchisee can easily damage the public's goodwill towards the franchisor's brand by providing inferior goods and services, and an incompetent franchisor can destroy its franchisees by failing to promote the brand properly or by squeezing them too aggressively for profits.

For example, Mcdonalds Corporation franchises its fast-food restaurants worldwide. Mcdonald's has always been a franchising company and has relied on its franchisees, our Owner/Operators, to play a major role in the System's success. Mcdonald's is one of only a handful of brands that command instant recognition in virtually every country of the world. Mcdonald's began with one restaurant in the US in 1955 and today there are more than 26,500 restaurants in over 119 countries, serving around 39 million people every day - making mcdonald's by far the largest food service company in the world.

Franchising is not for everyone though - to operate a mcdonald's franchise you need the managerial and personal skills necessary to run a business employing 50 or more people and serving half-a-million customers a year

Today, International franchising in India is one of the most exciting areas in the franchise industry. Globetrotters are more likely to do their shopping in franchised stores. Global franchise organizations like Pizza Hut, Marks and Spencer, McDonalds, Subway, Dominos, Kodak, KFC are bullish on the potential of franchising in India and have started their franchise operations.

When to choose franchising?

- Where a consistent output needs to be provided to the customers; so a high degree of control over products and services required
- Brands that are easily identifiable and travel well cross-culturally. E.g. Subway, McDonalds
- Systematic operating systems are well-developed and easy to train culturally
- High profitability potential for the franchisee; franchisees must be able to pay their royalties to the franchisor and still have a reasonable profit

Management contract

It is an arrangement wherein a firm in one country agrees to operate facilities or provide other management services (personnel to perform general or specialized management functions) to a firm in another country for an agreed-upon fee.
A **management contract** is an arrangement under which operational control of an enterprise is vested by contract in a separate enterprise which performs the necessary managerial functions in return for a fee. Management contracts involve not just selling a method of doing things (as with franchising or licensing) but involves actually doing them. A management contract can involve a wide range of functions, such as technical

operation of a production facility, management of personnel, accounting, marketing services and training.

Example: Disney receives management fees from managing theme parks in France and Japan. In Asia, many hotels operate under management contract arrangements, as they can more easily obtain economies of scale, a global reservation systems, brand recognition etc. It is not unusual for contracts to be signed for 25 years, and having a fee as high as 3.5% of total revenues and 6-10% of gross operating profit. The Marriott International Corporation operates solely on management contracts. Hoteliers such as Marriot and Hilton often do not own the expensive hotels that bear their brand names throughout the world but rather operate them under management contracts. in which one co. for another co.
Management contracts have been used to a wide extent in the airline industry, and when foreign government action restricts other entry methods. Management contracts are often formed where there is a lack of local skills to run a project. It is an alternative to foreign direct investment as it does not involve as high risk and can yield higher returns for the company.

The Taj group will manage the Pierre in New York. This is in line with its global ambitions and may also have a salutary effect on its hotels in India. The management contract signed for The Pierre would appear to be significant to the Taj's overall market strategy given New York's importance as a gateway to the US and one of the most competitive luxury markets across the globe. Besides the 56 hotels it operates in India, the Taj group, the flagship brand of Indian Hotels Company Ltd, now has 15 international hotels spread across the Maldives, Mauritius, Seychelles, Sri Lanka, the UK, the US, Dubai, Bhutan and Malaysia (Langkawi); the last four being added in the past six months alone.

InterContinental Hotels Group has signed a series of contracts for the management of six new hotels with leading Delhi-based developer, Amrapali Group.This partnership marks the launch of Holiday Inn Express in India – one of the fastest growing hotel brands in the limited service category, opening on average two hotels a week globally. IHG and the Amrapali Group will develop six hotels between the Holiday Inn Express and Holiday Inn brands in the next three to five years,

Turnkey projects

In a turnkey project agreement, a firm agrees to construct an entire plant in a foreign country and make it fully operational. It is known as turnkey because the licensor starts the operation and hands over the key of the operating plant of the licensee. Agreements for turnkey projects normally take place where the initial construction part of the plant is more complex then the operational part. Such projects are either self-engineered (licensor decides the design of the project) or made to specifications (licensee decides). This is a means of exporting process technologies to other countries. Turnkey projects are most common in the chemical, pharmaceutical, petroleum refining and metal refining industries, all of which use complex, expensive, production technologies

Advantages:

- Allow firms to specialize in their core competencies.
- Allow host governments to obtain world-class designs for their infrastructure projects.
- Advantageous where host govt. restrict inflow of capital. eg. Many oil exporting countries did not permit FDI in the oil sector. And have set out to build their own petroleum-refining industries. But because many of these countries lack petroleum-refining technology, they gain it by entering into turnkey projects with foreign firms that

have the technology. Such deals are often attractive to the selling firm because without them, they would have no way to earn a return on their valuable know-how.
Disadv:

- Suppliers of turnkey projects often fall back on their own monopoly position in the international market.
- If the firm's process technology is a source of competitive advantage, then selling this technology through a turnkey project is also selling competitive advantage to potential or actual competitors.
- No long-term interest in the foreign country; but the country subsequently proves to be a major market for the output of the process.

Larsen & Toubro: Founded in 1938, **Larsen & Toubro Limited (L&T)** is one of Asia's largest vertically integrated Engineering & Construction conglomeratesIn line with its strategy of aligning capabilities to meet emerging trends, L&T recently initiated a mega-transformation process, internally to ensure that it emerges, as a knowledge-based Indian multinational. Over the years the company has proactively created the necessary infrastructure for its global initiative with office locations in USA, Europe, Middle East and Japan.

The Engineering and Construction (E&C) Division forms the biggest segment of its parent group Larsen and Toubro's Business Portfolio. This division is capable of carrying out turnkey projects in core sector of Industry on EPC basis.

- COUNTER TRADE

Counter-trade is a sort of bilateral trade where one set of goods is exchanged for another set of goods. It is an alternative means of carrying out an international transaction when conventional means of payment are difficult, or non-existent. Where there are restrictions on currency convertibility (partial convertibility), it becomes problematic for exporters. Non-convertibility implies that the exporter may not be able to be paid in his or her home currency; counter-trade is often the solution. Counter-trade denotes a whole range of barter-like agreements; its principle is to trade goods and services for other goods and services when they cannot be traded for money.
Examples: 1. Saudi Arabia agreed to buy ten 747 jets from Boeing with payment in crude oil, discounted at 10% below posted world oil prices.
2. An Italian company manufacturing power generating equipment was awarded a contract ($17.7 million) by the Electricity Generating Authority of Thailand. The contract specified that the company had to accept ($5.4 million) Thai farm products as part of the payment.

The Growth of Counter-trade

In the modern era, counter-trade arose in the 1960s as a way for the Soviet Union and Communist states of Eastern Europe, whose currencies were generally non-convertible to purchase imports. During the 1980s, the technique grew in popularity among many developing nations that lacked the foreign exchange reserves required to purchase necessary imports. According to some estimates, more than 20% of the world trade by value in 1998 was in the form of counter trade. There was a notable increase in the volume of counter-trade after the Asian financial crisis of 1997. That crisis left many

Asian nations with little hard currency to finance international trade. In the tight monetary regime that followed the crisis in 1997, many Asian firms found it difficult to get access to export credits to finance their own international trade. Consequently, they turned to counter-trade.

The governments of some developing nations sometimes insist on a certain amount of counter trade to sell their own products.

Types of Counter-trade

Broadly, the trading arrangements under counter-trade can be grouped into five distinct categories.

1. Barter

It is the direct exchange of goods and services between two parties without a cash transaction. The quantum, quality and value of goods to be exchanged are well-defined. However, it has few problems. Firstly, if goods are not exchanged simultaneously, one party ends up financing the other for a period. Secondly, firms engaged in barter run the risk of having to accept goods they do not want, or have difficulty reselling at a reasonable price. For these reasons, barter is viewed as the most restrictive counter-trade arrangement. It is used primarily for one-time-only deals in transactions with trading partners who are not creditworthy.

2. Counter-purchase

It is a reciprocal buying agreement. It occurs when a firm agrees to purchase a certain amount of material back from a country to which a sale is made. Suppose a US firm agrees to spend some of its proceeds from the sale on handlooms/garments/textiles/agricultural products produced by India. Thus, although India must draw on its foreign exchange reserves to pay the US firm, it knows it will receive some of those dollars back because of the counter-purchase agreement.

The type and price of goods are generally not specified at the time of signing the contract. The exporter of goods agrees to accept, in return, a wide range of goods from the importer.

3. Offset

This is similar to a counter-purchase agreement in that one party agrees to purchase goods and services with a specified percentage of the proceeds from the original sale. The difference is that this party can fulfill the obligation with any firm in the country to which the sale is being made. From an exporter's perspective, this is more attractive than a straight counter-purchase agreement because it gives the exporter greater flexibility to choose the goods that it wishes to purchase.

4. Switch trading

This refers to the use of a specialized third-party trading house in a counter-trade agreement. When a firm enters a counter-purchase or an offset agreement with a country, it often ends up with what are called counter-purchase credits, which can be used to

purchase goods from that country. Switch trading occurs when a third party trading house buys the firm's counter-purchase credits and sells them to another firm that can better use them. For example, an Indian firm concludes a counter-purchase agreement with Indonesia for which it receives some number of counter-purchase credits for purchasing Indonesian goods. The Indian firm, however, does not want any Indonesian goods now; so it sells the credits to a third party trading house at a discount. The trading house then finds a firm that can use the credits and sells them at a profit.

5. Compensation or buybacks

A buyback occurs when a firm builds a plant in a country- or supplies technology, equipment, training or other services to the country- and agrees to take a certain percentage of the plant's output as partial payment for the contract. This is a form of industrial counter-trade and involves a large amount corresponding to the sale of industrial equipment or turnkey plants in exchange for the products manufactured by these industrial plants. Naturally, the contract period is longer varying from 10-20 years. In 1979, Austria sold pipeline equipment and related material to the then Soviet Union so that the latter could develop certain gas fields and could pipe a part of the output back to Austria. In case of developing countries, such agreements are common as they suffer from technology gap on a large scale.

Merits of Counter-trade

1. It gives firms a way to finance an export deal when other means are not available. For instance, developing nations often have problems in raising the necessary foreign exchange to pay for imports; counter-trade helps them in meeting their import requirements. Further, for the exporting countries, this may be the only option available while doing business with these countries.

2. Counter-trade helps stabilize export earnings because it predetermines the size of exports and imports.

3. Counter-trade may sometimes be needed to respond to competition. If a firm is unwilling to enter a counter-trade agreement, it may lose an export opportunity to a competitor that is willing to make a counter-trade agreement. For instance, Boeing often has to agree to counter-purchase agreements in order to capture orders for its commercial jet aircraft. For example, in exchange for gaining an order from Air India, Boeing may be required to purchase certain component parts, such as aircraft doors from an Indian company. Taking this one step further, Boeing can use its willingness to enter a counter-purchase agreement as a way of winning orders in the face of intense competition from its global rival, Airbus Industries. Thus, counter-trade in such a case can become a strategic marketing weapon.

4. It helps in diversification of exports by allowing greater outlet for exportable goods. This in turn creates a more competitive market.

5. It is helpful for developing and other countries that have foreign exchange problems.

Demerits of Counter-trade

1. Other things being equal, firms would normally prefer to be paid in hard currency. Counter-trade contracts may involve the exchange of unusable or poor quality goods that the firms cannot dispose off profitably. Further, even if the goods it receives are of a high quality, the firm still needs to dispose them off profitably. To do this, counter-trade requires the firm to invest in an in-house trading department dedicated to arranging and managing counter-trade deals. This can be expensive and time-consuming.

2. Lack of encouragement for quality improvement.

Conclusion: Given the pros and cons of counter-trade, it is most attractive to large, diverse MNCs that can use their worldwide network of contacts to dispose off goods acquired in counter-trade. The masters of counter-trade are Japan's giant trading firms, which use their vast network of affiliated companies to profitably dispose off goods acquired in counter-trade agreements. For example, the trading firm of Mitsui and company, has about 120 affiliated companies in almost every sector of the manufacturing and service industries. Western firms that are large, diverse and have a global reach (e.g., General Electric, Philip Morris etc.) have similar profit advantages from counter-trade agreements. Unless there is no alternative, small and medium-sized exporters should try to avoid counter-trade deals because they lack the worldwide network of operations that may be required to profitably utilize or dispose off goods acquired through them.

CASE STUDY

A small Canadian firm that has developed some valuable new medical products using its unique biotechnology know-how is trying to decide how best to serve the European Community market. Its choices are:

a. Manufacture the product at home and let foreign sales agents handle marketing.

b. Manufacture the products at home and set up a wholly owned subsidiary in Europe to handle marketing.

c. Enter into a strategic alliance with a large European pharmaceutical firm. The product would be manufactured in Europe by the 50/50 joint venture and marketed by the European firm.

The cost of investment in manufacturing facilities will be a major one for the Canadian firm, but it is not outside its reach. If these are the firm's only options, which one would you advise it to choose? Why?

ANSWER

The reasoning behind the answer here is what matters. Depending on the firm's comparative advantage and long-term strategy, along with market conditions for the product, any of these approaches might be reasonable.

a. If the firm has a focus on bio-tech and wants to develop long-term in this focused direction, developing and then manufacturing medical products, the first option would be reasonable. We assume that the product development and manufacture

is not too readily imitable and that it has copyright protection. Economies of scale may dictate one manufacturing facility, as well.

b. If this product is a blockbuster that has large margins and may generate huge profits for the company, and control is an issue, they may want to do the marketing through a wholly-owned subsidiary. That way, the company could control the knowledge and technology as well as the speed of market entry.

c. A joint venture would give the company access to local distribution and may help with any government approval process. It would also be less costly for the firm. At the same time, if the J-V is with a potential competitor, this market entry approach may diffuse the competitor's threat.

Once a co. moves beyond passive exporting, there are two general export strategies for the MNC: *direct or indirect exporting.*

1. **Direct exporting** is the more active and aggressive exporting strategy where exporters make direct contact with customers in the foreign market. In case of *direct export,* a company takes full responsibility for making its goods available in the target market by selling directly to its end users, normally through its own agents. Direct export is feasible when the exporter desires to involve itself greatly in international business; and at the same time possesses the capacity to do so. In certain cases like aircrafts and similar industrial products, direct export is more convenient. Direct exporters may set up their own branch offices in foreign countries.

Direct exporters can sell directly to foreign retailers. For eg., Samsung (Korea) and Sony (Japan) sell electronic products directly to large retailers like Walmart. Depending on their resources and local laws, direct exporters can also sell directly to foreign end-user customers. However, this direct sales approach is more common for companies selling industrial products to other companies than for an exporter trying to sell consumer products like toothpaste or shampoos to individual consumers.

2. **Indirect export** takes place when the exporting company does not possess the necessary infrastructure to involve itself in direct exporting. Here, the exporting company sells its products to intermediaries who, in turn sell the same products to the end users in the target market. Intermediaries can further be divided into:

- Export management companies (EMCs) – When a co. uses an EMC, it is outsourcing the functions that the co. otherwise does internally with an export unit. So, the EMC promotes the co.'s products to international buyers and distributors. EMC usually specialize in selling particular types of products or understanding the cultures and markets of particular countries or regions. For eg., an EMC might specialize in fruit products for the Asian market and an apple producer who wished to export to Japan would seek an MNC with that specialization. When an EMC functions as a distributor, it takes title to goods, sells them on its own account and assumes the trading risk. Alternatively, when it acts as an agent, it charges a commission. An EMC normally acts as an agent.
- Export Trading companies (ETCs) – provides services to exporters in addition to exporting activities, such as storage facilities, financing services and so on. Also, ETC usually take title to the product before exporting. Rather than representing a manufacturer in foreign market, the ETC identifies what products or services are in demand in a foreign market. It then seeks out domestic cos. that can provide what the foreign market desires.

Advantages of Exporting

1. It avoids substantial costs of establishing manufacturing operations in the host country.
2. By manufacturing the product in a centralized location and exporting it to other national markets, the firm may realize substantial scale economies from its global sales volume. This is how Sony came to dominate the global TV market; how

many Japanese automakers entered the US market; how Samsung (South Korea) gained market share in computer memory chips.

Disadvantages of Exporting

1. Exporting from the firm's home base may not be appropriate if lower-cost locations for manufacturing the product can be found abroad
2. High transport costs can make exporting uneconomical, particularly for bulk products.
3. Tariff barriers can make exporting uneconomical.
4. The firm cannot exercise tight control over marketing and sales, especially in indirect exporting. Where local agents are used for marketing and selling, they may not do as good a job as the firm would if it managed its marketing itself.

- INTERNATIONAL INVESTMENTS

The second major form of international business activity is international investments – capital supplied by residents of one country to residents of another. Generally, foreign investment takes two forms:

Foreign Direct Investment (FDI): A direct investment is one which gives the investor a controlling interest in a foreign company. It is made for the purpose of actively controlling property, assets or companies located in host countries. (When two or more cos. share ownership of an FDI, the operation is a ***joint venture***.)

Foreign Direct Investment (FDI) is the outcome of the mutual interests of multinational firms and host countries. The International Monetary Fund (1977, p.408) has defined FDI as "investment that is made to acquire a lasting interest in an enterprise operating in an economy other than that of the investor, the investor's purpose being to have an effective voice in the management of the enterprise." The essence of FDI is the transmission to the host country of a package of capital, managerial, skill and technical knowledge.

Portfolio Investment: A portfolio investment is a non-controlling interest in a company. They are purchases of foreign financial assets (stocks, bonds and certificates of deposits) for a purpose other than control. The basic idea behind buying shares of foreign cos. is to raise the rate of return on the asset portfolio rather than control a co.'s decision-making.

Foreign portfolio investments are important for most cos. that have extensive international operations. Cos. use them primarily for short-term financial gains.

FDI versus Portfolio Investment

As a matter of clarification, it is important to distinguish between FDI and portfolio investment. FDI is generally defined as a form of long-term international capital movement, made for the purpose of productive activity and accompanied by the intention of managerial control or participation in the management of a foreign firm. FDI should not be confused with portfolio investment which does not seek management control, but is

motivated by profit. Portfolio investment occurs when individual investors invest, mostly through stockbrokers, in stocks of foreign companies in foreign land in search of profit opportunities.

A United Nations report (1999a, p.35) has revealed that FDI flows are less volatile than portfolio flows. To quote, "FDI flows to developing and transition economies in 1998 declined by about 5 percent from the peak in 1997, a modest reduction in relation to the effects on other capital flows of the spread of the Asian financial crisis to global proportions. FDI flows are generally much less volatile than portfolio flows. The decline was modest in all regions, even in the Asian economies most affected by the financial crisis."

INTERNATIONAL STRATEGIC ALLIANCES (ISA)

ISA is an agreement between two or more firms from different countries to cooperate in any value chain activity form R&D to sales. Thus **ISA refer to cooperative agreements between two or more firms from different countries.**

Strategic Alliance is a formal relationship between two or more parties to pursue a set of agreed upon goals or to meet a critical business need while remaining independent organizations. Partners may provide the strategic alliance with resources such as products, distribution channels, manufacturing capability, project funding, capital equipment, knowledge, expertise. The alliance is a cooperation or collaboration which aims for a synergy where each partner hopes that the benefits from the alliance will be greater than those from individual efforts.

Stages of Alliance Formation

1. Strategy Development:

Strategy development involves studying the alliance's feasibility, objectives and rationale, focusing on the major issues and challenges and development of resource strategies for production, technology, and people. alliance objectives with the overall corporate strategy.

2. Partner Assessment: :

Analyzing a potential partner's strengths and weaknesses creating strategies for accommodating all partners' management styles preparing appropriate partner selection criteria understanding a partner's motives for joining the alliance addressing resource capability gaps that may exist for a partner.

3.Contract Negotiation: :

Determining whether all parties have realistic objectives forming high calibre negotiating teams defining each partner's contributions and rewards as well as protect any proprietary information, addressing termination clauses penalties for poor performance, highlighting the degree to which arbitration procedures are clearly stated and understood

4.Alliance Operation: :

Strategy Development
Partner's Assessment
Contract Negotiation.
Alliance operation

Addressing senior management's commitment, finding the calibre of resources devoted to the alliance, linking of budgets and resources with strategic priorities, measuring and rewarding alliance performance, assessing the performance and results of the alliance.

5.Alliance Termination :
Winding down the alliance, for instance when its objectives have been met or cannot be met, or when a partner adjusts priorities or re-allocates resources elsewhere.

Types of SA

Mainly, two basic options are available for an ISA:

1. ***International Joint Ventures (IJV)***: Two or more firms from different countries have an equity (or ownership) position in a new, separate company. Although 50:50 ownership between two cos. is the most common form, some IJVs have several participants and any individual co. may have a minority, majority or equal partnership in the IJV. Example – General Motors have a 50:50 JV with Shanghai Automotive industry Corp Group of China and the ISA has resulted in Shanghai General Motors Co. Ltd. in China.
2. ***International Cooperative Alliance (ICA)***: To form a non-equity based ICA, all that is necessary is that two or more firms from different countries agree to cooperate in any value-chain activity or a particular task. Unlike IJV, an ICA does not require the participating cos. to set up a separate co. Instead the participants usually sign a contract agreeing to cooperate in some venture. Example – French co. Renault and the US co. Ford jointly design, produce and sell utility vans in Europe for the commercial market. Although quite profitable on per unit sales, the market for commercial vans is not big enough to warrant single cos. investing in design and production and then competing with each other.

During the last decade, ISA have become one of the more popular entry strategies for MNCs. Even those larger MNCs that have the financial resources and international expertise to operate directly in foreign countries have turned increasingly to using ISA as entry strategies.

Advantages of ISA

1. Local partner's Knowledge of the market - ISA may facilitate entry into a foreign market. MNCs often use SAs with local firms in a foreign market to tap the local partner's knowledge of the market. Naturally, such a partner would have more insights regarding needs of local customers and local mechanism such as govt. regulations necessary to get a product or service to market. For example, many firms who plan to enter China enter into ISA with Chinese cos. who understand business conditions and who have good connections. Many a times foreign cos. have to go through complex approval process in China. Due to participation of Chinese firms, however, the JVs often go through streamlined approval process. So, Warner Bros,

have entered into JVs with 2 Chinese partners to produce and distribute films in China.

2. Risk sharing - ISA allow firms to share the fixed costs (and associated risks) of developing new products or processes. Sometimes, a potential venture is too risky for one co. to take on by itself. Factors that might increase risk include projects using a new or untested technology or when start-up costs of firms require a heavy investment. Some projects are so expensive relative to the size of firm that a failure would doom a single firm to bankruptcy. For example, in the commercial airline industry, no one European co. was willing to take on the US giant Boeing. Instead several European cos. formed a JV which became the Airbus consortium.

3. Sharing technology and complementary skills – Not all cos. have the same technological strength. So, MNCs use alliances with cos. from other countries that have complementary technological strengths. In combination, two or more cos. often can bring a new product to market more quickly and with higher quality. For example: Sony Ericsson is a 50:50 JV between Ericsson (Swedish telecom co.) and Sony(Japanese consumer electronics co.). After forming the JV, both cos. stopped making their own cellphones. The logic is to let the JV co. use Sony's knowledge in consumer electronics and Ericsson's expertise in cellular technology.

4. Meeting Govt. requirements in certain cases – In many developing countries, govts. often want to ensure that their nationals have an ownership position in any foreign venture. JVs could also be a condition for entry into a country. For example, UAE requires that 51% of the ownership be local. In many countries such as China, the govt. itself is often a JV partner. Just as a local partner can bring in a good knowledge of the local market, they can also bring a good knowledge of how to deal with local govt. bureaucracies.

Disadvantages of ISA

Examples of Strategic alliances in India

1. Tata Motors and Fiat are close to signing a worldwide agreement that will have the two automobile majors cooperating in a wide range of areas, including joint research and development for cars for overseas markets and the use of Fiat's retail presence abroad for marketing Tata cars. (April 2010)
2. Blue star has entered into a strategic alliance with Italian co., ISA, for providing a range of supermarkets and food refrigeration solutions.
3. IBM and Wipro announced a strategic alliance in 2002 to address India and the Asia Pacific region. As part of this alliance, Wipro will market and integrate IBM's wide range of server and storage products in India. In the Asia Pacific region, Wipro will work with IBM to provide customers, IT Services across the

region, including Japan. The Services offered will include ERP implementation, customer relationship management, Web enablement and workflow implementation services. IBM and Wipro today announced a strategic alliance to address India and the Asia Pacific region.

- **CONTRACTUAL ENTRY MODE**

LICENSING

To **license** or **grant license** is to give permission. A license is the document demonstrating that permission. License may be granted by a party ("licensor") to another party ("licensee") as an element of an agreement between those parties

It is a legal arrangement whereby a firm in one country licenses the use of its intellectual property (patents, trademarks, brand names, copyrights or trade secrets) to a firm in a second country in return for a royalty payment.

A licensor may grant **license** under "intellectual property" to do something (such as copy software or use a patented invention) without fear of a claim of intellectual property infringement brought by the licensor.

(Licensing is an arrangement by which a firm transfers its intangible properties such as expertise, technology, manufacturing design etc. to a firm located abroad or to its own unit abroad. The firm transferring technology etc. is known as the licensor and the firm receiving it is known as the licensee. The arrangement is meant for a specific period and the licensor gets technical service fees from the licensee. The licensee, on his part does not have to make huge investments in R&D.)

Patent: The term "patent" usually refers to a right granted to anyone who invents or discovers any new and useful process, machine, article of manufacture, or composition of matter, or any new and useful improvement thereof. E.g. row over basmati. Experts may be divided on the recent basmati case, with some arguing that far from losing, India has, in fact, won because no patent has been given to the us firm on basmati. However, if texmati is marketed as a brand superior to basmati, it goes without saying that the latter's market could be hit (The US patent and trademark office (uspto) recently upheld the patent granted to ricetec, a texas-based company, for three strains of basmati rice it made, including `texmati' which it claims is ``even superior to basmati').

Trademark: A trademark is a distinctive sign indicator of some kind which is used by an individual, business organization or other legal entity to uniquely identify the source of its products and/or services to consumers, and to distinguish its products or services from those of other entities. A trademark is a type of intellectual property, and typically comprises a name, word, phrase, logo, symbol, design, image, or a combination of these elements.

The concept of licensing is well-established, both in the area of patents and trademarks. Trademark licensing has a rich history in American business, largely beginning with the rise of mass entertainment such as the movies, comics and later television. Mickey Mouse's popularity in the 1930s and 1940s resulted in an explosion of toys, books, and consumer products with the lovable rodent's likeness on them, none of which were manufactured by the Walt Disney Company. Crème bell ice-cream in India has recently launched Mickey's ice-creams.

This process accelerated as movies and later television became a staple of American business. The rise of brand licensing did not begin until much later, when corporations found that consumers would actually pay money for products with the logos of their favorite brands on them. McDonalds play food, Burger King t-shirts and even ghastly Good Humor Halloween costumes became commonplace. Brand extensions later made the brand licensing marketplace much more lucrative, as companies realized they could make real dollars renting out their equity to manufacturers. Instead of spending untold millions to create a new brand, companies were willing to pay a royalty on net sales of their products to *rent* the product of an established brand name. Breyers yogurt, TGI Friday's frozen appetizers, Dodge power tools, and Lucite nail polish are only a fraction of the products carrying well-known brand names which are made under license by companies unrelated to the companies who own the brand.

So successful has the process become that some companies like Harley-Davidson and Nathan's make more money from licensing than from manufacturing.

Advantages of Licensing

1. The licensor does not have to bear the development cost and risks associated with opening a foreign market (since licensee puts up most of the capital).
2. Licensing can be attractive when a firm is unwilling to commit substantial financial resources to an unfamiliar territory.
3. Licensing can be used when a firm wishes to participate in a foreign market but is prohibited from doing so by barriers to investment.

Disadvantages of Licensing

1. It does not give the firm a tight control over manufacturing, marketing and strategy.
2. In case of technological know-how, there is a high risk involved. Since technological know-how forms the basis of many MNCs' competitive advantage, most firms wish to maintain control over how their know-how is used, and a firm can quickly lose control over its technology by licensing it. (Competitors in host country can quickly assimilate technology, if not properly controlled and use it to enter other markets thereby taking away market share of the pioneer firm).

When to choose licensing?

1. *The product*: If the co. has a product that no longer has domestic sales potential (because of old technology or market saturation). The old technology may still remain attractive in other countries, particularly developing countries.
2. *Characteristics of the target country*:
   a. Where a country has trade barriers such as tariffs or quotas, it adds to the costs of exported goods, thereby increasing price and reducing demand. In