chapter 3

Organizational Participants that Make International Business Happen

Learning Objectives

In this chapter, you will learn about:

1. Three types of participants in international business
2. Participants organized by value-chain activity
3. Focal firms in international business
4. Foreign market entry strategies of focal firms
5. Distribution channel intermediaries in international business
6. Facilitators in international business

Born Global Firms

Established in 1989, Geo Search Ltd. is a Japanese company that develops high-technology equipment to help engineers survey ground surfaces for cavities and build safe roads, highways, airports, and underground utility lines. At the request of the United Nations, Geo Search designed the world's first land mine detector, called Mine Eye, in 1997. The firm had an immediate international market because of millions of mines buried in countries like Kuwait, Cambodia, Afghanistan, and Lebanon. The firm works with non-governmental organizations (NGOs) to search for mines worldwide. Removing land mines is a risky undertaking, particularly plastic mines that cannot be found with metal detectors. Geo Search's electromagnetic radar can distinguish between mines and other objects buried underground. Images appear in three dimensions on a liquid crystal display, and there is no need to touch the ground surface.

Geo Search is one example of an increasing number of small- and medium-sized enterprises (SMEs) that are active in international business. SMEs make up the majority of all firms in a typical country and account for about 50 percent of economic activity. Compared to large multinational enterprises (MNEs) that historically

were the most common types of international firms, the typical SME has far fewer financial and human resources. In the past, international business was beyond the reach of most SMEs. But globalization and technological advances have made venturing abroad much less expensive, and created a global commercial environment in which there are many more small firms doing international business than ever before. Since the 1980s, companies that internationalize at or near their founding, *born-global firms*, have been springing up all over the world.

Despite the scarce resources that characterize most SMEs, managers in born globals tend to see the world as their marketplace from or near the firm's founding. The period from domestic establishment to initial foreign market entry is often three years or less. By internationalizing as early and rapidly as they do, born globals develop a borderless corporate culture. Management targets products and services to a dozen or more countries within a few years after launching the firm. Compared to MNEs, smaller size provides born globals with a high degree of flexibility, which helps them serve their foreign customers better. Born globals usually internationalize through exporting.

Some firms internationalize early for various reasons. Management may perceive big demand for the firm's products abroad. Management may also have a strong international orientation, and push the firm into foreign markets. In addition, firms sometimes specialize in a particular product category for which demand in the home market is too small. When this happens, management must seek markets abroad. For example, Neogen Corporation is a born global in the United States that manufactures chemicals that kill harmful bacteria and toxins in food crops. The fact that certain toxins are more common in foreign locations led Neogen to internationalize shortly after its founding.

The widespread emergence of born global firms is an exciting trend because it shows that *any* company, regardless of its size, age, or resource base, can participate actively in international business. We therefore need to revisit the traditional view of the large multinational corporation as the dominant player in international business. Today, born globals and other SMEs that are fairly active exporters make up a sizable proportion of internationally active firms. Their relative inexperience and limited financial resources no longer prevent them from succeeding in foreign markets. The trend is particularly relevant to college students who specialize in international business, because SMEs provide many new job opportunities as they aggressively pursue international ventures.

Sources: da Costa, Eduardo. (2001). *Global E-Commerce Strategies for Small Businesses*. Cambridge, MA: The MIT Press; Knight, G., and S. T. Cavusgil. (2004). "Innovation, Organizational Capabilities, and the Born-Global Firm." *Journal of International Business Studies* 35(2): 124–41; Mambula, C. J. (2004). "Relating External Support, Business Growth and Creating Strategies for Survival: A Comparative Case Study Analysis of Small Manufacturing Firms (SMFs) and Entrepreneurs." *Small Business Economics* 22:83–109; Oviatt, B., and P. McDougall. (1994). "Toward a Theory of International New Ventures," *Journal of International Business Studies* 25 (1): 45–64; OECD. (1997). *Globalization and Small and Medium Enterprises (SMEs)*. Paris: Organisation for Economic Co-operation and Development; McDougall, P., and B. Oviatt. (2000). "International Entrepreneurship: The Intersection of Two Research Paths." *Academy of Management Journal* 43 (5): 902–6; Rahman, Bayan. (1999). "Extra Eye on Land Mines." *Financial Times* (July): 19; Rennie, M. (1993). "Born Global." *McKinsey Quarterly* (4): 45–52.

In Chapter 2, we learned that market globalization is the growing integration of the world economy through the activities of firms. Factors that drive globalization include falling trade and investment barriers and technological advances. In this chapter, we discuss the people and organizations that make globalization happen and their role in the value chain.

Three Types of Participants in International Business

International business is a complex undertaking and requires numerous organizations to work together as a coordinated team. These organizations, or participants, contribute various types of expertise and inputs that facilitate international business. The participants vary in terms of their motives for going international, modes of entry, and types of operations. There are three major categories of participants:

Focal firm The initiator of an international business transaction, including MNEs and SMEs, that conceives, designs, and produces the offerings intended for consumption by customers worldwide.

Distribution channel intermediary A specialist firm that provides a variety of logistics and marketing services for focal firms as part of the international supply chain, both in the home country and abroad.

1. A **focal firm** is the initiator of an international business transaction, including MNEs and SMEs, that conceives, designs, and produces the offerings intended for consumption by customers worldwide. Focal firms take the center stage in international business. They include large multinational enterprises (MNEs; also known as Multinational Corporations or MNCs) and small- and medium-sized enterprises (SMEs). Some are privately owned companies, others are public, stock-held firms, and still others are state enterprises owned by governments. Some focal firms are manufacturing businesses, while others are in the service sector.

2. A **distribution channel intermediary** is a specialist firm that provides a variety of logistics and marketing services for focal firms as part of the international supply chain, both in the home country and abroad. Intermediaries such as dis-

tributors and sales representatives are typically located in foreign markets and provide distribution and marketing services on behalf of focal firms. Intermediaries are independent businesses in their respective markets, and work for focal firms on a contractual basis.

3. A **facilitator** is a firm or an individual with special expertise in legal advice, banking, customs clearance, or related support services, that assists focal firms perform international business transactions. Facilitators include logistics service providers, freight forwarders, banks, and other support firms that assist focal firms perform specific functions. A **freight forwarder** is a specialized logistics service provider that arranges international shipping on behalf of exporting firms, much like a travel agent for cargo. Facilitators are found in both home and foreign markets.

Facilitator A firm or an individual with special expertise in legal advice, banking, customs clearance, or related support services, that assists focal firms in the performance of international business transactions.

Freight forwarder A specialized logistics service provider that arranges international shipping on behalf of exporting firms, much like a travel agent for cargo.

International business transactions require the participation of numerous focal firms, intermediaries, and facilitators, all working closely together. The activities of the three groups of participants overlap to some degree. The focal firm performs certain activities internally and delegates other functions to intermediaries and facilitators when their special expertise is needed. In other words, the focal firm becomes a client of intermediaries and facilitators who provide services on a contractual basis.

While these three types of participants make up the international business landscape, keep in mind that international business transactions take place within political, legal, and regulatory environments. Nations also have a strong influence over their own economic development and the progress of their industries and firms. Governments create commercial environments that encourage the development of strong industries and technological prowess. Most nations have a trade infrastructure that consists of industry associations, chambers of commerce, universities, and helpful government agencies. For example, Japan registered exemplary economic growth (what was labeled an "economic miracle") during the 1980s through careful planning and a strong partnership between government and industry that skillfully mobilized technology, capital, and skilled labor.

While the focal firms, intermediaries, and facilitators represent the supply side of international business transactions, customers or buyers make up the demand side. Customers constitute the ultimate target of international business activity. For the most part, customers comprise individual *consumers and households*, *retailers* (businesses that purchase finished goods for the purpose of resale), and *organizational buyers* (businesses, institutions, and governments that purchase goods and services as inputs to a production process, or as supplies needed to run a business or organization). Governments and nonprofit organizations such as CARE and UNICEF are among major international customer groups.

Participants Organized by Value-Chain Activity

It is useful to think of the three categories of participants in terms of the firm's value chain we discussed in Chapter 2. The focal firms, intermediaries, and facilitators all are involved in one or more critical value-adding activities such as procurement, manufacturing, marketing, transportation, distribution, and support—configured across several countries. The value chain can be thought of as the complete business system of the focal firm. It comprises all of the activities that the focal firm performs.

In international business, the focal firm may retain core activities such as production and marketing within its own organization and delegate distribution and customer service responsibilities to independent contractors, such as foreign-market based distributors. Therefore, the resulting business system is subject to

	Market Research	Research and Development	Sourcing	Production	Marketing	Distribution	After-Sales Service
Distribution Channel Intermediaries		Innovation fairs	Trading company Broker Importer		Export management company Sales representative Distributor	Export management company Trading company Sales representative Distributor Broker Importer Retailer	Retailer
Facilitators	Consultant Market research firm Lawyer	Universities Research labs	Commercial bank Logistics service provider Insurance company Customs broker	Commercial bank	Consultant Market research firm	Lawyer Tax accountant Logistics service provider Freight forwarder Insurance company Consolidator Carrier Customs broker	Designated customer service firm

Exhibit 3.1

Typical Positions of Intermediaries and Facilitators in the International Value Chain

internationalization; that is, individual value-adding activities can be configured in multiple countries. Exhibit 3.1 shows the stages in the value chain where channel intermediaries and facilitators typically operate. It also identifies intermediaries and facilitators critical to the functioning of international business transactions that we discuss in this chapter.

In exporting firms, much of the value chain is concentrated within one nation—the home country. In highly international firms, management may perform a variety of value-chain activities—production, marketing, distribution—within several countries. In highly internationalized focal firms, the value chain is configured in numerous countries and often from multiple suppliers. Multinational enterprises strive to rationalize their value chain by locating each activity in a country with the most favorable combination of cost, quality, logistical considerations, and other criteria.

Exhibit 3.2 illustrates the national and geographic diversity of suppliers that provide content for an automobile. When General Motors redesigned the Chevrolet Malibu for the 2004 model year, it purchased key components from several dozen primary (so-called *tier one*) suppliers, such as alternators from Valeo, transmission chains from BorgWagner, door panels from Johnson Controls, and tires from Bridgestone/Firestone. These suppliers are headquartered in such countries as Germany, Japan, France, Korea, and the United Kingdom, in addition to the United States, but the components they sell are manufactured in typically low-cost countries and then shipped to the General Motors plant in Fairfax, Kansas. As you can see, manufacturing of products such as automobiles involves a truly international value chain.

An Illustration of an International Value Chain: Dell Inc.

Dell makes a variety of products, each with its own value chain. Depending on the number of products offered and the complexity of operations, companies may develop and manage numerous value chains. Exhibit 3.3 illustrates the value chain for the production and marketing of Dell notebook computers. Let's take the example of Tom, a Dell customer who placed an order for a notebook. Such orders can be placed online at Dell.com or by telephone with a Dell sales representative. After Tom placed his order, the representative input it into Dell's order management system, verified his credit card through Dell's work-flow connection with Visa, a global financial services facilitator, and released the order into Dell's production system.

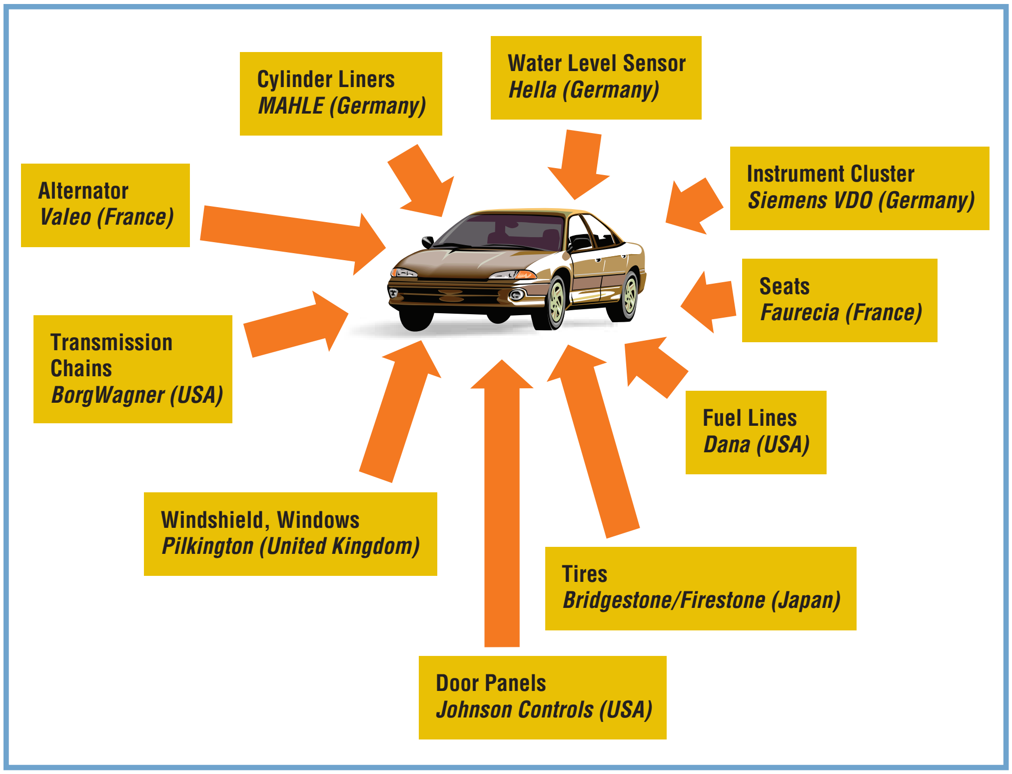

Exhibit 3.2

Sample Suppliers of Components for the Chevrolet Malibu

SOURCE: *Automotive News.*

Tom's order was processed at the Dell notebook factory in Malaysia, where the employees access parts that comprise the 30 key components of Dell notebooks from nearby suppliers. The total supply chain for Tom's computer, including multiple tiers of suppliers, involves about 400 companies, primarily in Asia, but also in Europe and the Americas.

Exhibit 3.3

Dell's International Value Chain

SOURCES: Adapted from Friedman, Thomas (2005). *The World Is Flat.* New York: Farrar, Straus, & Giroux; Lashinsky, A. (2004). "Where Dell is Going Next," *Fortune,* October 18, pp. 115–20.

Upstream Value-Chain Activities				Downstream Value-Chain Activities		
Market Research	R&D	Sourcing	Production	Marketing	Distribution	After-Sales Service
Dell conducts continuous market research, through direct interaction with thousands of customers everyday, worldwide.	R&D allows Dell to develop new notebook models and improve existing ones. Notebooks are completely redesigned every twelve months. Dell engineers in the United States conduct R&D jointly with specialized notebook designers in Taiwan.	The parts for the notebook are sourced worldwide, but mainly from suppliers in Asia. For example, Intel microprocessors are sourced from Intel factories in China, Costa Rica, and Malaysia; LCD displays are sourced from factories in South Korea, Japan, and Taiwan.	The notebook is assembled and software installed at one of Dell's six factories in Brazil, China, Ireland, Malaysia, or the United States.	Dell sells computers to buyers worldwide, but especially in the United States, where it holds one-third of the PC market, and online sales are common. Outside the United States, Dell has about 12 percent of total market share.	For its U.S. sales, Dell uses air transport to ship notebooks from its factories to the express delivery firm UPS, in Nashville, Tennessee. UPS then ships the notebooks to final customers. For sales in other countries, Dell uses local express delivery firms. The time period from order submission to final order delivery is typically less than two weeks.	Dell performs service and technical support in its major markets, especially Europe, Japan, and the United States. It employs technical support personnel in Europe, India, Japan, and the United States.

On a typical day, Dell processes orders for 150,000 computers, which are sold and distributed to customers around the world. Although based in Texas, non-U.S. sales account for roughly 40 percent of Dell's total sales (about $56 billion in 2006). As growth in U.S. sales flattens over time, the proportion of non-U.S. sales will grow. Shipping is handled via air transport. For instance, from the Dell Malaysia factory to the United States, Dell charters a China Airlines 747 that flies to Nashville, Tennessee six days a week. Each jet carries 25,000 Dell notebooks that weigh a total of 110,000 kilograms, or 242,500 pounds.

One of the hallmarks of Dell's value chain is collaboration. CEO Michael Dell and other members of top management constantly work with their suppliers to make process improvements in Dell's value chain.

Focal Firms in International Business

Imagine a typical theatrical production on Broadway in New York or on London's West End. There are script writers, stage managers, lighting technicians, musicians, set directors, business managers, and publicity staff, in addition to performing actors. Each participant contributes to the production in different ways. Much coordination among the players is required. Advance planning, preparation, timeliness, and synchronization are critical to ultimate success. Fulfillment of international business transactions similarly requires the participation of many specialist organizations, exact timing, and precision.

As we saw early in this chapter, focal firms initiate an international business transaction by conceiving, designing, and producing offerings intended for consumption by customers worldwide. Focal firms are the most prominent international players, partly because they include well-known multinational enterprises and small- and medium-sized exporting firms, including contemporary organizations such as the born globals discussed in the opening vignette. Let's learn more about each of these key actors in international business.

The Multinational Enterprise

Multinational enterprise (MNE) Is a large company with substantial resources that performs various business activities through a network of subsidiaries and affiliates located in multiple countries.

A Multinational enterprise (MNE) is a large company with substantial resources that performs various business activities through a network of subsidiaries and affiliates located in multiple countries. Leading MNEs are listed on the *Fortune Global 500* (www.fortune.com). Examples include well-known companies like Nestlé, Sony, Unilever, Nokia, Ford, Citibank, ABB, and Shell Oil. Although such firms employ a range of foreign market entry modes, MNEs are best known for their direct investment activities. They operate in multiple countries, especially in Asia, Europe, and North America, by setting up production plants, marketing subsidiaries, and regional headquarters. MNEs such as Exxon, Honda, and Coca-Cola derive a substantial portion of their total sales and profits, often more than half, from cross-border operations. Exhibit 3.4 highlights a sample of MNEs and illustrates the diverse industry sectors these focal firms represent.

Some focal firms operate in the services sector, including airlines, construction companies, and management consultancies. Examples include Citibank in banking, CIGNA in insurance, Bouygues in construction, Accor in hospitality, Disney in entertainment, Nextel in telecommunications, and Best Buy in retailing. Although retailers are usually classified as intermediaries, some large ones such as IKEA, Wal-Mart, and Gap are considered focal firms themselves. In addition, nontraditional *Internet*-mediated businesses that deliver knowledge-based offerings like music, movies, and software online have joined the ranks of global focal firms. Amazon and Netflix are examples.

Sector	*2005 Market Value (U.S. $ billions)*	*Percentage of World Total*	*Representative Firms*
Financials	$ 5,832	24.3%	Capital One, Danske Bank, Royal Bank of Scotland
Consumer discretionary	2,667	11.1	Coach, Adidas, Salomon, Matsushita Electric
Information technology	2,635	11.0	Microsoft, Oracle, Hoya, Taiwan Semiconductor Manufacturing
Industrials	2,431	10.1	Landstar Systems, Shenzhen Expressway, Haldex
Energy	2,316	9.7	Mobil, Total, China Oilfield Services
Health care	2,274	9.5	GlaxoSmithKline, Novartis, Baxter International
Consumer staples	2,134	8.9	Procter & Gamble, Unilever, China Mengniu Dairy, Honda
Telecom services	1,394	5.8	AT&T, China Mobile, Royal KPN
Materials	1,316	5.5	Dow Chemical, Alcan, Vitro SA
Utilities	956	4.0	Duke Energy, Empresa Nacional de Electricidad SA, Hong Kong and China Gas, Ltd.
Total	**23,955**	100.0	

Exhibit 3.4

Multinational Enterprises as Focal Firms (Ranked by Industry Sector Size)

SOURCES: Business Week Global 1200, www.businessweek.com, "Breaking It Down by Industry".

Not all focal firms are private businesses. In developing countries and centrally planned economies, some focal firms are partly or wholly owned by the government. For example, Lenovo Group is China's leading computer maker. It owns the former PC business of IBM and is 50 percent government-owned. CNOCC is a huge oil company that tried to buy Unocal in the United States in 2005. It is 71 percent government-owned. Numerous other leading Chinese MNEs—Sinopec and PetroChina in oil, China Mobile and China Netcom in telephony, First Auto Works and Shanghai Automotive in cars, China Minmetals in mining, and China Life in insurance—are wholly or partially owned by the Chinese government.

MNEs have played a major role in the current phase of globalization. In the years following World War II, most multinationals, typically from the United States and the United Kingdom, went abroad in search of raw materials, production efficiencies, and foreign-based customers. Today, these firms undertake sourcing, manufacturing, servicing, and marketing activities that span all areas of the world.

A typical MNE, and one whose products you may have sampled, is Sodexho, a French firm that is the world's second-largest contract foodservice provider. Its 300,000 employees provide cafeteria-style food to universities, hospitals, corporations, and public institutions in more than 75 countries. Typical Sodexho customers include the United Kingdom's Unilever, Germany's Ministry of Foreign Affairs, and the U.S. Marine Corps. Sodexho is the food source for numerous college cafeterias in Australia, Canada, and the United States. Chances are, if you eat in a university cafeteria, it is a Sodexho operation. In the 1990s, Sodexho expanded into Japan, Africa, Russia, and Eastern Europe.

Small and Medium-Sized Enterprises

Small and medium-sized enterprise (SME) A company with 500 or fewer employees in the United States, although this number may need to be adjusted downward for other countries

Another type of focal firm that initiates cross-border business transactions is the **small and medium-sized enterprise (SME)**. SMEs are typically small (with 500 or fewer employees in the United States) manufacturers or service providers and now comprise the majority of firms active in international business. Nearly all firms, including the large MNEs, started out small. Compared to the large multinationals, SMEs can be more flexible and quicker to respond to global business opportunities if they have less bureaucracy and fewer fixed assets tied up in foreign markets. SMEs can also be more innovative, more adaptable, and more entrepreneurial. They are often seen as the backbone for entrepreneurship and innovation in national economies.

Being smaller organizations, SMEs are constrained by limited financial and human resources. This explains why most smaller firms choose exporting as their major international business mode. Their limited resources prevent them from undertaking direct investment, which is an expensive entry mode. To compensate, SMEs leverage the services of intermediaries and facilitators to succeed abroad. As their operations grow, some gradually establish company-owned sales offices or subsidiaries in their key target markets.

Because of their size and relative inexperience, SMEs often target specialized products to market niches that MNEs consider too small to service. Smaller firms increasingly serve neglected global market segments because they have access to direct marketing, globe-spanning logistics specialists such as FedEx and DHL, and local distributors. Internationally active SMEs are typically avid users of information and communications technologies that allow management to segment customers into narrow global market niches and efficiently serve highly specialized needs of buyers around the world. As a result, SMEs are gaining equal footing with large multinationals in the marketing of sophisticated products for sale around the world.

In Eastern Europe, the development of emerging market countries is driven increasingly by the rise of small and midsize fast-growth firms. These firms range from Latvian coffee shop chain Double Coffee to Hungarian employment recruiter CVO Group. Many of Eastern Europe's small firms are not in manufacturing, but in intellectual, knowledge-intensive industries, such as software and consulting. The rise of small firms in Eastern Europe is the result of two trends: recent, growing access to the affluent markets of the European Union, and the interest on the part of foreign direct investors in such liberalizing economies.[1]

Born Global Firms

Born global firm A young entrepreneurial company that initiates international business activity very early in its evolution, moving rapidly into foreign markets.

Born global firms, such as Geo Search Ltd., featured in the opening vignette, represent a relatively new breed of the international SME—those that undertake early and substantial internationalization. Despite the scarce resources typical of most small businesses, born globals achieve considerable foreign sales early in their evolution. One example is History and Heraldry, a born global in England that specializes in gifts for history buffs and those with English ancestry. In its first five years, the firm expanded its sales into 60 countries, exporting about 70 percent of total production. The firm's biggest markets include France, Germany, Italy, Spain, and the Americas. It recently opened a North American subsidiary in Florida.[2] Indeed, some successful born globals grow large enough to be considered an MNE.

Another example is QualComm. Founded in California in 1985, the firm eventually grew to become a major MNE on the strength of substantial international sales. QualComm initially developed and launched the e-mail software, Eudora. The firm's early international success was OmniTRACS, a two-way satellite message and position reporting system used in the global transportation industry. QualComm's first international launch was to Europe, just four years after founding. The firm was soon exporting to Europe, Brazil, China, India, Indonesia, and Japan. QualComm's founders were entrepreneurs who, from the beginning, made little distinction between domestic and international markets. Technological prowess and managerial vision were strong factors in making the firm an early international success.

The born-global phenomenon represents a new reality in international business. In such diverse countries as Australia, Denmark, Ireland, and the United States, born globals account for a substantial proportion of national exports. In many cases, born globals offer leading-edge products with substantial potential for generating international sales. They are typically avid users of the Internet and modern communications technologies, which further facilitate early and efficient international operations.

ERG Group is an Australian-born global firm that produces fare management systems for the public transit industry worldwide.

The emergence of born globals is associated with *international entrepreneurship*, in which innovative, smaller firms increasingly pursue business opportunities everywhere, regardless of national borders. Communications and transportation technologies, falling trade barriers, and the emergence of niche markets worldwide make it possible for many contemporary entrepreneurial firms to view the world as their marketplace. Entrepreneurial managers are creative, proactive, have a strong feel for the business environment, and are ready to pursue new opportunities. They are comfortable dealing with risk and have the flexibility to make changes to company strategies as circumstances evolve. The appearance of born globals is heartening because it implies that any firm, regardless of size or experience, can succeed in international business.[3]

Foreign Market Entry Strategies of Focal Firms

One way to analyze focal firms in international business is in terms of the entry strategies that they typically use to expand abroad. Earlier, we noted that the larger MNEs tend to expand abroad through foreign direct investment. Smaller firms, including born globals, tend to be exporters. Both MNEs and SMEs rely on contractual relationships such as franchising and licensing.

A Framework for Classifying Market Entry Strategies

Exhibit 3.5 shows the array of foreign market entry modes that focal firms use and the foreign partners they seek. The exhibit helps us understand the diversity of foreign market entry strategies.

The first column in Exhibit 3.5 lists three categories of international business transactions: transactions that involve the trade of products, transactions that involve contractual exchange of services or intangibles; and transactions based on investing equity ownership in foreign-based enterprises. Therefore, firms are generally involved in one or more of three major types of cross-border transactions: buying or selling products, buying or selling services, and producing or selling products or services abroad by establishing a foreign presence through direct investment.

Nature of International Transaction	Types of Focal Firm	Foreign Market Entry Strategy	Location of Major Activities	Typical Foreign Partners
Trade of products	Small manufacturer	Exporting	Home country	Distributor, agent, or other independent representative
	Large manufacturer	Exporting	Mainly abroad	Company-owned office or subsidiary
	Manufacturer	Importing (e.g., sourcing)	Home	Independent supplier
	Importer	Importing	Home	Trader or manufacturer
	Trading company	Exporting and Importing	Home	Trader or manufacturer
Contractual exchange of services or intangibles	Service provider	Exporting	Usually abroad	Agent, branch, or subsidiary
	Supplier of expertise or technical assistance	Consulting services	Abroad (temporarily)	Client
	Licensor with patent	Licensing	Home	Licensee
	Licensor with know-how	Licensing (technology transfer)	Home	Licensee
	Franchisor	Franchising	Home	Franchisee
	Service contractor	Management/Marketing service contracting	Abroad	Business owner or sponsor
	Construction/Engineering/ Design/ Architectural Firm	Turnkey contracting or Build-Own-Transfer	Abroad (temporarily)	Project owner
	Manufacturer	Non-equity, project-based, partnerships	Home or abroad	Manufacturer
Equity ownership in foreign-based enterprises	MNE	FDI via greenfield investment	Abroad	None
	MNE	FDI via acquisition	Abroad	Acquired company
	MNE	Equity joint venture	Abroad	Local business partner(s)

Exhibit 3.5 International Business Transactions, Types of Focal Firms, and Foreign Market Entry Strategies

Licensor A firm that enters a contractual agreement with a foreign partner that allows the latter the right to use certain intellectual property for a specified period of time in exchange for royalties or other compensation.

Franchisor A firm that grants another the right to use an entire business system in exchange for fees, royalties, or other forms of compensation.

Turnkey contractors Focal firms or a consortium of firms that plan, finance, organize, manage, and implement all phases of a project and then hand it over to a foreign customer after training local personnel.

The second column in Exhibit 3.5 identifies the types of focal firms engaged in international business. Some focal firms are manufacturing businesses such as Ford, Sharp, and John Deere. They use manufacturing processes to produce tangible products that they sell in foreign markets. Trading companies are brokers of goods and services. Service providers are firms in the services sector, such as insurance companies and theme parks. Some services firms, suppliers of expertise, provide purely intangible offerings such as advice and teaching, often one-on-one, to clients. Examples include lawyers, teachers, and consulting firms.

The second column also identifies licensors of various types of intellectual property, including patents and know-how. A **licensor** is a firm that enters a contractual agreement with a foreign partner that allows the latter the right to use certain intellectual property for a specified period of time in exchange for royalties or other compensation. A **franchisor** is a firm that grants another the right to use an entire business system in exchange for fees, royalties, or other forms of compensation. Franchisors are sophisticated licensors that provide an entire business system to a foreign franchisee, such as McDonald's and Hertz Car Rental. In addition, many firms in the construction, engineering, design, or architectural industries provide their offerings via turnkey contracting. **Turnkey contractors** are focal firms or a consortium of firms that plan, finance, organize, manage, and implement all phases of a project and then hand it over to a foreign customer after training local personnel.

The third column in Exhibit 3.5 identifies the foreign market entry strategy, or the mode of internationalization. A foreign market entry strategy refers to the manner in which the focal firm internationalizes, whether through exporting, importing, licensing, or FDI. The type of entry mode depends on the nature of the business as well as the nature of the focal firm, its products, and goals. When the nature of business is dealing in intangibles, such as professional services, the focal firm may enter into agency relationships with a foreign partner. This is common among banks, advertising agencies, and market research firms. Licensing and franchising are common in the international transfer of intangibles. A franchisor makes a contract with a foreign franchisee; a supplier of expertise makes a contract with a foreign client, and so forth.

In undertaking international business, firms have the option of serving customers either through foreign investment, or relying upon the support of independent intermediaries located abroad. In the former case, the company will set up *company-owned* manufacturing and distribution facilities. Accordingly, another key characteristic of focal firms is whether the firm maintains a physical presence in the market of interest. The fourth column in Exhibit 3.5 identifies the location of major activities. For example, most exporters carry out major activities—manufacturing, marketing, and sales—in their home country; they produce goods at home and ship them to customers abroad. MNEs and other large firms, however, tend to carry out major activities in multiple countries; they produce goods and sell them to customers primarily located abroad.

The last column in Exhibit 3.5 identifies the nature of the foreign partner. In almost all cases, the focal firm will rely upon intermediaries as well as support firms located in foreign markets. Significant activities are typically delegated to these foreign partners, including marketing, distribution, sales, and customer service. MNEs have seen a strong trend in recent years away from fully integrated operations toward the delegation of certain noncore functions to outside vendors, a practice known as *outsourcing*. Outsourcing involves the firm in a variety of foreign partnerships. For example, Nike maintains its design and marketing operations within the firm, but outsources production to independent suppliers located abroad. We explore outsourcing and offshoring more fully in Chapter 16.

Focal Firms other Than the MNE and SME

Let's develop a full understanding of focal firms other than the MNEs and SMEs that are highlighted in Exhibit 3.5. Some focal firms expand into foreign markets by entering into contractual relationships with foreign partners. Licensing and franchising are examples of contractual relationships. Occasionally, the licensor sells essential components or services to the licensee as part of their ongoing relationship. Licensing allows companies to internationalize rapidly while remaining in their home market. For instance, Anheuser-Busch signed a licensing agreement with the Japanese beer brewer Kirin, under which Kirin produces and distributes Budweiser beer in Japan. The agreement has substantial potential, given Japan's \$30 billion-a-year beer market.[4] In another example, Canadian toymaker Mega Bloks signed an agreement with Disney that gives the SME the right to produce toys that feature Disney characters such as Winnie the Pooh and the Power Rangers. The toys are aimed at preschoolers and boys aged 4 to 7.[5]

Like licensors, the franchisor remains in its home market and permits its foreign partners to carry on local activities. The franchisor assists the franchisee in setting up its operation, and then maintains ongoing control over aspects of the franchisee's business, such as operations, procurement, quality control, and marketing. The franchisee benefits by gaining access to a proven business plan and substantial expertise.

Franchising is well accepted around the world and is popular among many types of service industry firms. For many successful service firms such as Subway or KFC, it is a relatively practical way to expand into many foreign markets. Exhibit 3.6 profiles some of the leading global franchisors. In China, Subway is the third-largest U.S. fast food chain, where its fish and tuna salad sandwiches are top sellers. Other

Franchisor	*Type of Business*	*International Profile*	*Major International Markets*
Subway	Submarine sandwiches and salads	24,838 shops in 82 countries	Canada, Australia, UK, New Zealand, China
Curves	Women's fitness and weight loss	9,000 centers in 17 countries	Canada, Mexico, Australia, Ireland, UK
UPS Store/Mail Boxes Etc.	Postal, business, and communications services	13 million packages in 200 countries	Canada, Germany, China
Pizza Hut	Pizza	12,500 outlets in 90 countries	China, Brazil
WSI Internet	Internet services	1,700 franchises in 87 countries	Canada, UK
KFC	Chicken	13,000 outlets in 90 countries	China, UK
RE/MAX	Real estate	100,000 agents in 50 countries	Canada, Australia, UK, New Zealand
Jani-King	Commercial cleaning	9,000 franchisees in 16 countries	Canada, Australia, Brazil, France, Turkey, New Zealand, Malaysia
McDonald's	Fast food restaurant	30,000 restaurants in 119 countries	Canada, France, UK, Australia, China
GNC	Vitamin and nutrition stores	5,000 stores in 38 countries	Canada, Mexico, Puerto Rico, Australia

Exhibit 3.6 Examples of Leading International Franchisors

SOURCES*:* Entrepreneur.com; Hoovers.com; company web sites and reports.

firms, such as The Athlete's Foot and Century 21, have been steadily growing in foreign markets through franchising. China recently passed its first laws that require franchisees to adhere closely to contractual obligations in the franchisor agreement.[6]

Turnkey contractors specialize in international construction, engineering, design, and architectural projects, typically involving airports, hospitals, oil refineries, and campuses. In a typical turnkey contract, the contractor plans, finances, organizes, manages, and implements all phases of a construction project. The contractors provide hardware and know-how to build a factory, power plant, railway, or some other integrated system that is capable of producing the products or services that the project sponsor requires. Hardware includes buildings, equipment, and inventory that comprise the tangible aspects of the system. Know-how is the knowledge about technologies, operational expertise, and managerial skills that the contractor transfers to the customer during and upon completion of the project.

These projects are typically awarded on the basis of open bidding, in which many potential contractors participate. Some contracts are highly publicized megaprojects, such as the European Channel Tunnel, the Three Gorges Dam in China, and the Hong Kong Airport. Typical examples of turnkey projects include upgrades to public transportation networks such as bridges, roadways, and rail systems. Financed largely from public budgets, most metro projects are in Asia and Western Europe, where demand is driven by intensifying urbanization and worsening congestion. One of the world's largest publicly funded heavy rail projects is underway in Delhi, India. Delhi Metro Rail Ltd. commissioned the estimated $2.3 billion turnkey project to build roads and tunnels that run through the city's central business district. The turnkey consortium includes numerous local firms as well as Skanska AB, Stockholm, one of the world's largest construction companies.[7] In Hong Kong, a private toll road operator awarded a $550-million turnkey contract to a French and Japanese joint venture for a new highway running into China. The team includes the Hong Kong subsidiary of the French giant Bouygues SA.[8] Bouygues has over 40 subsidiaries and affiliates in 80 countries.

ABB and Alstom are among the international construction contractors that have built the Three Gorges Dam on the Yangtze River in China's Hubei province. The project, which aims to control the country's mighty Yangtze River and tame the floods, is thought to have cost more than any other single construction project in China's history, with unofficial estimates as high as $75 billion.

An increasingly popular type of turnkey contract in the developing economies is the *build-own-transfer* venture. In this arrangement, the contractors acquire an ownership in the facility for a period of time until it is turned over to the client. In addition to owning a stake in the project, the contractors provide ongoing service in the form of advice, training, and assistance navigating regulatory requirements and obtaining needed approvals from government authorities. At some point after a successful period of operation, the contractors will divest their interest in the project.

Exhibit 3.7 identifies the top construction contractors in the world based on contracting revenues from projects outside their home countries. A quick perusal of the list reveals the highly global nature of the large-scale construction industry. The top firms in this industry come from various European countries, Japan, China, and the United States. These firms derive a considerable share of their total revenues from international projects. Many have established reputations in specialized project areas such as airports, steel plants, refineries, high-speed rail, and environmental projects.

International collaborative ventures represent a cross-border business alliance where partnering firms pool their resources and share the costs and risks of the new venture. Collaborative ventures are a middle ground between FDI-based foreign market entry and home country-focused operations such as exporting. In effect, a collaborative arrangement allows the focal firm to *externalize* some of its value-chain activities. Collaborative arrangements help the focal firm increase international business, compete more effectively with rivals, take advantage of complementary technologies and expertise, overcome trade barriers, connect with customers abroad, configure value chains more effectively, and generate economies of scale in production and marketing.

Joint ventures (JV) and project-based, nonequity ventures are both examples of international collaborative ventures. A **joint venture partner** is a focal firm that creates and jointly owns a new legal entity through equity investment or pooling of assets. Partners form JVs to share costs and risks, gain access to needed resources, gain economies of scale, and pursue long-term strategic goals.

Joint venture partner A focal firm that creates and jointly owns a new legal entity through equity investment or pooling of assets.

As an example, Hitachi formed a joint venture with MasterCard to promote a smart card system for banking and other applications. The Japanese electronics giant invested $2.4 million to take an 18 percent stake in the JV established in San Francisco. The firms created the venture to manage the brand and other operations of the *Multos* smart card worldwide. [9]In another instance, British Petroleum (BP) entered a joint venture in India in one of several deals intended to boost energy output in the Asian subcontinent. BP partnered with

Rank Based on 2006 Revenues	Contractor	2006 Revenue (U.S.$ millions) International	Total	Example of a Recently Completed Mega-Construction Project
1	Hochtief AG, Essen, Germany	$17,598	$19,795	Berlin's new mega-airport at the Schönefeld site, Germany
2	Skanska AB, Solna, Sweden	12,347	15,722	Øresund Bridge, Denmark
3	Vinci, Rueil-Malmaison, France	11,065	32,699	Channel Tunnel, France-Great Britain
4	Strabag SE, Vienna, Austria	10,799	13,502	Xiaolangdi Multi-Purpose Dam, China
5	Bouygues, Paris, France	9,576	24,960	Groene Hart Tunnel, The Netherlands
6	Bechtel, San Francisco, CA, U.S.A.	8,931	15,367	Hong Kong Airport, China
7	Technip, Paris-La Dèfense, France	8,084	8,245	Hong Kong New Airport Passenger Terminal Building, China
8	KBR, Houston, Texas, U.S.A.	7,426	8,150	The Great Man-Made River Project (GMRP), Libya
9	Bilfinger Berger AG, Mannheim, Germany	6,553	9,967	Taipei–Kaohsiung High Speed Railway, Taiwan
10	Fluor Corp., Irving, Texas, U.S.A.	6,338	11,273	Shell Rayong Refinery, Thailand

Exhibit 3.7 Top International Construction Contractors. Based on Contracting Revenues from Projects Outside Home Country.

SOURCE: Reprinted from Engineering News-Record.

the state-controlled Hindustan Petroleum Corporation. The new venture built a $3 billion refinery in Punjab and established a joint marketing business, including a network of retail service stations around India. BP is developing similar ventures in China.[10]

Project-based, nonequity venture partners Focal firms that collaborate through a project, with a relatively narrow scope and a well-defined timetable, without creating a new legal entity.

Partners in a project-based, nonequity venture are focal firms that collaborate through a project, with a relatively narrow scope and a well-defined timetable, without creating a new legal entity. In contrast to JVs, which involve equity investment by the parent companies, project-based partnerships are less formal nonequity ventures, and are intended for a fixed duration. The partners pool their resources and expertise to perform some mutually beneficial business task, such as joint R&D or marketing, but they do not invest equity to form a new enterprise. Firms often form project-based ventures to share the enormous fixed costs involved in knowledge-intensive research and development projects. Partners may share know-how and intellectual property to develop a new technological standard.

Cisco Systems is the worldwide leader in Internet networking technology, and has expanded much of its operations through strategic alliances with key foreign players. It formed an alliance with Japan's Fujitsu to jointly develop routers and switches that enable clients to build Internet protocol networks for advanced telecommunications. In Italy, Cisco teamed with the telecommunications company Italtel to jointly develop network solutions for the convergence of voice, data, and video to meet growing global demands. In China, Cisco formed an alliance with telecommunications company ZTE to tap the Chinese and Asian markets. The two companies are collaborating to provide equipment and services to telecommunications operators in the Asia-Pacific region.[11]

Distribution Channel Intermediaries in International Business

A second category of international business participant is the distribution channel intermediary. Intermediaries are physical distribution and marketing service providers in the value chain for focal firms. They move products and services in the home country and abroad, and perform key downstream functions in the target market on behalf of focal firms, including promotion, sales, and customer service. They may organize transportation of goods and offer various logistics services such as warehousing and customer support. Intermediaries are of many different types, ranging from large international companies to small, highly specialized operations. For most exporters, relying on an independent foreign distributor is a low-cost way to enter foreign markets. The intermediary's intimate knowledge, contacts, and services in the local market can provide a strong support system for exporters that are inexperienced in international business or too small to undertake market-based activities themselves. There are three major categories of intermediaries: those based in the foreign target market, those based in the home country, and those that operate through the Internet.

Intermediaries Based in the Foreign Market

Most intermediaries are based in the exporter's target market. They provide a multitude of services, including market research, appointing local agents or commission representatives, exhibiting products at trade shows, arranging local transportation for cargo, and clearing products through customs. Intermediaries also orchestrate local marketing activities, including product adaptation, advertising, selling, and after-sales service. Many intermediaries finance sales and extend credit, facilitating prompt payment to the exporter. In short, intermediaries based in the foreign market can function like the exporter's local partner, handling all needed local business functions.

A **foreign distributor** is a foreign market-based intermediary that works under contract for an exporter, takes title to, and distributes the exporter's products in a national market or territory, often performing marketing functions such as sales, promotion, and after-sales service. Foreign distributors are essentially independent wholesalers that purchase merchandise from exporters (at a discount) and resell it after adding a profit margin. Because they take title to the goods, foreign distributors are often called *merchant distributors*. The distributor promotes, sells, and maintains an inventory of the exporter's products in the foreign market. The distributor typically maintains substantial physical resources and provides financing, technical support, and after-sales service for the product, relieving the exporter of these functions abroad. Distributors may carry a variety of noncompeting complementary products, such as home appliances and consumer electronics. For consumer goods, the distributor usually sells to retailers. For industrial goods, the distributor sells to other businesses and/or directly to end users. Compared to sales representatives, distributors are usually a better choice for firms that seek a more stable, committed presence in the target market. A key advantage of using a foreign distributor is that they typically have substantial knowledge of the exporter's products and the nature of the local market.

Foreign distributor A foreign market-based intermediary that works under contract for an exporter, takes title to, and distributes the exporter's products in a national market or territory, often performing marketing functions such as sales, promotion, and after-sales service.

An **agent** is an intermediary (often an individual or a small firm) that handles orders to buy and sell commodities, products, and services in international business transactions for a commission. Also known as a *broker*, an agent may act for either buyer or seller but does not assume title or ownership of the goods. The typical agent is compensated by commission, expressed as a percentage of the price of the product sold. In economic terms, the agent brings buyers and sellers

Agent An intermediary (often an individual or a small firm) that handles orders to buy and sell commodities, products, and services in international business transactions for a commission.

together. Agents operate under contract for a definite period of time (often as little as one year), which is renewable by mutual agreement. The contract defines territory, terms of sale, compensation, as well as grounds and procedures for terminating the agreement.[12]

The function of the agent is especially important in markets made up of many small, widely dispersed buyers and sellers. For example, brokers on the London Metal Exchange (LME) deal in copper, silver, nickel, and other metals sourced from mining operations worldwide. The volume of metal buying and selling is huge (around $5 billion per year) and the suppliers are widely dispersed worldwide. The LME greatly increases the efficiency with which manufacturing firms access the metal ingredients they need to conduct manufacturing operations. Agents are common in the international trade of commodities, especially food products and base minerals. In the services sector, agents often transact sales of insurance and securities.

Manufacturer's representative An intermediary contracted by the exporter to represent and sell its merchandise or services in a designated country or territory.

A **manufacturer's representative** is an intermediary contracted by the exporter to represent and sell its merchandise or services in a designated country or territory. Manufacturer's representatives go by various names, depending on the industry in which they work—agents, sales representatives, or service representatives. In essence, they act as contracted sales personnel in a designated target market on behalf of the exporter, but usually with broad powers and autonomy. Manufacturer's representatives may handle various noncompetitive, complementary lines of products or services. They do not take title to the goods they represent and are most often compensated by commission. With this type of representation, the exporter usually ships merchandise directly to the foreign customer or end user. Manufacturer's representatives do not maintain physical facilities, marketing, or customer support capabilities, so these functions must be handled primarily by the exporter.

In consumer markets, the foreign firm must get its products to end users through *retailers* located in the foreign market. A retailer represents the last link between distributors and end-users. Some national retail chains have expanded abroad and are now providing retail services in multiple countries. For example, Seibu, Carrefour, Royal Ahold, Tesco and Sainsbury are major retail store chains based in Japan, France, the Netherlands, and the United Kingdom, respectively. Rolex and Ralph Lauren sell their products directly to these retailers. This type of transaction has emerged from the international growth of major retail chains. Often, a traveling sales representative facilitates such transactions. Large international retailers such as Carrefour and Wal-Mart maintain purchasing offices abroad. Wal-Mart and Toys "R" Us have opened hundreds of stores around the world, especially in Mexico, Canada, Japan, China, and Europe. IKEA, a Swedish company, is the world's largest furniture retailer. Dealing directly with foreign-based retailers is efficient because it results in a much shorter distribution channel and reduced channel costs.

Retailer Tesco's delivery vans distribute products to end-users throughout Britain.

Intermediaries Based in the Home Country

In contrast to those intermediaries located abroad, a select group of intermediaries are domestically based. For one, a variety of wholesaler *importers* bring in products or commodities from foreign countries for the purpose of selling them in the home market, re-exporting them, or for use in the manufacture of finished products. Manufacturers and retailers are also important importers. Manufacturers import a range of raw materials, parts, and components used in the production of higher value-added products. They may also import a complementary collection of products and services to supplement or augment their own product range. Retailers such as department stores, specialized stores, mail order houses, and catalogue firms import many of the products that they sell. A trip to retailers such as Best Buy, Home Depot, or Staples, for instance, quickly reveals that most of their offerings are sourced from abroad, especially low labor-cost countries. (You can learn more about the world's largest retailers from various studies, including those by PriceWaterhouseCoopers: www.pwc.com).

Wholesalers import input goods that they in turn sell to manufacturers and retailers. A typical importer in this category is Capacitor Industries Inc., an SME in Chicago that imports low-cost electronic components from China and sells them to motor makers and other manufacturers in the United States and other countries. Capacitors are tiny devices that store electrical charges, keep motors running, and protect computers from surges. Capacitor Industries' strategy is simple—buy from a low-cost country and sell at a profit in an advanced economy. Importing from China and other low-cost suppliers means that the prices of domestic suppliers can be undercut by up to 30 percent.

For exporting firms that prefer to minimize the complexity of selling internationally, a **trading company** serves as an intermediary that engages in import and export of a variety of commodities, products, and services. A trading company assumes the international marketing function on behalf of producers, especially those with limited international business experience. Large trading companies operate much like agents and may deal in thousands of products that they sell in markets worldwide. Typically, they are high-volume, low-margin resellers, and are compensated by adding profit margins to what they sell.

Trading company An intermediary that engages in import and export of a variety of commodities, products, and services.

Trading companies are very common in commodities and agricultural goods such as grain. Companies such as Minneapolis, Minnesota-based Cargill provide a useful service as international resellers of agricultural goods. With annual sales of more than $50 billion, Cargill is often listed as the largest private firm in the United States. The company employs roughly 150,000 employees in more than 60 countries. Cargill controls about 25 percent of U.S. grain exports and one-fifth of the corn-milling capacity. It buys, sorts, ships, and sells a wide range of commodities, including coffee, sugar, cotton, oil, hemp, rubber, and livestock. Most of its profits come from turning these commodities into value-added products, including oils, syrups, and flour. The company also processes all the ingredients that many food companies use to produce cereal, frozen dinners, and cake mixes.

Exhibit 3.8 provides a list of the largest trading companies in the world. What strikes you about these firms? First, note that these companies work with remarkably low margins in international trading; they tend to be high-volume, low-margin resellers. This is due to the trading companies' dealing largely in commodities such as grains, minerals, coal, and metals. Second, note that five of the ten largest trading companies are based in Japan. This is because trading companies have historically played a very important role in Japan's external trade. Being an island economy and lacking most raw materials needed for industrialization, Japan has to import them. Trading companies are also more common in South Korea, India, and Europe.

In Japan, large trading companies are known as *sogo shosha*. The sogo shosha are usually involved in both exporting and importing, and are specialists in low-margin, high-volume trading. They may also supply a range of manufacturing, financial, and logistical services. To stay close to foreign markets, managers of the sogo shosha use extensive networks of local offices, travel, and participate in trade shows, and establish business relationships with agents and distributors worldwide.

Exhibit 3.8

World's Largest Trading Companies

SOURCE: "Ten Largest companies by revenue" FORTUNE Global 500, July 24, 2006 issue, FORTUNE.

Rank Based on Annual Revenues	*Company (Home Country)*	*Revenues (U.S.$ millions)*	*Profits (U.S.$ millions)*	*Profits as Percentage of Total Revenues*
1	Mitsubishi (Japan)	$42,633	$3,092	7.3%
2	Mitsui (Japan)	36,349	1,788	4.9
3	Marubeni (Japan)	27,732	652	2.4
4	Sumitomo (Japan)	22,800	1,415	6.2
5	Sinochem (China)	21,089	260	1.2
6	Itochu (Japan)	19,592	1,282	6.5
7	SHV Holdings (Netherlands)	18,826	444	2.4
8	Samsung (South Korea)	15,114	77	0.5
9	COFCO (China)	14,654	199	1.4
10	SK Networks (South Korea)	14,571	467	3.2

The sogo shosha include giant firms that are little known in the West, such as Mitsui, Mitsubishi, Sumitomo, Itochu, and Marubeni, all firms on the Fortune magazine Global 500. In the 1990s, total trade of the nine top sogo shosha averaged about 25 percent of Japan's total GDP. They typically have extensive global operations. For instance, Marubeni has 23 corporate subsidiaries and a total of 121 offices in 72 countries. It owns 502 companies, of which 285 are outside Japan. The firm has about 27,000 employees, of which roughly 14,000 are overseas. Marubeni is consistently ranked in the upper end of the Global 500 and had recent annual sales of about $28 billion.

In the United States, trading companies have had a relatively negligible impact on the volume of export activity. The U.S. Congress passed the Export Trading Company (ETC) Act in 1982, providing firms with two important incentives to engage in joint exporting through the formation of export trading companies. First, immunity from antitrust legislation could allow firms to collaborate for export marketing purposes without the fear of being prosecuted for collusion. Second, U.S. bank holding companies could hold equity interest in ETCs and facilitate the formation of financially strong trading companies like the Japanese sogo shosha. This represented a significant departure from the longstanding policy of separating banking from commercial activities. Despite these incentives, trading companies are not forming to act on behalf of a group of manufacturers with limited international business experience. One of the deterrents has been the preference of U.S. firms to pursue international business expansion independently of other firms.[13]

Export management company (EMC) An intermediary that acts as an export agent on behalf of (usually inexperienced) a client company.

In the United States, a more common type of domestically based intermediary is the **export management company (EMC)**, which acts as an export agent on behalf of a (usually inexperienced) client company. In return for a commission, an EMC finds export customers on behalf of the client firm, negotiates terms of sale, and arranges for international shipping. While typically much smaller than a trading company, some EMCs have well-established networks of foreign distributors in place that allow exported products immediate access to foreign markets. EMCs are often supply driven, visiting the manufacturer's facilities regularly to learn about new products and even to develop foreign-market strategies. But because of the indirect nature of the export sale, the manufacturer runs the risk of losing control over how its products are marketed abroad, with possible negative consequences for its international image.

Online Intermediaries

The Internet has triggered much disintermediation—the elimination of traditional intermediaries. Some focal firms now use the Internet to sell products directly to customers rather than going through traditional wholesale and retail channels. By eliminating traditional intermediaries, companies can sell their products cheaper and faster. This benefits SMEs in particular because they typically have limited resources for international operations.[14]

Just when people thought disintermediation would be an important consequence of the Internet, another trend emerged: reintermediation. This occurs when a new firm—usually an online intermediary—injects itself between buyers and suppliers in the online buying and selling environment.[15] For example, consumers can buy high-definition TVs directly from Sony at its Web site or from an online intermediary, such as CompUSA.com or Tesco.com.

Today, countless online intermediaries are brokering transactions between myriad buyers and sellers worldwide. Intermediaries survive by adding value in the distribution process. If changes in the marketplace render an intermediary's role less valuable, then the intermediary must adapt. Emergent technologies offer—and sometimes require—new roles that intermediaries have not taken previously. Many traditional retailers establish Web sites or link with online service providers to create an electronic presence. The electronic sites of stores like Tesco and Wal-Mart complement existing physical distribution infrastructure and bring more customers into retail outlets. In total, countless intermediaries and support services provide a wide range of buyer-seller functions online. They have shifted the landscape of retailing and intermediation in the global marketplace. Read more about the new Internet-based international intermediaries in the *Global Trend* feature on the next page.

More broadly, intermediaries as well as focal firms and facilitators employ the Internet and information technology (IT) tools to achieve various tasks. The Internet and IT provide enormous opportunities to transform, manage, and communicate within value chains. The technologies have triggered fundamental changes in core aspects of global business processes, including supply-chain management, procurement, and manufacturing. Information systems, electronic data interchange networks, shared databases, and other electronic links connect firms with suppliers and buyers in unprecedented ways. These links are particularly beneficial to multinational firms, whose customers may be spread around the globe. The Internet allows suppliers to be more in touch with buyers, in more direct ways.

Nevertheless, easy accessibility of the Internet has also led many shady online marketers to cause harm to unsuspecting consumers. For example, a recent *Business Week* investigation has found that only 11 percent of Web pharmacies require a prescription.[16] An astounding 89 percent, scattered largely in developing countries, appear to operate illegally. By sending billions of spam e-mail messages a day for pharmaceuticals, unscrupulous companies generate millions of dollars of drug sales. Unfortunately, these drugs are often fake products with foreign substances that may cause serious harm to users. Phony Viagra made in Thailand was found to contain vodka; bogus Tamiflu has been manufactured with vitamin C and lactose; and sometimes a medication contains lethal amounts of dangerous chemicals. Even though the pharmaceutical industry, together with various governments have been actively identifying and pursuing these companies, they seem to be elusive and often out of the reach of legal prosecution.

GLOBAL TREND

Online Retailers: Contemporary Global Intermediaries

Online retailing is experiencing explosive growth. The leading online auctioneer, eBay, is attracting some 70 million buyers and sellers to its Web site in a typical month. Amazon.com is a leading online retailer with 40 million visitors. Offerings at eBay and Amazon resemble online versions of vast department stores. Amazon now sells more consumer electronics than books. The Web sites of conventional retailers—once considered stuck in the bricks-and-mortar era of retailing—are growing fast. The number of shoppers using Wal-Mart's Web site now exceeds those visiting Amazon. In the United Kingdom, popular e-retailers include Argos, a catalogue merchant, and Tesco, Britain's biggest supermarket chain. The hottest online products include toys, computer games, clothing, and jewelry.

Consumers like e-retailing because they can compare products and prices, and save time. For retailers, laws and restrictions that apply to retail stores are not as strict online, and selling online is cheap. Wal-Mart and Tesco use the Web to test the market for new products before offering them in their stores. Such advantages explain why traditional retailers have made the move to become major online sellers.

EBay's cross-border business is surging, with more than 30 sites straddling the globe, from Brazil to Germany. International transactions now generate half of eBay's overall trading revenues and are growing twice as fast as domestic operations. Roughly half of eBay's 125 million registered users are located outside the United States. EBay shoppers buy a soccer jersey every five minutes in Britain, a bottle of wine every three minutes in France, a garden gnome every six minutes in Germany, and a skincare product every 30 seconds in China. EBay has managed to rapidly transplant its business model around the world. Local managers adapt to local conditions without losing the core competencies at the heart of eBay. Germany is by far the biggest international site, generating roughly one-third the sales of the U.S. market. Germany boasts a far higher percentage of active users than any other country, with roughly three-quarters of registered users trading regularly.

The internationalization of online selling indicates an interesting trend: Most of the business of international online retailers occurs *within* individual countries. At eBay's Germany site, nearly all the products, information, and chat boards are created by local buyers and sellers. The site and conversations are nearly all in German, and virtually all the users are German citizens. The same is true for India and Italy. Only about 12 percent of eBay's total gross merchandise sales involve cross-border transactions. In most countries, eBay has acquired a strong local flavor as buyers and sellers create a local community. Each country is a self-contained marketplace.

Yet international online retailers must adapt to local conditions. A big challenge is getting global markets to accept online payment systems, such as PayPal. In much of Asia, electronic payment systems remain a mystery, and online deals often require face-to-face cash payments. Cultural differences play a role, too. Asians are typically reluctant to buy used goods. Even among siblings, it is uncommon to pass down clothing. Nevertheless, more and more Asians are acquiring online trading habits. With more than 90 million Internet users, China is a fast-growing market. Within a few years, more people will be surfing the Web in China than in the United States.

One challenge for online retailers is the fact that most of the world lacks access to the Internet. The success of international online retailers depends on the availability of IT infrastructure. Countries can be ranked in terms of *electronic readiness (e-readiness),* the degree to which its citizens can participate in the advantages and opportunities of a knowledge-based economy. By this measure, Denmark is the most e-ready country in the world, followed by the United States, Sweden, Switzerland, the United Kingdom, Hong Kong, Finland, and the Netherlands. By contrast, countries such as Russia, China, Indonesia, and India score relatively low on e-readiness. In such places, online retailers can target only a small portion of the local population. In Africa and parts of South Asia, poverty is prevalent and the level of e-readiness is even lower.

Sources: *Economist.* (2005). "E-readiness," May 7, p. 98; *Economist.* (2005). "Clicks, Bricks and Bargains," December 3, pp. 57–58; Schonfeld, Erick. (2005). "The World According to eBay," *Business 2.0* (January/February): 77–84.

Facilitators in International Business

The third category of participant in international business is the facilitator. While focal firms take center stage in global business, facilitators make it possible for international business transactions to occur efficiently, smoothly, and in a timely manner. They are independent individuals or firms that assist the internationalization and international operations of focal firms. Examples include banks, international trade lawyers, freight forwarders, customs brokers, and consultants. The number and role of facilitators have grown in recent years due to the complexity of international business operations, intense competition, and technological advances. Facilitators provide many useful services, ranging from conducting market research to identifying potential business partners and providing legal advice. They typically rely heavily on IT and the Internet to carry out their facilitating activities.

Some facilitators are supply-chain management specialists, responsible for physical distribution and logistics activities of their client companies. In the *Recent Grad in IB* feature on the next page, read about Cynthia Asoka, who is developing a career in global supply-chain management.

An important facilitator of international trade is the logistics service provider. A **logistics service provider** is a transportation specialist that arranges for physical distribution and storage of products on behalf of focal firms, also controlling information between the point of origin and the point of consumption. Companies such as DHL, FedEx, UPS, and TNT provide a cost-effective means for delivering cargo virtually anywhere in the world. They also increasingly provide traditional distributor functions such as warehousing, inventory management, and order tracking. FedEx, a leading express shipping company, delivers several million packages per day and offers supply-chain management services. The firm delivers to more than 210 countries and territories, covering virtually the entire planet with its fleet of over 640 aircraft and nearly 50,000 cars, trucks, and trailers. FedEx's business in Brazil, China, and India has grown rapidly.

Logistics service provider
A transportation specialist that arranges for physical distribution and storage of products on behalf of focal firms, also controlling information between the point of origin and the point of consumption.

Recently Red Wing, a U.S. shoe manufacturer, has taken advantage of UPS's supply chain services to bypass its own Salt Lake City distribution center, which is normally used to consolidate and repackage goods for shipment to retail stores. Red Wing produces some of its shoes in China, and sorts and repackages them at a UPS facility in southern China. Shoes are then delivered directly to Red Wing retail stores around the United States. By using outside express delivery firms, Red Wing gets its product to market faster and at lower cost. To serve the international distribution needs of companies like Red Wing, UPS has built over 50 warehouses in China.

Red Wing and countless other international manufacturers use *common carriers*, companies that own the ships, trucks, airplanes, and other transportation equipment used to transport goods around the world. Common carriers play a vital role in international business and global trade. A *consolidator* is a type of shipping company that combines the cargo of more than one exporter into international shipping containers for shipment abroad.

Most exporters utilize the services of freight forwarders because they are a critical facilitator in international business. Usually based in major port cities, freight forwarders arrange international shipments for the focal firm to a foreign entry port, and even to the buyer's location in the target foreign market. They are experts on transportation methods and documentation for international trade, as well as the export rules and regulations of the home and foreign countries. They arrange for clearance of shipments through customs on the importing side of the transaction. Freight forwarders are an excellent source of advice on shipping requirements such as packing, containerization, and labeling.

> RECENT GRAD IN IB

Cynthia Asoka

Cynthia's major: Business
Internships during college: GM auto plants in Argentina and Brazil
Jobs held since graduating:

- Peace Corps volunteer in the Dominican Republic
- Samsung in Korea
- Trade Promotion Organization (KOTRA) of Korea, Chicago office
- IBM

While growing up in the Detroit area in the 70s and 80s, you couldn't help but be aware of globalization while watching the local auto industry struggle to compete with Japanese imports. With hiring freezes on at the "Big 3" automakers, area graduates often headed right back to school. After getting her undergraduate business degree in 1990 from Oakland University (with a minor in International Management), Cynthia Asoka did just that.

After a semester in Vienna as an exchange student piqued an interest in language learning, Cynthia began a graduate program in linguistics studying Chinese and Spanish. She interrupted her studies to serve as a Peace Corps microenterprise development volunteer in the Dominican Republic, working on community projects funded by the Agency for International Development and teaching English in the evenings. She returned to graduate school to complete coursework in teaching English as a second language, then worked for Samsung for two years as a corporate trainer.

When Cynthia returned from Korea, she spent 18 months working for the Korean government's Trade Promotion Organization (KOTRA) in its Chicago office, sourcing Korean products for U.S. importers as well as promoting U.S. exports to Korea. Hoping to sharpen her skills so she could open her own trading company one day, she once again returned to graduate school to pursue her MBA degree in Supply-Chain Management.

Cynthia graduated in 1999 and was recruited by International Business Machines (IBM) to join its Supply Chain Leadership Training program. After completion of the two-year program, Cynthia sourced memory chips from Korean, German, and Taiwanese manufacturers, and then managed buyers of IT equipment and software. Acknowledging her company's increased emphasis on services, Cynthia switched to sourcing services for IBM's internal use in 2004, and now uses that expertise to source for IBM's customers who have outsourced that function to her firm's Business Transformation organization.

Cynthia's Advice for an International Business Career

Constantly seek out opportunities to learn new global skills. In multinational corporations, all solutions or processes you design should be applicable across many countries, forcing you to think and act globally, as well as work in teams (most often virtually) across the world. Although my dream was to open my own trading company, the skills and experience I have acquired working at a multinational corporation have served as an education I could never have acquired on my own.

Success Factors

Don't be afraid to be the trainee. When I found myself as an intern working at the GM auto plants in Argentina and Brazil, I struggled to carry on a conversation in my mediocre Spanish and practically non-existent Portuguese. After graduation the next year, I again spent two years as a trainee, moving every six months to work in different roles in various IBM plants across the United States and Canada. While your former classmates may already have become managers and directors at their companies, try to focus on skill acquisition rather than titles. Ultimately, a broad understanding of issues will help you identify better solutions and put global processes in place that will last.

Governments typically charge tariffs and taxes and devise complex rules for the import of products into the countries that they govern. **Customs brokers** are specialist enterprises that arrange clearance of products through customs on behalf of importing firms. They prepare and process the required documentation to get goods cleared through customs. They are to importing what freight forwarders are to exporting, specializing in getting goods cleared through customs in the country to which the goods are shipped. Also known as *customs house brokers*, customs brokers are specifically licensed to transact customs clearance procedures, with substantial expertise in navigating complex import procedures. They understand the regulations of the national customs service, as well as other governmental agencies that affect the import of products. Usually, the freight forwarder, based in the home country, works with a customs house broker based in the destination country in handling importing operations.

Customs brokers Specialist enterprises that arrange clearance of products through customs on behalf of importing firms.

Various other players facilitate the financial operations of international business. *Commercial banks* are an important player in the international activities of all firms by facilitating the exchange of foreign currencies and providing financing to buyers and sellers who usually require credit to finance transactions. The process of getting paid usually takes longer in international than in domestic transactions, so a focal firm may need a loan from a commercial bank. Commercial banks can also: transfer funds to individuals or banks abroad, provide introduction letters and *letters of credit* to travelers, supply credit information on potential representatives or foreign buyers, and collect foreign invoices, drafts, and other foreign receivables. Within each country, large banks located in major cities maintain correspondent relationships with smaller banks spread around the nation. Large banks also maintain correspondent relationships with banks throughout the world, or operate their own foreign branches, thus providing a direct channel to foreign customers.

Banking is one of the most multinational sectors. Barclays, Citicorp, and Fuji Bank have as many international branches as any of the largest manufacturing MNEs. These banks frequently provide consultation and guidance, free of charge, to their clients since they derive income from loans to the exporter and from fees for special services. They may be knowledgeable about particular countries and their business practices or industries.

Commercial banks such as this one at the Mall of the Emirates in Dubai are key facilitators in international commercial transactions.

When it comes to SMEs, however, banks are often reluctant to extend credit, as these smaller firms usually lack substantial collateral and experience a higher failure rate than large MNEs. When this occurs, smaller firms in the United States can turn to the *Export Import Bank* (Ex-IM Bank; www.exim.gov), a federal agency that assists exporters in financing sales of their products and services in foreign markets. The Ex-Im Bank provides direct loans, working capital loans, loan guarantees, and other financial products aimed at supporting the exporting activities of smaller firms.

In other countries, particularly in the developing world, it is commonplace for governments to provide financing, often through public *development banks* and agencies. Money is routinely available in developing countries to finance the construction of infrastructure projects such as dams and power plants. Government bank loans are generally offered at very favorable rates, and therefore attract various types of borrowers. Host governments provide loans, even to foreign firms, to the extent the incoming investment is likely to result in new jobs, technology transfer, or substantial foreign exchange. Governments in Australia, Canada, Ireland, France, Spain, the United Kingdom, and numerous other countries similarly provide financing to MNEs for the construction of factories and other large-scale operations in their countries. In the United States, several state development agencies have provided loans to MNE automakers such as BMW, Honda, Mercedes, and Toyota to establish plants in their regions.

Focal firms and other participants also use the services of *international trade lawyers* to help navigate international legal environments. The best lawyers are knowledgeable about their client's industry, the laws and regulations of target nations, and the most appropriate means for international activity in the legal/regulatory context. Foreign lawyers are familiar with the obstacles involved in doing business with individual countries, including import licenses, trade barriers, intellectual property concerns, and government restrictions in specific industries.

Firms need international trade lawyers to negotiate contracts for the sales and distribution of goods and services to customers, intermediaries, or facilitators. Lawyers play a critical role when negotiating joint venture and strategic alliance agreements, or for reaching agreement on international franchising and licensing. International trade lawyers also come into play when disputes arise with foreign business partners. When the firm needs to hire foreign employees, a good lawyer can explain labor law and employment rights and responsibilities. Internationalizing firms often apply for patents for their products and register their trademarks in the countries where they do business, which requires the services of a patent attorney. In addition, lawyers can help to identify and optimize tax benefits that may be available from certain entry modes or within individual countries.

Insurance companies provide coverage against commercial and political risks. Losses tend to occur more often in international business because of the wide range of natural and man-made circumstances to which the firm's products are exposed as they make their way through the value chain. For example, goods shipped across the ocean are occasionally damaged in transit. Insurance helps to defray the losses that would otherwise result from such damage.

International business *consultants* advise internationalizing firms on various aspects of doing business abroad and alert them to foreign market opportunities. Consultants help companies improve their performance by analyzing existing business problems and helping management develop future plans. Particularly helpful will be *tax accountants,* who can advise companies on minimizing tax obligations resulting from multicountry operations. *Market research firms* are a potential key resource for identifying and targeting foreign buyers. They possess or can gain access to information on markets, competitors, and the methods of international business.

DHL International: An Ambitious Competitor in Global Logistics Services

When Adrian Dalsey, Larry Hillbolm, and Robert Lynn founded DHL as a door-to-door express service between San Francisco and Honolulu in 1969, no one could have imagined the business evolving into a cross-border express delivery group linking 120,000 destinations in more than 220 countries and territories. Now owned by the German company Deutsche Post World Net, DHL offers express services, international air and ocean freight, contract logistics, and value-added services. While DHL is the market leader for courier express delivery in Europe and Asia, the brand struggled to develop a reputation for quality service in the United States.

Global Supply Chain and Logistics Industry

To address the needs of customers who want simple and convenient solutions at competitive prices, the supply-chain and logistics industry has changed dramatically since the early seventies. The industry includes companies that move raw materials, finished goods, packages, and documents throughout the world. Four trends are affecting the industry: globalization, deregulation, digitization, and outsourcing. Growing cross-border trade has increased the complexity of the supply chain, creating demand for professional management of the logistics activities of a focal firm. Focal firms clearly recognize the benefits of moving goods through a supply chain faster and more efficiently. As a result, specialized logistic service providers such as DHL, UPS, and FedEx have emerged to organize, coordinate, and control supply chains through technological advancements and a global presence. These facilitating firms developed global networks of offices and warehouses, acquired trucks and aircraft, and invested in extensive information tracking systems.

DHL's Internationalization

DHL entered the international express arena in 1971 with services to the Philippines. The next year, DHL initiated services to Japan, Hong Kong, Singapore, and Australia. The Asia-Pacific focus was further developed in 1980, when DHL entered China through an agency agreement with Sinotrans that was later upgraded to a 50/50 joint venture in 1986, making it the first international joint venture express company in China. In 1973 DHL expanded into Europe, with later entry in the Middle East and Africa. DHL was the first company to offer international air express services to Eastern European countries in the 1980s. To support customers worldwide, DHL established hub operations in Brussels, Cincinnati, and Manila from 1985 to 1995. Strategically positioned facilities were located in Athens, Bombay, Hong Kong, Kuala Lumpur, Moscow, Osaka, Sydney, and Bahrain. DHL formed alliances with Japan Airlines, Lufthansa, and trading company Nissho Iwai.

In 2002, the German-based company Deutsche Post acquired 100 percent ownership of DHL for $2.7 billion. Deutsche Post AG, formerly owned and operated by the German government, became a publicly traded company in 2000. Deutsche Post provides national and international services in four corporate divisions (mail, express, logistics, and financial services) under three brand names—Deutsche Post, DHL, and Postbank. Since 2002, Deutsche Post has focused on integrating its express delivery and logistics units, which include Euro Express and Danzas, under the DHL umbrella. DHL maintains five main brands: DHL Exel Supply Chain, DHL Express, DHL Freight, DHL Global Forwarding, and DHL Global Mail.

Global Positioning

In the courier, express, and parcel market, DHL International is ahead of competitors in Europe due to its efficient national express networks. With a 35 percent share of the international express segment in the Asia Pacific region, DHL is the market leader in Japan and China. A major advantage in China is its dedicated air network of more than 20 aircraft in dedicated freighter operations. DHL is investing heavily on upgrading capabilities in the China area, committing close to $1 billion dollars since 2002 to upgrade ground and air capabilities. DHL's 2005 acquisition of 81 percent of the Indian express company Blue Dart strengthens the company's ability to offer customers domestic and international express services in the key Asian markets of China and India.

In the growing logistics industry, the DHL brand has experienced double-digit increases in volume. It is the global leader in airfreight ahead of Nippon Express. DHL is able to offer airfreight in regions not served by competitors through its internal freight carrier and air fleet. It is also the leading provider of ocean freight and contract logistics.

As the express delivery service is traditionally low margin, DHL focuses on bundling services with the more lucrative, value-added contract logistics management in automotive, pharmaceutical, healthcare, electronics, telecommunications, consumer goods, and textiles/fashion sectors. These contracts are long term, an average of three years. With the acquisition of Exel, DHL has been able to extend a great majority of its existing agreements. Client companies that have recently awarded contracts to DHL include Standard Chartered Bank, Deutsche Telekom, Philips, PepsiCo, Ford, BMW, Sun Microsystems, Unisys, and Electrolux.

The Importance of the U.S. Market for DHL

The United States is an important strategic market for DHL as a global logistics service provider offering customers a global network. North American express traffic accounts for nearly half the worldwide total with highly attractive margins, reaching $46.9 billion in 2004. In 2004, 20 percent of DHL express volumes flowed into the United States or moved from there around the globe. More than one third of all global Fortune 500 companies are headquartered in the United States, where decisions on logistics and transport orders are increasingly made.

The courier service market in the United States is highly competitive and relatively consolidated, with the top five companies in the market accounting for about 47 percent of the total market value. The largest sector is ground courier service, accounting for 61 percent of sales and worth about $30 billion. The U.S. Postal Service, with a monopoly on delivering all nonurgent letters in the United States, remains the largest provider. The U.S. Postal Service and FedEx continue to broaden their range of nondelivery services, including logistics, supply-chain management, and e-commerce. By 2005, FedEx and UPS together commanded 78 percent of the U.S. parcel market, with DHL obtaining only a 7 percent share of the express delivery market. With the acquisition of Exel, DHL is the market leader of logistics in the United States.

Challenges in the U.S. Market

DHL has performed well in two other NAFTA (North American Free Trade Agreement) markets. In Canada, DHL purchased a national business to complement international activities and was able to reach break even in less than two years. In Mexico, DHL is number one in the overall express and parcel market, with a strong market position. Yet it faces considerable challenges in the United States market.

In the United States, DHL's ambition is to be a strong number three in the market after UPS and FedEx. Focusing on the small and medium-sized U.S. businesses that are increasingly involved in cross-border trade, the company aims to raise its market share. A significant move towards that goal began with the $1.1 billion acquisition in 2003 of Airborne Express, the nation's number three express service. However, the parcel market in the United States is shifting toward ground transport, due to high fuel prices making air shipment costly. DHL's limited ground network has hurt its ability to attract domestic customers who want to send parcels overland. DHL announced plans to invest $1.2 billion in its North American network to expand the company's ground delivery capacity by 60 percent. These efforts resulted in losses of $630 million in 2004 and $380 million in 2005.

DHL is facing various challenges in its operations as well. It experienced start-up difficulties when opening a central air hub in Wilmington, Ohio, that led to delivery delays and lost customers. In November of 2005, the company was responsible for losing a computer tape with the personal information of two million ABN AMRO residential mortgage customers. Although the tape later turned up in the Ohio facility, the damage to DHL's reputation was widespread. After extensive media coverage, and incurring the cost of providing all customers access to credit reporting services, ABN announced plans to use a "secure courier system" by FedEx, in which drivers stay with the computer tape the entire time.

DHL is also experiencing challenges by FedEx and UPS on regulatory grounds. These competitors have repeatedly contested Deutsche Post's operation in the United States by petitioning the U.S. Department of Transportation to cancel DHL's registration as a foreign-owned freight forwarder. UPS argued that Deutsche Post would use its monopoly profits to engage in predatory pricing in the United States. FedEx and UPS also called for a formal enforcement investigation of DHL Airways' citizenship, alleging that foreign nationals, including Germany's postal system Deutsche Post, would control DHL Airways. Under U.S. law, citizens of the United States must own at least 75 percent of the voting stock of a U.S. airline, and U.S. citizens must manage the operations. These debates generated much discussion regarding competition in the parcel delivery market. After years of motions and hearings, regulators denied the petitions and ruled in favor of DHL.

Marketing strategy in the United States includes spending $150 million in an identity rollout with a yellow and red logo. DHL had to repaint more than 17,000 trucks, purchase 20,000 worker uniforms, paint 467 service centers, replace 16,000 drop boxes and create the packaging, envelopes, and air bills used by employees and clients. These efforts coincided with the launch of an ad campaign intended to reintroduce the company to potential customers, attacking UPS and FedEx directly. The new look contributed to a 1 percent rise in market share in the United States, about $600 million in revenue.

AACSB: Reflective Thinking

Case Questions

1. DHL is integrating international express and logistic services. What value-added services does DHL provide? How do the services tie in to an organization's value chain activities? Can you anticipate changes to the supply chain that would further alter the express and logistic industry?
2. Who are the target clients for a company like DHL? What factors would influence the customer to choose a particular express courier and logistics provider?
3. Given the importance of the U.S. market to the global express industry, what would you recommend to DHL for changing its position in the United States? Do you feel that DHL' s current strategies will be successful?
4. It appears that DHL needs to focus on improved customer satisfaction through better service quality and a more customer-friendly workforce. In this increasingly competitive industry, personalized service and investment in a trained sales force seems to be critical in attracting clients. Would customers in the United States be willing to risk critical shipping activities to a fledgling operation? Will patience run out for the parent company Deutsche Post?

Note: This case was written by Tracy Gonzalez-Padron, under the supervision of Professor S. Tamer Cavusgil.

Sources: Berman, J. (2006). "Survey Indicates DHL Is Closing the Gap on U.S. competitors." Retrieved September 15, 2006, from www.logisticsmgmt.com; Boyd, J. (2006). "Deutsche Post Ag." (2006), in Hoover's company records, retrieved April 1, 2007, at <proquest.umi.com/pqdweb?index=0&did=168275191&SrchMode=1&sid=1&Fmt=3&VInst=PROD&VType=PQD&RQT=309&VName=PQD&TS=1177706376&clientId=20174>; "Couriers in the USA." *Euromonitor International* (October 2005); "Deutsche Post AG." (June 2006) Retrieved from www.datamonitor.com; Deutsche Post Worldwide Net. (2005). Annual Report. Retrieved from www.dpwn.de; "DHL International Limited." (June 2006). Retrieved from www.datamonitor.com; "DHL Parent DPWN Restructures." *Traffic World* 1; "DHL Worldwide Network S.A./N.V.," (2006). Hoover's company records, retrieved April 1, 2007, at <proquest.umi.com/pqdweb?index=4&did=168173401&SrchMode=1&sid=2&Fmt=3&VInst=PROD&VType=PQD&RQT=309&VName=PQD&TS=1177706548&clientId=20174>; Ewing, Jack, Dean Foust, and Michael Eidam. "DHL's American Adventure," *Business Week* November 29, 2004, 126; Introduction to the Transportation and Logistics Industry. Retrieved October 15, 2006, from Plunkett Research, Ltd. Web site: www.plunkettresearch.com; Mucha, T. (2005). "Pouring It On to Compete with UPS and FedEx, DHL Underwent a Corporate Makeover, with New Colors, New Commercials, and 17,000 Newly Painted Trucks." *Business 2.0*, 6 (2):60; Yerak, B. (2005). "USA Finance: Shipper Locates Missing Tape with Mortgage Data." *Chicago Tribune* (December 21, 2005); Zumwinkel, Klaus. (2006). Speech presented at the annual general meeting of Deutsche Post AG on May 10, 2006, in Cologne, Germany. Retrieved from www.dpwn Media Relations.

CHAPTER ESSENTIALS

Key Terms

agent, p. 75
born global firm, p. 68
customs brokers, p. 83
distribution channel intermediary, p. 62
export management company (EMC), p. 78
facilitator, p. 63
focal firm, p. 62
foreign distributor, p. 75
franchisor, p. 70
freight forwarder, p. 63
joint venture partner, p. 73
licensor, p. 70
logistics service provider, p. 81
manufacturer's representative, p. 76
multinational enterprise (MNE), p. 66
project-based, nonequity venture partners, p. 74
small and medium-sized enterprise, p. 68
trading company, p. 77
turnkey contractors, p. 70

Summary

In this chapter, you learned about:

1. **Three types of participants in international business**

   International business transactions require the participation of numerous focal firms, intermediaries, and facilitators. A **focal firm** is the initiator of an international business transaction that conceives, designs, and produces the offerings for customers worldwide. A **distribution channel intermediary** is a specialist firm that provides a variety of logistics and marketing services for focal firms as part of the international supply chain, both in the home country and abroad. A **facilitator** is a firm or individual with special expertise such as legal advice, banking, and customs clearance that assists focal firms in the performance of international business transactions. The three types of participants bring various types of expertise, infrastructure, and inputs that make international business take place.

2. **Participants organized by value-chain activity**

   Focal firms, intermediaries, and facilitators all make up participants in global value chains. The value chain is the complete business system of the focal firm. It comprises all of the focal firm's activities, including market research, R&D, sourcing, production marketing, distribution, and after-sales service. Channel intermediaries and facilitators support the focal firm by performing value-adding functions. In focal firms that export, most of the value chain is concentrated in the home country. In highly international firms, value-chain activities may be performed in various countries.

3. **Focal firms in international business**

   Focal firms include MNEs, large global corporations such as Sony and Ford. MNEs operate in multiple countries by setting up production plants, marketing subsidiaries, and regional headquarters. SMEs now comprise the majority of internationally active firms. They are relatively flexible firms that tend to emphasize exporting and leverage the help of intermediaries and facilitators to succeed in international business. **Born globals** are a category of international SMEs that internationalize at or near the firm's founding.

4. **Foreign market entry strategies of focal firms**

   Focal firms include a **licensor**, a firm that enters a contractual agreement with a foreign partner that allows the latter the right to use certain intellectual property for a specified period of time in exchange for royalties or other compensation. A **franchisor** is a firm that grants another the right to use an entire business system in exchange for fees, royalties, or other forms of compensation. A **turnkey contractor** is a focal firm or a consortium of firms that plans, finances, organizes, manages, and implements all phases of a project, and then hands it over to a foreign customer after training local personnel. A **joint venture partner** is a focal firm that creates and jointly owns a new legal entity through equity investment or pooling of assets. **Project-based, nonequity venture partners** are focal firms that collaborate through a project with a relatively narrow scope and a well-defined timetable, without creating a new legal entity.

5. **Distribution channel intermediaries in international business**

   Distribution channel intermediaries move products and services across national borders and eventually to end-users. They perform key downstream functions in the target market on behalf of focal firms, including marketing. A **foreign distributor** is a foreign market-based intermediary that works under contract for an exporter, takes title to, and distributes the exporter's products in a national market or territory, often performing marketing functions such as sales, promotion, and after-sales service. An **agent** is an intermediary that handles orders to buy and sell commodities, products, and services in international business transactions for a commission. A **manufacturer's representative** is an intermediary contracted by the exporter to represent and sell its merchandise or services in a designated country or territory. A **trading company** is an intermediary that engages in import and export of a variety of commodities, products, and services. An **export management company (EMC)** is an intermediary that acts as an export agent on behalf of client companies.

6. **Facilitators in international business**

   Facilitators assist with international business transactions. A **logistics service provider** is a transportation specialist that arranges for physical distribution and storage of products on behalf of focal firms, also controlling information between the point of origin and the point of consumption. A **freight forwarder** is a specialized logistics service provider that arranges international shipping on behalf of exporting firms, much like a travel agent for cargo. A **customs broker** is a specialist enterprise that arranges clearance of products through customs on behalf of importing firms. Other facilitators include *banks, lawyers, insurance companies, consultants,* and *market research firms.*

Test Your Comprehension

1. Identify and briefly define the three major categories of participants in international business.
2. In the stages of a typical international value chain, what role does each of the three categories of participants typically play?
3. What are the specific characteristics of focal firms? Distinguish the characteristics of international MNEs, SMEs, and born-global firms.
4. What is unique about such focal firms as franchisors, licensors, and turnkey contractors?
5. What role do distribution channel intermediaries provide?
6. What are major distribution channel intermediaries based in the home country and those based abroad?
7. What are online intermediaries? How do focal firms use the Internet to carry out international activities?
8. What are the characteristics of facilitators? List and define the major types of facilitators.

Apply Your Understanding AACSB: Reflective Thinking, Communication

1. The international business landscape is occupied by focal firms, distribution channel intermediaries, and facilitators. Each group of participants assumes a different and critical role in the performance of international business transactions. Think about the degree of interdependency that exists among the three groups. What would happen if distribution channel intermediaries could not provide competent services to the focal firm? What if adequate facilitators were not available to the focal firm? To what degree would the focal firm's international business performance be hampered? Under what circumstances would the focal firm choose to internalize its value-chain activities in international business rather than delegate them to channel intermediaries and facilitators? What would be the consequences of retaining distribution and support activities within the firm?
2. Think about a company for which you would like to work following graduation. Perhaps it is in one of the following industries: music (such as Virgin), banking (Citibank), engineering (Skanska AB), food (Kraft), automobiles (BMW), or another. Next, using the framework outlined in Exhibit 3.1 on page 64, sketch out the value chain that your chosen firm most likely uses in a particular product or service category. To complete this exercise, do library research or visit the Web site of this firm. Your value chain should include all of the major international business activities in which the firm is engaged. Next, develop a list of the intermediaries and facilitators that your company is likely to engage to configure its value chain. Indicate along your value chain where these participants are most likely to be located.
3. Following graduation, assume that you get a job at Kokanee Corporation, an SME that manufactures collars, leashes, grooming supplies, and other products for dogs and other household pets. Your boss, Mr. Eugene Kimball, wants to begin exporting Kokanee's products to foreign markets. Prepare a memo for Mr. Kimball in which you briefly describe the kinds of intermediaries and facilitators with whom Kokanee is likely to consult and work to maintain successful export operations.

AACSB: Reflective Thinking, Use of Information Technology

Refer to Chapter 1, page 27, for instructions on how to access and use globalEDGE™.

1. Visit the government agency or ministry in your country responsible for supporting international business. For example, in the United States, visit, the Department of Commerce (www.doc.gov). In Canada, visit Industry Canada (www.ic.gc.ca). In Denmark, visit the Ministry of Economic and Business Affairs (www.oem.dk). Identify and describe the most important support functions that the agency provides to companies that do international business. One approach is to sketch out a typical value chain, and then systematically identify the support services that the agency offers. For example, for the distribution link in the value chain, numerous governments provide "matchmaker" services, trade missions, and commercial services that link manufacturing firms with appropriate distributors located abroad.

2. Visit the Whirlpool Corporation (www.Whirlpool.com) and click on "International Sites" (under "Corporate Information"). Whirlpool has a complex value chain. Based on the information provided at the Web site address the following questions: What types of upstream value-chain activities does Whirlpool perform? What types of downstream value-chain activities does Whirlpool perform? Identify the types of participants (mainly intermediaries and facilitators) that Whirlpool is likely to use at each stage of the value chain.

3. Your company is about to initiate export activities in a country of your choice. You will need to identify distribution channel intermediaries and freight forwarders in order to have your products reach end-users in this country. Now visit the Resource Desk and Diagnostic Tools directories of globalEDGE™. What sources of information are especially helpful to you in identifying suitable foreign distributors and freight forwarders? What do you learn from these sources?

CKR Cavusgil Knight Riesenberger

Management Skill Builder©

Finding and Evaluating Freight Forwarders

As you learned in the chapter, a freight forwarder is a company that organizes the shipment of cargo via transportation modes including ships, airplanes, trucks, and railroads for manufacturers that export products. Freight forwarders do not ship cargo themselves but instead arrange for its transport by common carriers. Freight forwarders also prepare and process the documentation required for international shipments and arrange for transportation insurance and clearance through foreign customs. Freight forwarders charge a fee for their services that covers the total transport cost. Transportation is arranged from the exporter's factory or from a port in the exporter's country, to the customer's destination abroad, typically involving two or more transportation modes. UPS and DHL Worldwide Forwarding are two of the largest freight forwarders.

AACSB: Reflective Thinking, Use of Information Technology

Managerial Challenge

Evaluating and selecting a qualified freight forwarder is a critical strategic decision for managers in international operations. Freight forwarders are concentrated in large cities, and port cities, typically close to port facilities, transportation companies, and customs operations. By looking in the telephone directory of any such city, a manager can find dozens or even hundreds of freight forwarders. Freight forwarders vary widely in terms of their resources, capabilities, experience, and knowledge.

Background

It is estimated that more than 90 percent of all exporting firms have used the services of a freight forwarder. Roughly 75 percent of all international shipments involve the services of a freight forwarder. The rise of internationally active SMEs makes the services and expertise of freight forwarders even more important because smaller firms usually lack the resources or knowledge to conduct international shipping themselves.

Increased competition in both domestic and foreign markets has made the services of freight forwarders more important to exporters. First, on-time delivery can put an exporter ahead of many others. Second, firms exporting to emerging markets and developing economies need third parties with experience in these new markets or ports. Finally, parent companies that have increased trade with their foreign affiliates need reliable freight forwarders that facilitate timely transportation services, helping to ensure that production lines operate smoothly.

Managerial Skills You Will Gain

In this C/K/R Management Skill Builder©, as a prospective manager, you will:

1. Learn about freight forwarders and their role in international trade.
2. Learn the most important criteria for evaluating freight forwarders.
3. Research information to find the most appropriate freight forwarder for company needs.

Your Task

Assume that you are a manager in a small or medium-sized manufacturing firm. You are about to begin exporting your firm's products abroad. Choose a product category such as machinery or musical instruments to be shipped to foreign customers. Your task is to gather information on three different freight forwarders and then choose the best forwarder for your company.

Go to the C/K/R Knowledge Portal©

www.prenhall.com/cavusgil

Proceed to the C/K/R Knowledge Portal© to obtain the expanded background information, your task and methodology, suggested resources for this exercise, and the presentation template.