Presentation
on
Modes of Entry into International Business

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International Business

The transactions which involve cross border transfer of goods, services, knowledge, skills and resources between two or more nations are covered under international business.

According to International Business Journal, "International business is a commercial enterprise that performs economic activity beyond the bound of its location, has branches in two or more foreign countries and makes use of economic, cultural, political, legal and other differences between countries."

Need of engaging in International Business

1. All the goods and services needed by a country cannot be produced within the country due to shortage of resources.
2. Globalization make the availability of talented workforce with new ideas, knowledge and skills from all over the world which help in the growth of the business and nation as well
3. There is extension of customer base in international business.
4. New technology developed in other countries is made available with the help international business .
5. It helps in the international growth of domestic marketers.

Domestic business Vs International Business

Basis of Difference	Domestic Business	International Business
Geographic Limits	It is carried out within the national borders of the country.	It is carried out across national borders and at global level.
Tariffs and Quotas	Tariffs and quotas does not influence domestic business.	Tariffs and quotas are imposed in international business.
Investment	Investment is not very high.	Large investment is required.
Quality Standards	Quality standards are not very high.	Quality standards are very high.
Distribution	A company is free to select the distribution system.	The distribution network depend upon the system operating in the country with whom the business is carried out

Modes of entry into international business

1. Manufacturing at home
2. Manufacturing abroad
3. Investment entry
4. Counter trade
5. Other methods

1. Manufacturing at home

In this mode the company manufactures in home country and sells in foreign countries. It is an easy method of entry into international business . In this mode of international business lower risk is involved. Moreover lower level of commitment of funds are involved in this method.

Manufacturing at home

- Exporting
  a. Indirect export
  b. Direct export
- Complementary export/ piggy backing
- Co-operative export mode
- Intra corporate transfers
- Off shore services

Exporting: It is the most traditional method of entering into foreign trade in which a company produces goods in home country and then sells the products to customers in foreign countries.

- Example: Tata Iron and Steel exports its products to America, European Union, Jordan, Qatar etc.

Indirect exporting : in this mode a country exports with the help of an intermediary and does export directly to the customers in foreign countries. The intermediaries involved bear all the risk and responsibilities. The intermediaries can be:

1. Export houses (who sells in their own names)
2. Conforming houses (who brings buyers and sellers together)
3. Buying houses (who find sellers to fulfil the needs of the buyers)
4. Export management companies (who assume the risk instead of commission)

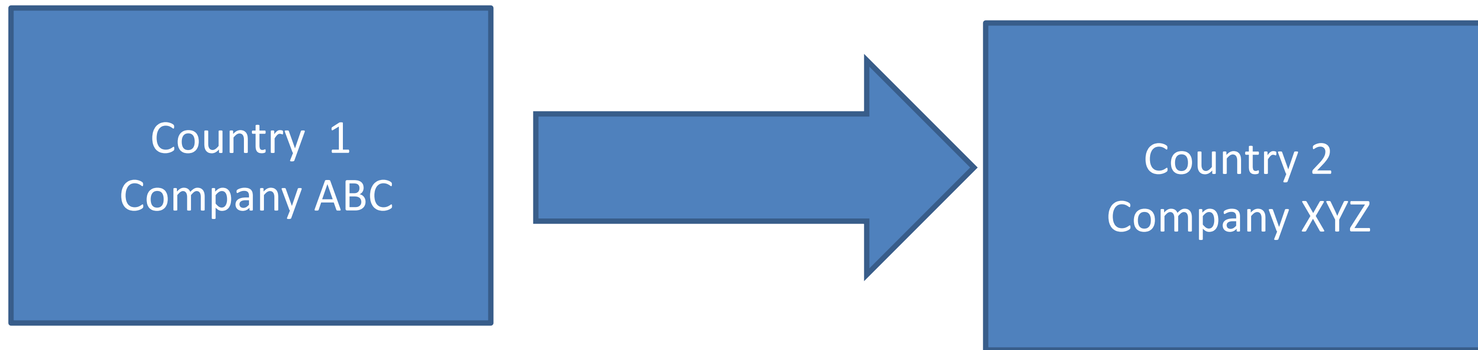
Advantages of indirect exporting:

1. Less risk is involved as risk is transferred to intermediaries.
2. Benefits of specialized services of intermediaries.
3. Less amount of funds are required.
4. Easy availability of funds, raw material due to the help of intermediary.
5. Easy method for small business houses.

Disadvantages of indirect exporting:

1. No direct information about the customers.
2. No control over the decisions of price, packaging and promotion.
3. No incentives.
4. Less revenue.
5. Heavy dependence on intermediaries.

Direct Export: In this mode a company exports to its customers in foreign countries in its own name and develop relationship with them. Moreover, buyers in foreign countries make payment through proper banking channel.



Company ABC in Country 1 exports to Company XYZ in Country 2

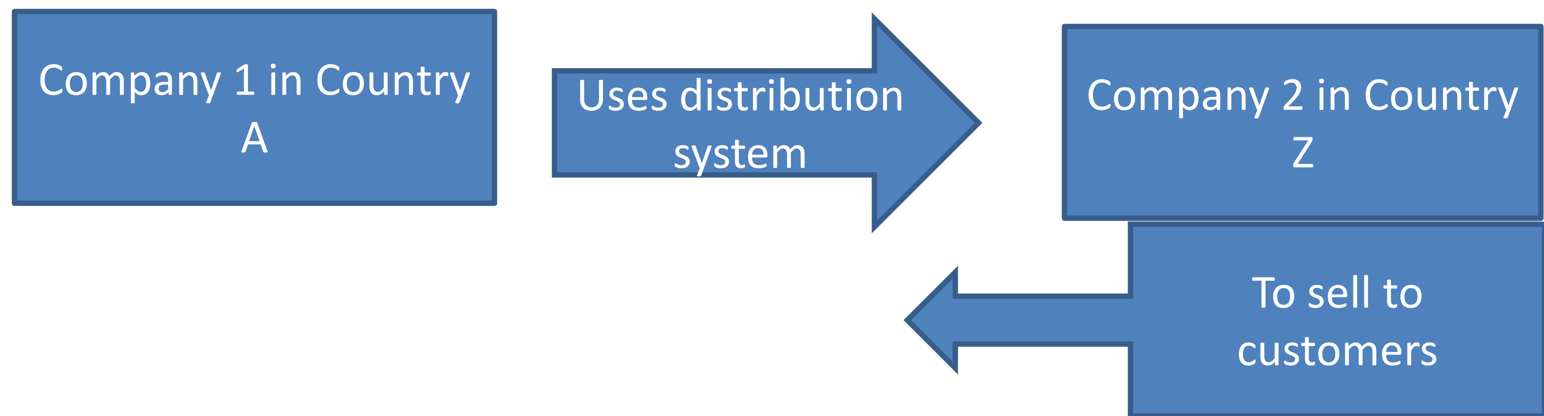
Advantages of Direct exporting

1. Extra cost to be paid to intermediary is not involved.
2. Company has greater control over its sales.
3. Direct link with customers.
4. Easy feedback.
5. Increased profits.
6. Exporter gets benefits from the government

Disadvantages of Direct exporting

1. Increased initial expenditure.
2. Greater risks are involved.
3. Larger stocks are required to be maintained.
4. Distribution cost is also increased.
5. Greater efficiency is required.

Complementary exporting or Piggy Backing: In this method the company (rider) which desires to export uses the distribution network of other foreign company (carrier). Both these companies are non-competing entities. With this mode company can export with the help of excellent distribution channels developed by another company.



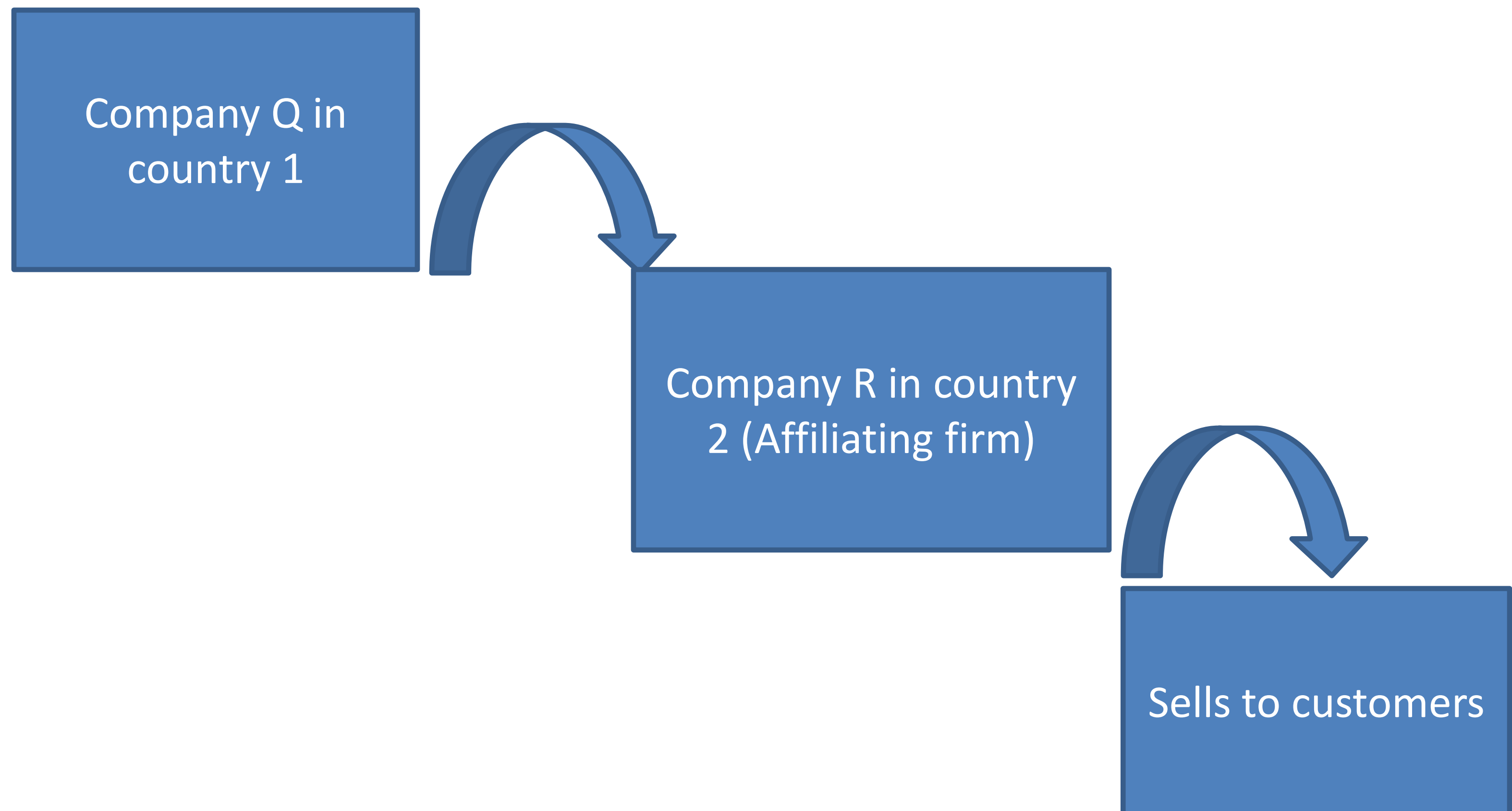
Advantages of Complementary exporting

1. No need to establish own distribution network.
2. Company can concentrate on production.
3. Easy mode of entry in international business.
4. Helps in gaining knowledge about the channels of distribution followed in other countries.

Disadvantages of Complementary exporting

1. No control over the marketing efforts of others.
2. Less revenue due to the involvement of other company.
3. No direct contact so there is no immediate feedback.
4. Wrong selection can lead to huge market loss.

Intra corporate transfers: in this mode a company sells its products to its affiliating unit in another country which in turn will the goods so got in the foreign market.



Advantages:

1. low cost
2. low efforts

Disadvantages

1. This method can be used only by the companies having subsidiaries abroad.

Off shore services: Business houses with the help of information technology and telecommunications are providing services to their customers in foreign countries. Like banks, insurance companies, airlines, finance companies transportation etc.

Off shore services	Outsourcing services
The task is done by the company on its own in foreign company.	Someone else do the task for the company

Advantages of Off Shore Services

- Helps in providing services as off-shoring services are provided where labour and other services are comparatively cheap.
- Political risks are involved as change in government will make change in the policies which may lead to negative effects.

2. Manufacturing Abroad

In this mode a company instead of manufacturing in own country and then exporting, moves to the foreign country and establishes the production facilities therein. With the help of this mode the production cost is reduced, moreover transportation of goods is also not involved from one country to another, so the cost of production gets reduced to a great extent.

Manufacturing Abroad

- Licensing
- Franchising
- Turn-key projects
- Contract manufacturing
- Management contracts

Licensing: In this mode the licensor leases the right to use intellectual property rights like copyright, patent, formula, invention, technical advice, brand name to licensee in other country for a fee called royalty. In this way a company establishes local production without capital investments.

Advantages

1. Lower financial risk is involved.
2. Low cost method to assess foreign market.
3. No tariffs and no restrictions.
4. Licensee have the knowledge of his own market.
5. Manufacturing near customers.

Disadvantages

1. No control over the activities of licensee.
2. Lesser opportunities.
3. Conflict can arise in future
4. Possibility of creation of future competitor.

Franchising: Under it franchisor provide the right to use the trademark, operating, product reputation as well as continuous support system like advertising, employee training, quality assurance etc to the franchisee for an amount called management fees. Under this method franchisor has more control over the activities of franchisee as he supplies the basic framework. Like McDonalds, Dominoz etc.

Advantages

1. Proven trademark
2. No risk of failure
3. Greater control
4. Quick development of international market

Disadvantages

1. High monitoring cost.
2. Problem with legislation
3. Does not provide experimental knowledge

Product distribution franchisee

- Pepsi
- Coca Cola

Business format franchising

- McDonalds
- Pizza Hut

Licensing	Franchising
1. Operations are done in own way.	1. Operations are done by following franchisor's rules.
2. Licensee pays royalty fees.	2. Franchisee pay management fees.
3. Product is the major concern.	3. It covers all the aspects like goodwill, know how etc.
4. Its life is 15-20 years.	4. Its life is 5-10 years
5. Licensor has less control over licensee.	5. Franchisor has greater control over franchisee.
6. Licenses are used by well established concerns.	6. Franchising is opted by new business concerns.

Turn Key Projects: Under this arrangement an international company engages in the designing and construction of entire operation in some other country. Once the project will be complete its management may be transferred to local personnel in exchange for a fees.

Types of Turn Key Projects

1. Build and transfer
2. Build, operate and transfer
3. Build operate own transfer
4. Build own operate

Build and transfer

- Under this the firm builds the production capabilities and after testing project transfers the project to foreign owners.

Build operate and transfer

- Under this the firm builds and operates the project for a certain period of time and then transfers the project to foreign owner.

Build operate own transfer

- Under this arrangement an international firm build operate and own the project for concessional period then transfer it to foreign owners.

Build own operate

- Under this company build its project in foreign country operate that very project and ownership lies with him only.

Advantages

- Possibility to enter in foreign market.
- Company earns huge profits

Disadvantages

- Risk of revealing secrets to rivals.
- Takeover of the plant by host country.

Contract Manufacturing: Under this arrangement a company enters into an agreement with the another company in foreign country to outsource production activities but retains the right of selling and promotion with itself only.

Advantages

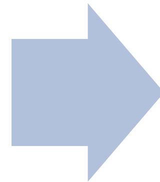
1. Lower risk
2. Focus on other activities of value chain
3. Control over research and marketing
4. Need not invest funds for establishing production facilities
5. Easy entry and exit mode as low financial commitment is there

Disadvantages

1. No control
2. Difficulty in finding reliable manufacturer
3. Contractee can become competitor in long run
4. Cultural and language barriers

Management contracts: A company lacking managerial expertise can enter into contract with another company in foreign country for managing its operations. The foreign company provides managerial assistance, technical assistance and specialized services for a certain period of time in return for a fees that can be lump-sum amount or percentage of sales or profit.

Company A in country 1 provides technical assistance



Company B in country 2 receives assistance for lump-sum fees or percentage

Advantages

1. Does not involve high risk.
2. Starts yielding income quickly.
3. Increases the reputation of company getting foreign assistance.

Disadvantages

1. Scarce management talent cannot be put to another use during contract period.
2. It will make the company dependent.

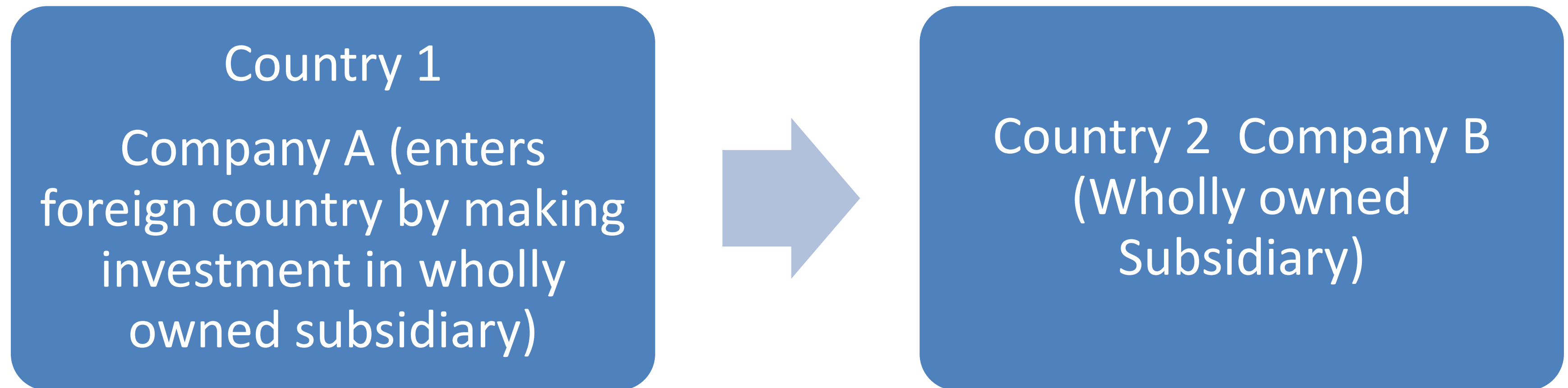
3. Investment Entry Mode

In this mode of entry a company enters the foreign country and establishes its production facilities thereat using own technology as well as management. This mode of entry is basically used in those countries where land and labour are available in abundance at cheaper rates and the physical infrastructure is quite well developed.

Investment Entry Mode

1. Wholly owned subsidiary
2. Assembly operations
3. Joint venture
4. Strategic alliance
5. Greenfield and Brownfield investment
6. Merger and acquisition

Wholly owned subsidiary: In this mode a company enters foreign market by establishing a wholly owned subsidiary thereat. It makes the whole investment and resumes the full control over its operations.



Advantages

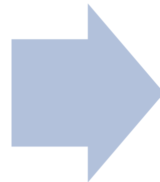
1. Reduces the risk of losing control over technological competence
2. Tight control
3. Enjoys the resources availability in host country
4. Saves transportation cost

Disadvantages

1. Larger commitment of funds
2. Larger risk
3. Costly method

Assembly operations: Under this method a company in home country manufactures the components required to make the product and export these components to foreign company who will then assemble the components to make final product and sell in the market.

Company A in country 1 (manufactures components a,b,c)



Company B in country 2 (assembles the components and sell)

Advantages

1. Saves import tariffs
2. Save labour cost
3. Full control over methodology
4. Control over production processes
5. Control over technology

Disadvantages

1. No control on assembly operations.
2. Product may not be assembled as per specifications

Joint Venture: A concern in foreign country enters into joint venture with a company in host country because host country unit has full knowledge about the domestic conditions and has well established distribution network.

Advantages

1. Sharing of risk
2. Joint financial strength
3. Smaller investment
4. Benefits of synergy

Disadvantages

1. Partners do not have full control over management.
2. Shared ownership may lead to conflicts

Strategic Alliance: Under this arrangement two companies of two different countries enters into agreement to establish a concern to have the benefits of large scale production and to meet market competition.

Advantages

1. Easy technology
2. Helps in meeting competition
3. Economies of scale
4. Easy entry and exit

Disadvantages

1. Difficulty in finding partner
2. Loss of market share
3. Risky proposal

Greenfield and Brownfield Investment: Greenfield investment means a parent company enters into foreign country by setting and constructing new production facilities there at. Brownfield investment means a parent company purchases an existing facility in foreign country to begin production and saves construction time.

Advantages

Greenfield:

1. Maximum design flexibility
2. More efficiency

Brownfield

1. Less start up cost

Disadvantages

Greenfield

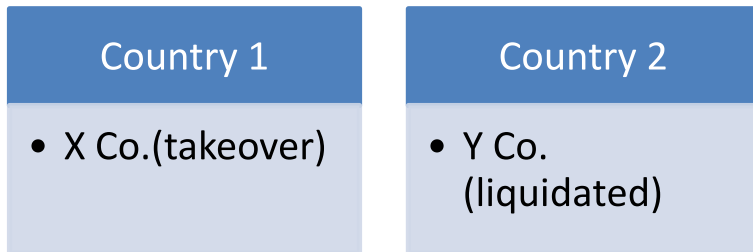
1. High costs
2. Large construction time

Brownfield

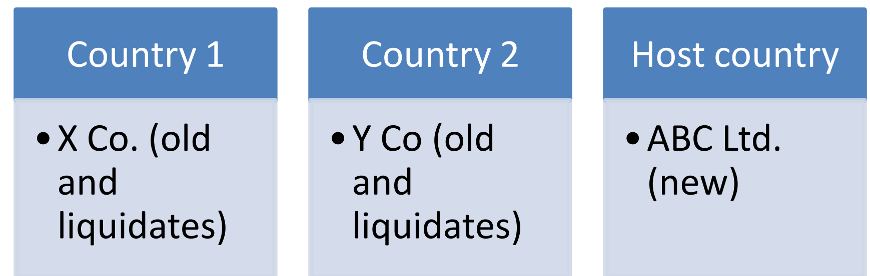
1. More maintenance due to old facilities.

Merger and acquisition: Under this a parent company join hands with some other company in foreign country to penetrate in new market.

Acquisition



Merger



Advantages

- Benefits of synergy
- Low cost

Disadvantages

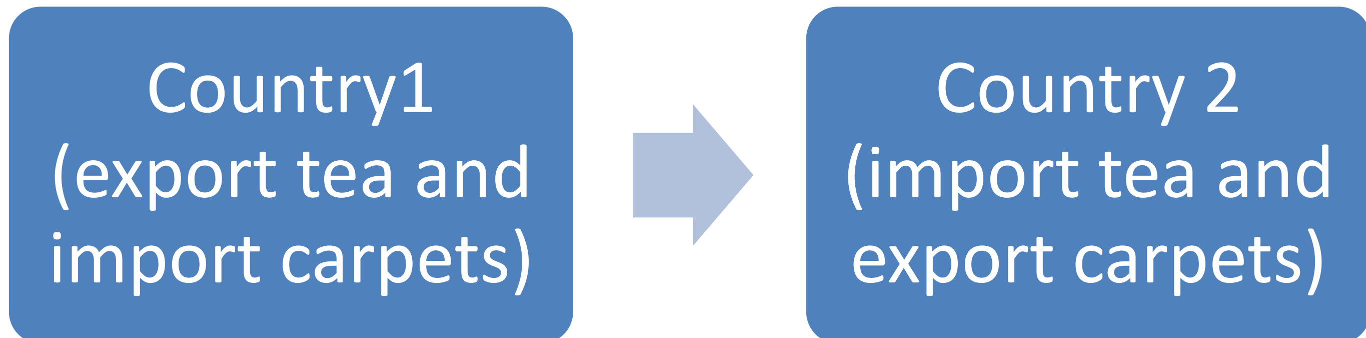
- High legal and procedural formalities
- If combining partner is inefficient then efficiency of another partner may reduce

Types of Mergers

1	Conglomerate	A merger between firms which are carrying out totally unrelated business.
2	Horizontal Merger	A merger of companies which are similar activities in order to have economies of large scale production.
3	Vertical Merger	A merger with a supplier of material to reduce uncertainty in supply of inputs.
4	Market Extension Merger	A merger between two companies producing same product but operating in separate markets. This is done to get better market access.
5	Product Extension Merger	A merger between two companies which are producing related products for the same market.

4. Counter trade

In this method the imports are paid in the form of export of certain items instead of money. This method is used where money becomes a barrier to efficient trade.



Other Methods

- Third country location: In this mode of transfer the trade between two nations are blocked. If a company desires to trade then it will have to operate from a third country base.
- Informal Co-operation: In this mode there is no formal agreement. Parties exchange information, technologies and personnel etc. in order to gain foreign exchange market share.
- Consortia: This is an alliance of many firms that pool their resources in research in order to have competitive advantage in foreign market.

There are various methods of entering in international trade. Companies do analyse the pros and cons of each method while entering into foreign market for successful business.

THANK YOU