Global Marketing In a Digital World

GLOBAL MARKETING IN A DIGITAL WORLD

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- 3.0 – Case Study: Tim Hortons by Jack Taron, March 2023
- 3.1 – Case: Student Perspective on Social and Cultural Environment by Alliane Akiyama, October 2022
- 4.2 – Case: McCain Foods by Bukunmi Gabriel Ogunsola, March 2023
- 6.1 – Case: Aritzia – Wholly Owned Subsidiaries by Bernice Chan, March 2023
- 6.4 – Case: Global Market Entry Modes by Diksha Dutta, March 2023
- 10.1 – Case: Fashion Nova IMC Strategy by Aderoju Bankole, October 2022
- 11.4 – Case: Lululemon's Marketing Strategy in Hong Kong by Zheng Zeng, October 2022
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ABOUT THIS BOOK

Global Marketing is one of the most important and rapidly evolving fields in management. With advanced technological developments, business organizations today are faced with both new challenges and presented with new global opportunities.

In the Spirt of Openness

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CHAPTER 1: INTRODUCTION TO GLOBAL MARKETING

Chapter Outline

1.0 INTRODUCTION

Learning Outcomes

After reading this section, students should be able to:

1. Define global marketing.
2. Define the term value chain, global value chain and outline its components.
3. Explain why firms enter and/or avoid international markets.
4. Explain the difference between domestic marketing, international marketing, export marketing, multinational marketing, and global marketing.
5. Outline the benefits of global marketing to firms and marketing managers.
6. List the challenges and opportunities presented by global markets.
7. Discuss the positive and negative effects of globalization.
8. Describe the flattening world perspective in the globalization debate.
9. Explain the multidomestic perspective in the globalization debate.
10. Compare standardized marketing to localized marketing.

Marketing is an organizational function and a set of processes for creating, communicating, and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stakeholders. A company that engages in global marketing focuses resources on global market opportunities and threats. Successful global marketers such as Nestle, Coca-Cola, and Honda use familiar marketing mix elements – the four Ps – to create global marketing programs.

Marketing, R&D, manufacturing, and other activities comprise a firm's value chain; the value equation (V =B/P) expresses the relationship between values and the marketing mix.

Global companies also maintain strategic focus while pursuing competitive advantage. The marketing mix, value chain, competitive advantage, and focus are universal in their applicability, irrespective of whether a company does business only in the home country or has a presence in many markets around the world.

However, in a global industry, companies that fail to pursue global opportunities risk being pushed aside by stronger global competitors.

A firm's global marketing strategy (GMS) can enhance its worldwide performance. The GMS addresses several issues. First is nature of the marketing program in terms of the balance between a standardization (extension) approach to the marketing mix and a localization (adaptation) approach that is responsive to country or regional differences. Second is the concentration of marketing activities in a few countries or the dispersal of such activities across many countries. Companies that engage in global marketing can also engage in coordination of marketing activities. Finally, a firm's GMS will address the issue of global market participation.

The importance of global marketing today can be seen in the company rankings compiled by the Wall Street Journal, Fortune, Financial Times, and other publications. Whether ranked by revenues, market capitalization, or some other measure, most of the world's major corporations are active regionally or globally. The size of global markets for individual industries or product categories helps explain why companies "go global". Global markets for some product categories represent hundreds of billions of dollars in annual sales; other markets are much smaller. Whatever the size of the opportunity, successful industry competitors find that increasing revenues and profits means seeking markets outside the home country.

1.1 DEFINING GLOBAL MARKETING

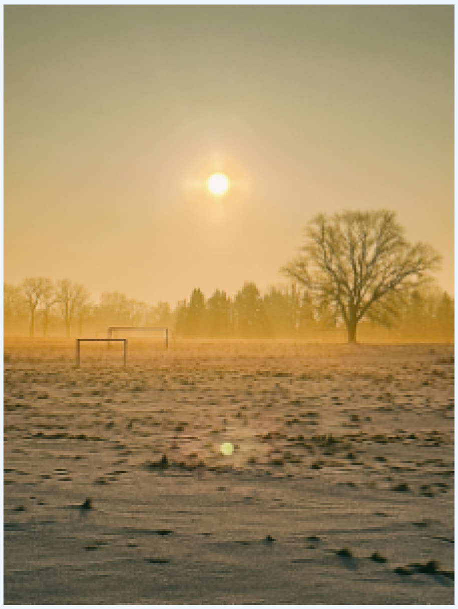
Case: Toyota has a vehicle for every market

Photo by EurovisionNim, CC BY-SA 4.0

Each market has unique cultural characteristics and contextual circumstances that must be considered. For example, in North America roads tend to be wide; highways can accommodate a broad array of vehicles with a high number of lanes, and people demand a mix of cars based on their needs. Conversely, in Europe roads tend to be narrow, and the market demands smaller, more fuel-efficient vehicles. Therefore, while a Toyota 4Runner tends to sell extremely well in the US or Canada, it would not be a very popular model in Europe for these very reasons.

As a result, Toyota invests billions of dollars every year into market research and market development to make sure they meet the needs and wants of its customers, in each specific country they sell their vehicles in. This has led to Toyota's success in the North American automotive market. With their #1 selling sedan, Toyota Camry, a wide array of hybrid models, trucks, and SUVs to meet the North American consumer's constantly-changing expectations. In the automotive industry, Toyota is arguably one of the strongest players among its competitors.

Case: Insurance Giant, Sunlife Financial in Today's Global Digital Market



Taken one morning on my way to Fanshawe College. Seeing the sun brightly shining during this winter season makes me happy and somehow Sun Life's slogan "Life's brighter under the sun" is true in every sense of the word. Photo by Ma Rona Loren Escrupolo CC-BY-NC-SA

Sun Life Financial has positioned itself as a trusted provider of financial products and services. It has embraced digital technology to provide customers with various financial solutions, including insurance, investments, retirement planning, and more. Its global marketing strategies include a focus on digital marketing and customer experience. Sun Life Financial has taken a proactive approach to the worldwide market by investing heavily in digital technologies to make its products and services easy to access and use. This includes developing a comprehensive digital platform that allows customers to access personalized advice and assistance from their homes. They provide customers with a more personalized experience through marketing campaigns, customer loyalty programs, and customized services. In 2016, Sun Life launched Ella, an interactive digital coach that helps their clients by providing information and can help anyone find a physiotherapist, a dentist, or a massage therapist. (Sun Life Assurance Company of Canada, 2023). Sun Life also seeks to stay ahead by leveraging digital technology to provide customers with the most up-to-date financial solutions and keep up with the evolving technology trend, thus partnering with MaRS, the largest innovation hub in North America (Sun Life Assurance Company of Canada, 2023).

Ma Rona Loren Escrupolo, March 2023

Now that the world has entered the next millennium, we are seeing the emergence of an interdependent global economy that is characterized by faster communication, transportation, and financial flows, all of which are creating new marketing opportunities and challenges. Given these circumstances, it could be argued that companies face a deceptively straightforward and stark choice: they must either respond to the challenges posed by this new environment or recognize and accept the long-term consequences of failing to do so. This need to respond is not confined to firms of a certain size or particular industries. It is a change that to a greater or lesser extent will ultimately affect companies of all sizes in virtually all markets. The pressures of the international environment are now so great, and the bases of competition within many markets are changing so fundamentally, that the opportunities to survive with a purely domestic strategy are increasingly limited to small and medium-sized companies in local niche markets.

Perhaps partly because of the rapid evolution of global marketing, a vast array of terms have emerged. Clarification of these terms is a necessary first step before we can discuss this topic more thoroughly.

Let us begin with the assumption that the marketing process that you have learned in any basic marketing course is just as applicable to domestic marketing as to international marketing. In both markets, we are goal-driven, do necessary marketing research, select target markets, employ the various tools of marketing (i.e., product, pricing, distribution, communication), develop a budget, and check our results. However, the uncontrollable factors such as cultural, social, legal, and economic factors, along with the political and competitive environment, all create the need for a myriad of adjustments in the marketing management process.

Global vs Domestic Marketing

One of the inevitable questions that surfaces concerning global marketing is, *how does global marketing truly differ from domestic marketing, if at all?*

Historically, there has been much discussion over commonalities and differences between global and domestic marketing, but the three most common points of view upon which scholars agree are the following:

1. All marketing is about the formulation and implementation of the basic policies known as the **4 Ps: Product, Price, Place, and Promotion.**
2. Global marketing, unlike domestic marketing, is understood to be carried out “across borders”.
3. Global marketing is not synonymous with international trade (Perry, 1990). Perhaps the best way to distinguish between the two is simply to focus on the textbook definition of international marketing. One comprehensive definition states that “international marketing means identifying needs and wants of customers in different markets and cultures, providing products, services, technologies, and ideas to give the firm a competitive marketing advantage, communicating information about these products and services and distributing and exchanging them internationally through one or a combination of foreign market entry modes” (Bradley, 2005).

At its simplest level, **global marketing** involves the firm making one or more marketing decisions across national boundaries. At its most complex, it involves the firm establishing manufacturing and marketing facilities overseas and coordinating marketing strategies across markets. Thus, how global marketing is defined and interpreted depends on the level of involvement of the company in the international marketplace.

1.2 THE GLOBAL VALUE CHAIN

In 1985, Michael E. Porter introduced the term 'Value Chain' in his book *Competitive Advantage: Creating and Sustaining Superior Performance*. Since then, this concept has been used extensively by organizations to improve their functionality and operations. The concept of 'Value Chain' stressed on the importance of 'Competitive Advantage' or being different and superior from competitors. Thus, value chain identifies how value is added throughout the creation of the final good or service produced and how operational activities costs represent a proportion of the final sale price of the good or service.

Global Value Chain is when an organization does the full range of activities including supply, production, marketing, sales, distribution, and support to the end consumer, across geographical locations to gain competitive advantage.

In simple words, when a company evolves into international trade and divide it's operations across countries, they participate in global value chain.

To learn more about how the global value chain works to successfully convert cocoa beans (raw material) into chocolate (final product) watch the video: Cocoa: a sweet value chain by STDF [8:53]. It will also introduce you to some of the safety measures taken to keep food products safe, which will be discussed in detail in further chapters.

Video: Cocoa: a sweet value chain by STDF [8:53] is licensed under the Standard YouTube License. Captions and transcripts are available on YouTube.

We live in a global marketplace. The food on your table might include fresh fruit from Chile, cheese from France, and bottled water from Scotland. The clothes you wear might be designed in Italy and manufactured in China. The toys you give to a child might have come from India (Greenlaw and Shapiro, 2017). Have you ever wondered how is it possible that the products manufactured around the world are available in your nearby supermarket? The answer to such questions is International Trade. Global Trade allows countries to expand their markets and access the products which are not available domestically.

Case: Just Whose iPhone is This?

"Papercraft iPhone 11 Pro Sliver" by Charlie, CC BY-NC-SA 2.0

The iPhone is a global product. Apple does not manufacture iPhone components, nor does it assemble them. The assembly is done by Foxconn Corporation, a Taiwanese company, at its factory in Sengzhen, China. But, Samsung, the electronics firm and competitor to Apple, actually supplies many of the parts that make up an iPhone—representing about 26% of the costs of production. That means, that Samsung is both the biggest supplier and biggest competitor for Apple. Why do these two firms work together to produce the iPhone? To understand the economic logic behind international trade, you have to accept, as these firms do, that trade is about mutually beneficial exchange. Samsung is one of the world's largest electronics parts suppliers. Apple lets Samsung focus on making the best parts, which allows Apple to concentrate on its strength — designing elegant products that are easy to use. If each company (and by extension each country) focuses on what it does best, there will be gains for all through trade (Greenlaw and Shapiro, 2017).

Global value chains (GVCs) have brought about revolutionary changes in international trade, industrialization, and economic development. The GVC story is still rapidly unfolding, as vividly demonstrated by the supply chain crisis, particularly for semiconductors and other components, that broke out during the COVID-19 pandemic, causing further anxiety (Alvarez et al., 2021).

Positioning Economies in Global Value Chains

With the rise of global value chains (GVCs), patterns of specialization have expanded to cover not only products but also tasks. Indeed, gross trade statistics may lead to the conclusion that an economy has a product specialization when in fact it has a functional specialization.

A case in point is developing countries with major electronics exports, such as the Philippines. These economies do not specialize in electronics, but in a particular segment in the electronics value chain (Timmer, Miroudot, and de Vries 2019).

Figure 1.1 shows since the forward GVC length is noticeably longer than the backward GVC length, this economy is said to be positioned relatively upstream in GVCs.

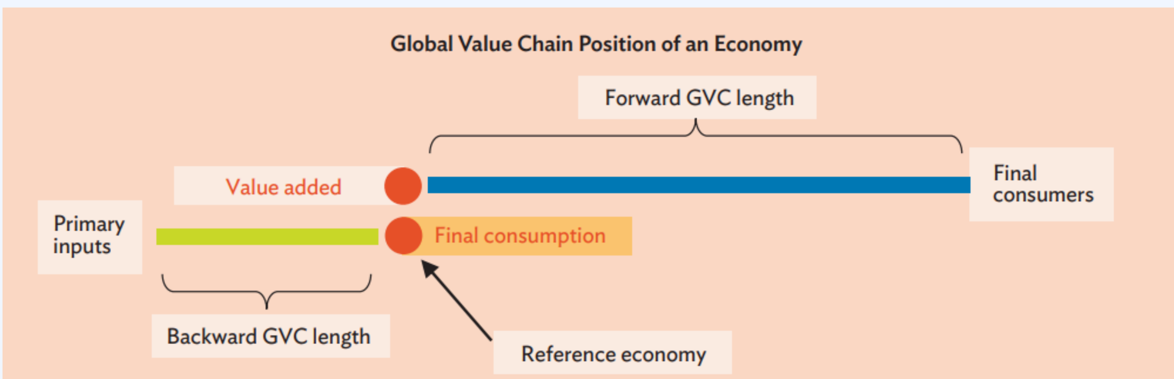


Fig. 1.1 "Global Value Chain Position of an Economy" by Alvarez, CC BY-NC 3.0

Components of Value Chain

The concept of Value Chain is used as an internal assessment tool to help a firm determine where it might be able to achieve a competitive advantage and answering questions as:

- In which areas of the primary and secondary activities is the firm particularly strong?
- Can that activity be leveraged to provide a competitive advantage over its rivals?

The Value Chain includes both Primary and Secondary Activities. **Primary activities** are actions that are directly involved in creation and distribution of goods and services. There are five primary activities in Porter's Value Chain namely Inbound Logistics, Operations, Outbound Logistics, Marketing & Sales and Services. **Secondary activities** are not directly involved in the evolution of a prodct, but instead provide important underlying support for primary activities. Four activities are attributed as Secondary in Porter's Value Chain namely Infrastructure, Human Resource Management, Technological Development and Procurement. These primary and secondary activities work together to produce a profit margin for the firm. Figure 1.2 below describes the value chain framework given by Michael Porter.

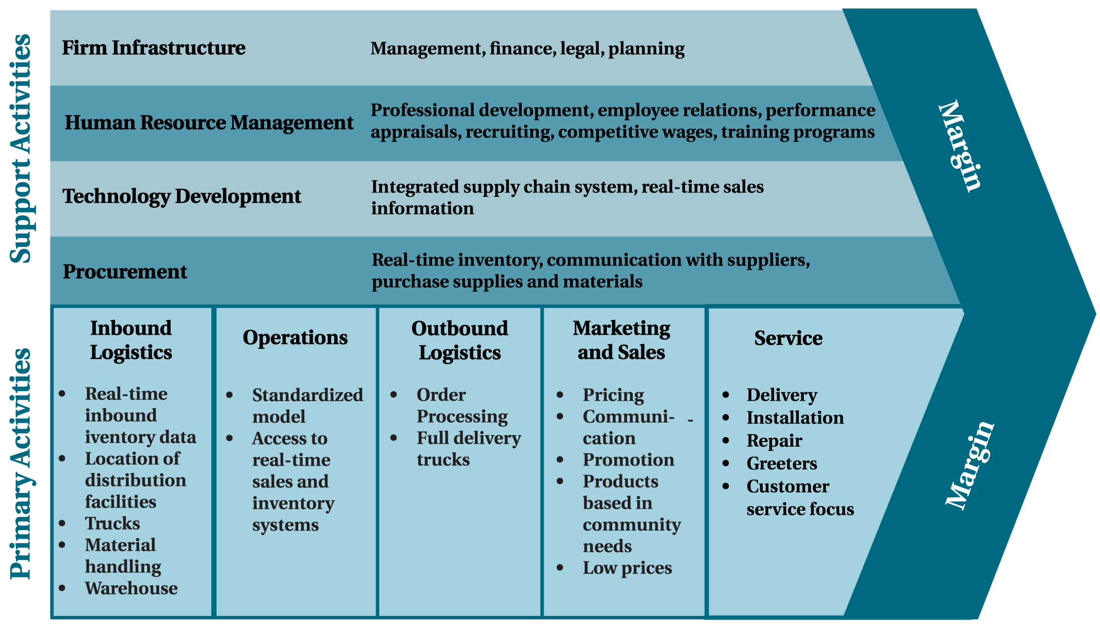


Fig 1.2 "The value chain" by Reed Kennedy, CC BY-NC-SA 4.0 *Colour was modified from original*

To learn more about primary and support activities, and how costs of creating value can be reduced, so that profit margin can grow, watch the video: Porter's value chain: How to create value in your organization by MindToolsVideos [3:23].

Video: Porter's value chain: How to create value in your organization by MindToolsVideos [3:23] is licensed under the Standard YouTube License. Captions and transcripts are available on YouTube.

Let's try to understand these activities from a very simple example of doughnut shops. Doughnut shops transform basic commodity products such as flour, sugar, butter, and grease into delectable treats. Value is added through this process because consumers are willing to pay much more for doughnuts than they would be willing to pay for the underlying ingredients. Figure 1.3 explains in detail how value is added while making donuts.

Fig. 1.3 "Adding Value within a Value Chain" by Reed Kennedy, CC BY-NC-SA 4.0

Donut shops buy commodity products (such as flour and sugar) and transform them into treats. Consumers are willing to pay much more for donuts than they would for the raw ingredients. See the table below which depicts how primary and support activities in the value chain add value for donut shops.

Primary Activities	Support Activities
• **Inbound logistics** of organic ingredients from a local farmers market makes the donut unique. • **Operations** at the Coffee an' Donut shop in Connecticut rely on a secret recipe . Former president Bill Clinton had the donuts shipped to the White House regularly. • Voodoo donuts in Portland Oregon, uses a van as part of it **outbound logistics.** The van takes their offerings far beyond their store. • **Marketing and sales** for Randy's Donuts in Inglewood, California is aided by an attention grabbing building. • What is a 'dirty snowball'? Helping customers understand their unique menu is an important **service** offered by Voodoo Donut's staff.	• As an example of **firm infrastructure**, the explosive growth of Tim Hortons under Ron Joyce's leadership led Canada to have the highest per-capita consumption of donuts in the world. • A key **human resource** management issue for all donut shops is ensuring that a friendly face greets each customer. • The conveyer belt used by Krispy Kreme is a **technology** that creates efficiency and a visual enticement for potential customers. • Large chains such as Dunkin Donuts enjoy low prices in their **procurement** process because they buy supplies in bulk.

Primary Activities

Primary Activities are essential for creating value and Competitive Advantage. There are five components of primary activities:

1. **Inbound Logistics:** Inbound logistics refers to the arrival of raw materials. Although doughnuts are seen by most consumers as notoriously unhealthy, the Doughnut Plant in New York City has carved out a unique niche for itself by obtaining organic ingredients from a local farmer's market.
2. **Operations:** Operations refers to the actual production process. Operations at the Tim Horton's or other such restaurants are trade secrets. It's nearly impossible to make a coffee that tastes like Tim Horton's French Vanilla at home unless you have coffee powder from Tim Horton's.
3. **Outbound Logistics:** Outbound logistics tracks the movement of finished products to customers. For instance, one of Southwest Airlines' unique capabilities is moving passengers more quickly than its rivals. This advantage in operations is based in part on Southwest's reliance on one type of airplane (which speeds maintenance) and its avoidance of advance seat assignments (which accelerates the passenger boarding process).
4. **Marketing and Sales:** Attracting potential customers and convincing them to make purchases is the domain of marketing and sales. For example, people cannot help but notice Randy's Donuts in

Inglewood, California, because the building has a giant doughnut on top of it.

5. **Services:** Service refers to the extent to which a firm provides assistance to their customers. Voodoo Donuts in Portland, Oregon, has developed a clever website (voodoodoughnut.com) that helps customers understand their uniquely named products, such as the Voodoo Doll, the Texas Challenge, the Memphis Mafia, and the Dirty Snowball.

Secondary Activities

Secondary/ Support Activities helps primary activities to work efficiently. There are four components of secondary activities.

1. **Firm Infrastructure:** Firm infrastructure refers to how the firm is organized and led by executives. The effects of this organizing and leadership can be profound. For example, Ron Joyce's leadership of Canadian doughnut shop chain Tim Hortons was so successful that Canadians consume more doughnuts per person than all other countries. In terms of resource-based theory, Joyce's leadership was clearly a valuable and rare resource that helped his firm prosper.
2. **Human Resource Management:** Human resource management is also important. Human resource management involves the recruitment, training, and compensation of employees. A recent research used data from more than twelve thousand organizations to demonstrate that the knowledge, skills, and abilities of a firm's employees can act as a strategic resource and strongly influence the firm's performance (Crook et al., 2011). Certainly, the unique level of dedication demonstrated by employees at Southwest Airlines has contributed to that firm's excellent performance over several decades.
3. **Technology:** Technology refers to the use of computerization and telecommunications to support primary activities. Although doughnut making is not a high-tech business, technology plays a variety of roles for doughnut shops, such as allowing customers to pay using credit cards.
4. **Procurement:** Procurement is the process of negotiating for and purchasing raw materials. Large doughnut chains such as Dunkin' and Krispy Kreme can gain cost advantages over their smaller rivals by purchasing flour, sugar, and other ingredients in bulk. Meanwhile, Southwest Airlines has gained an advantage over its rivals by using futures contracts within its procurement process to minimize the effects of rising fuel prices.

More Value Chain Examples

Would you like to know about value chain of Canadian Pacific Railways and Apple. Review these resources:

- How to perform a Value Chain Analysis (explained with Example)?
- A Simple Guide to Value Chain Analysis: How to build more Efficient Sales Processes.

1.3 THE MOTIVATION FOR GLOBAL MARKETING

Reasons for Entering Global Markets

Many marketers have found the international marketplace to be extremely hostile. A study by Barker and Kaynak (1992) for example, found that less than 20 percent of firms in Texas with export potential actually carried out business in international markets. But although many firms view in markets with trepidation, others still make the decision to go international. Why?

In the Barker and Kaynak study, the following motivating factors were given for initiating overseas marketing involvement (in order of importance):

- large market size
- stability through diversification
- profit potential
- unsolicited orders
- proximity of market
- excess capacity
- offer by foreign distributor
- increasing growth rate
- smoothing out business cycles

Other empirical studies over a number of years have pointed to a wide variety of reasons why companies initiate international involvement. These include the saturation of the domestic market, which leads firms either to seek other less competitive markets or to take on the competitor in their home markets; the emergence of new markets, particularly in the developing world; government incentives to export; tax incentives offered by foreign governments to establish manufacturing plants in their countries in order to create jobs; the availability of cheaper or more skilled labour; and an attempt to minimize the risks of a recession in the home country and spread risk (Chen & Hicks, 2000).

Reasons to Avoid International Markets

Despite attractive opportunities, most businesses do not enter foreign markets. The reasons given for not going international are numerous. The biggest barrier to entering foreign markets is seen to be a fear by these companies that their products are not marketable overseas and a consequent preoccupation with the domestic market. The following points were highlighted by the findings in the previously mentioned study by Barker and Kaynak (1992), who listed the most important barriers:

- too much red tape
- trade barriers
- transportation difficulties
- lack of trained personnel
- lack of incentives
- lack of coordinated assistance
- unfavourable conditions overseas
- slow payments by buyers
- lack of competitive products
- payment defaults
- language barriers

It is the combination of these factors that determines not only whether companies become involved in international markets, but also the degree of any involvement.

Case: Global Marketing Strategy

A major theme of Chapter One is the importance of having a global marketing strategy (GMS). A GMS improves international performance by creating a competitive advantage with a marketing mix tailored to the company's global needs. A Canadian example would be Canada Goose, which has successfully reached many countries and continents. From operations to marketing and outbound logistics, many of their marketing activities have traditionally been handled in Canada. Recently, they have opened international physical stores. This demonstrates a move towards more multinational marketing efforts. Since success in cities such as New York, London, and Tokyo has proven that they have a large market, they have been motivated to continue growing.

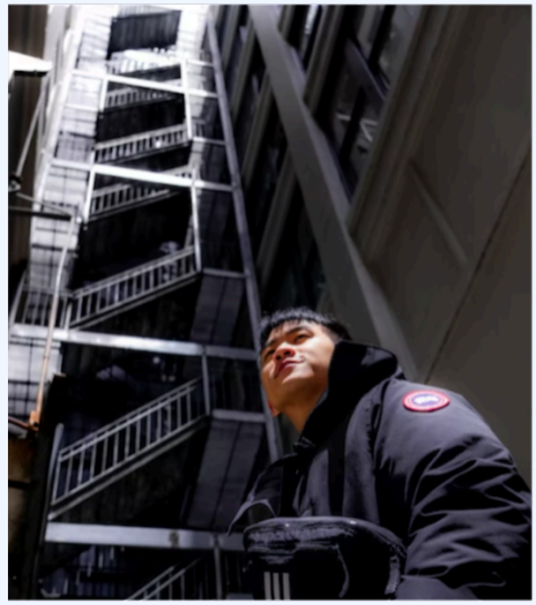


Photo by Fran, Unsplash Licence

A successful strategy they've implemented includes cold rooms in some of their stores. This is so that customers can experience products in colder temperatures (Reiss, n.d.). By going global with their cold rooms, they have anticipated the need of international consumers to be able to experience for themselves what it's like to wear this coat in cold temperatures. They have understood that their value proposition is the brand's image as being high quality (Reiss, n.d.). Additionally, they offer clothing for three seasons, demonstrating they understand and employ a localized strategy and understand the geography aspect of marketing. This enables them to extend their product lines to countries that are not as cold as Canada. Rather than focusing on pure luxury, they emphasize quality and craftsmanship. Moreover, they recognize that it is important to avoid having products that appear standardized and instead turn towards making their products unique as "Made in Canada" (Danziger, 2018).

Vicky Anborgh, March 2023

1.4 STAGES IN GLOBAL MARKETING

Earlier in our discussion on definitions, we identified several terms that relate to how committed a firm is to being international. Here we expand on these concepts and explain the rationale behind this process. Two points should be noted:

1. First, the process tends to be ranked in order of "least risk and investment" to "greatest involvement".
2. Second, these are not necessarily sequential steps, even though exporting is apparently most common as an initial entry.

Firms typically approach involvement in international marketing rather cautiously, and there appears to exist an underlying lifecycle that has a series of critical success factors that change as a firm moves through each stage. For small and medium-sized firms, in particular, exporting remains the most promising alternative to a full-blooded international marketing effort, since it appears to offer a degree of control over risk, cost, and resource commitment. Indeed, exporting, especially by the smaller firms, is often initiated as a response to an unsolicited overseas order-these are often perceived to be less risky. Therefore, the following possibilities exist:

Domestic marketing	This involves the company manipulating a series of controllable variables, such as price, advertising, distribution, and the product, in a largely uncontrollable external environment that is made up of different economic structures, competitors, cultural values, and legal infrastructure within specific political or geographic country boundaries.
International marketing	This involves the company operating across several markets in which not only do the uncontrollable variables differ significantly between one market and another, but the controllable factor in the form of cost and price structures, opportunities for advertising, and distributive infrastructure are also likely to differ significantly.
Export marketing	In this case, the firm markets its goods and/or services across national/political boundaries. In general, exporting is a simple and low risk-approach to entering foreign markets. Firms may choose to export products for several reasons. First, products in the maturity stage of their domestic life cycle may find new growth opportunities overseas, as Perrier chose to do in the US. Second, some firms find it less risky and more profitable to expand by exporting current products instead of developing new products. Third, firms who face seasonal domestic demand may choose to sell their products to foreign markets when those products are "in season" there. Finally, some firms may elect to export products because there is less competition overseas.

Export Marketing

A firm can export its products in one of three ways: indirect exporting, semi-direct exporting, and direct exporting.

- **Indirect exporting** is a common practice among firms that are just beginning their exporting. Sales, whether foreign or domestic, are treated as domestic sales. All sales are made through the firm's domestic sales department, as there is no export department. Indirect exporting involves very little investment, as no overseas sales force or other types of contacts need to be developed. Indirect exporting also involves little risk, as international marketing intermediaries have knowledge of markets and will make fewer mistakes than sellers.
- In **semi-direct exporting**, an American exporter usually initiates the contact through agents, merchant middlemen, or other manufacturers in the US. Such semi-direct exporting can be handled in a variety of ways: (a) a combination export manager, a domestic agent intermediary that acts as an exporting department for several non-competing firms; (b) the manufacturer's export agent (MEA) operates very much like a manufacturer's agent in domestic marketing settings; (c) a Webb-Pomerene Export Association may choose to limit cooperation to advertising, or it may handle the exporting of the products of the association's members and; (d) piggyback exporting, in which one manufacturer (carrier) that has export facilities and overseas channels of distribution handles the exporting of another firm (rider) non-competing but complementary products.
- When **direct exporting** is the means of entry into a foreign market, the manufacturer establishes an export department to sell directly to a foreign film. The exporting manufacturer conducts market research, establishes physical distribution, and obtains all necessary export documentation. Direct exporting requires greater investment and also carries a greater risk. However, it also provides greater potential return and greater control of its marketing program.

Multinational Marketing

Here the marketing activities of an organization include activities, interests, or operations in more than one country, and where there is some kind of influence or control of marketing activities from outside the country in which the goods or services will actually be sold. Each of these markets is typically perceived to be independent and a profit centre in its own right.

Global Marketing

The entire organization focuses on the selection and exploration of global marketing opportunities and marshals resources around the globe with the objective of achieving a global competitive advantage. The primary objective of the company is to achieve synergy in the overall operation, so that by taking advantage of different exchange rates, tax rates, labour rates, skill levels, and market opportunities, the organization as a whole will be greater than the sum of its parts.

Case: Toyota Motors

Toyota Motors started out as a domestic marketer, eventually exported its cars to a few regional markets, grew to become a multinational marketer, and today is a true global marketer, building manufacturing plants in the foreign country as well as hiring local labour, using local ad agencies, and complying to that country's cultural mores. As it moved from one level to the next, it also revised attitudes toward marketing and the underlying philosophy of business.

Ultimately, the successful marketer is the one who is best able to manipulate the controllable tools of the marketing mix within the uncontrollable environment. The principal reason for failure in international marketing results from a company not conducting the necessary research, and as a consequence, misunderstanding the differences and nuances of the marketing environment within the country that has been targeted.

1.5 CHALLENGES OF GLOBAL MARKETING

A global company is generally referred to as a multinational corporation (MNC). An MNC is a company that operates in two or more countries, leveraging the global environment to approach varying markets in attaining revenue generation. These international operations are pursued as a result of the strategic potential provided by technological developments, making new markets a more convenient and profitable pursuit both in sourcing production and pursuing growth.

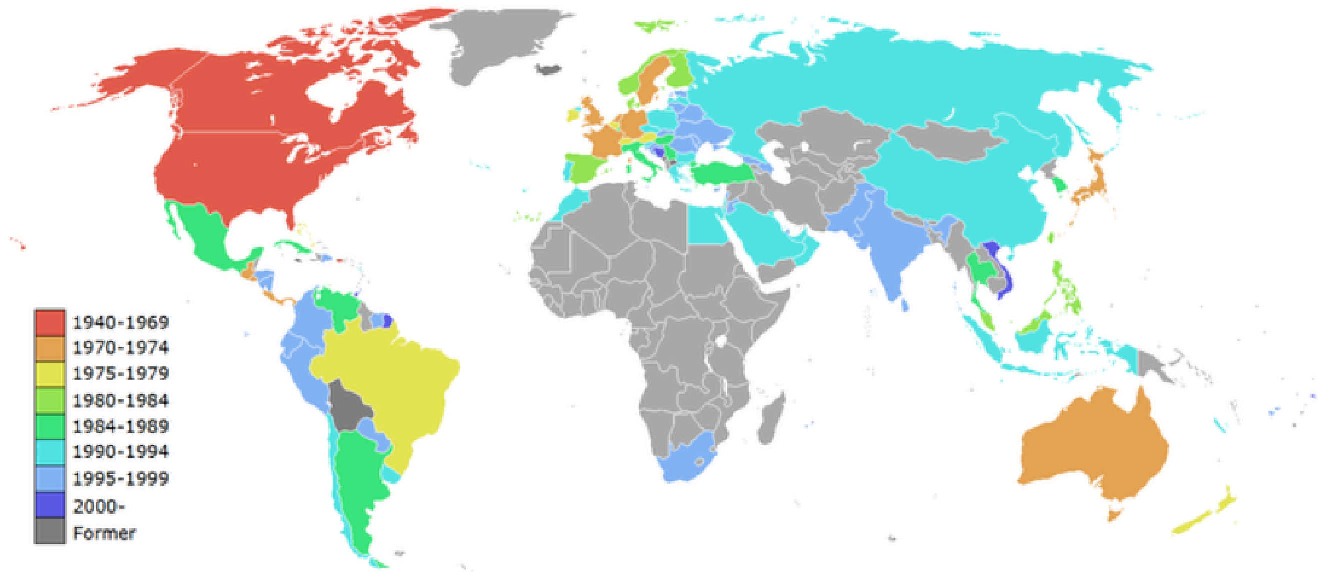


Fig. 1.4 McDonald's Locations: Over the last 70 years, McDonald's has become a global corporation.

International operations are therefore a direct result of either achieving higher levels of revenue or a lower cost structure within the operations or value-chain. MNC operations often attain **economies of scale**, through mass producing in external markets at substantially cheaper costs, or economies of scope, through horizontal expansion into new geographic markets. If successful, these both result in positive effects on the income statement (either larger revenues or stronger margins), but contain the innate risk in developing these new opportunities.

Economies of scale – refers to the situation where, as the quantity of output goes up, the cost per unit goes down. This is the idea behind "warehouse stores" like Costco or Walmart. In everyday language: a larger factory can produce at a lower average cost than a smaller factory.

Opportunities

As **gross domestic product (GDP)** growth migrates from mature economies, such as the US and EU member states, to developing economies, such as China and India, it becomes highly relevant to capture growth in higher-growth markets. It is a particularly strong visual representation of the advantages a global corporation stands to capture, where the darker green areas represent where the highest GDP growth potential resides. High growth in the external environment is a strong opportunity for most incumbents in the market.

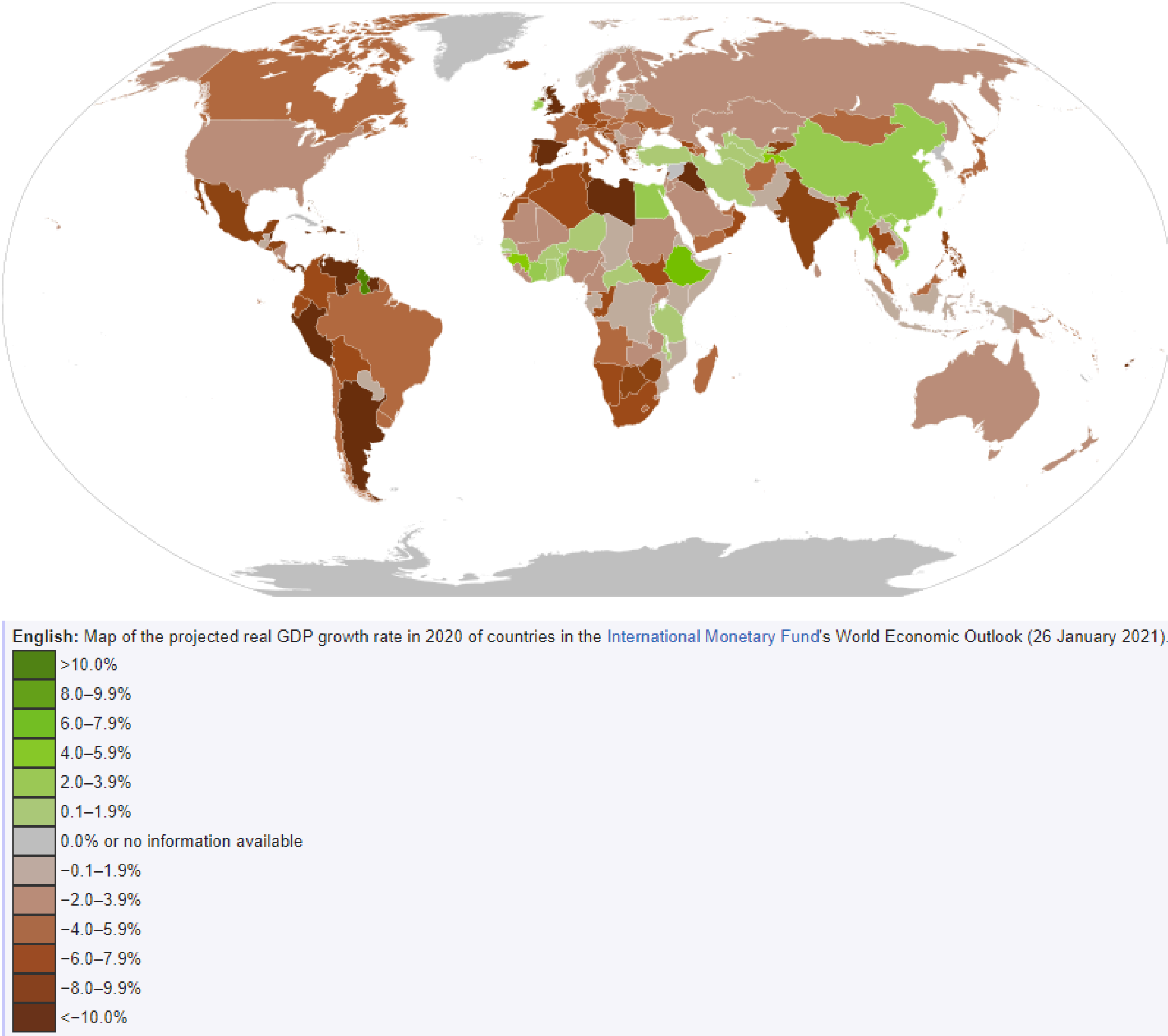


Fig 1.5 *GDP Growth Rate*: *This map highlights (via dark green) where the strongest growth opportunities currently are as of 2021.* "IMF World Economic Outlook January 2021 Real GDP growth rate" by Brobt, CC BY-SA 4.0

Challenges

However, despite the general opportunities a global market provides, there are significant challenges MNCs face in penetrating these markets. These challenges can loosely be defined through four factors:

- **Public Relations**: Public image and branding are critical components of most businesses. Building this public relations potential in a new geographic region is an enormous challenge, both in effectively localizing the message and in the capital expenditures necessary to create momentum.
- **Ethics**: Arguably the most substantial of the challenges faced by MNCs, ethics have historically played a

dramatic role in the success or failure of global players. For example, Nike had its brand image hugely damaged through utilizing 'sweat shops' and low-wage workers in developing countries. Maintaining the highest ethical standards while operating in developing countries is an important consideration for all MNCs.

- **Organizational Structure**: Another significant hurdle is the ability to efficiently and effectively incorporate new regions within the value chain and corporate structure. International expansion requires enormous capital investments in many cases, along with the development of a specific strategic business unit (SBU) in order to manage these accounts and operations. Finding a way to capture value despite this fixed organizational investment is an important initiative for global corporations.
- **Leadership:** The final factor worth noting is attaining effective leaders with the appropriate knowledge base to approach a given geographic market. There are differences in strategies and approaches in every geographic location worldwide, and attracting talented managers with high intercultural competence is a critical step in developing an efficient global strategy.

Combining these four challenges for global corporations with the inherent opportunities presented by a global economy, companies are encouraged to chase the opportunities while carefully controlling the risks to capture the optimal amount of value. By effectively maintaining ethics and a strong public image, companies should create strategic business units with strong international leadership in order to capture value in a constantly expanding global market.

Globalization

Opportunities

Those in favour of globalization theorize that a wider array of products, services, technologies, medicines, and knowledge will become available and that these developments will have the potential to reach significantly larger customer bases. This means larger volumes of sales and exchange, larger growth rates in GDP, and more empowerment of individuals and political systems through acquiring additional resources and capital. These benefits of globalization are viewed as utilitarian, providing the best possible benefits for the largest number of people.

Challenges

Along with arguments supporting the benefits of a more globally-connected economy, there are criticisms that question the profits that are captured. Opponents argue that the expansion of global trade creates unfair exchanges between larger and smaller economies, arguing that developed economies capture significantly more value because of financial leverage. Other commonly raised concerns include damage to the environment, decreased food safety, unethical labour practices in sweatshops, increased consumerism, and the weakening of traditional cultural values.

1.6 THE GLOBALIZATION DEBATE

In today's global economy, everyone is accustomed to buying goods from other countries—electronics from Taiwan, vegetables from Mexico, clothing from China, cars from Korea, and skirts from India. Most modern shoppers take the "Made in [a foreign country]" stickers on their products for granted. Long-distance commerce wasn't always this common, although foreign trade—the movement of goods from one geographic region to another—has been a key factor in human affairs since prehistoric times. Thousands of years ago, merchants transported only the most precious items—silk, gold and other precious metals and jewels, spices, porcelains, and medicines—via ancient, extended land and sea trade routes, including the famed Silk Road through central Asia. Moving goods great distances was simply too hard and costly to waste the effort on ordinary products, although people often carted grain and other foods over shorter distances from farms to market towns (Bernstein, 2008).

What is the globalization debate? Well, it's not so much a debate as it is a stark difference of opinion on how the internationalization of businesses is affecting countries' cultural, consumer, and national identities—and whether these changes are desirable. For instance, the ubiquity of such food purveyors as Coca-Cola and McDonald's in practically every country reflects the fact that some consumer tastes are converging, though at the likely expense of local beverages and foods. Remember, globalization refers to the shift toward a more interdependent and integrated global economy. This shift is fuelled largely by:

1. declining trade and investment barriers
2. new technologies, such as the Internet. The globalization debate surrounds whether and how fast markets are actually merging together.

We Live in a Flat World

The flat-world view is largely credited to Thomas Friedman and his 2005 best seller, *The World Is Flat*. Although the next section provides you with an alternative way of thinking about the world (a multidomestic view), it is nonetheless important to understand the flat-world perspective. Friedman covers the world for the New York Times, and his access to important local authorities, corporate executives, local Times bureaus and researchers, the Internet, and a voice recorder enabled him to compile a huge amount of information. Many people consider globalization a modern phenomenon, but according to Friedman, this is its third stage.

- The first stage of global development, what Friedman calls **"Globalization 1.0,"** started with Columbus's discovery of the New World and ran from 1492 to about 1800. Driven by nationalism and religion, this lengthy stage was characterized by how much industrial power countries could produce and apply.

- **"Globalization 2.0,"** from about 1800 to 2000, was disrupted by the Great Depression and both World Wars and was largely shaped by the emerging power of huge, multinational corporations. Globalization 2.0 grew with the European mercantile stock companies as they expanded in search of new markets, cheap labour, and raw materials. It continued with subsequent advances in sea and rail transportation. This period saw the introduction of modern communications and cheaper shipping costs.
- **"Globalization 3.0"** began around 2000, with advances in global electronic interconnectivity that allowed individuals to communicate as never before.

In Globalization 1.0, nations dominated global expansion. Globalization 2.0 was driven by the ascension of multinational companies, which pushed global development. In Globalization 3.0, major software advances have allowed an unprecedented number of people worldwide to work together with unlimited potential.

Companies can outsource any service or business that can be broken down to its key components and converted to computerized operations. This includes everything from making restaurant reservations to reporting corporate earnings to reading x-rays. And it doesn't stop at basic services. With the "globalization of innovation," multinationals in India are filing increasing numbers of US patent applications, ranging from aircraft-engine designs to transportation systems and microprocessor chips. Japanese-speaking Chinese nationals in Dailian, China, now answer call-center questions from Japanese consumers. Due to Dailian's location near Japan and Korea, as well as its numerous universities, hospitals, and golf courses, some 2,800 Japanese companies outsource operations there. While many companies are outsourcing to other countries, some are using "home sourcing"—allowing people to work at home. JetBlue uses home sourcing for reservation clerks. Today, about 16 percent of the US workforce works from home. In many ways, outsourcing and home sourcing are related; both allow people to work from anywhere.

How the World Got Flat

Friedman identifies ten major events that helped reshape the modern world and make it flat (Friedman, 2005):

1. **11/9/89: When the walls came down and the windows went up.** The fall of the Berlin Wall ended old-style communism and planned economies. Capitalism ascended.
2. 8/9/95: When Netscape went public. Internet browsing and e-mail helped propel the Internet by making it commercially viable and user friendly.

3. Work-flow software: Let's do lunch. Have your application talk to my application. With more powerful, easier-to-use software and improved connectivity, more people can share work. Thus, complex projects with more interdependent parts can be worked on collaboratively from anywhere.

4. Open-sourcing: Self-organizing, collaborative communities. Providing basic software online for free gives everyone source code, thus accelerating collaboration and software development.

5. Outsourcing: Y2K. The Internet lets firms use employees worldwide and send specific work to the most qualified, cheapest labour, wherever it is. Enter India, with educated and talented people who work at a fraction of US or European wages. Indian technicians and software experts built an international reputation during the Y2K millennium event. The feared computer-system breakdown never happened, but the Indian IT industry began handling e-commerce and related businesses worldwide.

6. Offshoring: Running with gazelles, eating with lions. When it comes to jobs leaving and factories being built in cheaper places, people think of China, Malaysia, Thailand, Mexico, Ireland, Brazil, and Vietnam. But going offshore isn't just moving part of a manufacturing or service process. It means creating a new business model to make more goods for non-US sale, thus increasing US exports.

7. Supply-chaining: Eating sushi in Arkansas. Walmart demonstrates that improved acquisition and distribution can lower costs and make suppliers boost quality.

8. Insourcing: What the guys in funny brown shorts are really doing. This kind of service collaboration happens when firms devise new service combinations to improve service. Take United Parcel Service (UPS). The "brown" company delivers packages globally, but it also repairs Toshiba computers and organizes delivery routes for Papa John's pizza. With insourcing, UPS uses its logistics expertise to help clients create new businesses.

9. Informing: Google, Yahoo!, MSN Web Search. Google revolutionized information searching. Its users conduct some one billion searches annually. This search methodology and the wide access to knowledge on the Internet transforms information into a commodity people can use to spawn entirely new businesses.

10. The steroids: Digital, mobile, personal, and virtual. Technological advances range from wireless communication to processing, resulting in extremely powerful computing capability and transmission. One new Intel chip processes some 11 million instructions per second (MIPS), compared to 60,000 MIPS in 1971.

These ten factors had powerful roles in making the world smaller, but each worked in isolation until, Freidman writes, the convergence of three more powerful forces:

1. new software and increased public familiarity with the Internet
2. the incorporation of that knowledge into business and personal communication
3. the market influx of billions of people from Asia and the former Soviet Union who want to become more prosperous—fast. Converging, these factors generated their own critical mass. The benefits of each event became greater as it merged with another event. Increased global collaboration by talented people without regard to geographic boundaries, language, or time zones created opportunity for billions of people.

Political allegiances are also shifting. While critics say outsourcing costs US jobs, it can also work the other way. When the state of Indiana bid for a new contract to overhaul its employment claims processing system, a computer firm in India won. The company's bid would have saved Indiana $8 million, but local political forces made the state cancel the contract. In such situations, the line between the exploited and the exploiter becomes blurred.

Case: Hewlett-Packard (HP)

Corporate nationality is also blurring. Hewlett-Packard (HP) is based in California, but it has employees in 178 countries. HP manufactures parts wherever it's cheapest to do so. Multinationals like HP do what's best for them, not what's best for their home countries. This leads to critical issues about job loss versus the benefits of globalization.

Since the world's flattening can't be stopped, new workers and those facing dislocation should refine their skills and capitalize on new opportunities. One key is to become an expert in a job that can't be delegated offshore. This ranges from local barbers and plumbers to professionals such as surgeons and specialized lawyers.

We Live in a Multidomestic World, Not a Flat One!

International business professor Pankaj Ghemawat takes strong issue with the view that the world is flat and instead espouses a world he characterizes as "semiglobalized" and "multidomestic." If the world were flat, international business and global strategy would be easy. According to Ghemawat (2001), it would be domestic strategy applied to a bigger market. In the semiglobalized world, however, global strategy begins with noticing national differences.

Ghemawat's 2001 research suggests that to study "barriers to cross-border economic activity" you will use a "CAGE" analysis. The CAGE framework covers these four factors:

1. Culture. Generally, cultural differences between two countries reduce their economic exchange. Culture refers to a people's norms, common beliefs, and practices. Cultural distance refers to differences based in language, norms, national or ethnic identity, levels of trust, tolerance, respect for entrepreneurship and social networks, or other country-specific qualities. Some products have a strong national identification, such as the Molson beer company in Canada (see Molson's "I am Canadian" ad campaign).[7] Conversely, genetically modified foods (GMOs) are commonly accepted in North America but highly disdained in Western Europe. Such cultural distance for GMOs would make it easier to sell GMO corn in the United States but impossible to sell in Germany. Some differences are surprisingly specific (such as the Chinese dislike of dark beverages, which Coca-Cola marketers discovered too late).

2. Administration. Bilateral trade flows show that administratively similar countries trade much more with each other. Administrative distance refers to historical governmental ties, such as those between India and the United Kingdom. This makes sense; they have the same sorts of laws, regulations, institutions, and policies. Membership in the same trading block is also a key similarity. Conversely, the greater the administrative differences between nations, the more difficult the trading relationship—whether at the national or corporate level. It can also refer simply to the level and nature of government involvement in one industry versus another. Farming, for instance, is subsidized in many countries, and this creates similar conditions.

3. Geography. This is perhaps the most obvious difference between countries. You can see that the market for a product in Los Angeles is separated from the market for that same product in Singapore by thousands of miles. Generally, as distance goes up, trade goes down, since distance usually increases the cost of transportation. Geographic differences also include time zones, access to ocean ports, shared borders, topography, and climate. You may recall from the opening case that even Google was affected by geographic distance when it felt the speed of the Internet connection to Google.com was slowed down because the Chinese were accessing server farms in other countries, as none were set up in China (prior to the setup of Google.cn).

4. Economics. Economic distance refers to differences in demographic and socioeconomic conditions. The most obvious economic difference between countries is size (as compared by gross domestic product, or GDP). Another is per capita income. This distance is likely to have the greatest effect when (1) the nature of demand varies with income level, (2) economies of scale are limited, (3) cost differences are significant, (4) the distribution or business systems are different, or (5) organizations have to be highly responsive to their customers' concerns. Disassembling a company's economy reveals other differences, such as labour costs, capital costs, human capital (e.g., education or skills), land value, cheap natural resources, transportation networks, communication infrastructure, and access to capital.

Each of these CAGE dimensions shares the common notion of distance. CAGE differences are likely to matter most when the CAGE distance is great. That is, when CAGE differences are small, there will likely be a greater opportunity to see business being conducted across borders. A CAGE analysis also requires examining an organization's particular industry and products in each of these areas. When looking at culture, consider how culturally sensitive the products are. When looking at administration, consider whether other countries coddle certain industries or support "national champions." When looking at geography, consider whether products will survive in a different climate. When looking at economics, consider such issues as the effect of per capita income on demand.

Pankaj Ghemawat (2007) provides this anecdote in partial support of his multidomestic (or anti-flat-world) view. "It takes an aroused man to make a chicken affectionate" is probably not the best marketing slogan ever devised. But that's the one Perdue Chicken used to market its fryers in Mexico. Mexicans were nonplussed, to say the least, and probably wondered what was going on in founder Frank Perdue's henhouse. How did the slogan get approved? Simple: it's a literal translation of Perdue's more appetizing North American slogan "It takes a tough man to make a tender chicken." As Perdue discovered, at least through his experience with the literal translation of his company motto into Spanish, cultural and economic globalization have yet to arrive. Consider the market for capital. Some say capital "knows no boundaries." Recent data, however, suggests capital knows its geography quite well and is sticking close to home. For every dollar of capital investment globally, only a dime comes from firms investing "outside their home countries." For every $100 US investors put in the stock market, they spend $15 on international stocks. For every one hundred students in the Organization for Economic Co-operation (OECD) universities, perhaps five are foreigners. These and other key measures of internationalization show that the world isn't flat. It's 90 percent round, like a rugby ball.

1.7 STANDARDIZATION AND CUSTOMIZATION

Most of the basic principles for effective marketing apply equally well to domestic and global marketing activity. However, globalization introduces a number of challenges that are unique to operating simultaneously in different countries and global markets.

What is the best way to enter a global market?

When should you adjust a product's features to customize it to consumer needs in a different global market?

How do you manage the costs and complexities of product promotion when it must take place in different locations, with different languages, cultural sensitivities and consumer expectations?

What considerations should go into product pricing, when a good is offered in different markets using different currencies and exchange rates?

In 1983, Harvard marketing professor Theodore Levitt wrote an article entitled, "The Globalization of Markets", and nothing about marketing has been the same since. According to Levitt, a new economic reality-the emergence of global consumer markets for single standard products-has been triggered in part by technological developments. Worldwide communications ensure the instant diffusion of new lifestyles and pave the way for a wholesale transfer of goods and services.

Adopting this global strategy provides a competitive advantage in cost and effectiveness. In contrast to multinational companies, standardized (global) corporations view the world or its major regions as one entity instead of a collection of national markets. These world marketers compete on a basis of appropriate value: i.e. an optimal combination of price, quality, reliability, and delivery of products that are identical in design and function. Ultimately, consumers tend to prefer a good price/quality ratio to a highly customized but less cost-effective item. Levitt distinguished between products and brands. While the global product itself is standardized or sold with only minor modifications, the branding, positioning, and promotion may have to reflect local conditions.

Critics of Levitt's perspective suggest that his argument for global standardization is incorrect and that each market strategy should be customized for each country. Kotler notes that one study found that 80 per cent of US exports required one or more adaptations. Furthermore, the average product requires at least four to five adaptations out of a set of eleven marketing elements: labelling, packaging, materials, colours, name, product features, advertising themes, media, execution, price, and sales promotion. Kotler suggests that all eleven factors should be evaluated before standardization is considered.

To date, no one has empirically validated either perspective. While critics of Levitt can offer thousands of anecdotes contradicting the validity of standardization, a more careful read of Levitt's ideas indicate that he offers standardization as a strategic option, not a fact. Although global marketing has its pitfalls, it can also yield impressive advantages. Standardized products can lower operating costs. Even more important, effective coordination can exploit a company's best product and marketing ideas.

Too often, executives view global marketing as an either/or proposition-either full standardization or local control. But when a global approach can fall anywhere on a spectrum-from tight worldwide coordination on programming details to loose agreements on a product ideas-there is no reason for this extreme view. In applying the global marketing concept and making it work, flexibility is essential. The big issue today is not whether to go global, but how to tailor the global marketing concept to fit each business and how to make it work.

Global Marketing Strategies

U.S. firms choose to engage in global marketing for many reasons, the most attractive of which are market expansion and new profit opportunities. When a firm chooses to market internationally, it must decide whether to adjust its domestic marketing program—depending on how much centralized control a firm wishes to maintain over its marketing.

- If an organization wants to maintain strong centralized control and uniformity in its products and marketing activities, it is choosing a strategy called **standardization**.
- If an organization wants to adjust products, messaging, and marketing activities to fit the needs and preferences of local markets around the world, it is choosing a **localization** strategy.

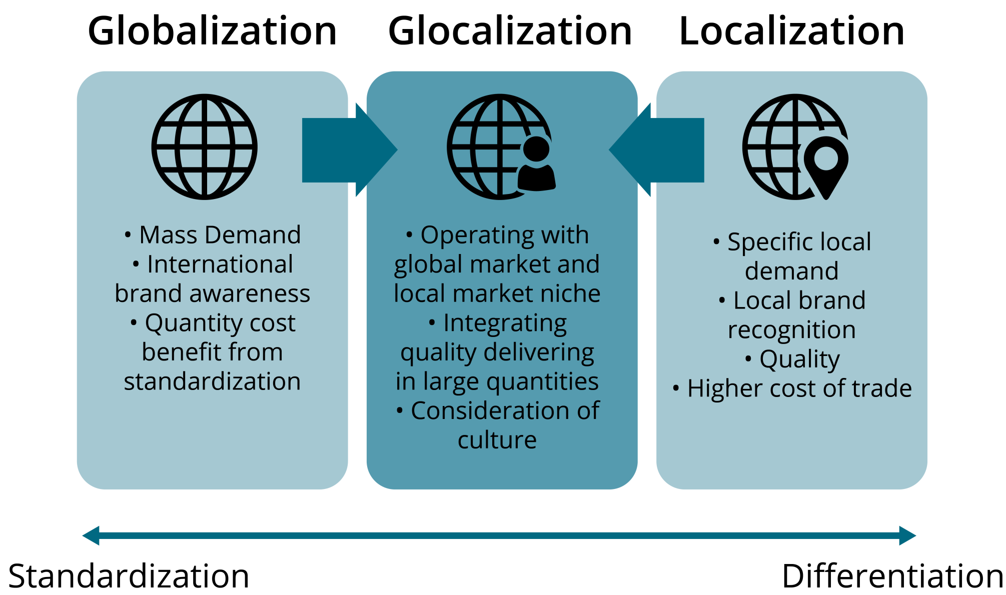


Fig 1.6 "Glocalization" by Alyssa Giles CC BY-NC-SA 4.0

Global Standardization: The Argument for Standardized Marketing

To the extent that global consumers desire standardized products, companies can pursue a global standardization strategy. Using this approach, a product and the way in which it is marketed are largely uniform across the world, with little variation in the marketing mix from country to country. Advocates of standardization strategy argue that companies can achieve competitive advantage by offering the optimal combination of price, quality, and reliability with products that are identical in design and function throughout the world; they also claim that consumers will prefer this standardized product to a highly localized product that is also more expensive.

- Standardization can translate into **lower operating costs** because there aren't extra costs associated with developing and marketing unique products tailored to local market needs. It also expands the customer base receptive to a common global product. There is no need to adjust product features, naming, or other attributes for each new market, and marketing materials themselves can be repurposed across different world regions. Below are the primary benefits of a global standardization strategy:
- Marketers can use the **same approach** for developing, promoting, and delivering products and services worldwide, creating lower operating costs and economies of scale in product development and marketing

- The ability to develop and invest in a unified brand and/or company identity throughout the world, along with the opportunity to develop brand awareness and brand equity that give a competitive advantage
- Product lines that consist of a **small number of global brands** rather than a plethora of localized product brands and extensions, along with cost savings and improved efficiencies associated with managing a smaller total number of brands
- Companies that pursue this approach assume that **consumer needs** are relatively **homogenous** around the world and that the same basic marketing mix will work across global markets. These organizations typically have a centralized approach to the marketing function and try to minimize the need for developing localized marketing strategies.

The case for a standardization strategy was made by Harvard marketing professor Theodore Levitt in his 1983 article, "The Globalization of Markets." He argued that technology and worldwide communications have helped trigger the emergence of global consumer markets that are receptive to single, standardized global products. According to Levitt, adopting a standardized global strategy provides a competitive advantage in cost and effectiveness.

Localization: The Argument to Localize Marketing

On the other end of the spectrum is localization strategy, in which firms adjust their products and marketing mix for each target market. Advocates of localization argue that, in reality, global standardization doesn't work, and in fact nearly all exported products require one or more adaptations to be successful. In work by Kotler (1986), one study found that 80 percent of U.S. exports require one or more adaptations, and the average product requires at least four to five adaptations out of eleven different elements: labelling, packaging, materials, colours, name, product features, advertising themes, media, execution, price, and sales promotion.

- Localization strategy recognizes that **diversity** exists in global markets and that marketers need to understand and respond to this diversity in the goods they offer and the way they market to consumers in these markets. Language, culture, customs, the physical environment, the degree of economic development, societal institutions, and other factors all contribute to how well a product fits a local market's needs. Localization may involve:
    - 1) altering existing products to fit the needs of the local target market or
    - 2) creating completely new products to fit the needs of the local target market.
- Although localization does **increase the cost and complexity** associated with developing and marketing tailored products, its supporters argue that it results in products and marketing strategy that are a better fit for local market needs and ultimately a greater sales success. A localized approach can protect companies from high-profile, disastrous consequences when a standardized product fails.

Standardization is often responsible for marketing misfires like offensive marketing images, catastrophic naming, and product-design glitches. Its critics argue that standardization strategy overestimates how well any single, uniform product and marketing approach will succeed in markets all over the world.

The Middle Ground: Blending Standardization and Localization

In reality, global marketing is not an either/or proposition requiring either full standardization or localized control of product and marketing. In fact, a successful global approach can fall anywhere on a spectrum–from tight worldwide coordination on programming details to loose agreements on product ideas. Most organizations find that flexibility is essential in order to allow organizations to capitalize global opportunities available to them. The right answer for each business depends on organizational structure, leadership and operations; the product category; the markets in question; and other factors. Both strategies offer attractive benefits as well as costs and risks. Most organizations find ways to balance the options available to them with a focus on how to maximize success in their target markets. Few would disagree that fast-food chain McDonald's is a master of global marketing. McDonald's has blended elements of a global standardization strategy with a localization strategy to penetrate global markets and offer products that align perfectly with local appetites and preferences.

Watch the video: What McDonald's Menu Items Look Like Around The World by Food Insider [8:09].

Video: What McDonald's Menu Items Look Like Around The World by Food Insider [8:09] is licensed under the Standard YouTube License. Captions and transcripts are available on YouTube.

Case: Snack Company Expansion

Suppose you're in the marketing department for a highly successful snack food company in the U.S. You're in a brainstorming meeting about expanding into China, and the discussion is starting to get heated. Should you lead with your company's best-selling nacho-cheese-flavoured snacks to take China by storm? Or would it be better to start out with the ranch-dressing-flavoured snack instead, because it's so quintessentially American and it'd be a great way to introduce the Chinese to the tastes Americans love?

Or would something else be a better fit?

It's time to vote: your manager wants everyone on the team to name the flavor they want to lead with. What are you going to choose? Set aside your top pick while you watch Chinese Flavors for American Snacks by Lumen Learning [1:58].

Video: Chinese Flavors for American Snacks by Lumen Learning [1:58] is licensed under the Standard YouTube License. Captions and transcripts are available on YouTube.

So . . . how did you do? How close did you come to favourite flavors in the video? Were you in the ballpark? Are you ready for a career developing snack foods for global markets?

If you're like most Americans, your recommendation probably wasn't very close to the mark, and you're probably thinking that many of the flavours that are delicious to Chinese consumers sound a bit odd to you. Well, now you know how a lot of Chinese consumers probably feel when presented with Cheetos Crunchy Flamin' Hot Limon Cheese Flavored Snacks or Zapp's Spicy Cajun Crawtator potato chips. A little queasy.

Hopefully, this scenario helps highlight some of the challenges of global marketing, as companies start selling products in other countries. How should you enter a new market? Are you offering products that consumers in other countries will want to buy? What should you do to make sure your product–and the rest of your marketing mix–is a good fit for the global customers you want to attract?

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1.9 KEY TERMS

Key Terms

“Globalization 1.0”: The first stage of global development, what Friedman calls “Globalization 1.0,” started with Columbus’s discovery of the New World and ran from 1492 to about 1800. Driven by nationalism and religion, this lengthy stage was characterized by how much industrial power countries could produce and apply. 1.6

“Globalization 2.0”: From about 1800 to 2000, was disrupted by the Great Depression and both World Wars and was largely shaped by the emerging power of huge, multinational corporations. Globalization 2.0 grew with the European mercantile stock companies as they expanded in search of new markets, cheap labour, and raw materials. It continued with subsequent advances in sea and rail transportation. This period saw the introduction of modern communications and cheaper shipping costs. 1.6

“Globalization 3.0”: Began around 2000, with advances in global electronic interconnectivity that allowed individuals to communicate as never before 1.6

Administration: Bilateral trade flows show that administratively similar countries trade much more with each other. Administrative distance refers to historical governmental ties, such as those between India and the United Kingdom. 1.6

Culture: Generally, cultural differences between two countries reduce their economic exchange. Culture refers to a people’s norms, common beliefs, and practices. 1.6

Direct Exporting: Is the means of entry into a foreign market, the manufacturer establishes an export department to sell directly to a foreign film. 1.4

Diversity: Exists in global markets and marketers need to understand and respond to this diversity in the goods they offer and the way they market to consumers in these markets. 1.7

Domestic Marketing: This involves the company manipulating a series of controllable variables, such as price, advertising, distribution, and the product, in a largely uncontrollable external environment that is made up of different economic structures, competitors, cultural values, and legal infrastructure within specific political or geographic country boundaries. 1.4

Economics: Economic distance refers to differences in demographic and socioeconomic conditions. The most obvious economic difference between countries is size (as compared by gross domestic product, or GDP). 1.6

Economies of Scale: This refers to the situation where, as the quantity of output goes up, the cost per unit goes down. This is the idea behind "warehouse stores" like Costco or Walmart. In everyday language: a larger factory can produce at a lower average cost than a smaller factory. 1.5

Export marketing: A firm can export its products in one of three ways: indirect exporting, semi-direct exporting, and direct exporting 1.4

Firm Infrastructure: Firm infrastructure refers to how the firm is organized and led by executives. The effects of this organizing and leadership can be profound. For example, Ron Joyce's leadership of the Canadian doughnut shop chain Tim Hortons was so successful that Canadians consume more doughnuts per person than all other countries. 1.2

Global Marketing: Involves the firm making one or more marketing decisions across national boundaries. At its most complex, it involves the firm establishing manufacturing and marketing facilities overseas and coordinating marketing strategies across markets. 1.1

Global Value Chain: This is when an organization does the full range of activities including supply, production, marketing, sales, distribution, and support to the end consumer, across geographical locations to gain a competitive advantage. 1.2

Gross Domestic Product (GDP): Growth migrates from mature economies, such as the US and EU member states, to developing economies, such as China and India, it becomes highly relevant to capture growth in higher-growth markets. 1.5

Human Resource Management: Human resource management is also important. Human resource management involves the recruitment, training, and compensation of employees. Recent research used data from more than twelve thousand organizations to demonstrate that the knowledge, skills, and abilities of a firm's employees can act as a strategic resource and strongly influence the firm's performance (Crook et al., 2011). 1.2

Inbound Logistics: Inbound logistics refers to the arrival of raw materials. 1.2

Increase The Cost and Complexity: Associated with developing and marketing tailored products, its supporters argue that it results in products and marketing strategies that are a better fit for local market needs and ultimately a greater sales success. 1.6

Indirect Exporting: Is a common practice among firms that are just beginning their exporting. Sales, whether foreign or domestic, are treated as domestic sales. All sales are made through the firm's domestic sales department, as there is no export department. 1.4

International Marketing: This involves the company operating across several markets in which not only do the uncontrollable variables differ significantly between one market and another, but the controllable factor in the form of cost and price structures, opportunities for advertising, and distributive infrastructure are also likely to differ significantly. 1.4

Marketing and Sales: Attracting potential customers and convincing them to make purchases is the domain of marketing and sales. 1.2

Operations: Operations refers to the actual production process. 1.2

Outbound Logistics: Outbound logistics tracks the movement of finished products to customers. 1.2

Primary Activities: Are actions that are directly involved in the creation and distribution of goods and services. There are five primary activities in Porter's Value Chain namely Inbound Logistics, Operations, Outbound Logistics, Marketing & Sales and Services. 1.2

Procurement: Procurement is the process of negotiating for and purchasing raw materials. 1.2

Public Relations: Public image and branding are critical components of most businesses. Building this public relations potential in a new geographic region is an enormous challenge, both in effectively localizing the message and in the capital expenditures necessary to create momentum. 1.5

Secondary Activities: Are not directly involved in the evolution of a product, but instead provide important underlying support for primary activities. Four activities are attributed as Secondary in Porter's Value Chain namely Infrastructure, Human Resource Management, Technological Development and Procurement. 1.2

Semi-Direct Exporting: An American exporter usually initiates the contact through agents, merchant middlemen, or other manufacturers in the US. Such semi-direct exporting can be handled in a variety of ways. 1.4

Services: Service refers to the extent to which a firm provides assistance to its customers. Voodoo Donuts in Portland, Oregon, has developed a clever website (voodoodoughnut.com) that helps customers understand their uniquely named products, such as the Voodoo Doll, the Texas Challenge, and the Memphis Mafia, and the Dirty Snowball. 1.2

Technology: Technology refers to the use of computerization and telecommunications to support primary activities. 1.2

CHAPTER 2: THE ECONOMIC AND POLITICAL ENVIRONMENT

Chapter Outline

2.0 INTRODUCTION

Learning Objectives

After reading this section, students should be able to:

1. Outline the importance of the economic environment.
2. Discuss the implication of inflation, deflation and balance of payments.
3. Discuss the importance of the political environment.
4. Define political risk.
5. Explain the effect of government policy changes on international marketing.
6. Define legal risk.
7. Outline the importance of the legal environment.

The economic environment is a major determinant of global market potential and opportunity. In today's global economy, capital movements are the driving force, production is uncoupled from employment, and capitalism has vanquished communism. Based on patterns of resource allocation and ownership, the world's economies can be categorized as market capitalism, centrally-planned capitalism, centrally-planned socialism, and market socialism. The final years of the twentieth century were marked by transitions toward market capitalism in many countries that had been centrally controlled. However, there still exists a great disparity among the nations of the world in terms of economic freedom.

The **political environment** of global marketing is the set of governmental institutions, political parties, and organizations that are the expression of the people in the nations of the world. In particular, anyone engaged in global marketing should have an overall understanding of the importance of sovereignty to national governments. The political environment varies from country to country, and political risk assessment is crucial. It is also important to understand a particular government's actions with respect to taxes and seizure of assets. Historically, the latter have taken the form of expropriation, confiscation, and nationalization.

When global managers explore how to expand, they start by looking at the world. Knowing the major markets and the stage of development for each allows managers to determine how best to enter and expand. The manager's goal is to hone in on a new country—hopefully, before their competitors and usually before the popular media does. China and India were expanding rapidly for several years before the financial press, such as the *Wall Street Journal*, elevated them to their current hot status.

It's common to find people interested in doing business with a country simply because they've read that it's the new "hot" economy. They may know little or nothing about the market or country—its history, evolution of thought, people, or how interactions are generally managed in a business or social context. Historically, many companies have only looked at new global markets once potential customers or partners have approached them. However, trade barriers are falling, and new opportunities are fast emerging in markets of the Middle East and Africa—further flattening the world for global firms. Companies are increasingly identifying these and other global markets for their products and services and incorporating them into their long-term growth strategies.

The **legal environment** consists of laws, courts, attorneys, legal customs, and practices. International law is comprised of the rules and principles that nation-states consider binding upon themselves. The countries of the world can be broadly categorized in terms of common-law legal systems or civil-law legal system. The United States and Canada and many former British colonies are common law countries; most other countries are civil-law. A third system, Islamic law, predominates in the Middle East. Some of the most important legal issues pertain to jurisdiction, antitrust, and licensing. In addition, bribery is pervasive in many parts of the world; the Foreign Corrupt Practice Act (FCPA) applies to American companies operating abroad. Intellectual property protection is another critical issue. Counterfeiting is a major problem in global marketing; it often involves infringement of a company's copyright or trademark ownership. When legal conflicts arise, companies can pursue the matter in court or use arbitration.

Savvy global managers realize that to be effective in a country, they need to know its recent political, economic, and legal history. This helps them evaluate not only the current business opportunity but also the risk of political, economic, and social changes that can impact their business.

2.1 THE ECONOMIC ENVIRONMENT

The economic environment is important because of the rapid integration of international economic markets. Increasingly, businesses, consumers, and governments realize that their lives are affected not only by what goes on in their own town, state, or country but also by what is happening around the world. Consumers can walk into their local shops today and buy goods and services from all over the world. Local businesses must compete with these foreign products. However, many of these same businesses also have new opportunities to expand their markets by selling to a multitude of consumers in other countries. The advance of telecommunications is also rapidly reducing the cost of providing services internationally, while the Internet has changed the nature of how many products and services are sold and marketed.

A nation's economic situation represents its current and potential capacity to produce goods and services. The key to understanding market opportunities lies in the evaluation of the stage of a nation's economic growth. **Economic growth** is the increase in the amount of the goods and services produced by an economy over time. It is conventionally measured as a percentage change in the **Gross Domestic Product (GDP)** or **Gross National Product (GNP)**. These two measures, which are calculated slightly differently, total the amounts paid for the goods and services that a country produced. As an example of measuring economic growth, a country that creates 9,000,000 in goods and services in 2020 and then creates 9,090,000 in 2021 has a nominal economic growth rate of 1% for 2021.

In order to compare per capita economic growth among countries, the total sales of the countries to be compared may be quoted in a single currency. This requires converting the value of currencies of various countries into a selected currency, for example, U.S. dollars. One way to do this conversion is to rely on exchange rates among the currencies, for example, how many Mexican pesos buy a single U.S. dollar? Another approach is to use the purchasing power parity method. This method is based on how much consumers must pay for the same "basket of goods" in each country.

Inflation or deflation can make it difficult to measure economic growth. If GDP, for example, goes up in a country by 1% in a year, was this due solely to rising prices (inflation) or because more goods and services were produced and saved? To express real growth rather than changes in prices for the same goods, statistics on economic growth are often adjusted for inflation or deflation.

For example, a table may show changes in GDP in the period 2010 to 2020, as expressed in 2010 U.S. dollars. This means that the single currency being used is the U.S. dollar, with the purchasing power it had in the U.S. in 2010. The table might mention whether the figures are "inflation-adjusted" or real. If no adjustments were made for inflation, the table might make no mention of inflation-adjustment or might mention that the prices are nominal.

A country's balance of payments is a record of its economic transactions with the rest of the world; this record shows whether a country has a **trade surplus** (value of exports exceeds the value of imports) or a **trade deficit** (value of imports exceeds the value of exports). Trade figures can be further divided into merchandise trade and services trade accounts; a country can run a surplus in both accounts, a deficit in both accounts, or a combination of the two. In 2021, the U.S. imported $3.4 trillion in goods and services and exported $2.5 trillion, totalling a trade deficit of $859.1 billion (Amadeo, 2022).

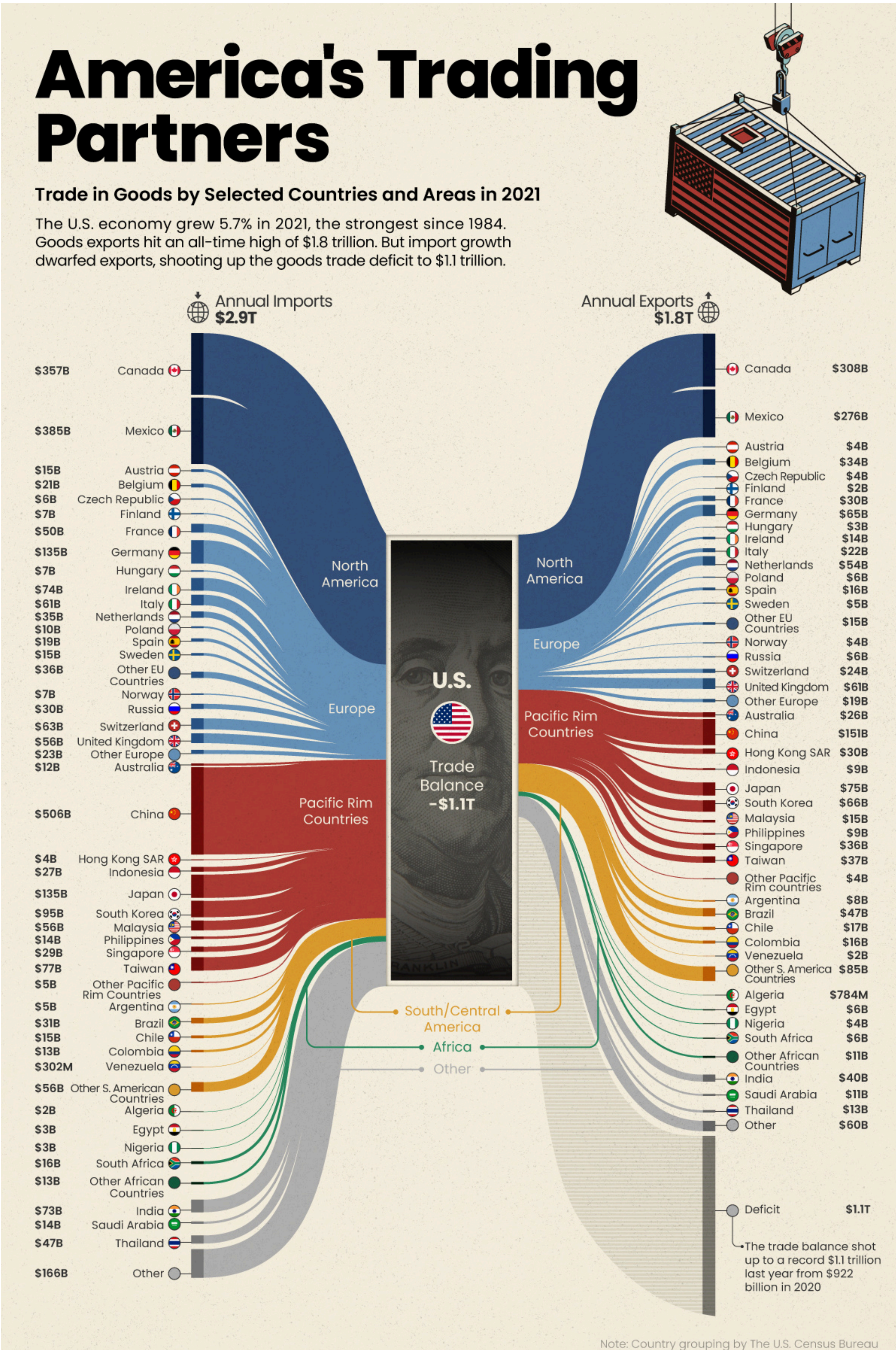
America's Trading Partners
Trade in Goods by Selected Countries and Areas in 2021
The U.S. economy grew 5.7% in 2021, the strongest since 1984. Goods exports hit an all-time high of $1.8 trillion. But import growth dwarfed exports, shooting up the goods trade deficit to $1.1 trillion.
Annual Imports $2.9T
Annual Exports $1.8T
$357B Canada
$385B Mexico
$15B Austria
$21B Belgium
$6B Czech Republic
$7B Finland
$50B France
$135B Germany
$7B Hungary
$74B Ireland
$61B Italy
$35B Netherlands
$10B Poland
$19B Spain
$15B Sweden
$36B Other EU Countries
$7B Norway
$30B Russia
$63B Switzerland
$56B United Kingdom
$23B Other Europe
$12B Australia
$506B China
$4B Hong Kong SAR
$27B Indonesia
$135B Japan
$95B South Korea
$56B Malaysia
$14B Philippines
$29B Singapore
$77B Taiwan
$5B Other Pacific Rim Countries
$5B Argentina
$31B Brazil
$15B Chile
$13B Colombia
$302M Venezuela
$56B Other S. American Countries
$2B Algeria
$3B Egypt
$3B Nigeria
$16B South Africa
$13B Other African Countries
$73B India
$14B Saudi Arabia
$47B Thailand
$166B Other
North America
Europe
Pacific Rim Countries
U.S.
Trade Balance -$1.1T
South/Central America
Africa
Other
Canada $308B
Mexico $276B
Austria $4B
Belgium $34B
Czech Republic $4B
Finland $2B
France $30B
Germany $65B
Hungary $3B
Ireland $14B
Italy $22B
Netherlands $54B
Poland $6B
Spain $16B
Sweden $5B
Other EU Countries $15B
Norway $4B
Russia $6B
Switzerland $24B
United Kingdom $61B
Other Europe $19B
Australia $26B
China $151B
Hong Kong SAR $30B
Indonesia $9B
Japan $75B
South Korea $66B
Malaysia $15B
Philippines $9B
Singapore $36B
Taiwan $37B
Other Pacific Rim countries $4B
Argentina $8B
Brazil $47B
Chile $17B
Colombia $16B
Venezuela $2B
Other S. America Countries $85B
Algeria $784M
Egypt $6B
Nigeria $4B
South Africa $6B
Other African Countries $11B
India $40B
Saudi Arabia $11B
Thailand $13B
Other $60B
Deficit $1.1T
The trade balance shot up to a record $1.1 trillion last year from $922 billion in 2020
Note: Country grouping by The U.S. Census Bureau

Fig 2.1 "Ranked: Visualizing the Largest Trading Partners of the U.S." by Visual Capitalist, reproduced without modification. (Click to enlarge)

Trade

The growth of international trade and investment has been stimulated partly by the steady decline of trade barriers since the Great Depression of the 1930s. In the post–World War II era, the **General Agreement on Tariffs and Trade** or GATT, prompted regular negotiations among a growing body of members to reciprocally reduce tariffs (import taxes) on imported goods. During each of these regular negotiations (eight of these rounds was completed between 1948 and 1994), countries promised to reduce their tariffs on imports in exchange for concessions—that means tariffs reductions—by other GATT members.

When the **Uruguay Round**, the most recently completed round, was finalized in 1994, the member countries succeeded in extending the agreement to include liberalization promises in a much larger sphere of influence. Now countries not only would lower tariffs on goods trade but also would begin to liberalize the agriculture and services markets. They would eliminate the many quota systems—like the multifiber agreement in clothing—that had sprouted up in previous decades. And they would agree to adhere to certain minimum standards to protect intellectual property rights such as patents, trademarks, and copyrights. The **World Trade Organization (WTO)** was created to manage this system of new agreements, to provide a forum for regular discussion of trade matters, and to implement a well-defined process for settling trade disputes that might arise among countries.

"WTO Public Forum 2010" by the World Trade Organization,

Foreign exchange provides a means for settling accounts across borders. The dynamics of international finance can have a significant impact on a nation's economy as well as the fortunes of individual companies. Currencies can be subject to devaluation or revaluation as a result of actions taken by a country's central banker. Currency trading by international speculators can also lead to devaluation. When a country's economy is strong or when demand for its goods is high, its currency tends to appreciate in value. When currency values fluctuate, global firms face various types of economic exposure. Firms can manage exchange rate exposure by hedging.

Case: Saudi Vision 2030 Transformation and Opportunities

Entrepreneurs and business leaders recognize that finding new opportunities for growth and enhancing revenues is a natural progression for a successful business. Having worked in the Arabian Gulf countries for 18 years before moving to Canada, I have learned about the great opportunities that markets in that region offer that are often overlooked or underestimated. Saudi Arabia and the United Arab Emirates, both of which have relatively developing markets, have large young populations with strong purchasing power.

Saudi enjoys high political stability and offers ample business opportunities as it's been traditionally known as a major oil exporter; this now still makes up 90% of KSA's income. However, under Vision 2030, Saudi is moving towards diversification and investing in new sectors like petrochemicals, power, telecoms, healthcare, and even tourism. These sectors are emerging sectors, which are new businesses, that bring in foreign investment, create new opportunities, attract talent and push economic and cultural diversification and growth.

Photo by Akil Imran, Unsplash Licence

Saudi has a GDP of $754 billion in 2014 (World Bank, current estimated prices), and is considered the largest economy in the Middle East. However, working in Saudi doesn't come without challenges and businesses need to understand these implications. First, it is impossible for new businesses operating there to succeed without the "right relationships" and hiring local staff. It is also important to understand and abide by Islamic law and be aware of different business etiquette. For example, having a different work week has implications for dealing with banks internationally. It is also extremely important to re-evaluate the branding to make sure that it can work in Saudi Arabia and resonates with Saudi audiences. Although, It was difficult in the past to obtain visas but Saudi is now open and expats can obtain visas easily through an online system. It is therefore important to highlight this missed opportunity and the great transformation and development achieved after the launch of its Vision 2030.

Rania Alwreikat, March 2023

2.2 THE POLITICAL ENVIRONMENT

The political environment abroad is quite different from that of North America. Most nations desire to become self-reliant and to raise their status in the eyes of the rest of the world. This is the essence of **nationalism.** The nationalistic spirit that exists in many nations has led them to engage in practices that have been very damaging to other countries' marketing organizations. For example, foreign governments can intervene in marketing programs in the following ways:

- contracts for the supply and delivery of goods and services
- the registration and enforcement of trademarks, brand names, and labelling
- patents
- marketing communications
- pricing
- product safety, acceptability, and environmental issues

Political Stability

Business activity tends to grow and thrive when a nation is politically stable. When a nation is politically unstable, multinational firms can still conduct business profitably. Their strategies will be affected however. Most firms probably prefer to engage in the export business rather than invest considerable sums of money in investments in foreign subsidiaries. Inventories will be low and currency will be converted rapidly. The result is that consumers in the foreign nation pay high prices, get less satisfactory products, and have fewer jobs.

2.3 POLITICAL RISK

Political risk is the risk to business interests as a result of political decisions or events. Political risks can be macro, meaning they impact everyone in a country, or micro, meaning that a particular industry or company is impacted. Political risk may be caused by actions of legitimate governments such as controls on prices, outputs, activities, and currency and remittance restrictions. Political risk may also result from events outside of government controls such as war, revolution, terrorism, labour strikes, and extortion.

Political risk can adversely affect all aspects of the international business from the right to export or import goods to the right to own or operate a business. AON for example, categorizes risk based on: economic; exchange transfer; strike, riot, or civil commotion; war; terrorism; sovereign non-payment; legal and regulatory; political interference; and supply chain vulnerability (AON Group, Inc., 2020).

Forms of investment and risk

For a firm considering a new foreign market, there are three broad categories of international business: trade, international licensing of technology and intellectual property, and foreign direct investment. A company developing a business plan may have different elements of all three categories depending on the type of product or service.

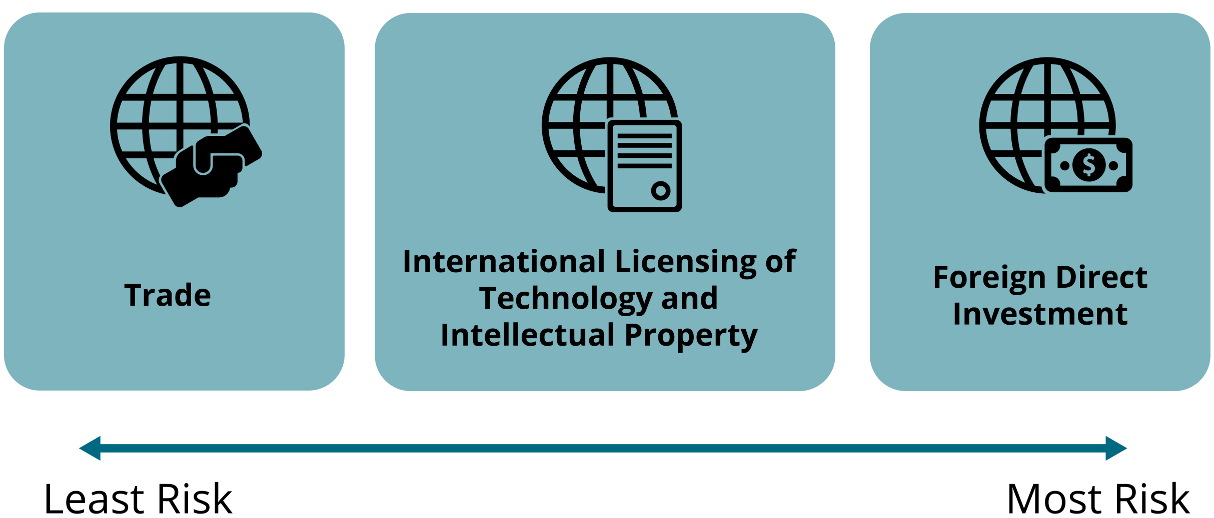

Fig 2.2 "Forms of Risk" by Alyssa Giles, CC BY-NC-SA 4.0.

The risk between these three categories of market entry varies significantly with trade ranked the least risky if the company does not have offices overseas and does not keep inventories there. On the other side of the spectrum is direct foreign investment, which generally brings the greatest economic exposure and thus the greatest risk to the company.

Protection from political risk

Companies can reduce their exposure to political risk by careful planning and monitoring political developments. The company should have a deep understanding of domestic and international affairs for the country they are considering entering. The company should know how politically stable the country is, the strength of its institutions, the existence of any political or religious conflicts, ethnic composition, and minority rights. The country's standing in the international arena should also be part of the consideration; this includes its relations with neighbours, border disputes, membership in international organizations, and recognition of international law.

If the company does not have the resources to conduct such research and analysis, it may find such information at their foreign embassies, international chambers of commerce, political risk consulting firms, insurance companies, and international businessmen familiar with a particular region. In some countries, governments will establish agencies to help private businesses grow overseas. Governments may also offer political risk insurance to promote exports or economic development. Private businesses may also purchase political risk insurance from insurance companies specialized in international business. Insurance companies offering political risk insurance will generally provide coverage against inconvertibility, expropriation, and political violence, including civil strife (AON Group, Inc., 2022). Careful planning and vigilance should be part of any company's preparation for developing an international presence.

Government policy changes and trade relations

Governments may change their policies toward foreign enterprises for many reasons. High unemployment, widespread poverty, nationalistic pressure, and political unrest are just a few of the reasons that can lead to changes in policy. Changes in policies can impose more restrictions on foreign companies to operate or limit their access to financing and trade. In some cases, changes in policy may be favourable to foreign businesses as well. To solve domestic problems, governments often use trade relations. As a result, international businesses can experience frequent changes in regulations and policies, which can add additional costs of doing business overseas.

2.4 LEGAL RISK

Legal risk is the risk arising from failure to comply with statutory or regulatory obligations. Generally, all laws in the host country will apply to an entrepreneur's local business operations. Examples include filing procedures, employment law, environmental law, tax law, and ownership requirements.

Many countries limit foreign ownership of assets and legally force foreign companies into a joint venture with a local partner in order to do business there.

Foreign Direct Ownership Limits

"farmland in poland" by Coltera, CC BY-NC-SA 2.0

Poland, for example, limits foreign ownership of farmland and will continue to do so for another decade under agreements with the EU (Dadak, 2004). It is important to remember that while doing business outside of the home country certain home country laws will still apply. Applicable laws differ from country to country, but one common extension is employment law. In order to minimize exposure to legal risks arising from confusion and excess cost, a company should seek legal advice if possible. In making such arrangements, written contracts should be used. This can minimize confusion in case of litigation.

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2.6 KEY TERMS

Key Terms

Economic growth is the increase in the amount of the goods and services produced by an economy over time. 2.1

Foreign Exchange provides a means for settling accounts across borders. 2.1

General Agreement on Tariffs and Trade, or GATT: Prompted regular negotiations among a growing body of members to reciprocally reduce tariffs (import taxes) on imported goods. 2.1

Gross Domestic Product (GDP) is the value of all final goods and services produced within a country in a given year. 2.1

Gross National Product (GNP) includes what is produced domestically and what is produced by domestic labour and business abroad in a year. 2.1

Inflation is a general and ongoing rise in the level of prices in an entire economy. 2.1

Legal Environment Consists of Laws: Courts, attorneys, legal customs, and practices. International law is comprised of the rules and principles that nation-states consider binding upon themselves. 2.0

Legal Risk: Is the risk arising from failure to comply with statutory or regulatory obligations 2.4

Nationalism: Most nations desire to become self-reliant and to raise their status in the eyes of the rest of the world. The nationalistic spirit that exists in many nations has led them to engage in practices that have been very damaging to other countries' marketing organizations. 2.2

Political Environment of Global Marketing: This is the set of governmental institutions, political parties, and organizations that are the expression of the people in the nations of the world. 2.0

Political Risk: Is generally defined as the risk to business interests resulting from political instability or political change. Political risk exists in every country around the globe and varies in magnitude and type from country to country. 2.3

Trade Deficit is when a country's value of imports exceeds the value of exports.2.1

Trade Surplus is when a country's value of exports exceeds the value of imports.2.1

Uruguay Round: Round pf multilateral trade negotiations under the GATT that was finalized in 1994. Member countries succeeded in extending the agreement to include liberalization promises in a much larger sphere of influence. 2.1

World Trade Organization (WTO):was created to manage international trade agreements, to provide a forum for regular discussion of trade matters, and to implement a well-defined process for settling trade disputes that might arise among countries. 2.1

CHAPTER 3: SOCIAL AND CULTURAL ENVIRONMENT

Chapter Outline

3.0 INTRODUCTION

Learning Objectives

After reading this section, students should be able to:

1. Discuss the role of external environmental factors that shape the global marketing environment.
2. List the various elements in a firm's cultural environment.
3. Outline the importance of culture on markets.
4. Define culture.
5. Identify different kinds of culture.
6. Define and apply Hofstede's and Hall's categories for cultural identification.
7. Identify and discuss additional determinants of culture.

Most people hear about culture and business and immediately think about protocol—a list of dos and don'ts by country. For example, don't show the sole of your foot in Saudi Arabia; know how to bow in Japan. While these practices are certainly useful to know, they are just the tip of the iceberg. We often underestimate how critical local culture, values, and customs can be in the business environment. We assume, usually incorrectly, that business is the same everywhere. Culture does matter, and more and more people are realizing its impact on their business interactions.

Culture, in the broadest sense, refers to how and why we think and function. It encompasses all sorts of things—how we eat, play, dress, work, think, interact, and communicate. Everything we do, in essence, has been shaped by the cultures in which we are raised. Similarly, a person in another country is also shaped by his or her cultural influences. These cultural influences impact how we think and communicate.

Culture, a society's "programming of the mind," has both a pervasive and changing influence on each national market environment. Global marketers must recognize the influence of culture and be prepared to either respond to it or change it. Human behaviour is a function of a person's own unique personality and that person's interaction with the collective forces of the particular society and culture in which he or she has lived. In particular, attitudes, values, and beliefs can vary significantly from country to country.

Also, differences pertaining to religion, aesthetics, dietary customs, and language and communication can affect local reaction to brands or products as well as the ability of company personnel to function effectively in different cultures. A number of concepts and theoretical frameworks provide insights into these and other cultural issues.

Cultures can be classified as high- or low-context; communication and negotiation styles can differ from country to country. Hofstede's social value typology sheds light on national cultures in terms of power distance, individualism vs. collectivism, masculinity vs. femininity, uncertainty avoidance, and long-versus short-term orientation. By understanding the self-reference criterion, global marketers can overcome the unconscious tendency for perceptual blockage and distortion.

Case Study: Tim Hortons

An example of a Canadian company culturally adapting to the expansion of its business into other countries is that of Tim Hortons. If you're Canadian, you've been to a Tim Hortons. It's a staple for any coffee or donut-loving Canadian, but the business now also operates in 15 different countries, which means that people from many different cultures can experience this Canadian business in their own country. With expansions to different countries, comes offering items exclusively culturally suited for the countries in which they operate. One culturally adapted Tim Hortons food item that is exclusive to their own country's menu includes a Chicken Tikka Croissant Sandwich

Image by Victorcampuslat, CC BY-SA 4.0

offered in India. This menu item is a mix of culturally adapting a food item popular in its country (Tikka) and keeping its brand identity with the inclusion of a croissant (an item offered in Canadian Tim Hortons').

Jack Taron, March 2023

3.1 WHAT IS CULTURE

Case: Dunkin' Donuts and Baskin-Robbins: Making Local Global

"Ummm, Yumm" by Thomas Hawk, CC BY-NC 2.0

High-tech and digital news may dominate our attention globally, but no matter where you go, people still need to eat. Food is a key part of many cultures. It is part of the bonds of our childhood, creating warm memories of comfort food or favourite foods that continue to whet our appetites. So it's no surprise that sugar and sweets are a key part of our food focus, no matter what the culture. Two of the most visible American exports are the twin brands of Dunkin' Donuts and Baskin-Robbins.

Owned today by a consortium of private equity firms known as the Dunkin' Brands, Dunkin' Donuts and Baskin-Robbins have been sold globally for more than fifty years. Today, the firm has more than 14,800 points of distribution in forty-four countries with $6.9 billion in global sales.

After an eleven-year hiatus, Dunkin' Donuts returned to Russia in 2010 with the opening of twenty new stores. Under a new partnership, "the planned store openings come 11 years after Dunkin' Donuts pulled out of Russia, following three years of losses exacerbated by a rogue franchisee who sold liquor and meat pies alongside coffee and crullers" (Helliker, 2010). Each culture has different engrained habits, particularly in the choices of food and what foods are appropriate for what meals. The more globally aware businesses are mindful of these issues and monitor their overseas operations and partners. One of the key challenges for many companies operating globally with different resellers, franchisees, and wholly owned subsidiaries is the ability to control local operations.

This wasn't the first time that Dunkin' had encountered an overzealous local partner who tried to customize operations to meet local preferences and demands. In Indonesia in the 1990s, the company was surprised to find that local operators were sprinkling a mild, white cheese on a custard-filled donut. The company eventually approved the local customization since it was a huge success (Jenkins, 2010).

Dunkin' Donuts and Baskin-Robbins have not always been owned by the same firm. They eventually came under one entity in the late 1980s—an entity that sought to leverage the two brands. One of the overall strategies was to have the morning market covered by Dunkin' Donuts and the afternoon-snack market covered by Baskin-Robbins. It is a strategy that worked well in the United States and was one the company employed as it started operating and expanding in different countries. The company was initially unprepared for the wide range of local cultural preferences and habits that would culturally impact its business. In Russia, Japan, China, and most of Asia, donuts, if they were known at all, were regarded more as a sweet type of bakery treat, like an éclair or cream puff. Locals primarily purchased and consumed them at shopping malls as an "impulse purchase" afternoon-snack item and not as a breakfast food.

In fact, in China, there was no equivalent word for "donut" in Mandarin, and European-style baked pastries were not common outside the Shanghai and Hong Kong markets. To further complicate Dunkin' Donuts's entry into China, which took place initially in Beijing, the company name could not even be phonetically spelled in Chinese characters that made any sense, as Baskin-Robbins had been able to do in Taiwan. After extensive discussion and research, company executives decided that the best name and translation for *Dunkin' Donuts* in China would read *Sweet Sweet Ring* in Chinese characters.

Local cultures also impacted flavours and preferences. For Baskin-Robbins, the flavour library is controlled in the United States, but local operators in each country have been the source of new flavour suggestions. In many cases, flavors that were customized for local cultures were added a decade later to the main menus in major markets, including the United States. Mango and green tea were early custom ice cream flavours in the 1990s for the Asian market. In Latin America, *dulce de leche* became a favourite flavor. Today, these flavors are staples of the North American flavour menu.

One flavour suggestion from Southeast Asia never quite made it onto the menu. The durian fruit is a favourite in parts of Southeast Asia, but it has a strong, pungent odour. Baskin-Robbins management was concerned that the strong odour would overwhelm factory operations. (The odour of the durian fruit is so strong that the fruit is often banned in upscale hotels in several Asian countries.) While the durian never became a flavour, the company did concede to making ice cream flavoured after the *ube*, a sweetened purple yam, for the Philippine market. It was already offered in Japan, and the company extended it to the Philippines. In Japan, sweet corn and red bean ice cream were approved for local sale and became hot sellers, but the two flavours never made it outside the country.

When reviewing local suggestions, management conducts a market analysis to determine if the global market for the flavour is large enough to justify the investment in research and development and eventual production. In addition to the market analysis, the company always has to make sure they have access to sourcing quality flavors and fruit. Mango proved to be a challenge, as finding the correct fruit puree differed by country or culture. Samples from India, Hawaii, Pakistan, Mexico, the Philippines, and Puerto Rico were taste-tested in the mainland United States. It seems that the mango is culturally regarded as a national treasure in every country where it is grown, and every country thinks its mango is the best. Eventually the company settled on one particular flavour of mango.

A challenging balance for Dunkin' Brands is to enable local operators to customize flavours and food product offerings without diminishing the overall brand of the companies. Russians, for example, are largely unfamiliar with donuts, so Dunkin' has created several items that specifically appeal to Russian flavor preferences for scalded cream and raspberry jam (Helliker, 2010). In some markets, one of the company's brands may establish a market presence first. In Russia, the overall "Dunkin' Brands already ranks as a dessert purveyor. Its Baskin-Robbins ice-cream chain boasts 143 shops there, making it the No. 2 Western restaurant brand by number of stores behind the hamburger chain McDonald's Corp" (Helliker, 2010). The strength of the company's ice cream brand is now enabling Dunkin' Brands to promote the donut chain as well.

As the case about Dunkin' Brands illustrates, local preferences, habits, values, and culture impact all aspects of doing business in a country. But what exactly do we mean by culture? Culture is different from personality. For our purposes here, let's define **personality** as a person's identity and unique physical, mental, emotional, and social characteristics (Dictionary.com, n.d.). No doubt one of the highest hurdles to cross-cultural understanding and effective relationships is our frequent inability to decipher the influence of culture from that of personality. Once we become culturally literate, we can more easily read individual personalities and their effect on our relationships.

So, What Is Culture, Anyway?

Culture in today's context is different from the traditional, more singular definition, used particularly in Western languages, where the word often implies refinement. **Culture** is the beliefs, values, mind-sets, and practices of a group of people. It includes the behaviour pattern and norms of that group—the rules, the assumptions, the perceptions, and the logic and reasoning that are specific to a group. In essence, each of us is raised in a belief system that influences our individual perspectives to such a large degree that we can't always account for, or even comprehend, its influence. We're like other members of our culture—we've come to share a common idea of what's appropriate and inappropriate.

Culture is really the collective programming of our minds from birth. It's this collective programming that distinguishes one group of people from another. Much of the problem in any cross-cultural interaction stems from our expectations. The challenge is that whenever we deal with people from another culture—whether in our own country or globally—we expect people to behave as we do and for the same reasons. Culture awareness most commonly refers to having an understanding of another culture's values and perspective. This does not mean automatic acceptance; it simply means understanding another culture's mind-set and how its history, economy, and society have impacted what people think. Understanding so you can properly interpret someone's words and actions means you can effectively interact with them.

When talking about culture, it's important to understand that there really are no rights or wrongs. People's value systems and reasoning are based on the teachings and experiences of their culture. Rights and wrongs then really become perceptions. Cross-cultural understanding requires that we reorient our mind-set and, most importantly, our expectations, in order to interpret the gestures, attitudes, and statements of the people we encounter. We reorient our mind-set, but we don't necessarily change it.

There are a number of factors that constitute a culture—manners, mind-set, rituals, laws, ideas, and language, to name a few. To truly understand culture, you need to go beyond the lists of dos and don'ts, although those are important too. You need to understand what makes people tick and how, as a group, they have been influenced over time by historical, political, and social issues. Understanding the "why" behind culture is essential.

When trying to understand how cultures evolve, we look at the factors that help determine cultures and their values. In general, a value is defined as something that we prefer over something else—whether it's a behaviour or a tangible item. Values are usually acquired early in life and are often nonrational—although we may believe that ours are actually quite rational. Our values are the key building blocks of our cultural orientation.

Odds are that each of us has been raised with a considerably different set of values from those of our colleagues and counterparts around the world. Exposure to a new culture *may* take all you've ever learned about what's good and bad, just and unjust, and beautiful and ugly and stand it on its head.

Human nature is such that we see the world through our own cultural shades. Tucked in between the lines of our cultural laws is an unconscious bias that inhibits us from viewing other cultures objectively. Our judgments of people from other cultures will always be coloured by the frame of reference we've been taught. As we look at our own habits and perceptions, we need to think about the experiences that have blended together to impact our cultural frame of reference.

In coming to terms with cultural differences, we tend to employ generalizations. This isn't necessarily bad. Generalizations can save us from sinking into what may be abstruse, esoteric aspects of a culture. However, recognize that cultures and values are not static entities. They're constantly evolving—merging, interacting, drawing apart, and reforming. Around the world, values and cultures are evolving from generation to generation as people are influenced by things outside their culture. In modern times, media and technology have probably single-handedly impacted cultures the most in the shortest time period—giving people around the world instant glimpses into other cultures, for better or for worse. Recognizing this fluidity will help you avoid getting caught in outdated generalizations. It will also enable you to interpret local cues and customs and to better understand local cultures.

Understanding what we mean by culture and what the components of culture are will help us better interpret the impact on business at both the macro and micro levels. Confucius had this to say about cultural crossings: "Human beings draw close to one another by their common nature, but habits and customs keep them apart."

Case: Student Perspective on Social and Cultural Environment

Photo by Avel Chuklanov, Unsplash License

Born and raised in the Philippines with Filipino and Japanese parents, and now living in Canada – one of the most notable characteristics of us Filipinos is our strong family and community relationships. We keep our family ties strong and always show our respect to our elders by using the gesture "mano po"- which is to get the hand of the elder and put it onto your forehead. We even have endearments that are used to call older sisters and older brothers. "Ate" and "Kuya". Quite similar to my Japanese roots as we use "Onee-san" and "Onii-san". This is something that I noticed as one of the biggest cultural differences since my arrival here in Canada. I felt and observed that there is a strong individualism as opposed to the Philippines, where collectivism is highly practised. Here, people seem to go on in their own ways, while we would usually be involved in everyone's businesses. Religious beliefs are also diverse as Canada has a very multicultural population, while in the Philippines, our beliefs are mostly centred on Catholicism.

Alliane Akiyama, October 2022

What Kinds of Culture Are There?

Political, economic, and social philosophies all impact the way people's values are shaped. Our cultural base of reference—formed by our education, religion, or social structure—also impacts business interactions in critical ways. As we study cultures, it is very important to remember that all cultures are constantly evolving. When we say "cultural," we don't always just mean people from different countries. Every group of people has its own unique culture—that is, its own way of thinking, values, beliefs, and mind-sets. For our purposes in this chapter, we'll focus on national and ethnic cultures, although there are subcultures within a country or ethnic group.

Precisely where a culture begins and ends can be murky. Some cultures fall within geographic boundaries; others, of course, overlap. Cultures within one border can turn up within other geographic boundaries looking dramatically different or pretty much the same. For example, Indians in India or Americans in the United States may communicate and interact differently from their countrymen who have been living outside their respective home countries for a few years.

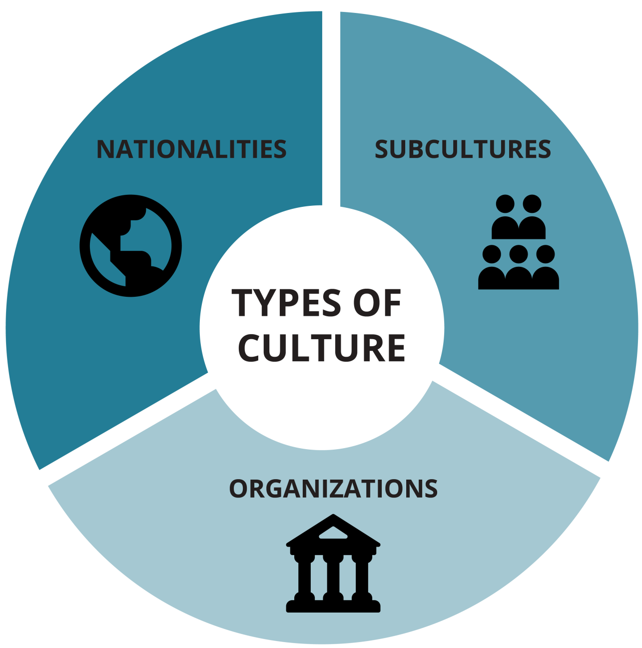

Fig 3.1 "Types of Culture" by Alyssa Giles, CC BY-NC-SA 4.0.

The countries of the Indian subcontinent, for example, have close similarities. And cultures within one political border can turn up within other political boundaries looking pretty much the same, such as the Chinese culture in China and the overseas Chinese culture in countries around the world. We often think that cultures are defined by the country or nation, but that can be misleading because there are different cultural groups (as depicted in the preceding figure). These groups include nationalities; subcultures (gender, ethnicities, religions, generations, and even socioeconomic class); and organizations, including the workplace.

Nationalities

A national culture is—as it sounds—defined by its geographic and political boundaries and includes even regional cultures within a nation as well as among several neighbouring countries. What is important about nations is that boundaries have changed throughout history. These changes in what territory makes up a country and what the country is named impact the culture of each country.

In the past century alone, we have seen many changes as new nations emerged from the gradual dismantling of the British and Dutch empires at the turn of the 1900s. For example, today the physical territories that constitute the countries of India and Indonesia are far different than they were a hundred years ago. While it's easy to forget that the British ran India for two hundred years and that the Dutch ran Indonesia for more than one hundred and fifty years, what is clearer is the impact of the British and the Dutch on the respective bureaucracies and business environments. The British and the Dutch were well known for establishing large government bureaucracies in the countries they controlled. Unlike the British colonial rulers in India, the Dutch did little to develop Indonesia's infrastructure, civil service, or educational system. The British, on the other hand, tended to hire locals for administrative positions, thereby establishing a strong and well-educated Indian bureaucracy. Even though many businesspeople today complain that this Indian bureaucracy is too slow and focused on rules and regulations, the government infrastructure and English-language education system laid out by the British helped position India for its emergence as a strong high-tech economy.

Even within a national culture, there are often distinct regional cultures—the United States is a great example of diverse and distinct cultures all living within the same physical borders. In the United States, there's a national culture embodied in the symbolic concept of "all-American" values and traits, but there are also other cultures based on geographically different regions—the South, Southwest, West Coast, East Coast, Northeast, Mid-Atlantic, and Midwest.

Subcultures

Many groups are defined by ethnicity, gender, generation, religion, or other characteristics with cultures that are unique to them. For example, the ethnic Chinese business community has a distinctive culture even though it may include Chinese businesspeople in several countries. This is particularly evident throughout Asia, as many people often refer to Chinese businesses as making up a single business community. The overseas Chinese business community tends to support one another and forge business bonds whether they are from Indonesia, Malaysia, Singapore, or other ASEAN (Association of Southeast Asian Nations) countries. This group is perceived differently than Chinese from mainland China or Taiwan. Their common experience being a minority ethnic community with strong business interests has led to a shared understanding of how to quietly operate large businesses in countries. Just as in mainland China, *guanxi*, or "connections," are essential to admission into this overseas Chinese business network. But once in the network, the Chinese tend to prefer doing business with one another and offer preferential pricing and other business services.

Organizations

Every organization has its own workplace culture, referred to as the organizational culture. This defines simple aspects such as how people dress (casual or formal), how they perceive and value employees, or how they make decisions (as a group or by the manager alone). When we talk about an entrepreneurial culture in a company, it might imply that the company encourages people to think creatively and respond to new ideas fairly quickly without a long internal approval process. One of the issues managers often have to consider when operating with colleagues, employees, or customers in other countries is how the local country's culture will blend or contrast with the company's culture.

Organizational Culture

For example, Apple, Google, and Microsoft all have distinct business cultures that are influenced both by their industries and by the types of technology-savvy employees that they hire, as well as by the personalities of their founders. When these firms operate in a country, they have to assess how new employees will fit their respective corporate cultures, which usually emphasize creativity, innovation, teamwork balanced with individual accomplishment, and a keen sense of privacy. Their global employees may appear relaxed in casual work clothes, but underneath there is often a fierce competitiveness. So how do these companies effectively hire in countries like Japan, where teamwork and following rules are more important than seeking new ways of doing things? This is an ongoing challenge that human resources (HR) departments continually seek to address.

3.2 DESCRIBING CULTURE: HOFSTEDE

The study of cross-cultural analysis incorporates the fields of anthropology, sociology, psychology, and communication. The combination of cross-cultural analysis and business is a new and evolving field; it's not a static understanding but changes as the world changes. Within cross-cultural analysis, two names dominate our understanding of culture—Geert Hofstede and Edward T. Hall. Although new ideas are continually presented, Hofstede remains the leading thinker on how we see cultures.

This page will review both the thinkers and the main components of how they define culture and the impact on communications and business. At first glance, it may seem irrelevant to daily business management to learn about these approaches. In reality, despite the evolution of cultures, these methods provide a comprehensive and enduring understanding of the key factors that shape a culture, which in turn impact every aspect of doing business globally. Additionally, these methods enable us to compare and contrast cultures more objectively. By understanding the key researchers, you'll be able to formulate your own analysis of the different cultures and the impact on international business.

Hofstede and Values

Geert Hofstede, sometimes called the father of modern cross-cultural science and thinking, is a social psychologist who focused on a comparison of nations using a statistical analysis of two unique databases. The first and largest database composed of answers that matched employee samples from forty different countries to the same survey questions focused on attitudes and beliefs. The second consisted of answers to some of the same questions by Hofstede's executive students who came from fifteen countries and from a variety of companies and industries. He developed a framework for understanding the systematic differences between nations in these two databases. This framework focused on value dimensions. Values, in this case, are *broad preferences for one state of affairs over others*, and they are mostly unconscious.

Most of us understand that values are our own culture's or society's ideas about what is good, bad, acceptable, or unacceptable. Hofstede developed a framework for understanding how these values underlie organizational behaviour. Through his database research, he identified five key value dimensions that analyze and interpret the behaviours, values, and attitudes of a national culture:

1. Power distance
2. Individualism
3. Masculinity
4. Uncertainty avoidance (UA)

5. Long-term orientation (Hofstede, 2011).
6. Indulgence

Power distance

Power distance refers to how openly a society or culture accepts or does not accept differences between people, as in hierarchies in the workplace, in politics, and so on.

For example, *high power distance* cultures openly accept that a boss is "higher" and as such deserves a more formal respect and authority. Examples of these cultures include Japan, Mexico, and the Philippines. In Japan or Mexico, the senior person is almost a father figure and is automatically given respect and usually loyalty without questions.

In Southern Europe, Latin America, and much of Asia, power is an integral part of the social equation. People tend to accept relationships of servitude. An individual's status, age, and seniority command respect—they're what make it all right for the lower-ranked person to take orders. Subordinates expect to be told what to do and won't take initiative or speak their minds unless a manager explicitly asks for their opinion.

At the other end of the spectrum are *low power distance* cultures, in which superiors and subordinates are more likely to see each other as equal in power. Countries found at this end of the spectrum include Austria and Denmark. To be sure, not all cultures view power in the same ways. In Sweden, Norway, and Israel, for example, respect for equality is a warranty of freedom. Subordinates and managers alike often have carte blanche to speak their minds.

Interestingly enough, research indicates that the United States tilts toward low power distance but is more in the middle of the scale than Germany and the United Kingdom.

Let's look at the culture of the United States, Germany, Brazil and China in relation to these five dimensions. The United States actually ranks somewhat lower in power distance—forty as noted in the figure below. The United States has a culture of promoting participation at the office while maintaining control in the hands of the manager. People in this type of culture tend to be relatively laid-back about status and social standing—but there's a firm understanding of who has the power.

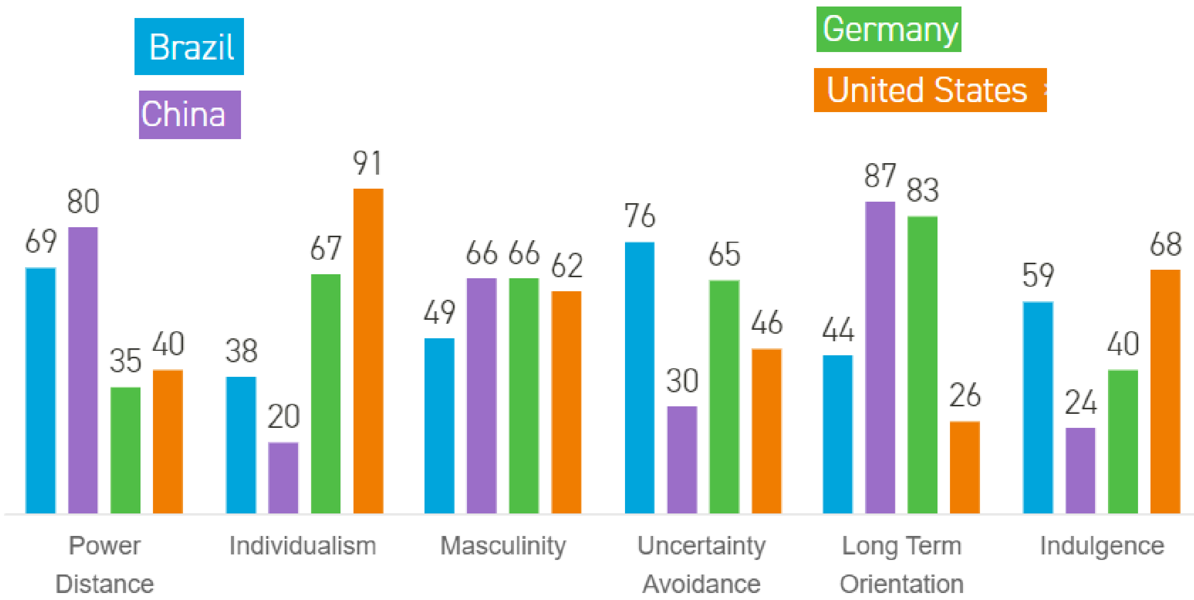

Fig 3.2 "Hofstede's cultural dimensions theory" by Piotrus, CC BY-SA 4.0

Individualism

Individualism is just what it sounds like. It refers to people's tendency to take care of themselves and their immediate circle of family and friends, perhaps at the expense of the overall society. In individualistic cultures, what counts most is self-realization. Initiating alone, sweating alone, achieving alone—not necessarily collective efforts—are what win applause. In individualistic cultures, competition is the fuel of success.

The United States and Northern European societies are often labelled as individualistic. In the United States, individualism is valued and promoted—from its political structure (individual rights and democracy) to entrepreneurial zeal (capitalism). Other examples of high-individualism cultures include Australia and the United Kingdom.

On the other hand, in collectivist societies, group goals take precedence over individuals' goals. Basically, individual members render loyalty to the group, and the group takes care of its individual members. Rather than giving priority to "me," the "us" identity predominates. Of paramount importance is pursuing the common goals, beliefs, and values of the group as a whole—so much so, in some cases, that it's nearly impossible for outsiders to enter the group. Cultures that prize collectivism and the group over the individual include Singapore, Korea, Mexico, and Arab nations. The protections offered by traditional Japanese companies come to mind as a distinctively group-oriented value.

Masculinity

The next dimension is **masculinity,** which may sound like an odd way to define a culture. When we talk about masculine or feminine cultures, we're not talking about diversity issues. It's about how a society views traits that are considered masculine or feminine.

This value dimension refers to how a culture ranks on traditionally perceived "masculine" values: assertiveness, materialism, and less concern for others. In masculine-oriented cultures, gender roles are usually crisply defined. Men tend to be more focused on performance, ambition, and material success. They cut tough and independent personas, while women cultivate modesty and quality of life. Cultures in Japan and Latin America are examples of masculine-oriented cultures.

In contrast, feminine cultures are thought to emphasize "feminine" values: concern for all, an emphasis on the quality of life, and an emphasis on relationships. In feminine-oriented cultures, both genders swap roles, with the focus on quality of life, service, and independence. The Scandinavian cultures rank as feminine cultures, as do cultures in Switzerland and New Zealand. The United States is actually more moderate, and its score is ranked in the middle between masculine and feminine classifications. For all these factors, it's important to remember that cultures don't necessarily fall neatly into one camp or the other.

Uncertainty Avoidance

The next dimension is **uncertainty avoidance (UA)**. This refers to how much uncertainty a society or culture is willing to accept. It can also be considered an indication of the risk propensity of people from a specific culture. People who have high uncertainty avoidance generally prefer to steer clear of conflict and competition. They tend to appreciate very clear instructions. At the office, sharply defined rules and rituals are used to get tasks completed. Stability and what is known are preferred to instability and the unknown. Company cultures in these countries may show a preference for low-risk decisions, and employees in these companies are less willing to exhibit aggressiveness. Japan and France are often considered clear examples of such societies.

In countries with low uncertainty avoidance, people are more willing to take on risks, companies may appear less formal and structured, and "thinking outside the box" is valued. Examples of these cultures are Denmark, Singapore, Australia, and to a slightly lesser extent, the United States. Members of these cultures usually require less formal rules to interact.

Long-term Orientation

The fifth dimension is **long-term orientation**, which refers to whether a culture has a long-term or short-term orientation. This dimension was added by Hofstede after the original four you just read about. It resulted in the effort to understand the difference in thinking between the East and the West. Certain values are associated with each orientation. The long-term orientation values persistence, perseverance, thriftiness, and having a sense of shame. These are evident in traditional Eastern cultures. Based on these values, it's easy to see why a Japanese CEO is likely to apologize or take the blame for a faulty product or process.

The short-term orientation values tradition only to the extent of fulfilling social obligations or providing gifts or favours. These cultures are more likely to be focused on the immediate or short-term impact of an issue. Not surprisingly, the United Kingdom and the United States rank low on long-term orientation.

Long- and short-term orientation and the other value dimensions in the business arena are all evolving as many people earn business degrees and gain experience outside their home cultures and countries, thereby diluting the significance of a single cultural perspective. As a result, in practice, these five dimensions do not occur as single values but are really woven together and interdependent, creating very complex cultural interactions. Even though these five values are constantly shifting and not static, they help us begin to understand how and why people from different cultures may think and act as they do. Hofstede's study demonstrates that there are national and regional cultural groupings that affect the behaviour of societies and organizations and that these are persistent over time.

Indulgence (vs. Restraint)

The sixth dimension is **Indulgence**. This dimension is a relatively new addition to the model. It is described as how far people try to moderate their urges and impulses as a result of their upbringing. Indulgence is a term for a lack of control, while restraint is a term for firm control. This means cultures might be classified as either indulgent or restrained. Indulgence refers to a culture that provides for the relatively unrestricted satisfaction of basic and natural human desires such as enjoyment of life and fun.

Indulgent societies might be more receptive to new and innovative products and services that offer immediate pleasure and gratification through unconventional marketing strategies. In contrast, societies with low indulgence are more responsive to traditional marketing strategies with an emphasis on reliability and stability.

3.3 DESCRIBING CULTURE: HALL

Edward T. Hall was a respected anthropologist who applied his field to the understanding of cultures and intercultural communications. Hall is best noted for three principal categories that analyze and interpret how communications and interactions between cultures differ: **context, space, and time**.

Context: High-Context versus Low-Context Cultures

High and low context refers to how a message is communicated. In high-context cultures, such as those found in Latin America, Asia, and Africa, the physical context of the message carries a great deal of importance. People tend to be more indirect and to expect the person they are communicating with to decode the implicit part of their message. While the person sending the message takes painstaking care in crafting the message, the person receiving the message is expected to read it within context. The message may lack the verbal directness you would expect in a low-context culture. In high-context cultures, body language is as important and sometimes more important than the actual words spoken.

In contrast, in low-context cultures such as the United States and most Northern European countries, people tend to be explicit and direct in their communications. Satisfying individual needs is important. You're probably familiar with some well-known low-context mottos: "Say what you mean" and "Don't beat around the bush." The guiding principle is to minimize the margins of misunderstanding or doubt. Low-context communication aspires to get straight to the point.

Communication between people from high-context and low-context cultures can be confusing. In business interactions, people from low-context cultures tend to listen only to the words spoken; they tend not to be cognizant of body language. As a result, people often miss important clues that could tell them more about the specific issue.

	Low-Context	High-Context
Communication		
Type of Communication	Explicit Communication	Implicit Communication
Communication Focus	Focus on Verbal Communication	Focus on Nonverbal Communication
Context of Message	Less Meaningful	Very Meaningful
Politeness	Not Important	Very Important
Approach to People	Direct and Confrontational	Indirect and Polite
Cultural Orientation		
Emotions	No Room for Emotions	Emotions Have Importance
Approach to Time	Monochromatic	Polychromatic
Time Orientation	Present-Future	Past
In/Out-Groups	Flexible and Transient Grouping patterns	Strong Distinctions Between In and Out-Groups
Identity	Based on Individual	Based on Social System
Values	Independence and Freedom	Tradition and Social Rules/Norms
Business		
Work Style	Individualistic	Team-Oriented
Work Approach	Task-Oriented	Relationship-Oriented
Business Approach	Competitive	Cooperative
Learning	Knowledge is Transferable	Knowledge is Situational
Sales Orientation	Hard Sell	Soft Sell
View of Change	Change over Tradition	Tradition over Change

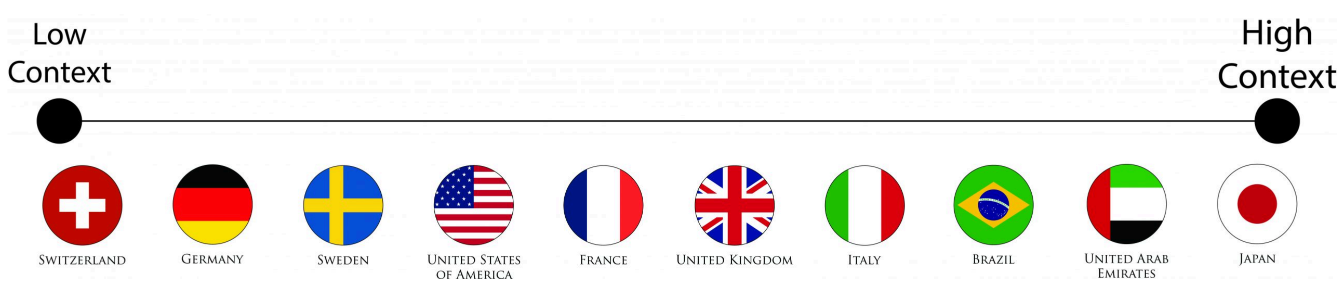

Fig 3.3 Low to High Context: Switzerland, Germany, Sweden, U.S.A, France, U.K., Italy, Brazil, United Arab Emirates, Japan.
"High and Low Context" by JasonSWrench, CC BY-NC-SA 2.0

Space

Space refers to the study of physical space and people. Hall called this the study of proxemics, which focuses on space and distance between people as they interact. **Space** refers to everything from how close people stand to one another to how people might mark their territory or boundaries in the workplace and in other settings. Stand too close to someone from the United States, which prefers a "safe" physical distance, and you are apt to make them uncomfortable. How close is too close depends on where you are from. Whether consciously or unconsciously, we all establish a comfort zone when interacting with others. Standing distances shrink and expand across cultures. Latins, Spaniards, and Filipinos (whose culture has been influenced by three centuries of Spanish colonization) stand rather close even in business encounters. In cultures that have a low need for territory, people not only tend to stand closer together but also are more willing to share their space—whether it be a workplace, an office, a seat on a train, or even ownership of a business project.

Time: Polychronic versus Monochronic Cultures

Hall identified that time is another important concept greatly influenced by culture. In polychronic cultures—*polychronic* literally means "many times"—people can do several things at the same time. In monochronic cultures or "one-time" cultures, people tend to do one task at a time.

This isn't to suggest that people in polychronic cultures are better at multitasking. Rather, people in monochronic cultures, such as Northern Europe and North America, tend to schedule one event at a time. For them, an appointment that starts at 8 a.m. is an appointment that starts at 8 a.m.—or 8:05 at the latest. People are expected to arrive on time, whether for a board meeting or a family picnic. Time is a means of imposing order. Often the meeting has a firm end time as well, and even if the agenda is not finished, it's not unusual to end the meeting and finish the agenda at another scheduled meeting.

In polychronic cultures, by contrast, time is nice, but people and relationships matter more. Finishing a task may also matter more. If you've ever been to Latin America, the Mediterranean, or the Middle East, you know all about living with relaxed timetables. People might attend to three things at once and think nothing of it. Or they may cluster informally, rather than arrange themselves in a queue. In polychronic cultures, it's not considered an insult to walk into a meeting or a party well past the appointed hour.

In polychronic cultures, people regard work as part of a larger interaction with a community. If an agenda is not complete, people in polychronic cultures are less likely to simply end the meeting and are more likely to continue to finish the business at hand.

Those who prefer monochronic order may find polychronic order frustrating and hard to manage effectively. Those raised with a polychronic sensibility, on the other hand, might resent the "tyranny of the clock" and prefer to be focused on completing the tasks at hand.

3.4 NONVERBAL COMMUNICATION

Nonverbal communication is the process of conveying a message without the use of words. It can include gestures and facial expressions, tone of voice, timing, posture and where you stand as you communicate. It can help or hinder the clear understanding of your message, but it doesn't reveal (and can even mask) what you are really thinking. Nonverbal communication is far from simple, and its complexity makes your study and your understanding a worthy but challenging goal.

Nonverbal communication involves the entire body, the space it occupies and dominates, the time it interacts, and not only what is not said, but how it is not said. Confused? Try to focus on just one element of nonverbal communication and it will soon get lost among all the other stimuli. Consider one element, facial expressions. What do they mean without the extra context of chin position, or eyebrows to flag interest or signal a threat? Nonverbal action flows almost seamlessly from one movement to the next, making it a challenge to interpret one element, or even a series of elements. How well can you correctly identify the feelings behind facial expressions?

Below are eight types of nonverbal communication:

1. Space
2. Time
3. Physical characteristics
4. Body movements
5. Touch
6. Paralanguage
7. Artifacts
8. Environment

Space

When we discuss space in a nonverbal context, we mean the space between objects and people. Space is often associated with social rank and is an important part of business communication. Who gets the corner office? Why is the head of the table important and who gets to sit there?

People from diverse cultures may have different normative space expectations. If you are from a large urban area, having people stand close to you may be normal. If you are from a rural area or a culture where people expect more space, someone may be standing "too close" for comfort and not know it.

Territory is related to control. As a way of establishing control over your own room, maybe you painted it your favourite colour, or put up posters that represent your interests or things you consider unique about yourself. Families or households often mark their space by putting up fences or walls around their houses. This sense of a right to control your space is implicit in territory. Territory means the space you claim as your own, are responsible for, or are willing to defend.

Among most humans there is a basic need for personal space, but the normative expectations for space vary greatly by culture. You may perceive that in your home people sleep one to each bed, but in many cultures people sleep two or more to a bed and it is considered normal. If you were to share that bed, you might feel uncomfortable, while someone raised with group sleeping norms might feel uncomfortable sleeping alone. From where you stand in an aerobics class in relation to others, to where you place your book bag in class, your personal expectations of space are often at variance with others.

Watch the following video: Personal Space – How Close is Too Close by CBS with special correspondent Taryn Winter Brill about personal space [2:55].

Video: Personal Space – How Close is Too Close by CBS with special correspondent Taryn Winter Brill about personal space [2:55] is licensed under the Standard YouTube License. Captions and transcripts are available on YouTube.

In the same way that there are cultural contexts and expectations for nonverbal behaviour, public speaking also happens in contexts. In North America, eye contact with the audience is expected. Big movements and gestures are not generally expected and can be distracting. The speaker occupies a space on the "stage," even if it's in front of the class. When you occupy that space, the audience will expect to behave in certain ways. If you talk to the screen behind you while displaying a PowerPoint presentation, the audience may perceive that you are not paying attention to them. Speakers are expected to pay attention to, and interact with, the audience, even if in the feedback is primarily nonverbal. Your movements should coordinate with the tone, rhythm, and content of your speech. Pacing back and forth, keeping your hands in your pockets, or crossing your arms may communicate nervousness, or even defensiveness, and detract from your message.

Time

Do you know what time it is? How aware you are of time varies by culture and normative expectations of adherence (or ignorance) of time. Some people, and the communities and cultures they represent, are very time-oriented.

When you give a presentation, does your audience have to wait for you? Time is a relevant factor of the communication process in your speech. The best way to show your audience respect is to honour the time expectation associated with your speech. Always try to stop speaking before the audience stops listening; if the audience perceives that you have "gone over time," they will be less willing to listen. This in turn will have a negative impact on your ability to communicate your message.

Physical Characteristics

You didn't choose your genes, your eye colour, the natural colour of your hair, or your height, but people spend millions every year trying to change their physical characteristics. You can get coloured contacts; dye your hair; and if you are shorter than you'd like to be, buy shoes to raise your stature a couple of inches. However, no matter how much you stoop to appear shorter, you won't change your height until time and age gradually makes itself apparent. If you are tall, you might find the correct shoe size, pant length, or even the length of mattress a challenge, but there are rewards.

Regardless of your eye or hair colour, or even how tall you are, being comfortable with yourself is an important part of your presentation. Act naturally and consider aspects of your presentation you can control in order to maximize a positive image for the audience.

Body Movements

The study of body movements, called kinesics, is key to understanding nonverbal communication.

Body movements can complement the verbal message by reinforcing the main idea. For example, you may be providing an orientation presentation to a customer about a software program. As you say, "Click on this tab," you may also initiate that action. Your verbal and nonverbal messages reinforce each other. You can also reinforce the message by repeating it. If you first say, "Click on the tab," and then motion with your hand to the right, indicating that the customer should move the cursor arrow with the mouse to the tab, your repetition can help the listener understand the message.

In addition to repeating your message, body movements can also regulate conversations. Nodding your head to indicate that you are listening may encourage the customer to continue asking questions. Holding your hand up, palm out, may signal them to stop and provide a pause where you can start to answer.

Body movements also substitute or replace verbal messages. For example, if the customer makes a face of frustration while trying to use the software program, they may need assistance. If they push away from the computer and separate themselves physically from interacting with it, they may be extremely frustrated. Learning to gauge feelings and their intensity as expressed by customers takes time and patience, and your attention to them will improve your ability to facilitate positive interactions.

OK or Not OK?

Various motions and postures can mean altogether divergent things in different cultures. Hand gestures are a classic example. The American sign for OK means “zero” in Tunisia and southern France, which far from signalling approval, is considered a threat. The same gesture, by the way, delivers an obscenity in Brazil, Germany, Greece, and Russia. If you want to tell your British colleagues that victory on a new deal is close at hand by making the V sign with your fingers, be sure your palm is facing outward; otherwise you’ll be telling them where to stick it, and it’s unlikely to win you any new friends.

Eye contact is also an important bit of unspoken vocabulary. People in Western cultures are taught to look into the eyes of their listeners. Likewise, it’s a way the listener reciprocates interest. In contrast, in the East, looking into someone’s eyes may come off as disrespectful, since focusing directly on someone who is senior to you implies disrespect. So when you’re interacting with people from other cultures, be careful not to assume that a lack of eye contact means anything negative. There may be a cultural basis to their behaviour.

Touch

Before giving your presentation, you may interact with people by shaking hands and making casual conversation. This interaction can help establish trust before you take the stage. Once on stage, most people do not touch audience members physically, but you can interact with audience members through visual aids, note cards, and other objects.

Watch the following video: The Top 10 Bad Business Handshakes by BusinessGovAu [3:00]

Video: The Top 10 Bad Business Handshakes by BusinessGovAu [3:00] is licensed under the Standard YouTube License. Captions and transcripts are available on YouTube.

Kiss, Shake, Hug, or Bow

Additionally, touching is a tacit means of communication. In some cultures, shaking hands when greeting someone is a must. Where folks are big on contact, grown men might embrace each other in a giant bear hug, such as in Mexico or Russia.

Japan, by contrast, has traditionally favoured bowing, thus ensuring a hands-off approach. When men and women interact for business, this interaction can be further complicated. If you're female interacting with a male, a kiss on the cheek may work in Latin America, but in an Arab country, you may not even get a handshake. It can be hard not to take it personally, but you shouldn't. These interactions reflect centuries-old traditional cultural norms that will take time to evolve.

Paralanguage

Paralanguage is the exception to the definition of nonverbal communication. You may recall that nonverbal communication was defined as "not involving words" but paralanguage is a unique form of nonverbal communication that exists when we are speaking, using words. Paralanguage involves tone and nonverbal aspects of speech that influence meaning, including how loudly or softly you are speaking, intensity, pausing, and even silence.

Perhaps you've also heard of a pregnant pause, a silence between verbal messages that is full of meaning. The meaning itself may be hard to understand or decipher, but it is there nonetheless. For example, your coworker Jan comes back from a sales meeting speechless. You may ask if the meeting went all right. "Well, ahh…" may be the only response you get. The pause speaks volumes. Something happened, though you may not know what.

Silence or vocal pauses can communicate hesitation, indicate the need to gather thought, or serve as a sign of respect. Sometimes we learn just as much, or even more, from what a person does not say as what they do say.

Watch the following video: Paralanguage – It's Not What You Say, It's How You Say It by Janet Harliee [1:18].

Video: Paralanguage – It's Not What You Say, It's How You Say It by Janet Harliee [1:18] is licensed under the Standard YouTube License. Captions and transcripts are available on YouTube.

Artifacts

Do you cover your tattoos when you are at work? Do you know someone who does? Or perhaps you know someone who has a tattoo and does not need to cover it up on their job? Expectations vary a great deal, and body art or tattoos may still be controversial in the workplace. In your line of work, a tattoo might be an important visual aid, or it might detract from your effectiveness as a business communicator. Body piercings may express individuality, but you need to consider how they will be interpreted by employers and customers.

Artifacts are forms of decorative ornamentation that are chosen to represent self-concept. They can include rings and tattoos, but may also include brand names and logos. From clothes to cars, watches, briefcases, purses, and even eyeglasses, what we choose to surround ourselves with communicates something about our sense of self. Artifacts may project gender, role or position, class or status, personality, and group membership or affiliation. Paying attention to a customer's artifacts can give you a sense of the self they want to communicate, and may allow you to more accurately adapt your message to meet their needs.

Watch this video: Inked @ UTSC by the University of Toronto Scarborough which Adon Irani shares the story behind his tattoos [1:24].

Video: Inked @ UTSC by the University of Toronto Scarborough [1:24] is licensed under the Standard YouTube License. Captions and transcripts are available on YouTube.

Environment

Environment involves the physical and psychological aspects of the communication context. More than the tables and chairs in an office, environment is an important part of the dynamic communication process. The perception of one's environment influences one's reaction to it. For example, Google is famous for its work environment, with spaces created for physical activity and even in-house food service around the clock. The expense is no doubt considerable, but Google's actions speak volumes. In Google's view, the results produced in the environment, designed to facilitate creativity, interaction, and collaboration, are worth the effort.

To summarize, nonverbal communication can be categorized into eight types: space, time, physical characteristics, body movements, touch, paralanguage, artifacts, and environment.

3.5 THE SOCIAL AND CULTURAL ENVIRONMENT

The **cultural environment** consists of the influence of religious, family, educational, and social systems in the marketing system. Marketers who intend to market their products overseas may be very sensitive to foreign cultures. While the differences between our cultural background in Canada and those of foreign nations may seem small, marketers who ignore these differences risk failure in implementing marketing programs. Failure to consider cultural differences is one of the primary reasons for marketing failures overseas.

This task is not as easy as it sounds as various features of a culture can create an illusion of similarity. Even a common language does not guarantee similarity of interpretation. For example, in Canada and the U.S. we purchase "cans" of various grocery products, but the British purchase "tins".

A number of cultural differences can cause marketers problems in attempting to market their products overseas. These include: (a) language, (b) colour, (c) customs and taboos, (d) values, (e) aesthetics, (f) time, (g) business norms, (h) religion, and (i) social structures. Each is discussed in the following sections.

Student Perspective: Mexico & the U.S.

I travel out of the country to Mexico almost every year. I can see the immense cultural differences between Mexico and the United States, from the language to colors, to the values, religious beliefs, and business norms. As soon as I step out of the plane in Mexico, I feel like I am in a different world. In terms of the language, the primary is obviously Spanish; however, in the past few years, I have noticed signs in the airport with translations to English and Chinese. In terms of values, they seem to focus more on survival. For example, marketing food, shelter products, and clothing. Their religious beliefs are centred around Catholicism.

Photo by Marisol Benitez, Unsplash License

Elizabeth Garcia

Class of 2020

Language

The importance of language differences cannot be overemphasized, as there are almost 3,000 languages in the world. Language differences cause many problems for marketers in designing advertising campaigns and product labels. Language problems become even more serious once the people of a country speak several languages. For example, in Canada, labels must be in both English and French. In India, there are over 200 different dialects, and a similar situation exists in China.

Colours

Colours also have different meanings in different cultures. For example, in Egypt, the country's national colour of green is considered unacceptable for packaging, because religious leaders once wore it. In Japan, black and white are colours of mourning and should not be used on a product's package. Similarly, purple is unacceptable in Hispanic nations because it is associated with death.

Consider how the following examples could be used in development of international marketing programs:

- In Russia, it is acceptable for men to greet each other with a kiss, but this custom is not acceptable in the US.
- Germans prefer their salad dressing in a tube, while Americans prefer it in a bottle.
- In France, wine is served with most meals, but in America, milk, tea, water, and soft drinks are popular.

McDonald's Corporation has opened 20 restaurants in India. Since 80 percent of Indians are Hindu, McDonald's will use a non-beef meat substitute for its traditional hamburger. The likely beef substitute will be lamb, a very popular meat in India. In anticipation of its restaurant openings, McDonald's conducted extensive market research, site selection studies, and developed a relationship with India's largest chicken supplier. McDonald's has opted to market its product in India, largely because India's population of more than 900 million represents one-sixth of the world's population.

Values

An individual's values arise from his/her moral or religious beliefs and are learned through experiences. For example, in America, we place a very high value on material well-being and are much more likely to purchase status symbols than people in India. Similarly, in India, the Hindu religion forbids the consumption of beef, and fast-food restaurants such as McDonald's and Burger King would encounter tremendous difficulties without product modification. Americans spend large amounts of money on soap, deodorant, and mouthwash because of the value placed on personal cleanliness. In Italy, salespeople call on women only if their husbands are at home.

Aesthetics

The term *aesthetics* is used to refer to the concepts of beauty and good taste. The phrase, "Beauty is in the eye of the beholder" is a very appropriate description for the differences in aesthetics that exist between cultures.

For example, Americans believe that suntans are attractive, youthful, and healthy. However, the Japanese do not.

Time

Americans seem to be fanatical about time when compared to other cultures. Punctuality and deadlines are routine business practices in the US. However, salespeople who set definite appointments for sales calls in the Middle East and Latin America will have a lot of time on their hands, as business people from both of these cultures are far less bound by time constraints. To many of these cultures, setting a deadline such as "I have to know next week" is considered pushy and rude.

Student Perspective: Daily Schedule

Photo from PxHere, CC0 1.0

While travelling this past summer I was able to spend time in Italy. It took me a while to get used to having to plan around their typical schedule. During lunch they take what is called a riposo, or an extended lunch break where they go home to eat and spend time with their families and relax. This is in direct contrast to the culture in America, where I have on many occasions worked through lunch breaks. In the world of business, this would be something people would need to be sensitive to so that there would be no issues with trying to schedule meetings or even work lunches.

Brittney Harvey

Class of 2020

Business Norms

The norms of conducting business also vary from one country to the next. Here are several examples of foreign business behaviour that differ from US business behaviour:

- In France, wholesalers do not like to promote products. They are mainly interested in supplying retailers with the products they need.
- In Russia, plans of any kind must be approved by a seemingly endless string of committees. As a result, business negotiations may take years.
- South Americans like to talk business "nose to nose". This desire for close physical proximity causes American businesspeople to back away from the constantly forward-moving South Americans.
- In Japan, business people have mastered the tactic of silence in negotiations. Americans are not prepared for this, and they panic because they think something has gone wrong. The result is that Americans become impatient, push for a closure, and often make business concessions they later regret.

These norms are reflected in the difficulty of introducing the Web into Europe.

Religious Beliefs

A person's religious beliefs can affect shopping patterns and products purchased in addition to his/her values, as discussed earlier. In the United States and other Christian nations, Christmastime is a major sales period. But for other religions, religious holidays do not serve as popular times for purchasing products. Women do not participate in household buying decisions in countries in which religion serves as opposition to women's rights movements.

Every culture has a social structure, but some seem less widely defined than others. That is, it is more difficult to move upward in a social structure that is rigid. For example, in the US, the two-wage earner family has led to the development of a more affluent set of consumers. But in other cultures, it is considered unacceptable for women to work outside the home.

3.6 IMPACTS ON GLOBAL MARKETING

While the same basic domestic marketing principles apply to global marketing, there are additional layers of complexity for marketers to consider when working across markets in different countries and world regions. Much of this complexity centres the need to develop a keen understanding of the consumer and the target market—a task essential for effective marketing, whether global or domestic. But in the global environment, there are additional questions to ask and issues to consider in order to fully appreciate the consumer and the marketing opportunities in a target market.

Additional complexity resides in the business environment created by government, regulatory bodies, and other societal institutions that shape the behaviours of individuals and institutions. This business environment is somewhat unique to every country and target market. Understanding these dynamics can help marketers work more effectively to achieve their organizations' business objectives.

Cross-cultural marketing is defined as the process of marketing among consumers whose culture differs from that of the marketer's own culture; such as language, religion, social norms and values, education and living style (Vaddadi & Thandava, 2019).

If Marketers want to succeed in a foreign market, they must design a marketing mix that meets the cultural expectations of that new market's consumers. It involves recognizing that people all over the world have different needs and expectations. For a multicultural marketing strategy to succeed, cultural differences must be identified, understood and respected.

The following aspects are considered vital for a company to succeed in doing business globally:

- culture impacts on marketing (international versus domestic)
- cross-cultural dimensions of marketing research
- cross-cultural aspects of the marketing mix (products, price, promotion, and place)
- cross-cultural marketing education and professional training
- and cross-cultural practice in electronic marketing (Vaddadi & Thandava, 2019).

To overcome cross-cultural differences and the possibility of cross-cultural marketing mistakes, companies need to study and understand the foreign culture they are entering. There needs to be a high level of appreciation and respect for the consumers' religion and culture. They also need to understand and study the language differences and how this can affect translated products or slogans.

Student Perspective: McDonald’s

“Glocalization in France: McDonalds and their Croque McDo” by Richard Allaway, CC BY 2.0

McDonald’s has done a great job introducing its chain around the world and moving into numerous markets and cultures. One location that I think is a great example of cross-cultural marketing is McDonald’s in France. The French have a very different culture than the United States. They live their life at a much slower pace and their meals are more about socializing and enjoying the time with people rather than eating and getting out. McDonald’s has created some new menu items for their French locations such as an Alpine burger and the McBaguette. McDonald’s also designed the French chains so that they are more spacious and decorated tastefully so that it does encourage the French to sit down and enjoy their meal at their own pace. There are also separate McCafe locations around France that are decorated with big comfortable chairs and couches to encourage socialization. In addition, the coffee is served in real coffee mugs and not it to-go cups.

Before entering the country, McDonald’s surely did their research because they not only added French-like items to the menu, but they also incorporated a French-like atmosphere. I think this is a very good example of cross-cultural marketing because these locations really encourage a dine-in and more relaxed experience compared to the fast pace take-out that Americans are used to. Many French people have actually commented on the fact that McDonald’s in France does not feel like a fast-food restaurant at all. With this information, I think it is easy to say that their research and cross-cultural marketing plan for France has been a success.

Courtney Kent

Class of 2020

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3.8 KEY TERMS

Key Terms

Cross-cultural marketing is defined as the process of marketing among consumers whose culture differs from that of the marketer's own culture; such as language, religion, social norms and values, education and living style. 3.6

Culture: In the broadest sense, refers to how and why we think and function. It encompasses all sorts of things—how we eat, play, dress, work, think, interact, and communicate. Everything we do, in essence, has been shaped by the cultures in which we are raised. Similarly, a person in another country is also shaped by his or her cultural influences. These cultural influences impact how we think and communicate. 3.0

Cultural Environment: Consists of the influence of religious, family, educational, and social systems in the marketing system. 3.5

High and Low Context: Refers to how a message is communicated. In high-context cultures, such as those found in Latin America, Asia, and Africa, the physical context of the message carries a great deal of importance. 3.3

Individualism: Is just what it sounds like. It refers to people's tendency to take care of themselves and their immediate circle of family and friends, perhaps at the expense of the overall society. 3.2

Long-Term Orientation: Which refers to whether a culture has a long-term or short-term orientation. 3.2

Masculinity: This may sound like an odd way to define a culture. When we talk about masculine or feminine cultures, we're not talking about diversity issues. It's about how society views traits that are considered masculine or feminine. 3.2

National Culture: As it sounds—defined by its geographic and political boundaries and includes even regional cultures within a nation as well as among several neighbouring countries. What is important about nations is that boundaries have changed throughout history. 3.1

Nonverbal Communication: Is the process of conveying a message without the use of words. It can include gestures and facial expressions, tone of voice, timing, posture and where you stand as you communicate.3.4

Organizations: Every organization has its own workplace culture, referred to as the organizational culture. This defines simple aspects such as how people dress (casual or formal), how they perceive and value employees, or how they make decisions (as a group or by the manager alone). 3.1

Personality: As a person's identity and unique physical, mental, emotional, and social characteristics. 3.1

Power Distance: Refers to how openly a society or culture accepts or does not accept differences between people, as in hierarchies in the workplace, in politics, and so on. 3.2

Space: Refers to everything from how close people stand to one another to how people might mark their territory or boundaries in the workplace and in other settings. 3.3

Subcultures: Many groups are defined by ethnicity, gender, generation, religion, or other characteristics with cultures that are unique to them. 3.1

Uncertainty Avoidance (UA): This refers to how much uncertainty a society or culture is willing to accept. It can also be considered an indication of the risk propensity of people from a specific culture. People who have high uncertainty avoidance generally prefer to steer clear of conflict and competition. 3.2

CHAPTER 4: GLOBAL MARKET PLANNING

Chapter Outline

4.0 INTRODUCTION

Learning Objectives

After reading this section, students should be able to:

1. Identify the key factors in selecting global markets.
2. Describe the components of the CAGE analysis.
3. Explain the three strategies for handling institutional voids.
4. Conduct a Country Attractiveness Analysis to select countries to enter.
5. Outline the ways in which markets are segmented.
6. List the demographic variables to consider for global marketing.
7. Explain the principles behind target market selection.

A wide variety of internationalization moves are available after choosing to expand. Moreover, some flatteners make global moves easier, while some make them more difficult. Indeed, even importing and outsourcing can be considered stealth, or at least early, steps in internationalization, because they involve doing business across borders. As companies look for growth in new areas of the world, they typically prioritize which countries to enter. Because many markets look appealing due to their market size or low-cost production, it is important for firms to prioritize which countries to enter first and to evaluate each country's relative merits. For example, some markets may be smaller in size, but their strategic complexity is lower, which may make them easier to enter and easier from an operations point of view. Sometimes there are even substantial regional differences within a given country, so careful investigation, research, and planning are important to do before entry.

Evaluating whether to enter a new market is like peeling an onion—there are many layers. For example, when evaluating whether to enter China, the advantage most people see immediately is its large market size. Further analysis shows that the majority of people in that market can't afford US products, however. But even deeper analysis shows that while many Chinese are poor, the number of people who can afford consumer products is increasing (Kleiner, 2011).

Through global market segmentation, a company can identify and group customers or countries according to common needs and wants. Demographic segmentation can be based on country income and population, age, ethnic heritage, or other variables. Psychographic segmentation groups people according to attitudes, interests, opinions, and lifestyles. Behavioural segmentation utilizes user status and usage rate as segmentation variables. Benefits segmentation is based on the benefit buyers seek. Global teens and global elites are two examples of global market segments.

After marketers have identified segments, the next step is targeting: The identified groups are evaluated and compared, and one or more segments with the greatest potential is selected from them. The groups are evaluated on the basis of several factors, including segment size and growth potential, competition, and compatibility and feasibility. Target market assessment also entails a thorough understanding of the product-marketing question and determining marketing model drivers and enabling conditions in the countries under study. The timing of market entry should take into account whether a first-mover advantage is likely to be gained. After evaluating the identified segments, marketers must decide on an appropriate targeting strategy. The three basic categories of global target marketing strategies are standardized global marketing, niche marketing, and differentiated multi-segment marketing.

Positioning a product or brand to differentiate it in the minds of target customers can be accomplished in various ways: positioning by attribute or benefit, positioning by quality/price, positioning by use or user, and positioning by competition. In global marketing global consumer culture positioning (GCCP), foreign consumer culture positioning (FCCP), and local consumer culture positioning (LCCP) are additional strategic options.

4.1 MEASURING MARKET ATTRACTIVENESS

Four key factors in selecting global markets are:

1. *market's size and growth rate*
2. particular country or region's *institutional contexts*
3. region's *competitive environment*
4. market's *cultural*, *administrative*, *geographic*, and *economic distance* from other markets the company serves.

Market Size and Growth Rate

There is no shortage of country information for making market portfolio decisions. A wealth of country-level economic and demographic data are available from a variety of sources including governments, multinational organizations such as the United Nations or the World Bank, and consulting firms specializing in economic intelligence or risk assessment. However, while valuable from an overall investment perspective, such data often reveal little about the prospects for selling products or services in foreign markets to local partners and end users or about the challenges associated with overcoming other elements of distance. Yet many companies still use this information as their primary guide to market assessment simply because country market statistics are readily available, whereas real product market information is often difficult and costly to obtain.

What is more, a country or regional approach to market selection may not always be the best. Even though Theodore Levitt's vision of a global market for uniform products and services has not come to pass, and global strategies exclusively focused on the "economics of simplicity" and the selling of standardized products all over the world rarely pay off, research increasingly supports an alternative "global segmentation" approach to the issue of market selection, especially for branded products. In particular, surveys show that a growing number of consumers, especially in emerging markets, base their consumption decisions on attributes beyond direct product benefits, such as their perception of the global brands behind the offerings.

Specifically, research by John Quelch (2003) and others suggests that consumers increasingly evaluate global brands in "cultural" terms and factor three global brand attributes into their purchase decisions: (a) what a global brand signals about quality, (b) what a brand symbolizes in terms of cultural ideals, and (c) what a brand signals about a company's commitment to corporate social responsibility. This creates opportunities for global companies with the right values and the savvy to exploit them to define and develop target markets across geographical boundaries and create strategies for "global segments" of consumers. Specifically, consumers who perceive global brands in the same way appear to fall into one of four groups:

1. *Global citizens* rely on the global success of a company as a signal of quality and innovation. At the same time, they worry whether a company behaves responsibly on issues like consumer health, the environment, and worker rights.
2. *Global dreamers* are less discerning about, but more ardent in their admiration of, transnational companies. They view global brands as quality products and readily buy into the myths they portray. They also are less concerned with companies' social responsibilities than global citizens.
3. *Antiglobals* are skeptical that global companies deliver higher-quality goods. They particularly dislike brands that preach American values and often do not trust global companies to behave responsibly. Given a choice, they prefer to avoid doing business with global firms.
4. *Global agnostics* do not base purchase decisions on a brand's global attributes. Instead, they judge a global product by the same criteria they use for local brands (Holt et al., 2004).

Companies that use a "global segment" approach to market selection, such as Coca-Cola, Sony, or Microsoft, to name a few, therefore must manage two dimensions for their brands. They must strive for superiority on basics like the brand's price, performance, features, and imagery, and, at the same time, they must learn to manage brands' global characteristics, which often separate winners from losers. A good example is provided by Samsung, the South Korean electronics maker. In the late 1990s, Samsung launched a global advertising campaign that showed the South Korean giant excelling, time after time, in engineering, design, and aesthetics. By doing so, Samsung convinced consumers that it successfully competed directly with technology leaders across the world, such as Nokia and Sony. As a result, Samsung was able to change the perception that it was a down-market brand, and it became known as a global provider of leading-edge technologies. This brand strategy, in turn, allowed Samsung to use a global segmentation approach to making market selection and entry decisions.

Institutional Contexts

Khanna and others (2005) developed a five-dimensional framework to map a particular country or region's institutional contexts. Specifically, they suggest careful analysis of a country's:

- *political and social systems*,
- *openness*,
- *product markets*,

- *labour markets*, and
- *capital markets*.

Political System

A country's political system affects its product, labour, and capital markets. In socialist societies like China, for instance, workers cannot form independent trade unions in the labour market, which affects wage levels. A country's social environment is also important. In South Africa, for example, the government's support for the transfer of assets to the historically disenfranchised native African community has affected the development of the capital market.

Openness

The more open a country's economy, the more likely it is that global intermediaries can freely operate there, which helps multinationals function more effectively. From a strategic perspective, however, openness can be a double-edged sword: a government that allows local companies to access the global capital market neutralizes one of the key advantages of foreign companies.

Product markets

Even though developing countries have opened up their markets and grown rapidly during the past decade, multinational companies struggle to get reliable information about consumers. Market research and advertising are often less sophisticated and, because there are no well-developed consumer courts and advocacy groups in these countries, people can feel they are at the mercy of big companies.

Labour Markets

Recruiting local managers and other skilled workers in developing countries can be difficult. The quality of local credentials can be hard to verify, there are relatively few search firms and recruiting agencies, and the high-quality firms that do exist focus on top-level searches, so companies scramble to identify middle-level managers, engineers, or floor supervisors.

Capital Markets

Capital and financial markets in developing countries often lack sophistication. Reliable intermediaries like credit-rating agencies, investment analysts, merchant bankers, or venture capital firms may not exist, and multinationals cannot count on raising debt or equity capital locally to finance their operations.

Emerging economies present unique challenges. Capital markets are often relatively inefficient and dependable sources of information, scarce while the cost of capital is high and venture capital is virtually nonexistent. Because of a lack of high-quality educational institutions, labour markets may lack well-trained people requiring companies to fill the void. Because of an underdeveloped communications infrastructure, building a brand name can be difficult just when good brands are highly valued because of lower product quality of the alternatives. Finally, nurturing strong relationships with government officials often is necessary to succeed. Even then, contracts may not be well enforced by the legal system.

Competitive Environment

The number, size, and quality of competitive firms in a particular target market compose a second set of factors that affect a company's ability to successfully enter and compete profitably. While country-level economic and demographic data are widely available for most regions of the world, competitive data are much harder to come by, especially when the principal players are subsidiaries of multinational corporations. As a consequence, competitive analysis in foreign countries, especially in emerging markets, is difficult and costly to perform and its findings do not always provide the level of insight needed to make good decisions. Nevertheless, a comprehensive competitive analysis provides a useful framework for developing strategies for growth and for analyzing current and future primary competitors and their strengths and weaknesses.

Case: Which BRIC Countries? A Key Challenge for Carmakers

Today, automobile manufacturers face a critical challenge: deciding which BRIC countries (Brazil, Russia, India, and China) to bet on. In each, as per capita income rises, so will per capita car ownership—not in a straight line but in classic "S-curve" fashion. Rates of vehicle ownership stay low during the first phases of economic growth, but as the GDP or purchasing power of a country reaches a level of sustained broad prosperity, and as

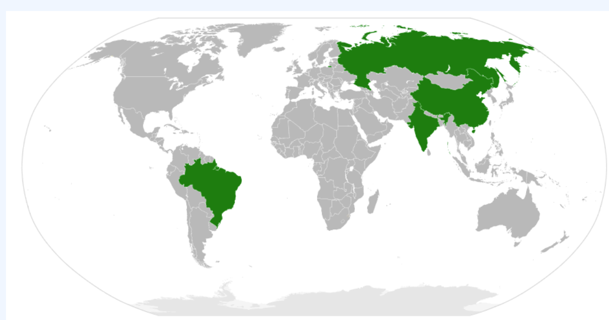

Fig 4.1 "BRIC" by Felipe Menegaz, CC BY-SA 3.0

urbanization reshapes the work patterns of a country, vehicle sales take off. But that is about where the similarities end. Each of the four BRIC nations has a completely different set of market and industry dynamics that make decision choices about which countries to target, including making difficult decisions about which markets to avoid, extremely difficult.

For one thing, vehicle manufacturing is a high-profile industry that generates enormous revenue, employs millions of people, and is often a proxy for a nation's manufacturing prowess and economic influence. Governments are extensively involved in regulating or influencing virtually every aspect of the product and the way the industry operates—including setting emissions and safety standards, licensing distributors, and setting tariffs and rules about how much manufacturing must take place locally. This reality makes the job of understanding each market and appreciating the differences more vital. For example, a summary overview of the BRIC nations reveals the differences among these markets and the operating complexities in all of them.

Brazil, with Russia, is one of the smaller BRIC countries, with 188 million people (by comparison, China and India each have more than 1 billion, Russia has 142 million). Yet car usage is already relatively high: 104 cars in use per 1,000 people, nearly 10 times the rate of usage in India, according to the *Economist* Intelligence Unit. Because of this, growth projections for Brazil are relatively low—more in line with developed nations than with the other BRIC countries. Projections made by the industry research firm Global Insight show that sales will grow just 2% until 2013, underperforming even the U.S. market's projected growth rate.

On the plus side, Brazil is socioeconomically stable, with increasing wealth and a maturing finance system that is helping to propel growth among rural, first-time buyers who prefer compact cars. Few domestic brands exist, as the market is dominated by GM, Ford, Fiat, and Volkswagen. Prompted by generous government incentives, high import taxes, and exchange rate risks, foreign automakers have invested significantly in Brazil, which has thus become an unrivaled production hub for the rest of South America. Brazilian consumers live in a country with large rural areas and very rough terrain; they demand fairly large, SUV-like cars, made with economical small engines and flex-fuel power trains friendly to the country's biofuel industry. When a Latin American family buys its first automobile, chances are it was made in Brazil.

Given Russia's proximity to Europe, consumer preferences there are more akin to those of the developed markets than to those of China or India, and expensive, status-enhancing European models remain popular, although European safety features, interior components, and electronics are often stripped out to reduce costs. For vehicle manufacturers, the attractions of the Russian market include an absence of both local partnership requirements and significant local competitors. But there is high political risk. So far, the Russian government has permitted foreign carmakers to operate relatively freely, but the Kremlin's history of meddling in private enterprise and undercutting private ownership worries some executives. These concerns were heightened in November 2008, when Russia implemented tariffs against car imports in hopes of avoiding layoffs that might spark labour unrest among the country's 1.5 million car industry workers.

India has 1.1 billion people, but its level of car adoption is still low, with only 11 cars in use per 1,000 people. The upside is higher potential growth: among the BRIC countries, India is expected to have the fastest-growing auto sales, almost 15% per year until 2013, according to Global Insight. Sales of subcompact cars are strong, even during the global recession. The popularity of these small cars combines with India's energy shortages and the country's chronic pollution to provide foreign carmakers with an ideal opportunity to further develop electric power-train technologies there.

Until the early 1990s, foreign automobile manufacturers were mostly shut out of India. That has changed radically. Today, foreign automakers are welcomed and the government promotes foreign ownership and local manufacturing with tax breaks and strong intellectual property protection. And because foreign companies were shut out for a long period of time, India has capable manufacturers and suppliers for foreign vehicle manufacturers to partner with. Local competition is strong but is thus far concentrated among three players: Maruti Suzuki India, Ltd., Tata, and the Hyundai Corporation, which is well established in India.

China is almost as large as the other three combined in total auto sales and production. Its overall auto usage is just 18 cars per 1,000 households, but annual sales growth until 2013 is expected to be almost 10%. Its size and growth potential make China a dominant force in the industry going forward; new models and technologies developed there will almost certainly become available elsewhere.

But the Chinese government plays a central role in shaping the auto industry. Current ownership policies mandate that foreign vehicle manufacturers enter into 50-50 joint ventures with local automakers, and poor intellectual property rights enforcement puts the design and engineering innovations of foreign car companies at constant risk. At the same time, to cope with energy shortages and rampant pollution, the Chinese government is strongly encouraging research and development on alternative power trains, including electric cars and gasoline-electric hybrids. As a result, Chinese car companies may develop significant power-train capabilities ahead of their competitors.

Like their Indian counterparts, Chinese car companies have outpaced global automakers in developing cars specifically for emerging markets. A few Western companies, like Volkswagen AG, which has sold its Santana models in China through a joint venture (Shanghai Volkswagen Automotive Company) since 1985, are competitive. Some Chinese carmakers, like BYD Company, aspire to become global leaders in the industry. But many suffer from a talent shortage and inexperience in managing across borders. This may prompt them to acquire all or part of distressed

Western automobile companies in the near future or to hire skilled auto executives from established companies and their suppliers.

In short, each of the four BRIC nations has a completely different set of market and industry dynamics. And the same is true for the other developing nations. Meanwhile, the number of autos in use in the developing world is projected to expand almost six-fold by 2018.

(Haddock & Jullens, 2009)

Cultural, Administrative, Geographic, and Economic Distance

Explicitly considering the four dimensions of *distance* can dramatically change a company's assessment of the relative attractiveness of foreign markets. In his book, *The Mirage of Global Markets*, David Arnold describes the experience of Mary Kay Cosmetics (MKC) in entering Asian markets. MKC is a direct marketing company that distributes its products through independent "beauty consultants" who buy and resell cosmetics and toiletries to contacts either individually or at social gatherings. When considering market expansion in Asia, the company had to choose: enter Japan or China first? Country-level data showed Japan to be the most attractive option by far: it had the highest per capita level of spending on cosmetics and toiletries of any country in the world, disposable income was high, it already had a thriving direct marketing industry, and it had a high proportion of women who did not participate in the work force. MKC learned, however, after participating in both markets, that the market opportunity in China was far greater, mainly because of economic and cultural distance: Chinese women were far more motivated than their Japanese counterparts to boost their income by becoming beauty consultants. Thus, the entrepreneurial opportunity represented by what MKC describes as "the career" (i.e., becoming a beauty consultant) was a far better predictor of the true sales potential than high-level data on incomes and expenditures. As a result of this experience, MKC now employs an additional business-specific indicator of market potential within its market assessment framework: the average wage for a female secretary in a country (Arnold, 2004, p. 34).

MKC's experience underscores the importance of analyzing distance. It also highlights the fact that different product markets have different success factors: some are brand-sensitive while pricing or intensive distribution are key to success in others. Country-level economic or demographic data do not provide much help in analyzing such issues; only locally gathered marketing intelligence can provide true indications of a market's potential size and growth rate and its key success factors.

4.2 GLOBAL MARKET OPPORTUNITY ASSESSMENT – CAGE ANALYSIS

CAGE Analysis

Pankaj "Megawatt" Ghemawat (2001) is an international strategy guru who developed the CAGE framework to offer businesses a way to evaluate countries in terms of the "distance" between them. In this case, distance is defined broadly to include not only the physical geographic distance between countries but also the cultural, administrative (currencies, trade agreements), and economic differences between them. As summarized in Table 6.1 "The CAGE Framework", the CAGE (cultural, administrative, geographic, and economic) framework offers a broader view of distance and provides another way of thinking about location and the opportunities and concomitant risks associated with global arbitrage (Ghemawat, 2003).

Table 4.1 The CAGE Framework

Cultural Distance	Administrative Distance	Geographic Distance	Economic Distance
Attributes Creating Distance			
Different languages	Absence of colonial ties	Physical remoteness	Differences in consumer incomes Differences in costs and quality of the following:
Different ethnicities; lack of connective ethnic or social networks	Absence of shared monetary or political association	Lack of a common border	• Natural resources • Financial resources • Human resources • Infrastructure • Intermediate inputs • Information or knowledge
Different religions	Political hostility	Lack of sea or river access	
Different social norms	Government policies	Size of country	
	Institutional weakness	Weak transportation or communication links	
		Differences in climates	
Industries or Products Affected by Distance			
Products have high-linguistic content (TV).	Government involvement is high in industries that are • producers of staple goods (electricity), • producers of other "entitlements" (drugs), • large employers (farming), • large suppliers to government (mass transportation), • national champions (aerospace), • vital to national security (telecommunications), • exploiters of natural resources (oil, mining), and • subject to high-sunk costs (infrastructure).	Products have a low value-of-weight or bulk ratio (cement).	Nature of demand varies with income level (cars).

Cultural Distance	Administrative Distance	Geographic Distance	Economic Distance
Products affect cultural or national identity of consumers (foods).		Products are fragile or perishable (glass or fruit).	Economies of standardization or scale are important (mobile phones).
Product features vary in terms of size (cars), standards (electrical appliances), or packaging.		Communications and connectivity are important (financial services).	Labour and other factor cost differences are salient (garments).
Products carry country-specific quality associations (wines).		Local supervision and operational requirements are high (many services).	Distribution or business systems are different (insurance).
			Companies need to be responsive and agile (home appliances).

Figure Source: (Ghemawat, 2001)

To apply the CAGE framework, identify locations that offer low raw material costs, access to markets or consumers, or other key decision criteria. You might, for instance, determine that you're interested in markets with strong consumer buying power, so you would use per capita income as your first sorting criterion. As a result, you would likely end up with some type of ranking. Ghemawat provides an example for the fast-food industry, where he shows that on the basis of per capita income, countries like Germany and Japan would be the most attractive markets for the expansion of a North American fast-food company. However, when he adjusts this analysis for distance using the CAGE framework, he shows that Mexico ranks as the second most attractive market for international expansion, far ahead of Germany and Japan (Ghemawat, 2001).

Recall though, that any international expansion strategy still needs to be supported by the specific resources and capabilities possessed by the firm, regardless of the picture presented by the CAGE analysis. To understand the usefulness of the CAGE framework, consider Dell and its efforts to compete effectively in China. The vehicles it used to enter China were just as important in its strategy as its choice of geographic arena. For Dell's corporate clients in China, the CAGE framework would likely have revealed relatively little distance on all four dimensions—even geographic—given the fact that many personal-computer components have been sourced from China. However, for the consumer segment, the distance was rather great, particularly on the dimensions of culture, administration, and economics. For example, Chinese consumers didn't buy over the Internet, which is the primary way Dell sells its products in the United States. One possible outcome could have been for Dell to avoid the Chinese consumer market altogether. However, Dell opted to choose a strategic alliance with distributors whose knowledge base and capabilities allowed Dell to better bridge the CAGE-framework distances. Thus the CAGE framework can be used to address the question of where (which arena) and how (by which entry vehicle) to expand internationally.

CAGE Analysis and Institutional Voids

While you can apply CAGE to consider some first-order distances (e.g., physical distance between a company's home market and the new foreign market) or cultural differences (e.g., the differences between home-market and foreign-market customer preferences), you can also apply it to identify institutional differences. Institutional differences include differences in political systems and in financial markets. The greater the distance, the harder it will be to operate in that country. Emerging markets in particular can have greater differences because these countries lack many of the specialized intermediaries that make institutions like financial markets work. Table 6.2 "Specialized Intermediaries within a Country or Other Geographic Arena" lists examples of specialized intermediaries for different institutions. If an institution lacks these specialized intermediaries, there is an institutional void. An institutional void refers to the absence of key specialized intermediaries found in the markets of finance, managerial talent, and products, which otherwise reduce transaction costs.

Table 4.2 Specialized Intermediaries within a Country or Other Geographic Arena

Institution	**Specialized Intermediary**
Financial markets	• Venture-capital firms • Private equity providers • Mutual funds • Banks • Auditors • Transparent corporate governance
Markets for managerial talent	• Management institute or business schools • Certification agencies • Headhunting firms • Relocation agencies
Markets for products	• Certification agencies • Consumer reports • Regulatory authorities (e.g., the Food and Drug Administration) • Extrajudicial dispute resolution services
All markets	• Legal and judiciary (for property rights protection and enforcement)

Three Strategies for Handling Institutional Voids

When a firm detects an institutional void, it has three choices for how to proceed in regard to the potential target market: (1) adapt its business model, (2) change the institutional context, or (3) stay away.

For example, when McDonald's tried to enter the Russian market, it found an institutional void: a lack of local suppliers to provide the food products it needs. Rather than abandoning market entry, McDonald's decided to adapt its business model. Instead of outsourcing supply-chain operations like it does in the United States, McDonald's worked with a joint-venture partner to fill the voids. It imported cattle from Holland and russet potatoes from the United States, brought in agricultural specialists from Canada and Europe to improve Russian farmers' management practices, and lent money to farmers so that they could invest in better seeds and equipment. As a result of establishing its own supply-chain and management systems, McDonald's controlled 80 percent of the Russian fast-food market by 2010. The process, however, took fifteen years and $250 million in investments" (Economic Times of India, 2010).

An example of the second approach to dealing with an institutional void—changing the institutional context—is that used by the "Big Four" audit firms (i.e., Ernst & Young, KPMG, Deloitte Touche Tohmatsu, and PricewaterhouseCoopers) when they entered Brazil. At the time, Brazil had a fledgling audit services market. When the four firms set up branches in Brazil, they raised financial reporting and auditing standards across the country, thus bringing a dramatic improvement to the local market (Khanna et al., 2005).

Finally, the firm can choose the strategy of staying away from a market with institutional voids. For example, The Home Depot's value proposition (i.e., low prices, great service, and good quality) requires institutions like reliable transportation networks (to minimize inventory costs) and the practice of employee stock ownership (which motivates workers to provide great service). The Home Depot has decided to avoid countries with weak logistics systems and poorly developed capital markets because the company would not be able to attain the low cost–great service combination that is its hallmark (Khanna et al., 2005).

Case: Nestlé's Nespresso

Nestlé's Nespresso division is one of the company's fastest-growing divisions. The division makes a single-cup espresso machine along with single-serving capsules of coffees from around the world. Nestlé is headquartered in Switzerland, but the coffee it needs to buy is primarily grown in rural Africa and Latin America. Nespresso set up local facilities in these regions that measure the quality of the coffee. Nespresso also helps local farmers improve the quality of their coffee, and then it pays more for coffee beans that are of higher quality. Nespresso has gone even further by advising farmers on farming practices that improve the yield of beans farmers get per hectare. The results have proven beneficial to all parties: farmers earn more money, Nespresso gets better quality beans, and the negative environmental impact of the farms has diminished (Porter & Kramer, 2011).

Case: McCain Foods

McCain Foods is a Canadian firm that specialized in frozen potato products. With activities in over 160 countries, the corporation has a significant worldwide footprint. McCain Foods' motives for entering worldwide markets include extending its client base, generating revenue, and capitalizing on economies of scale.

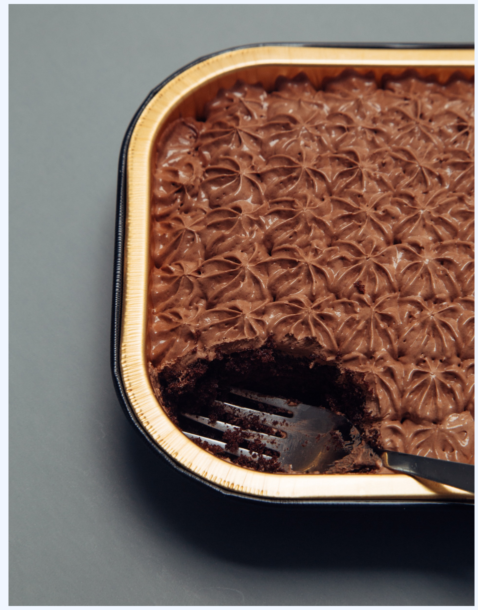

Photo by charlesdeluvio, Unsplash Licence

Countries Entered and How:

McCain Foods entered the global market through partnerships and joint ventures with local enterprises in several nations. In the 1960s, the corporation expanded its activities to the United States, and later to other nations such as Europe, Asia, and South America. McCain Foods has also expanded into new areas such as China and India, where demand for ready foods is increasing quickly.

Challenges Faced:

McCain struggled with expansion in India. In 2013, McCain entered the Indian market with the acquisition of a potato processing plant in the state of Gujarat. However, the company faced a number of challenges, including issues with supply chain management, local regulations, and cultural differences (Taneja, 2018). These challenges ultimately led to slower-than-expected growth in the Indian market.

Export Strategy:

Entry into the Chinese market in 2005. McCain partnered with a local company, the Luhua Group, to establish a joint venture that would produce and distribute frozen potato products in China (McCain Foods Limited, n.d.). This strategy allowed McCain to leverage the local knowledge and expertise of its partner to navigate the complex Chinese market, while also providing access to McCain's technology and expertise in frozen food production.

CAGE Framework:

The CAGE framework is being used by McCain in its entry into the Russian market. In 2011, McCain established a potato processing plant in the Lipetsk region of Russia, which was designed to serve the local market as well as export to neighbouring countries (Bolshakova & Soboleva, 2015). To overcome the cultural and administrative differences between Canada and Russia, McCain formed a joint venture with a local company, the Agroholding "Voskhod" group, which helped them navigate local regulations and customs.

Marketing Strategies:

McCain Foods' "It's All Good" campaign, launched in 2014 to showcase the firm's dedication to utilizing basic, healthful ingredients in its products, is one example of a marketing technique utilized by the company. The worldwide campaign, which featured television commercials, social media promos, and in-store displays, was launched in the United States, Canada, and Europe. McDonald Foods (2014)

Bukunmi Gabriel Ogunsola, March 2023

Market Attractiveness Analysis using the Cage Framework

Columbia Coffee Chain - Juan Valdez - entering a new potential market
Rating Scale: 1-10
1 - Low/Bad, 5 - Moderate, 10 - High/Good

Factors/Criteria	Weight	Country #1: Canada		Country #2: Brazil	
		Rating	**Assessment**	**Rating**	**Assessment**
Cultural	**30%**				
Criteria 1: Language	10%	5	5%	7	7%
Criteria 2: Cultural Diversity	10%	6	6%	7	7%
Criteria 3: Language	10%	8	8%	7	7%
Administrative	**25%**				
Criteria 1: Political Stability	10%	9	9%	6	6%
Criteria 2: Government Regulations	10%	8	8%	7	7%
Criteria 3: Competitive Conditions	5%	8	4%	6	3%
Geographic	**15%**				
Criteria 1: Market Size		5	2.50%	8	4%
Criteria 2: Weather		7	3.50%	7	3.50%
Criteria 3: Bordering Countries		8	4%	5	2.50%
Economic	**30%**				
Criteria 1: Economic Growth GDP	10%	8	8%	6	6%
Criteria 2: Trade	10%	8	8%	7	7%

How to calculate the percentage of a rating:

If a criteria has a weight of 10% and is rated 8 out of 10, 8÷10×10=8%

If a criteria has a weight of 5% and is rated 8/10, 8÷10×5=4%

Market Attractiveness Analysis using the Cage Framework

Columbia Coffee Chain - Juan Valdez - entering a new potential market
Rating Scale: 1-10
1 - Low/Bad, 5 - Moderate, 10 - High/Good

Criteria 3: Currency	10%	8	8%	6	6%
Total	**100%**		**74%**		**66%**

4.3 GLOBAL MARKET OPPORTUNITY ASSESSMENT – SCENARIO PLANNING AND ANALYSIS

The History and Role of Scenario Planning and Analysis

Strategic leaders use the information revealed by the application of PESTEL analysis, global dimensions, and CAGE analysis to uncover what the traditional SWOT framework calls opportunities and *threats*. A SWOT (strengths, weaknesses, opportunities, and threats) assessment is a strategic-management tool that helps you take stock of an organization's internal characteristics, or its strengths and weaknesses, such that any action plan builds on what it does well while overcoming or working around weaknesses; the SWOT assessment also helps a company assess external environmental conditions, or opportunities and threats, that favour or threaten an organization's strategy. In particular, you can use it to evaluate the implications of your industry analysis, both for your focal firm specifically and for the industry in general. However, a SWOT assessment works best with one situation or scenario and provides little direction when you're uncertain about potential changes to critical features of the scenario. Scenario planning can help in these cases.

Scenario Planning

Scenario planning helps leaders develop a detailed, internally consistent picture of a range of plausible outcomes as an industry evolves over time. You can also incorporate the results of scenario planning into your strategy formulation and implementation. Understanding the PESTEL conditions—as well as the level, pace, and drivers of industry globalization and the CAGE framework—will probably equip you with some insight into the outcomes of certain scenarios. The purpose of scenario planning, however, is to provide a bigger picture—one in which you can see specific trends and uncertainties. Developed in the 1950s at the global petroleum giant Shell, the technique is now regarded as a valuable tool for integrating changes and uncertainties in the external context into overall strategy (Schoemaker, 1991; Schoemaker, 1993; Schoemaker & van der Heijden, 1992). Since September 11, 2001, the use of scenario planning has increased in businesses. Analysis of Bain & Company's *Management Tools and Trends Survey* shows that in the post-9/11 period, approximately 70 percent of 8,500 global executives reported that their firms used scenarios, in contrast to a usage rate of less than 50 percent in most of the 1990s (Rigby & Bilodeau, 2007).

Unlike forecasts, scenarios are not straight-line, one-factor projections from present to future. Rather, they are complex, dynamic, interactive stories told from a future perspective. To develop useful scenarios, executives need a rich understanding of their industry along with broad knowledge of the diverse PESTEL and global conditions that are most likely to affect them. The six basic steps in scenario planning are detailed below.

Six Basic Steps of Scenario Planning

- **Step 1.** Choose the target issue, scope and time frame that the scenario will explore. The scope will depend on your level of analysis (i.e., industry, subindustry, or strategic group), the stage of planning, and the nature and degree of uncertainty and the rate of change. Generally, four scenarios are developed and summarized in a grid. The four scenarios reflect the extremes of possible worlds. To fully capture critical possibilities and contingencies, it may be desirable to develop a series of scenario sets.
- **Step 2.** Brainstorm a set of key drivers and decision factors that influence the scenario. This could include social unrest, shifts in power, regulatory change, market or competitive change, and technology or infrastructure change. Other significant changes in external contexts, like natural disasters, might also be considered.
- **Step 3.** Define the two dimensions of greatest uncertainty. These two dimensions form the axes of the scenario framework. These axes should represent two dimensions that provide the greatest uncertainty for the industry. For instance, the example on the global credit-union industry identifies changes in the playing field and technology as the two greatest areas of uncertainty up through the year 2005.
- **Step 4.** Detail the four quadrants of the scenarios with stories. Describe how the four worlds would look in each scenario. It's often useful to develop a catchy name for each world as a way to further develop its distinctive character. One of the worlds will likely represent a slightly future version of the status quo, while the others will be significant departures from it. As shown in the credit-union scenarios, *Chameleon* describes a world in which both the competitive playing field and technology undergo radical change, while *Wallet Wars* is an environment of intense competition but milder technological change. In contrast, in *Technocracy*, the radical changes are in technology, whereas in *Credit Union Power*, credit unions encounter only minor changes on either front.
- **Step 5.** Identify indicators that could signal which scenario is unfolding. These can either be trigger points that signal the change is taking place or milestones that mean the change is more likely. An indicator may be a large industry supplier like Microsoft picking up a particular but little-known technological standard.
- **Step 6.** Assess the strategic implications of each scenario. Microscenarios may be

developed to highlight and address business-unit-specific or industry-segment-specific issues. Consider needed variations in strategies, key success factors, and the development of a flexible, robust strategy that might work across several scenarios.

The process of developing scenarios and then conducting business according to the information that the scenarios reveal makes it easier to identify and challenge questionable assumptions. It also exposes areas of vulnerability (e.g., in a country, an industry, or a company), underscores the interplay of environmental factors and the impact of change, allows for robust planning and contingency preparation, and makes it possible to test and compare strategic options. Scenarios also help firms focus their attention on the trends and uncertainties that are likely to have the greatest potential impact on their future.

Once you've determined your target issue, scope, and time frame, you can draw up a list of driving forces that is as complete as possible and is organized into relevant categories (e.g., science-technology, political-economic, regulatory, consumer-social, or industry-market). As you proceed, be sure to identify *key* driving forces—the ones with the greatest potential to affect the industry, subindustry, or strategic group in which you're interested.

Trends and Uncertainties

Among the driving forces for change, be sure to distinguish between *trends* and *uncertainties*. Trends are forces for change whose direction—and sometimes timing—can be predicted. For example, experts can be reasonably confident in projecting the number of consumers in North America, Europe, and Japan who will be over sixty-five years old in the year 2020 because those people are alive now. If your firm targets these consumers, then the impact of this population growth will be significant to you; you may view it as a key trend. For other trends, you may know the direction but not the pace. China and India, for example, are experiencing a trend of economic growth, and many foreign investments depend on the course of infrastructure development and consumer-spending power in this enormous market. Unfortunately, the future pace of these changes is uncertain.

African Market

In his book *Africa Rising*, Vijay Mahajan documents how trends surrounding the 900 million African consumers may offer businesses more opportunities than they're currently taking advantage of:

Many tourists come to Africa every year to see the big game there—the elephants, lions, and rhinos. But I came for a different type of big game. I was seeking out the successful enterprises that are identifying and capitalizing on the market opportunities, and seeking lessons from those that are not so successful, too. In Nairobi, Maserame Mouyeme of The Coca-Cola Company told me how important it is 'to walk the market.' Then, in Harare, I first heard the term 'consumer safari' in a meeting with Unilever executives. This is what they call their initiatives to spend a day with consumers in their homes to understand how they use products. Years after I started on this journey, I now had a term to describe the quest I was on. I was on a consumer safari. The market landscape that is Africa is every bit as marvellous and surprising as its geographic landscape. It presents as big an opportunity as China and India (Mahajan, 2008).

In contrast, uncertainties—forces for change whose direction and pace are largely unknown—are more important for your scenario. European consumers, for example, tend to distrust the biotechnology industry, and given the number of competing forces at work—industries, academia, consumer groups, regulators, and so on—it is difficult to predict whether the consumers will be more or less receptive to biotechnology products in the future. Labelling regulations, for instance, may be either strengthened or relaxed in response to changing consumer opinion.

You might also want to consider the possibility of significant disruptions—that is, steep changes that have an important and unalterable impact on the business environment. A major disaster—such as the September 11 terrorist attacks—can spur regulatory and other legal reforms with major and lasting impact on certain technologies and competitive practices. Table 6.3 "Developing Scenarios for the Global Credit-Union Industry" provides sample scenarios created for the credit-union industry, providing an idea of how you would do this if asked to apply scenario analysis to another industry setting. As you can see, identifying the entry of new competitors and the impact of technology are the two primary sources of uncertainty about the future.

Changes in the Playing Field

Table 4.3 Developing Scenarios for the Global Credit-Union Industry

	Minor	Major
TECHNOLOGICAL CHANGE	**Gradual**	**Credit Union Power:** Both technology and the playing field have changed at a moderate pace, making this the most stable scenario. Even with moderate change in these areas, however, the changing basis of competition, new business models, human resources challenges, and industry dynamics are different enough to pose significant challenges for many financial-services companies.
	Radical	**Technocracy:** The wide-scale adoption of the Internet by US consumers has led to massive technological innovation for financial-services companies, increasing the range of distribution channels as well as the products, services, and geographic scope of financial-services organizations. Regulations and other changes in the playing field, however, have been slow to follow.

Note: After considering a PESTEL analysis, experts in the credit-union industry would identify the two most significant macroeconomic factors as (1) regulatory factors affecting both the types of businesses that credit unions can compete in and the entry of new players and consolidation of existing ones, and (2) technological factors, or the speed with which new technologies related to banking are both developed and adopted by consumers. These two dimensions define the major areas of uncertainty facing credit union executives in the next decade. Considering those dimensions and following the six basic steps in scenario planning, you might then develop the following four scenarios.

Source: Adapted from "Scenarios for Credit Unions 2010: An Executive Report," Credit Union Executives Society, 2004, accessed May 10, 2011, http://www.dsicu.com/pdfs/2010_Scenarios.pdf.

4.4 SELECTING THE COUNTRIES TO ENTER

In this section, we introduce a new tool, the 'Country Attractiveness Analysis (CAA)', which provides in-depth screening models for selecting and entering foreign markets. The process for evaluating foreign markets for potential entry typically consists of three stages:

1. Preliminary Screening stage
2. In-depth screening page
3. Final selection

Preliminary Screening

In the Preliminary Screening stage, potential countries are evaluated on macro-level indicators such as political stability, economic development, geographic distance, etc. The preliminary analysis can include one or more of the tools that were presented in the previous sections of this chapter – e.g., the PESTEL Analysis, the CAGE Analysis, and/or the Scenario Planning and Analysis.

Countries that pass through the preliminary screening process are then examined in more detail during the In-depth Screening stage. In the second stage, criteria specific to market success for the industry and product markets are identified, and countries are evaluated on them. The in-depth screening process is the core of country attractiveness analysis, since it brings to bear criteria that management feels are critical to business success. Because criteria must be relevant to industry and product market success factors, in-depth screening must be customized and updated.

Country Attractiveness Analysis

Step 1: Identify Criteria

The first step in conducting the CAA involves in identifying the criteria that are critical to business success. This will be different for different products. For example, the success factors for a toothpaste category would be Consumer Demand, Consumer Access to Supply, Competition, Distance, and Regulation. The specific criteria related to the 'Consumer Demand' of a toothpaste will be population, GDP per capita, GDP growth rate, inflation rate (the lower the better), toothpaste sales growth, toothpaste sales, etc. Similarly, the specific criteria related to the 'Supply' of a toothpaste will be sales-force expenses, average expenses (the lower the better), and distribution fixed costs (the lower the better). The specific criteria related to the 'Competition' factor for a toothpaste will be # of competitors, total marketing expenditures, # of MNCs, and largest competitor's share, the lower the better for all these criteria.

Another example: a company whose niche is luxury goods sold through wholesalers to retail stores and on to end users may identify two important factors: level of affluence and distribution network. Criteria used to assess affluence could be disposable income, income growth, and GDP.

Step 2: Weight Criterion

The next step is to weight the importance of each criterion. Weighting each criterion is necessary since not all criteria are equally important. Obviously, criteria are selected because they meet some minimum threshold level of importance. Yet some criteria are more important than others, and these differences need to be taken into account. A common approach is to allocate 100 points (or 100%) across all of the criteria, where more points (or a higher percentage) are awarded to criteria that are more important. An ideal way to do this is to first assign weights to the factors so that the sum of all weights adds up to 100%, and then divide the weight of each factor among their criteria.

Step 3: Rating

Third, each country needs to be rated on each criterion. The rating is designed to determine how well a country performs or is characterized on a particular criterion. A common rating scale ranges from one to ten, where 1 = very poor and 10 = very good.

Step 4: Calculate Score

Finally, calculate the 'Assessment' score for each country by multiplying the weight of each criteria and its rating. Sum the criterion assessment scores within each factor to derive factor assessments. Sum the factor (or criteria) assessment scores to derive an overall assessment for each market opportunity

Final Selection

Based on the assessment scores calculated for each country, one or more countries can be selected for market entry. The results of the in-depth screening illustrate the relative attractiveness of the countries investigated. Before making investment decisions, due diligence analyses will be performed to better forecast costs, revenues, capital (financial, human) requirements, cash flow, expected rate of return, etc. These forecasts will likely differ depending on entry mode. As due diligence analyses are very complex and time consuming, an important contribution of in-depth screening is to narrow down the number of markets for due diligence analysis.

Factors/Criteria	**Weight**	**Country 1**		**Country 2**		**Country 3**	
		Rating	**Assessment**	**Rating**	**Assessment**	**Rating**	**Assessment**
Factor #1 ____________: Criteria 1. Criteria 2. Criteria 3.							
Factor #2 ____________: Criteria 1. Criteria 2. Criteria 3.							
Factor #3 ____________: Criteria 1. Criteria 2. Criteria 3.							
TOTAL	100%	-		-		-	

Table 4.4 In-depth screening calculations

4.5 GLOBAL MARKET SEGMENTATION

Segmentation is an important strategic tool in international marketing because the main difference between calling a firm international and global is based on the scope and bases of segmentation. An international firm has different marketing strategies for different segments of countries, while a global firm views the whole world as a market, and then segments this whole world based on viable segmentation bases. Generally, there are three approaches to segmentation in international marketing:

1. macro-segmentation
2. micro-segmentation
3. hybrid approach.

Macro-segmentation

Macro-segmentation or country-based segmentation identifies clusters of countries that demand similar products. Macro-segmentation uses geographic, demographic and socioeconomic variables such as location, GNP per capita, population size or family size to group countries intro market segments, and then selects one or more segments to create marketing strategies for each of the selected segments. This strategy enables a company to centralize its operations and save on production, sales, logistics and support functions. However, macro-segmentation doesn't take into consideration consumer differences within each country and among the country markets that are clustered together, and fails to acknowledge the existence of segments that go beyond the borders of a particular geographic region. Therefore, the company may be leaving money on the table, because the firm may be losing opportunities to solve the need of consumer segments across these country segments. Macro-segmentation leads to misleading national stereotyping, which results in neglect of within-country heterogeneity. Ignoring similarity in needs across country boundaries results in countries losing economies of scale benefits that can be achieved by serving the needs of a wider population across country (macro-segment) boundaries.

Micro-segmentation

Micro-segmentation or consumer-based segmentation involves grouping consumers based on common characteristics using psychographic and/or behaviouristic segmentation variables such as cultural preferences, values and attitudes, lifestyle choices. Table 6.6 "Micro-segmentation bases" and Table 6.7 "Common Ways of Segmenting Buyers" show some of the different types of buyer characteristics used for micro-segmentation. Notice that the characteristics fall into one of four segmentation categories: behavioural, demographic, geographic, or psychographic.

We'll discuss each of these categories in a moment. For now, you can get a rough idea of what the categories consist of by looking at them in terms of how marketing professionals might answer the following questions:

Categories	Questions	Ways to Segment
Behavioural segmentation	What benefits do customers want, and how do they use our product?	Benefits sought from the product How often the product is used (usage rate) Usage situation (daily use, holiday use, etc.) Buyer's status and loyalty to product (nonuser, potential user, first-time users, regular user)
Demographic segmentation	How do the ages, races, and ethnic backgrounds of our customers affect what they buy?	Age/generation, Income, Gender, Family life cycle, Ethnicity, Family size, Occupation, Education, Nationality, Religion, and Social class
Geographic segmentation:	Where are our customers located, and how can we reach them? What products do they buy based on their locations?	Region (continent, country, state, neighbourhood), Size of city or town, Population density and Climate
Psychographic segmentation	What do our customers think about and value? How do they live their lives?	Activities, Interests, Opinions, Values, Attitudes, Lifestyle

Segmenting by Behaviour

Behavioural segmentation divides people and organization into groups according to how they behave with or act toward products. Benefits segmentation—segmenting buyers by the benefits they want from products—is very common. Take toothpaste, for example. Which benefit is most important to you when you buy a toothpaste: The toothpaste's price, ability to whiten your teeth, fight tooth decay, freshen your breath, or something else? Perhaps it's a combination of two or more benefits. If marketing professionals know what those benefits are, they can then tailor different toothpaste offerings to you (and other people like you).

Another way in which businesses segment buyers is by their usage rates—that is, how often, if ever, they use certain products. Companies are interested in frequent users because they want to reach other people like them. They are also keenly interested in nonusers and how they can be persuaded to use products. The way in which people use products can also be a basis for segmentation.

Segmenting by Demographics

Segmenting buyers by personal characteristics such as age, income, ethnicity and nationality, education, occupation, religion, social class, and family size is called demographic segmentation. Demographics are commonly utilized to segment markets because demographic information is publicly available in databases around the world.

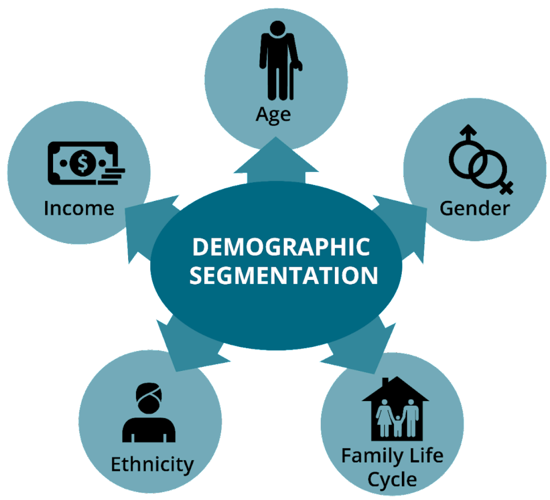

Fig 4.2 "Demographic Segmentation" by Alyssa Giles, CC BY-NC-SA 4.0.

Age

At this point in your life, you are probably more likely to buy a car than a funeral plot. Marketing professionals know this. That's why they try to segment consumers by their ages. To learn more about the different generations in Canada, review the Stats Can report: A Generational Portrait of Canada's Aging Population – 2021 Census

How do companies decide which groups to target? Although it's hard to be all things to all people, many companies try to broaden their customer bases by appealing to multiple generations so they don't lose market share when demographics change. Several companies have introduced lower-cost brands targeting Generation Xers, who have less spending power than boomers. For example, kitchenware and home-furnishings company Williams- Sonoma opened the Elm Street chain, a less-pricey version of the Pottery Barn franchise. The Starwood hotel chain's W hotels, which feature contemporary designs and hip bars, are aimed at Generation Xers (Miller, 2009).

The video game market is very proud of the fact that along with Generation X and Generation Y, many older Americans still play video games. (You probably know some baby boomers who own a Nintendo Wii.)

Products and services in the spa market used to be aimed squarely at adults, but not anymore. Parents are now paying for their tweens to get facials, pedicures, and other pampering in numbers no one in years past could have imagined.

As early as the 1970s, U.S. automakers found themselves in trouble because of changing demographic trends. Many of the companies' buyers were older Americans inclined to "buy American." These people hadn't forgotten that Japan bombed Pearl Harbor during World War II and weren't about to buy Japanese vehicles, but younger Americans were. Plus, Japanese cars had developed a better reputation. Despite the challenges U.S. automakers face today, they have taken great pains to cater to the "younger" generation—today's baby boomers who don't think of themselves as being old. If you are a car buff, you perhaps have noticed that the once-stodgy Cadillac now has a sportier look and stiffer suspension. Likewise, the Chrysler 300 looks more like a muscle car than the old Chrysler Fifth Avenue your great-grandpa might have driven.

Automakers have begun reaching out to Generations X and Y, too. General Motors (GM) has sought to revamp the century-old company by hiring a new younger group of managers—managers who understand how Generation X and Y consumers are wired and what they want. "If you're going to appeal to my daughter, you're going to have to be in the digital world," explained one GM vice president (Cox, 2009).

Income

Tweens might appear to be a very attractive market when you consider they will be buying products for years to come. But would you change your mind if you knew that baby boomers account for 50 percent of all consumer spending in the United States? Americans over sixty-five now control nearly three-quarters of the net worth of U.S. households; this group spends $200 billion a year on major "discretionary" (optional) purchases such as luxury cars, alcohol, vacations, and financial products (Reisenwitz et al., 2007).

Income is used as a segmentation variable because it indicates a group's buying power and may partially reflect their education levels, occupation, and social classes. Higher education levels usually result in higher paying jobs and greater social status. The makers of upscale products such as Rolexes and Lamborghinis aim their products at high-income groups. However, a growing number of firms today are aiming their products at lower-income consumers. The fastest-growing product in the financial services sector is prepaid debit cards, most of which are being bought and used by people who don't have bank accounts. Firms are finding that this group is a large, untapped pool of customers who tend to be more brand loyal than most. If you capture enough of them, you can earn a profit (von Hoffman, 2006). Based on the targeted market, businesses can determine the location and type of stores where they want to sell their products.

Gender

Gender is another way to segment consumers. Men and women have different needs and also shop differently. Consequently, the two groups are often, but not always, segmented and targeted differently. Marketing professionals don't stop there, though. For example, because women make many of the purchases for their households, market researchers sometimes try to further divide them into subsegments. (Men are also often subsegmented.) For women, those segments might include stay-at-home housewives, plan-to-work housewives, just-a-job working women, and career-oriented working women.

Family Life Cycle

Family life cycle refers to the stages families go through over time and how it affects people's buying behaviour. For example, if you have no children, your demand for pediatric services (medical care for children) is likely to be slim to none, but if you have children, your demand might be very high because children frequently get sick. You may be part of the target market not only for pediatric services but also for a host of other products, such as diapers, daycare, children's clothing, entertainment services, and educational products. A secondary segment of interested consumers might be grandparents who are likely to spend less on day-to-day childcare items but more on special-occasion gifts for children. Many markets are segmented based on the special events in people's lives. Think about brides (and want-to-be brides) and all the products targeted at them, including Web sites and television shows such as Say Yes to the Dress, My Fair Wedding, Platinum Weddings, and Bridezillas.

Resorts also segment vacationers depending on where they are in their family life cycles. When you think of family vacations, you probably think of Disney resorts. Some vacation properties, such as Sandals, exclude children from some of their resorts. Perhaps they do so because some studies show that the market segment with greatest financial potential is married couples without children (Hill, et al., 1990).

Keep in mind that although you might be able to isolate a segment in the marketplace, including one based on family life cycle, you can't make assumptions about what the people in it will want. Just like people's demographics change, so do their tastes. For example, over the past few decades U.S. families have been getting smaller. Households with a single occupant are more commonplace than ever, but until recently, that hasn't stopped people from demanding bigger cars (and more of them) as well as larger houses, or what some people jokingly refer to as "McMansions."

The trends toward larger cars and larger houses appear to be reversing. High energy costs, the credit crunch, and concern for the environment are leading people to demand smaller houses. To attract people such as these, D. R. Horton, the nation's leading homebuilder, and other construction firms are now building smaller homes.

Ethnicity

People's ethnic backgrounds have a big impact on what they buy. If you've visited a grocery store that caters to a different ethnic group than your own, you were probably surprised to see the types of products sold there. It's no secret that the United States is becoming—and will continue to become—more diverse. Even within various ethnic groups there are many differences in terms of the goods and services buyers choose. Consequently, painting each group with a broad brush would leave you with an incomplete picture of your buyers.

Segmenting by Geography

Suppose your great new product or service idea involves opening a local store. Before you open the store, you will probably want to do some research to determine which geographical areas have the best potential. For instance, if your business is a high-end restaurant, should it be located near the local college or country club? If you sell ski equipment, you probably will want to locate your shop somewhere in the vicinity of a mountain range where there is skiing. You might see a snowboard shop in the same area but probably not a surfboard shop. By contrast, a surfboard shop is likely to be located along the coast, but you probably would not find a snowboard shop on the beach.

Geographic segmentation divides the market into areas based on location and explains why the checkout clerks at stores sometimes ask for your zip code. It's also why businesses print codes on coupons that correspond to zip codes. When the coupons are redeemed, the store can find out where its customers are located—or not located. Geocoding is a process that takes data such as this and plots it on a map. Geocoding can help businesses see where prospective customers might be clustered and target them with various ad campaigns, including direct mail. One of the most popular geocoding software programs is PRIZM NE, which is produced by a company called Claritas. PRIZM NE uses zip codes and demographic information to classify the populations into segments. The idea behind PRIZM is that "you are where you live." Combining both demographic and geographic information is referred to as geodemographics or neighborhood geography. The idea is that housing areas in different zip codes typically attract certain types of buyers with certain income levels.

In addition to figuring out where to locate stores and advertise to customers in that area, geographic segmentation helps firms tailor their products. Chances are you won't be able to find the same heavy winter coat you see at a Walmart in Montana at a Walmart in Florida because of the climate differences between the two places. Market researchers also look at migration patterns to evaluate opportunities. TexMex restaurants are more commonly found in the southwestern United States. However, northern states are now seeing more of them as more people of Hispanic descent move northward.

Segmenting by Psychographics

If your offering fulfills the needs of a specific demographic group, then the demographic can be an important basis for identifying groups of consumers interested in your product. What if your product crosses several market segments? For example, the group of potential consumers for cereal could be "almost" everyone although groups of people may have different needs with regard to their cereal. Some consumers might be interested in the fibre, some consumers (especially children) may be interested in the prize that comes in the box, other consumers may be interested in the added vitamins, and still other consumers may be interested in the type of grains. Associating these specific needs with consumers in a particular demographic group could be difficult. Marketing professionals want to know why consumers behave the way they do, what is of high priority to them, or how they rank the importance of specific buying criteria. Think about some of your friends who seem a lot like you. Have you ever gone to their homes and been shocked by their lifestyles and how vastly different they are from yours? Why are their families so much different from yours?

Psychographic segmentation can help fill in some of the blanks. Psychographic information is frequently gathered via extensive surveys that ask people about their activities, interests, opinion, attitudes, values, and lifestyles. One of the most well-known psychographic surveys is VALS (which originally stood for "Values, Attitudes, and Lifestyles") and was developed by a company called SRI International in the late 1980s.

Hybrid Segmentation

Hybrid or Universal segmentation looks for similarities across world markets. This strategy solves the disadvantages of using macro- and micro-segmentation bases to segment international markets, as they tend to ignore similarities and highlight only the differences. Certain segments identified in a micro-segmentation strategy may have the same characteristics present on a global scale. One such segment is the Global Teen segment – young people between the ages of 12 and 19. It is likely that a group of teenagers randomly chosen from different parts of the world share many of the same tastes. Another such global segment is the Global Elite segment, comprising affluent consumers who have the money to spend on prestigious products with an image of exclusivity. The global elite segment can be associated with older individuals who have accumulated wealth over the course of a long career, including movie stars, musicians, athletes, and people who have achieved financial success at a relatively young age.

Hybrid segmentation involves looking for similarities across micro–segments identified in the countries selected in the final step of the CAA procedure. Under this process, country borders are honorary, as the segmentation process considers the countries selected in the final step of the CAA procedure as one market and searches for similar segments across these countries.

4.6 USING DEMOGRAPHICS TO GUIDE GLOBAL MARKETING STRATEGY

Whether marketing to domestic or international markets, demographic information can provide important insights about a target market and how to address consumer needs. Demographics refer to statistical information about the characteristics of a population.

Marketers typically combine several variables to create a demographic profile of a target market. A demographic profile (often shortened to a "demographic") is a term used in marketing and broadcasting to describe a demographic grouping or a market segment. Common demographic variables to consider for global and domestic marketing purposes include the following:

Age:	Age bands, such as 18–24, 25–34, etc. are great predictors of interest in some types of products. For example, few teenagers wish to purchase denture cream.
Social class:	Social-class bands such as wealthy, middle, and lower classes. The rich, for instance, may want different products than middle and lower classes, and may be willing to pay more.
Gender:	Males and females have different physical attributes that require different hygiene and clothing products. They also tend to have distinctive male/female mindsets and roles in the family and household decision making.
Religious affiliations:	Religion is linked to individual values as well as holiday celebrations, often tied to consumer preferences and spending patterns.
Income brackets:	Indicating level of wealth, disposable income, and quality of life.
Education:	Level of education is often tied to consumer preferences, as well as income.
Geography:	Area of residence, urban vs. rural, and population density can all be important inputs into marketing strategy and decisions about where and how to target advertising and other elements of the promotion mix.

Demographic research may include a variety of other characteristics used to separate a country's population into groups that fit a company's target customer profile. A demographic profile also provides enough information about the typical member of this group to create a mental picture of this hypothetical aggregate. For example, a marketer might speak of the single, female, middle-class, aged 18–24, college-educated demographic.

Researchers examining demographics typically have two objectives in mind: first, to segment the market by determining which subgroups exist in the overall population; and second, to create a clear and complete picture of the characteristics displayed by typical members of each segment. Once these profiles are constructed, marketers can use them to develop the targeting strategy and accompanying marketing strategy and marketing plan.

With demographic profiles about target segments in hand, marketers evaluate the marketing mix. They make recommendations about whether to change, decrease, or increase the goods or services offered. Based on demographic data, marketers may adjust product features, distribution strategy, or other factors in order to reach a market segment that has the most potential.

A demographic profile can be very useful in determining the promotional mix and how to achieve maximum results. Advertising is usually part of the promotional mix, especially when businesses are still in the early stages of entering a global market and launching products that are new to that market. Advertisers want to get the most results for their money, and so in global markets as in domestic markets, careful media research is conducted to match the demographic profile of the target market to the demographic profile of the advertising medium.

Cautions About Demographic Profiling in Global Markets

Demographic profiling is essentially an exercise in making generalizations about groups of people. As with all such generalizations, many individuals within these groups will not conform to the profile. Demographic information is aggregate and offers probabilistic data about groups—not specific individuals. Critics of demographic profiling argue that such broad-brush generalizations can only offer limited insight.

Marketers must also be careful to avoid interpreting demographic information using the the mindset of their own "home" cultures. For example, the generalizations that apply to "tweens" (9–12-year-olds) in the U.S. may not apply at all to children in this same age range in other geographies. Similarly, assumptions about how social class affects consumer preferences may be very different in a socially mobile society versus one with very rigid separation between groups from different social classes. Marketing research should seek to understand a complete picture of how demographic characteristics tend to influence consumer behaviour in a given market, rather than simply applying stereotypes from elsewhere.

4.7 TARGET MARKET SELECTION

Few companies can afford to enter all markets open to them. Even the world's largest companies must exercise strategic discipline in choosing the markets they serve. They must also decide when to enter them and weigh the relative advantages of a direct or indirect presence in different regions of the world. Small and midsized companies are often constrained to an indirect presence; for them, the key to gaining a global competitive advantage is often creating a worldwide resource network through alliances with suppliers, customers, and, sometimes, competitors. What is a good strategy for one company, however, might have little chance of succeeding for another.

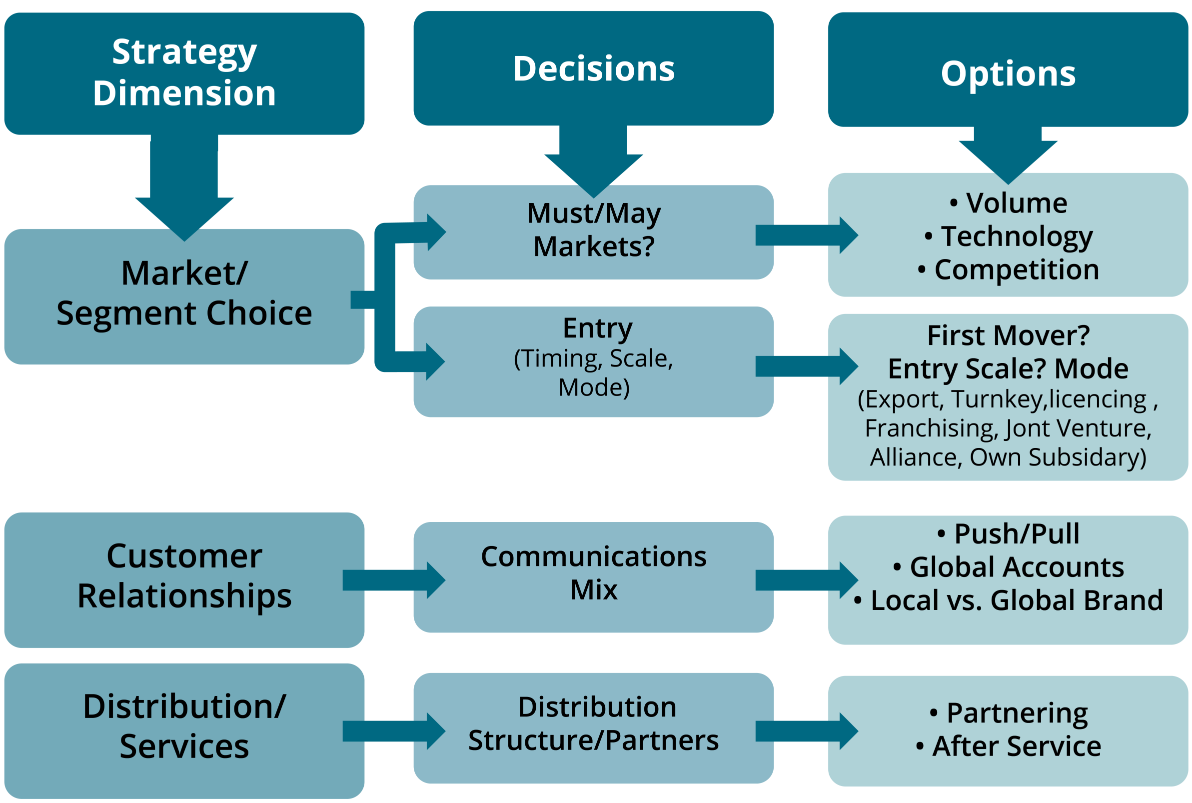

Fig 4.3 Market Participation adapted from original: Colour change and re-organized

The track record shows that picking the most attractive foreign markets, determining the best time to enter them, and selecting the right partners and level of investment has proven difficult for many companies, especially when it involves large emerging markets such as China. For example, it is now generally recognized that Western carmakers entered China far too early and overinvested, believing a "first-mover advantage" would produce superior returns. Reality was very different. Most companies lost large amounts of money, had trouble working with local partners, and saw their technological advantage erode due to "leakage." None achieved the sales volume needed to justify their investment.

Even highly successful global companies often first sustain substantial losses on their overseas ventures, and occasionally have to trim back their foreign operations or even abandon entire countries or regions in the face of ill-timed strategic moves or fast-changing competitive circumstances. What makes global market selection and entry so difficult? Research shows there is a pervasive the-grass-is-always-greener effect that infects global strategic decision-making in many, especially globally inexperienced, companies and causes them to overestimate the attractiveness of foreign markets. Distance can be a major impediment to global success: cultural differences can lead companies to overestimate the appeal of their products or the strength of their brands; administrative differences can slow expansion plans, reduce the ability to attract the right talent, and increase the cost of doing business; geographic distance impacts the effectiveness of communication and coordination, and economic distance directly influences revenues and costs (Ghemawat, 2001).

A related issue is that developing a global presence takes time and requires substantial resources. Ideally, the pace of international expansion is dictated by customer demand. Sometimes it is necessary, however, to expand ahead of direct opportunity in order to secure a long-term competitive advantage. But as many companies that entered China in anticipation of its membership in the World Trade Organization have learned, early commitment to even the most promising long-term market makes earning a satisfactory return on invested capital difficult. As a result, an increasing number of firms, particularly smaller and mid-sized ones, favour global expansion strategies that minimize direct investment. Strategic alliances have made vertical or horizontal integration less important to profitability and shareholder value in many industries. Alliances boost contribution to fixed costs while expanding a company's global reach. At the same time, they can be powerful windows on technology and greatly expand opportunities to create the core competencies needed to effectively compete on a worldwide basis.

Finally, a complicating factor is that a global evaluation of market opportunities requires a multidimensional perspective. In many industries, we can distinguish between "must" markets—markets in which a company must compete in order to realize its global ambitions—and "nice-to-be-in" markets—markets in which participation is desirable but not critical. "Must" markets include those that are critical from a *volume* perspective, markets that define *technological leadership*, and markets in which key *competitive* battles are played out. In the cell phone industry, for example, Motorola looks to Europe as a primary competitive battleground, but it derives much of its technology from Japan and sales volume from the United States.

American Companies That Failed In China

Despite the size and potential of the market, China is not an easy place for foreign businesses to enter. As this infographic shows, many of America's biggest names eventually admitted defeat.

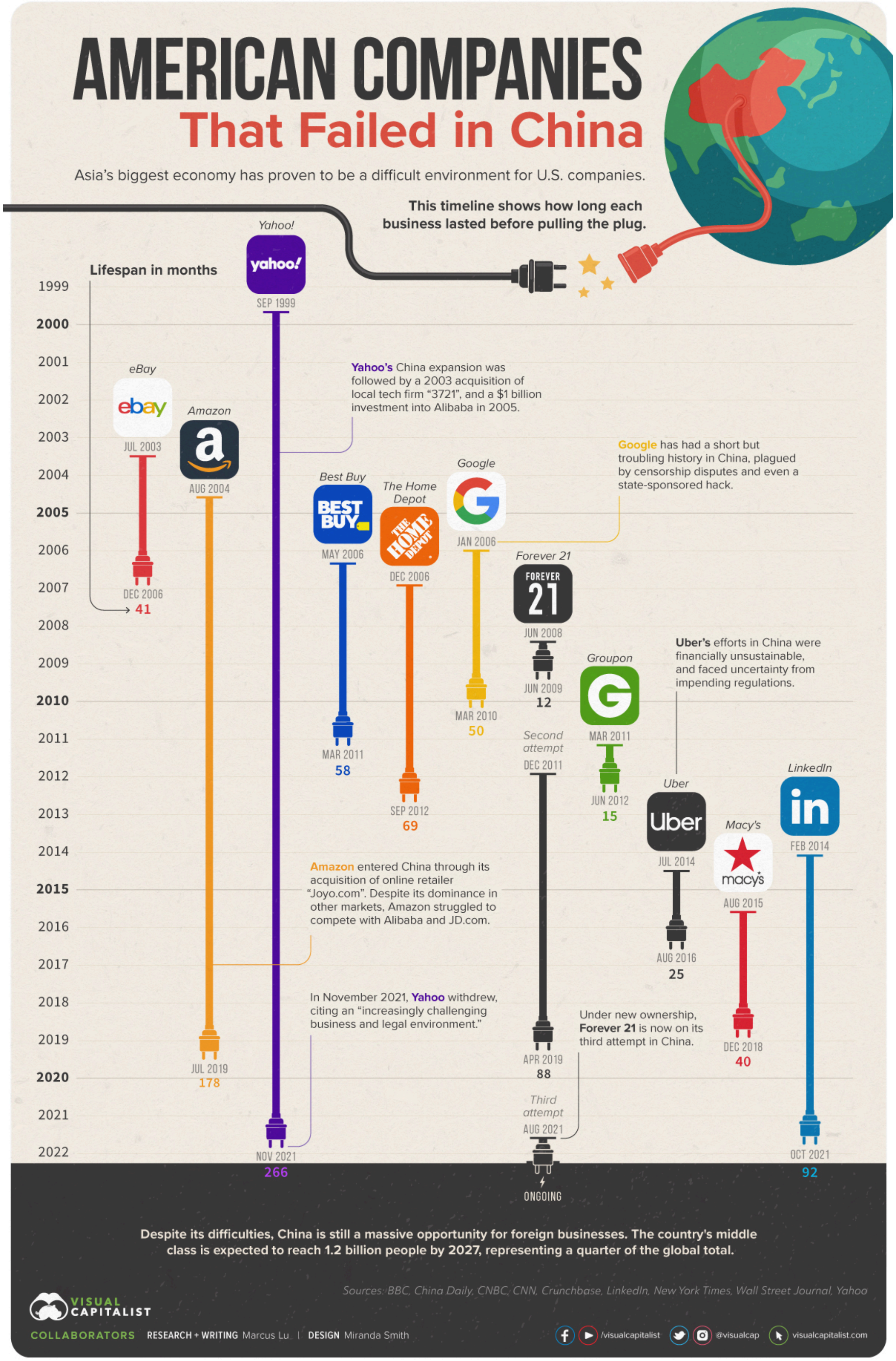

Figure by Visual Capitalist, reproduced without modification.

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4.9 KEY TERMS

Key Terms

Age: Age bands, such as 18–24, 25–34, etc., are great predictors of interest in some types of products. For example, few teenagers wish to purchase denture cream. 4.6

Antiglobals: Are skeptical that global companies deliver higher-quality goods. They particularly dislike brands that preach American values and often do not trust global companies to behave responsibly. Given a choice, they prefer to avoid doing business with global firms. 4.1

Credit Union Power: Both technology and the playing field have changed at a moderate pace, making this the most stable scenario. Even with moderate change in these areas, however, the changing basis of competition, new business models, human resources challenges, and industry dynamics are different enough to pose significant challenges for many financial services companies. 4.4

Demographic Research: This may include a variety of other characteristics used to separate a country's population into groups that fit a company's target customer profile. 4.6

Education: Level of education is often tied to consumer preferences, as well as income. 4.6

Gender: Males and females have different physical attributes that require different hygiene and clothing products. They also tend to have distinctive male/female mindsets and roles in the family and household decision-making. 4.6

Geography: Area of residence, urban vs. rural, and population density can all be important inputs into marketing strategy and decisions about where and how to target advertising and other elements of the promotion mix. 4.6

Global Agnostics: Do not base purchase decisions on a brand's global attributes. Instead, they judge a global product by the same criteria they use for local brands(Holt, Quelch, & Taylor, 2004). 4.1

Global Citizens: Rely on the global success of a company as a signal of quality and innovation. At the same time, they worry whether a company behaves responsibly on issues like consumer health, the environment, and worker rights. 4.1

Global Dreamers: Are less discerning about but more ardent in their admiration of, transnational companies. They view global brands as quality products and readily buy into the myths they portray. They also are less concerned with companies' social responsibilities than global citizens. 4.1

Income Brackets: Indicating level of wealth, disposable income, and quality of life. 4.6

Macro-Segmentation: Or country-based segmentation identifies clusters of countries that demand similar products. Macro-segmentation uses geographic, demographic and socioeconomic variables such as location, GNP per capita, population size or family size to group countries into market segments, and then selects one or more segments to create marketing strategies for each of the selected segments. 4.5

Micro-Segmentation: Or consumer-based segmentation involves grouping consumers based on common characteristics using psychographics and/or behaviouristic segmentation variables such as cultural preferences, values and attitudes, and lifestyle choices. 4.5

Openness: The more open a country's economy, the more likely it is that global intermediaries can freely operate there, which helps multinationals function more effectively. 4.1

Political System: A country's political system affects its product, labour, and capital markets. In socialist societies like China, for instance, workers cannot form independent trade unions in the labour market, which affects wage levels. 4.1

Religion: Is linked to individual values as well as holiday celebrations, often tied to consumer preferences and spending patterns. 4.6

Segmentation: This is an important strategic tool in international marketing because the main difference between calling a firm international and global is based on the scope and bases of segmentation. An international firm has different marketing strategies for different segments of countries, while a global firm views the whole world as a market, and then segments this whole world based on viable segmentation bases. 4.5

Social-Class: Bands such as wealthy, middle, and lower classes. The rich, for instance, may want different products than the middle and lower classes and may be willing to pay more. 4.6

Technocracy: The wide-scale adoption of the Internet by US consumers has led to massive technological innovation for financial-services companies, increasing the range of distribution channels as well as the products, services, and geographic scope of financial-services organizations. Regulations and other changes in the playing field, however, have been slow to follow. 4.4

CHAPTER 5: COMPETING IN A GLOBAL MARKETPLACE

Chapter Overview

5.0 INTRODUCTION

Learning Objectives

After reading this chapter, you should be able to:

1. Describe the strategic analysis process and why firms need to analyze their competitive environment.
2. Discuss the importance of SWOT analysis when looking at global competitors.
3. Outline a PESTEL analysis.
4. Identify what makes up a firm's external macro environment.
5. Identify what makes up a firm's external micro environment.
6. Explain Porter's Five Forces.
7. Discuss the strategy in building a firm's competitive advantage.
8. Explain the elements that go into determining a firm's strategic position.

Exploring Managerial Careers

Lauri Goodman Lampson, Planning Design Research Corporation

Lauri Goodman Lampson is president and CEO of Planning Design Research Corporation, a firm that analyzes work environments to understand how employees work and what kind of spaces and facilities they need to do their best, most productive work (PDR, 2016). Lampson was hired by

Accenture, a consulting firm, to evaluate and improve its location in Houston. Accenture's Houston office was a three-story, 66,000-square-foot building that served 800 employees (Steelcase, n.d.). Accenture employees are consultants themselves, and they typically spend up to two-thirds of their working time away from the office serving clients.

Lampson worked with Accenture director of workplaces Dan Johnson and Steelcase, an office furniture manufacturer, to study how Accenture was using its Houston space. To achieve this outcome, Lampson and Steelcase analyzed employee demographics and expectations and studied how employees actually interacted with each other and performed tasks in the workplace. Accenture wanted to have a workspace that fostered its corporate goals of: worker innovation, collaboration, and flexibility (Steelcase, 2011).

Understanding a firm's strengths is an important step in strategic analysis, and Lampson's focus on supporting those strengths in the workplace environment led to Workplace 2.0, Accenture's reimagined facility. Not only does the new workspace provide better physical and technological support for collaboration among Accenture employees, but Lampson and Steelcase were able to identify opportunities for Accenture to significantly reduce the size of its offices. Accenture saves money by using less space (it was able to downsize to a single floor of 25,000 square feet to serve the same number of workers) and supports worker interaction and engagement by providing a more effective workspace. You can watch a video of this transformation here: **Accenture Case Study [YouTube]**

5.1 GAINING ADVANTAGES BY UNDERSTANDING THE COMPETITIVE ENVIRONMENT

Strategic analysis is the process that firms use to study and understand the many different layers and aspects of their competitive environment. Why do firms spend time and money trying to understand what is going on around them? Firms do not operate in a vacuum. They are impacted by forces and factors from inside their organizations and outside in the world at large. Understanding these forces and factors is crucial to achieving success as a business. For example, the growth in the Spanish-speaking population in the United States has led many firms to change the signage in their stores and labels on their products to include Spanish, in order to make their stores easier to shop in and their products easier to identify for this growing market. The external environment is continually changing, and the most successful firms are able to prepare for and adapt to environmental changes because they have done their homework and understand how external forces impact their operations.

To react to change more easily and develop products consumers want, managers and consultants engage in **environmental scanning**—the systematic and intentional analysis of both a firm's internal state and its external, competitive environment. From a local coffee shop to an international corporation, firms of all sizes benefit from strategic analysis. Let's examine some important strategic factors in more detail.

The Competitive Environment

A firm's **competitive environment** includes components inside the firm and outside the firm. **External factors** are things in the global environment that may impact a firm's operations or success, examples are a rise in interest rates, or a natural disaster. External factors cannot be controlled, but they must be managed effectively and to understand them so that the firm can be as successful. For example, the unemployment rate will affect a firm's ability to hire qualified employees at a reasonable rate of pay. If unemployment is high, meaning that a lot of people are looking for jobs, then a firm will probably have a lot of applicants for any positions it needs to fill. It will be able to choose more highly qualified applicants to hire and may be able to hire them at a lower pay rate because the employee would rather work for a lower pay rate than not have a job at all. On the other hand, when unemployment is low, meaning that not many people are looking for jobs, firms may have to offer higher pay or settle for lower qualifications to find someone to fill a position.

Internal factors are characteristics of the firm itself. To plan to compete against other firms, a firm needs to understand what physical, financial, and human resources it has, what it is good at, and how it is organized.

For example, Walmart has a sophisticated IT system that tracks inventory and automatically orders products before they run out, by calculating how long it will take for the new product to arrive and comparing that to the rate at which the product is selling off the shelves. The system orders new product so that it will arrive just as the product on the shelves is running out, so that Walmart stores do not need to have storage space for inventory. All Walmart inventory is on the store shelves, ready to be sold to customers. How does this system benefit Walmart? It does not have to spend money on storing or keeping track of inventory, all products in the store can generate revenue because they are available for customers to buy, and when the system is working optimally, the store never runs out of items customers want.

5.2 USING SWOT FOR STRATEGIC ANALYSIS

You may already have heard of one very common tool firms use to analyze their strategic and competitive situations: **SWOT**, which is an acronym for **s**trengths, **w**eaknesses, **o**pportunities, and **t**hreats. Firms use SWOT analysis to get a general understanding of what they are good or bad at and what factors outside their doors might present chances for success or difficulty. Let's take a look at SWOT analysis piece by piece (Figure 5.1).

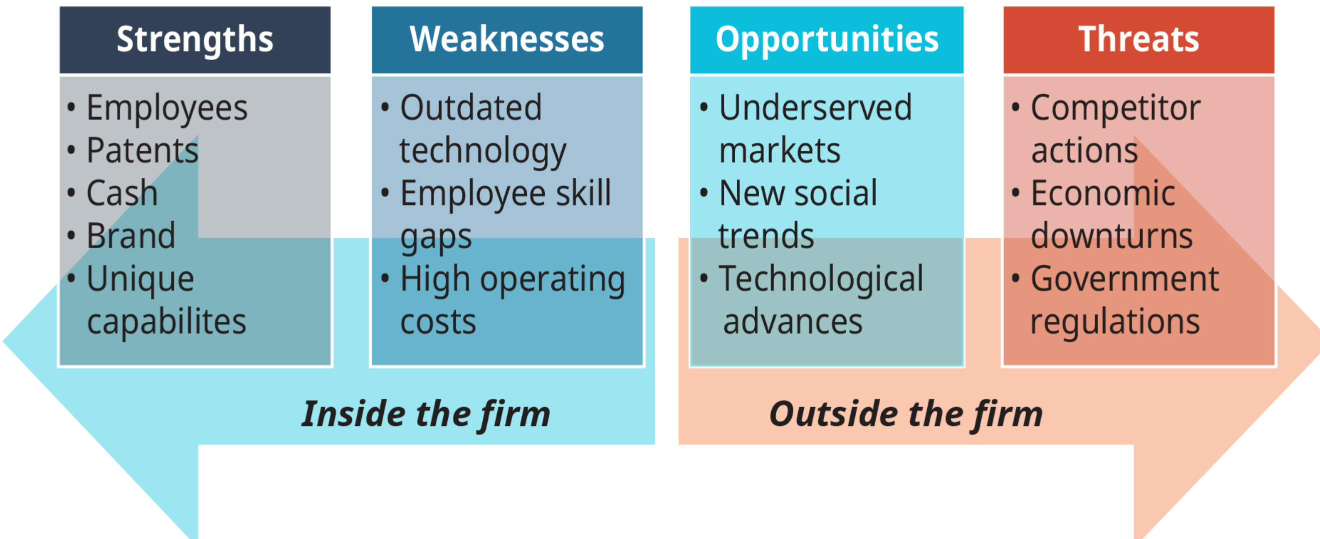

Fig. 5.1 The Components of SWOT Image © Rice University & OpenStax, CC BY 4.0

Strengths

A firm's **strengths** are, to put it simply, what it is good at. Nike is good at marketing sports products, McDonald's is good at making food quickly and inexpensively, and Ferrari is good at making beautiful fast cars. When a firm analyzes its strengths, it compiles a list of its capabilities and assets. Does the firm have a lot of cash available? That is a strength. Does the firm have highly skilled employees? Another strength. Knowing exactly what it is good at allows a firm to make plans that exploit those strengths. Nike can plan to expand its business by making products for a sport it doesn't currently serve. Its sports marketing expertise will help it successfully launch that new product line.

Weaknesses

A firm's **weaknesses** are what it is not good at—things that it does not have the capabilities to perform well. Weaknesses are not necessarily faults—remember that not all firms can be great at all things. When a firm understands its weaknesses, it will avoid trying to do things it does not have the skills or assets to succeed in, or it will find ways to improve its weaknesses before undertaking something new. A firm's weaknesses are simply gaps in capabilities, and those gaps do not always have to be filled within the firm.

SWOT analysis alerts firms to the gaps in their capabilities so they can work around them, find help in those areas, or develop capabilities to fill the gaps. For example, Paychex is a firm that handles payroll for over 600,000 firms (Paychex, 2017). Paychex processes hours, pay rates, tax and benefits deductions, and direct deposit for firms that would rather not have to perform those tasks themselves. A large firm would need to have a team of employees dedicated to fulfilling that task and equip that team with software systems to do the job efficiently and accurately. For Paychex, these capabilities are a company strength—that's what it does. Other companies that do not have the resources to develop this capability or may not be interested in doing so can hire Paychex to do the job for them.

Opportunities

While strengths and weaknesses are internal to an organization, but opportunities and threats are always external. An **opportunity** is a potential situation that a firm is equipped to take advantage of. Think of opportunities in terms of things that happen in the market. Opportunities offer positive potential, however sometimes a firm is not equipped to take advantage of an opportunity which is why considering the entire SWOT is important before deciding what to do. For example, as cities are becoming more populated, parking is becoming scarcer. Younger consumers who live in cities are starting to question whether it makes sense to own a car at all, when public transportation is available and parking is not. Sometimes, however, a person might need a car to travel outside the city or transport a special purchase. Daimler, the manufacturer of Mercedes-Benz and Smart cars, started a car-sharing service in Europe, North America, and China called Car2Go to offer cars to this new market of part-time drivers. By establishing Car2Go, Daimler has found a way to sell the use of its products to people who would not buy them outright.

Threats

When a manager assesses the external competitive environment, she labels anything that would make it harder for her firm to be successful as a **threat**. A wide variety of situations and scenarios can threaten a firm's chances of success, from a downturn in the economy to a competitor launching a better version of a product the firm also offers. A good threat assessment looks thoroughly at the external environment and identifies threats to the firm's business so it can be prepared to meet them. Opportunities and threats can also be a matter of perspective or interpretation: the Car2Go service that Daimler developed to serve young urban customers who don't own cars could also be cast as a defensive response to the trend away from car ownership in this customer group. Daimler could have identified decreasing sales among young urban professionals as a threat and developed Car2Go as an alternative way to gain revenue from these otherwise lost customers.

The Limitations of SWOT Analysis

Although a SWOT analysis can identify important factors and situations that affect a firm, it only works as well as the person doing the analysis. SWOT can generate a good evaluation of the firm's internal and external environments, but it is more likely to overlook key issues because it is difficult to identify or imagine everything that could, for example, be a threat to the firm. That's why the remainder of this chapter will present tools for developing a strategic analysis that is more thorough and systematic in examining both the internal and external environments that firms operate in.

5.3 A FIRM'S EXTERNAL MACRO ENVIRONMENT: PESTEL

The world at large forms the **external environment** for businesses. A firm must confront, adapt to, take advantage of, and defend itself against what is happening in the world around it to succeed. To make gathering and interpreting information about the external environment easier, strategic analysts have defined several general categories of activities and groups that managers should examine and understand. Figure 5.2 illustrates layers and categories found in a firm's environment.

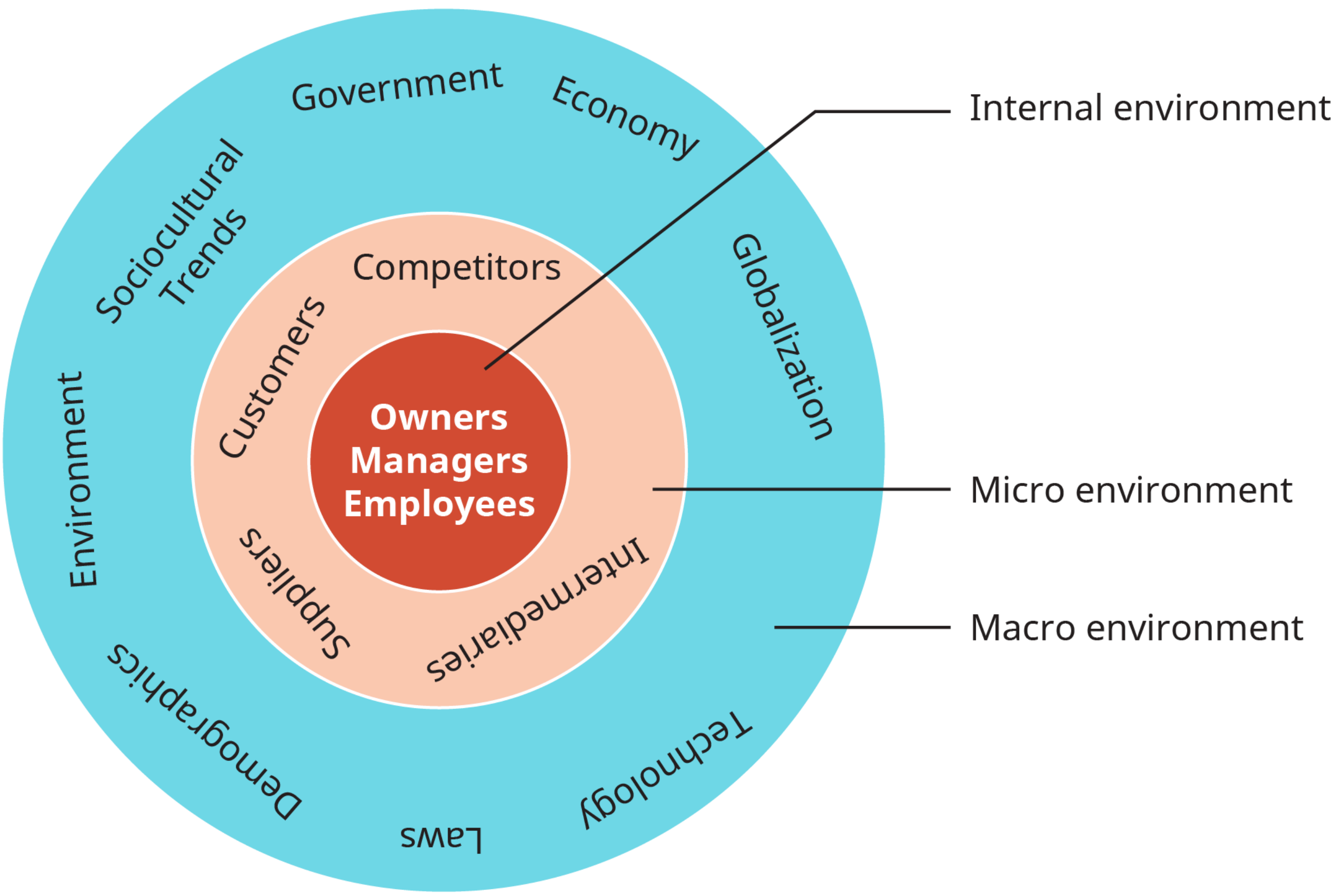

Fig. 5.2 Components of a Firm's Environment

A firm's **macro environment** contains elements that can impact the firm but are generally beyond its direct control. These elements are characteristics of the world at large and are factors that all businesses must contend with, regardless of the industry they are in or type of business they are. In the Figure 5.2, the macro environment is indicated in blue. Note that the terms contained in the blue ring are all "big-picture" items that exist independently of business activities. That is not to say that they do not affect firms or that firm activities cannot affect macro environmental elements; both can and do happen, but firms are largely unable to directly change things in the macro environment.

Strategists study the macro environment to learn about facts and trends that may present opportunities or threats to their firms. However, they do not usually just think in terms of SWOT. Strategists have developed more discerning tools to examine the external environment.

PESTEL Analysis

PESTEL analysis is an important and widely used tool that helps show the big picture of a firm's external environment, particularly as related to foreign markets. PESTEL is an acronym for the political, economic, sociocultural, technological, environmental, and legal contexts in which a firm operates. A PESTEL analysis helps managers gain a better understanding of the opportunities and threats they face; consequently, the analysis aids in building a better vision of the future business landscape and how the firm might compete profitably. This useful tool analyzes for market growth or decline and, therefore, the position, potential, and direction for a business. When a firm is considering entry into new markets, these factors are of considerable importance. Moreover, PESTEL analysis provides insight into the status of key market *flatteners*, both in terms of their present state and future trends.

Firms need to understand the macroenvironment to ensure that their strategy is aligned with the powerful forces of change affecting their business landscape. When firms exploit a change in the environment—rather than simply survive or oppose the change—they are more likely to be successful. A solid understanding of PESTEL also helps managers avoid strategies that may be doomed to fail given the circumstances of the environment.

Finally, understanding PESTEL is critical prior to entry into a new country or region. The fact that a strategy is congruent with PESTEL in the home environment gives no assurance that it will also align in other countries. For example, when Lands' End, the online clothier, sought to expand its operations into Germany, it ran into local laws prohibiting it from offering unconditional guarantees on its products. In the United States, Lands' End had built a reputation for quality on its no-questions-asked money-back guarantee. However, this was considered illegal under Germany's regulations governing incentive offers and price discounts. The political skirmish between Lands' End and the German government finally ended when the regulations banning unconditional guarantees were abolished. While the restrictive regulations didn't put Lands' End out of business in Germany, they did inhibit its growth there until the laws were abolished.

There are three steps in the PESTEL analysis. First, consider the relevance of each of the PESTEL factors to your context. Next, identify and categorize the information that applies to these factors. Finally, analyze the data and draw conclusions. Common mistakes in this analysis include stopping at the second step or assuming that the initial analysis and conclusions are correct without testing the assumptions and investigating alternative scenarios.

Examples of elements analyzed in each of these segments are shown in Table 5.1.

Table 5.1 PESTEL Analysis

Political	**Economic**
How stable is the political environment?	What are current and forecasted interest rates?
What are local taxation policies, and how do these affect your business?	What is the level of inflation, what is it forecast to be, and how does this affect the growth of your market?
Does the government have trade agreements such as EU, NAFTA, ASEAN, or others?	What are local employment levels per capita and how are they changing?
What are the foreign trade regulations?	What are the long-term prospects for the economy gross domestic product (GDP) per capita, and so on?
What are the social welfare policies?	What are exchange rates between critical markets and how will they affect production and distribution of your goods?
Social or Socio-cultural	**Technical or Technological**
What are local lifestyle trends?	What is the level of research funding in government and the industry, and are those levels changing?
What are the current demographics, and how are they changing?	What is the government and industry's level of interest and focus on technology?
What is the level and distribution of education and income?	How mature is the technology?
What are the dominant local religions and what influence do they have on consumer attitudes and opinions?	What is the status of intellectual property issues in the local environment?
What is the level of consumerism and popular attitudes toward it?	Are potentially disruptive technologies in adjacent industries creeping in at the edges of the focal industry?
What pending legislation is there that affects corporate social policies (e.g., domestic partner benefits, maternity/paternity leave)?	How fast is technology changing? How is its pace impacting the industry?
What are the attitudes toward work and leisure?	What role does technology play in competitive advantage?
Environmental	**Legal**
What are local environmental issues?	What are the regulations regarding monopolies and private property?
Are there any ecological or environmental issues relevant to your industry that are pending?	Does intellectual property have legal protections?
How do the activities of international pressure groups affect your business (e.g., Greenpeace, Earth First, PETA)?	Are there relevant consumer laws?
Are there environmental protection laws? What are the regulations regarding waste disposal and energy consumption?	What is the status of employment, health and safety, and product safety laws?

Figure 5.3 illustrates the components of PESTEL, which will be discussed individually below.

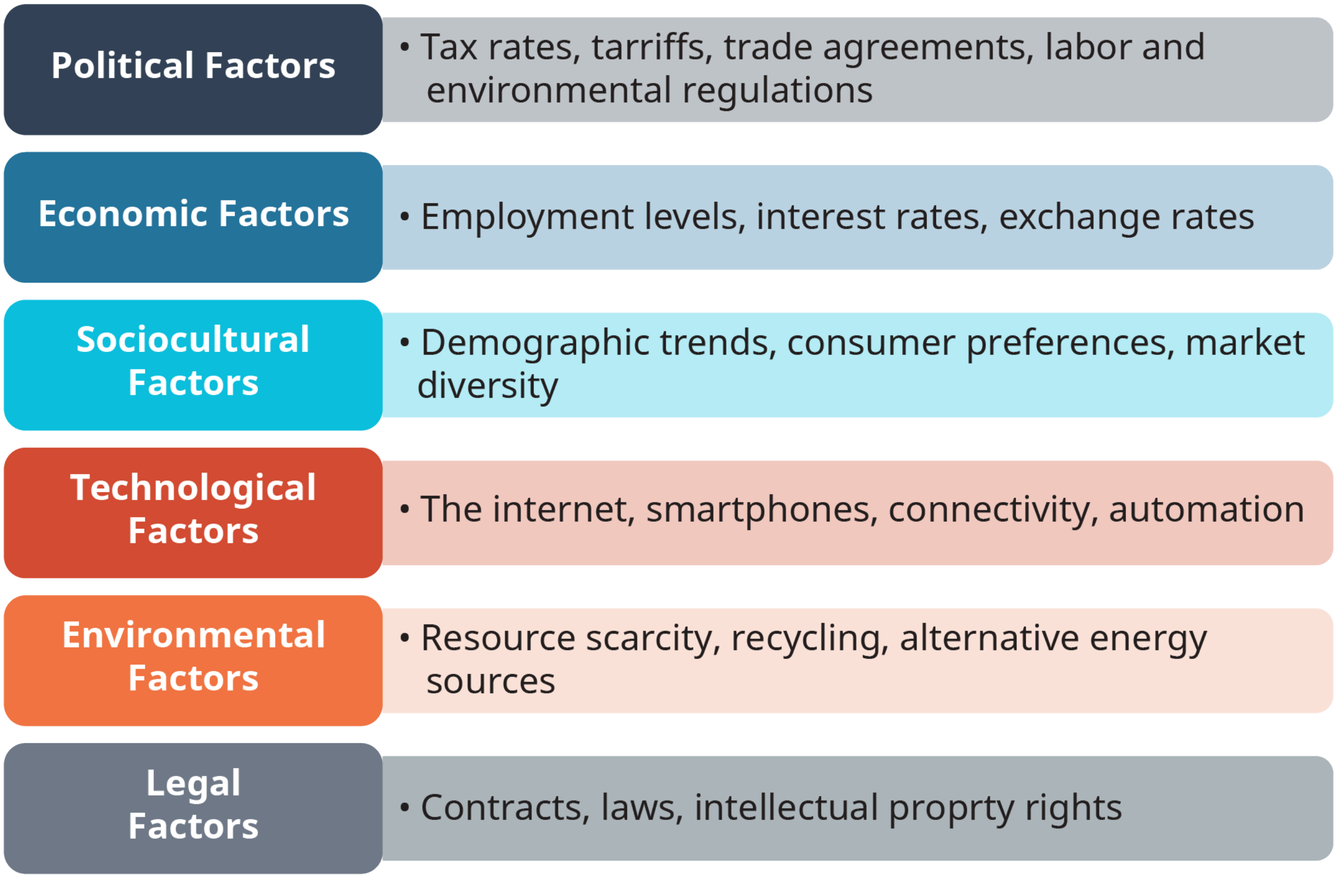

Fig 5.3 The PESTEL Model for External Environmental Analysis

Political Factors

Political factors in the macro environment include taxation, tariffs, trade agreements, labour regulations, and environmental regulations. Note that in PESTEL, factors are not characterized as opportunities or threats. They are simply things that a firm can take advantage of or treat as problems, depending on its own interpretation or abilities. American Electric Power, a large company that generates and distributes electricity, may be negatively impacted by environmental regulations that restrict its ability to use coal to generate electricity because of pollution caused by burning coal. However, another energy firm has taken advantage of the government's interest in reducing coal emissions by developing a way to capture the emissions while producing power. The Petra Nova plant, near Houston, was developed by NRG and JX Nippon, who received Energy Department grants to help fund the project (Mooney, 2017). Although firms do not directly make government policy decisions, many industries and firms invest in lobbying efforts to try to influence government policy development to create opportunities or reduce threats.

Economic Factors

All firms are impacted by the state of the national and global economies. The increased interdependence of individual country economies has made evaluating the **economic factors** in a firm's macro environment more complex. Firms analyze economic indicators to make decisions about entering or exiting geographic markets, investing in expansion, and hiring or laying off employees. As discussed earlier in this chapter, employment rates impact the quantity, quality, and cost of employees available to firms. Interest rates impact sales of big-ticket items that consumers normally finance, such as appliances, cars, and homes. Interest rates also impact the cost of capital for firms that want to invest in expansion. Exchange rates present risks and opportunities to all firms that operate across national borders, and the price of oil impacts many industries, from airlines and transportation companies to solar panel producers and plastic recycling companies. Once again, any scenario can be a threat to one firm and an opportunity to another, so economic forces should not be assumed to be intrinsically good or bad.

Sociocultural Factors

Quite possibly the largest category of macro environmental factors an analyst might examine are **sociocultural factors**. This broad category encompasses everything from changing national demographics to fashion trends and many things in between. **Demographics**, a subset of this category, includes facts about income, education levels, age groups, and the ethnic and racial composition of a population. All of these facts present market challenges and possibilities. Firms can target products to specific market segments by studying the needs and preferences of demographic groups, such as working women (they might need day-care services but not watch daytime television), college students (who would be interested in affordable textbooks but couldn't afford to buy new cars), or the elderly (who would be willing to pay for lawn-mowing services but might not be interested in adventure tourism).

Changes in people's values and interests are also included in this category. Environmental awareness has spurred demand for solar panels and electric and hybrid cars. A general interest in health and fitness has created industries in gyms, home gym equipment, and organic food. The popularity of social media has created an enormous demand for instant access to information and services, not to mention smartphones. Values and interests are constantly changing and vary from country to country, creating new market opportunities as well as communication challenges for companies trying to enter unfamiliar new markets.

Technological Factors

The rise of the Internet may be the most disruptive technological change of the last century. The globe has become more interconnected and interdependent because of the fast, low-cost communications the Internet provides. Customer service agents in India can serve customers in Kansas because technology has advanced to the point that the customer's account information can be instantly accessed by the service provider in India. Entrepreneurs around the world can reach customers anywhere through companies such as eBay, Alibaba, and Etsy, and they can get paid, regardless of their customers' currency, through PayPal. The Internet has enabled Jeff Bezos, who started an online bookselling company called Amazon in 1994, to transform how consumers shop for goods.

How else have **technological factors** impacted business? The Internet is not the only technological advance that has transformed how businesses operate. Automation has increased efficiency for manufacturers. MRP (materials requirement planning) systems have changed how companies and their suppliers work together, and global-positioning technology has helped construction engineers manage large projects more accurately. Consumers and firms have nearly unlimited access to information, and this access has empowered consumers to make more-informed buying decisions and challenged firms to develop ways to analyze the large amounts of data their businesses generate.

Environmental Factors

The physical environment, which provides natural resources for manufacturing and energy production, has always been a key part of human business activity. As resources become scarcer and more expensive, **environmental factors** impact businesses more every day. Firms are developing technology to operate more cleanly and using fewer resources. Political pressure on businesses to reduce their impact on the natural environment has increased globally and dramatically in the 21st century. In 2017, London, Barcelona, and Paris announced their plans to ban cars with internal combustion engines over the next few decades, in order to combat air-quality issues (Smith, 2017).

This external environment category often overlaps with others in PESTEL because concern for the environment is also a sociocultural trend, as more consumers look for recycled products and buy electric and hybrid cars. On the political front, firms are facing increased regulation around the world on their carbon emissions and natural resource use. Although SWOT would characterize these factors as either opportunities or threats, PESTEL simply identifies them as aspects of the external environment that firms must consider when planning for their futures.

Legal Factors

Legal factors in the external environment often coincide with political factors because laws are enacted by government entities. This does not mean that the categories identify the same issues, however. Although labour laws and environmental regulations have deep political connections, other legal factors can impact business success. For example, in the streaming video industry, licensing fees are a significant cost for firms. Netflix pays billions of dollars every year to movie and television studios for the right to broadcast their content. In addition to the legal requirement to pay the studios, Netflix must consider that consumers may find illegal ways to view the movies they want to see, making them less willing to pay to subscribe to Netflix. Intellectual property rights and patents are major issues in the legal realm.

Note that some external factors are difficult to categorize in PESTEL. For instance tariffs can be viewed as either a political or economic factor while the influence of the internet could be viewed as either a technological or social factor. While some issues can overlap two or more PESTEL areas, it does not diminish the value of PESTEL as an analytical tool.

Impact of PESTEL Factors on an Entire Industry

As coronavirus's impact continued to expand, regulators in countries such as the U.K. began urging companies to conduct risk assessments. The outbreak has caused damage to supply chains in China and internationally. The debt and asset positions of many companies have been affected, the share prices of international companies, and the volume of business in China have fallen sharply. The PESTEL analysis confirms its importance. The whole business environment will be affected by similar emergencies in the future, and companies need to make strategic plans according to PESTEL to reduce their risks after emergencies (Ojea, 2020).

PESTEL and Globalization

Over the past decade, new markets have been opened to foreign competitors, whole industries have been deregulated, and state-run enterprises have been privatized. Globalization involves much more than companies simply exporting products to another country. Some industries that aren't normally considered global do, in fact, have strictly domestic players. But these companies often compete alongside firms with operations in multiple countries; in many cases, both sets of firms are doing equally well. In contrast, in a truly global industry, the core product is standardized, the marketing approach is relatively uniform, and competitive strategies are integrated in different international markets (Porter, 1986). In these industries, competitive advantage clearly belongs to the firms that can compete globally.

A number of factors reveal whether an industry has globalized or is in the process of globalizing. The sidebar below groups globalization factors into four categories: *markets*, *costs*, *governments*, and *competition*. These dimensions correspond well to Thomas Friedman's flatteners (as described in his book *The World Is Flat*), though they are not exhaustive (Friedman, 2005).

Factors Favouring Industry Globalization

1. Markets
   o Homogeneous customer needs

   o Global customer needs

   o Global channels

   o Transferable marketing approaches

2. Costs
   o Large-scale and large-scope economies

   o Learning and experience

   o Sourcing efficiencies

   o Favourable logistics

   o Arbitrage opportunities

   o High research-and-development (R&D) costs

3. Governments
   o Favourable trade policies

   o Common technological standards

   o Common manufacturing and marketing regulations

4. Competition

o Interdependent countries

o Global competitors(Porter, 1986).

Markets

The more similar markets in different regions are, the greater the pressure for an industry to globalize. Coca-Cola and PepsiCo, for example, are fairly uniform around the world because the demand for soft drinks is largely the same in every country. The airframe-manufacturing industry, dominated by Boeing and Airbus, also has a highly uniform market for its products; airlines all over the world have the same needs when it comes to large commercial jets.

Costs

In both of these industries, costs favour globalization. Coca-Cola and PepsiCo realize economies of scope and scale because they make such huge investments in marketing and promotion. Since they're promoting coherent images and brands, they can leverage their marketing dollars around the world. Similarly, Boeing and Airbus can invest millions in new-product R&D only because the global market for their products is so large.

Governments and Competition

Obviously, favourable trade policies encourage the globalization of markets and industries. Governments, however, can also play a critical role in globalization by determining and regulating technological standards. Railroad gauge—the distance between the two steel tracks—would seem to favour a simple technological standard. In Spain, however, the gauge is wider than in France. Why? Because back in the 1850s, when Spain and neighbouring France were hostile to one another, the Spanish government decided that making Spanish railways incompatible with French railways would hinder any French invasion.

These are a few key drivers of industry change. However, there are particular implications of technological and business-model breakthroughs for both the pace and extent of industry change. The *rate* of change may vary significantly from one industry to the next; for instance, the computing industry changes much faster than the steel industry. Nevertheless, change in both fields has prompted complete reconfigurations of industry structure and the competitive positions of various players. The idea that all industries change over time and that business environments are in a constant state of flux is relatively intuitive. As a strategic decision maker, you need to ask yourself this question: how accurately does current industry structure (which is relatively easy to identify) predict future industry conditions?

Importing as a Stealth Form of Internationalization

Ironically, the drivers of globalization have also given rise to a greater level of imports. Globalization in this sense is a very strong flattener. Importing involves the sale of products or services in one country that are sourced in another country. In many ways, importing is a stealth form of internationalization. Firms often claim that they have no international operations and yet—directly or indirectly—base their production or services on inputs obtained from outside their home country. Firms that engage in importing must learn about customs requirements, informed compliance with customs regulations, entry of goods, invoices, classification and value, determination and assessment of duty, special requirements, fraud, marketing, trade finance and insurance, and foreign trade zones. Importing can take many forms—from the sourcing of components, machinery, and raw materials to the purchase of finished goods for domestic resale and the outsourcing of production or services to nondomestic providers.

Outsourcing occurs when a company contracts with a third party to do some work on its behalf. The outsourcer may do the work within the same country or may take the work to another country (i.e., offshoring). Offshoring occurs when you take a function out of your country of residence to be performed in another country, generally at a lower cost. International outsourcing, or outsourcing work to a nondomestic third party, has become very visible in business and corporate strategy in recent years. But it's not a new phenomenon; for decades, Nike has been designing shoes and other apparel that are manufactured abroad. Similarly, Pacific Cycle doesn't make a single Schwinn or Mongoose bicycle in the United States but instead imports them entirely from manufacturers in Taiwan and China. It may seem as if international outsourcing is new because businesses are now more often outsourcing services, components, and raw materials from countries with developing economies (e.g., China, Brazil, and India).

In addition to factors of production, information technologies (IT)—such as telecommunications and the widespread diffusion of the Internet—have provided the impetus for outsourcing services. Business-process outsourcing (BPO) is the delegation of one or more IT-intensive business processes to an external provider that in turn owns, administers, and manages the selected process on the basis of defined and measurable performance criteria. The firms in service and IT-intensive industries—insurance, banking, pharmaceuticals, telecommunications, automotive, and airlines—are among the early adopters of BPO. Of these, insurance and banking are able to generate the bulk of the savings, purely because of the large proportion of processes that they can outsource (i.e., the processing of claims and loans and providing service through call centres). Among those countries housing BPO operations, India experienced the most dramatic growth in services where language skills and education were important.

Case: Sustainability and Responsible Management – *Can LEGO Give up Plastic?*

"In 2012, the LEGO Group first shared its ambition to find and implement sustainable alternatives to the current raw materials used to manufacture LEGO products by 2030. The ambition is part of the LEGO Group's work to reduce its environmental footprint and leave a positive impact on the planet our children will inherit." (Trangæk, 2015, para. 7).

Danish toy company LEGO announced in 2015 that it would invest almost $160 million dollars into its efforts to meet the goal it announced in 2012. You know LEGO—they are the coloured plastic bricks that snap together to make toys ranging from Harry Potter castles to Star Wars fighter craft. The family-owned company was founded in 1932 by Ole Kirk Christiansen and has since grown to be the world's number one toy brand (Brand Finance, 2017).

Given that LEGO and plastic seem to go hand in hand, why would the company want to give up on the material that makes their toys so successful? LEGO's manufacturing process relies on plastic to make highly precise plastic bricks that always fit together securely and easily. Replacing the plastic with another material that is durable, can be brightly coloured, and can be molded as precisely is a difficult task. LEGO's leadership has decided that a strategic position based on fossil fuels is not sustainable and is making plans now to transition to a more environmentally friendly material to manufacture its products.

Switching from oil-based plastic might make economic sense as well. Manufacturers who rely on petroleum-based products must weather volatile oil prices. LEGO's raw materials costs could skyrocket overnight if the price of oil climbs again as it did in 2011. That price spike was due to conflict in Libya and other parts of the Arab world (Holodny, 2016), something entirely beyond the control of any business.

Technological innovations in bio-based plastics may be the answer for LEGO (Peters, 2015), which is working with university researchers around the globe to find a solution to its carbon-footprint problem.

Critical Thinking Questions

1. How would you approach this issue if you were the manager in charge of sourcing raw materials for LEGO? How would PESTEL analysis inform your actions?
2. What PESTEL challenges is LEGO trying to address by changing the raw materials used in its products?
3. Explain what favorable PESTEL factors support LEGO's efforts.

5.4 A FIRM'S MICRO ENVIRONMENT: PORTER'S FIVE FORCES

A firm's **micro environment** is directly connected to the firm in some way, and firms must understand the micro environment in order to successfully compete in an industry. All firms are part of an **industry**—a group of firms all making similar products or offering similar services, for example, automobile manufacturers or airlines. Firms in an industry may or may not compete directly against one another, as we'll discuss shortly, but they all face similar situations in terms of customer interests, supplier relations, and industry growth or decline.

Harvard strategy professor Michael Porter developed an analysis tool to evaluate a firm's micro environment. **Porter's Five Forces** is a tool used to examine different micro-environmental groups in order to understand the impact each group has on a firm in an industry (Figure 5.4). Each of the forces represents an aspect of competition that affects a firm's potential to be successful in its industry. It is important to note that this tool is different than Porter's generic strategy typology that we will discuss later.

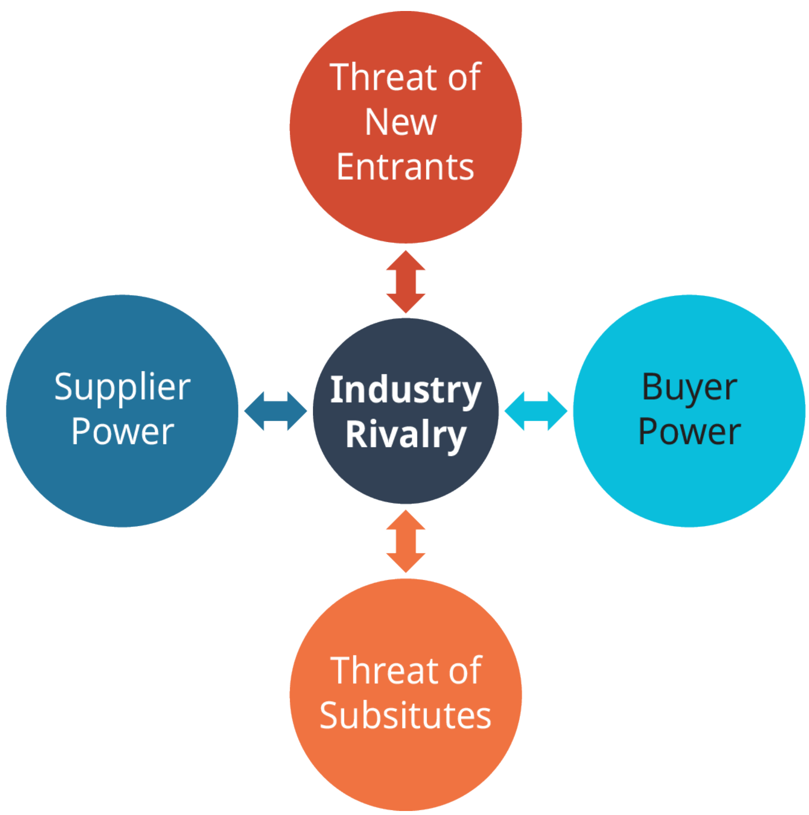

Fig. 5.4 Porter's Five Forces Model of Industry Competition
Image © Rice University & OpenStax, CC BY 4.0

Industry Rivalry

Industry rivalry, the first of Porter's forces, is in the centre of the diagram. Note that the arrows in the diagram show two-way relationships between rivalry and all of the other forces. This is because each force can affect how hard firms in an industry must compete against each other to gain customers, establish favourable supplier relationships, and defend themselves against new firms entering the industry.

When using Porter's model, an analyst will determine if each force has a strong or weak impact on industry firms. In the case of rivalry, the question of strength focuses on how hard firms must fight against industry rivals (competitors) to gain customers and market share. Strong rivalry in an industry reduces the profit potential for all firms because consumers have many firms from which to purchase products or services and can make at least part of their purchasing decisions based on prices. An industry with weak rivalry will have few firms, meaning that there are enough customers for everyone, or will have firms that have each staked out a unique position in the industry, meaning that customers will be more loyal to the firm that best meets their particular needs.

The Threat of New Entrants

In an industry, there are incumbent (existing) firms that compete against each other as rivals. If an industry has a growing market or is very profitable, however, it may attract **new entrants**. These either are firms that start-up in the industry as new companies or are firms from another industry that expand their capabilities or target markets to compete in an industry that is new to them.

Different industries may be easier or harder to enter depending on **barriers to entry**, and factors that prevent new firms from successfully competing in the industry. Common barriers to entry include cost, brand loyalty, and industry growth. For example, the firms in the airline industry rarely face threats from new entrants because it is very expensive to obtain the equipment, airport landing rights, and expertise to start up a new airline.

Brand loyalty can also keep new firms from entering an industry, because customers who are familiar with a strong brand name may be unwilling to try a new, unknown brand. Industry growth can increase or decrease the chances a new entrant will succeed. In an industry with low growth, new customers are scarce, and a firm can only gain market share by attracting customers from other firms. Think of all the ads you see and hear from competing cell phone providers. Cell phone companies are facing lower industry growth and must offer consumers incentives to switch from another provider. On the other hand, high-growth industries have an increasing number of customers, and new firms can successfully appeal to new customers by offering them something existing firms do not offer. It is important to note that barriers to entry are not always external, firms often lobby politicians for regulations that can be a barrier to entry. These types of barriers will be covered in greater depth in more upper-level courses.

Threat of Substitutes

In the context of Porter's model, a **substitute** is any other product or service that can satisfy the same need of a customer as an industry's offerings. Be careful not to confuse substitutes with rivals. Rivals offer similar products or services and directly compete with one another. Substitutes are completely different products or services that consumers would be willing to use instead of the product they currently use. For example, the fast-food industry offers quickly prepared, convenient, low-cost meals. Customers can go to McDonald's, Wendy's, Burger King, or Taco Bell—all of these firms compete against each other for business. However, their customers are really just hungry people. What else could you do if you were hungry? You could go to the grocery store and buy food to prepare at home. McDonald's does not directly compete against Kroger for customers because they are in different industries, but McDonald's does face a threat from grocery stores because they both sell food. How does McDonald's defend itself from the threat of Kroger as a substitute? By making sure their food is already prepared and convenient to purchase—your burger or salad is ready to eat and available without even getting out of your car.

Supplier Power

Virtually all firms have suppliers who sell parts, materials, labour, or products. **Supplier power** refers to the balance of power in the relationship between firms and their suppliers in an industry. Suppliers can have the upper hand in a relationship if they offer specialized products or control rare resources. For example, when Sony develops a new PlayStation model, it often works with a single supplier to develop the most advanced processor chip it can for their game console. That means its supplier will be able to command a fairly high price for the processors, an indication that the supplier has power. On the other hand, a firm that needs commodity resources such as oil, wheat, or aluminum in its operations will have many suppliers to choose from and can easily switch suppliers if price or quality is better from a new partner. Commodity suppliers usually have low power.

Buyer Power

The last of Porter's forces is **buyer power**, which refers to the balance of power in the relationship between a firm and its customers. If a firm provides a unique good or service, it will have the power to charge its customers premium prices, because those customers have no choice but to buy from the firm if they need that product. In contrast, when customers have many potential sources for a product, firms will need to attract customers by offering better prices or better value for the money if they want to sell their products. One protection firms have against buyer power is **switching costs**, the penalty consumers face when they choose to use a particular product made by a different company. Switching costs can be financial (the extra price paid to choose a different product) or practical (the time or hassle required to switch to a different product). For example, think about your smartphone. If you have an iPhone now, what would be the penalty for you to switch to a non-Apple smartphone? Would it just be the cost of the new phone? Smartphones are not inexpensive, but even when cell phone service providers offer free phones to new customers, many people still don't switch. The loss of compatibility with other Apple products, the need to transfer apps and phone settings to another system, and the loss of favourite iPhone features, such as iMessage, are enough to keep many people loyal to their iPhones.

5.5 THE INTERNAL ENVIRONMENT

The **internal environment** consists of members of the firm itself, investors in the firm, and the assets a firm has. Employees and managers are good examples; they are firm members who have skills and knowledge that are valuable assets to their firms. Evaluating a firm's internal environment is not just a matter of counting heads, however. Successful firms have a wide range of resources and capabilities that they can use to maintain their success and grow into new ventures. A thorough analysis of a firm's internal situation provides a manager with an understanding of the resources available to pursue new initiatives, innovate, and plan for future success.

Resources and Capabilities

A firm's resources and capacities are the unique skills and assets it possesses. **Resources** are things a firm has to work with, such as equipment, facilities, raw materials, employees, and cash. **Capabilities** are things a firm can do, such as deliver good customer service or develop innovative products to create value. Both are the building blocks of a firm's plans and activities, and both are required if a firm is going to compete successfully against its rivals. Firms use their resources and leverage their capabilities to create products and services that have some advantage over competitors' products. For example, a firm might offer its customers a product with higher quality, better features, or lower prices. Not all resources and capabilities are equally helpful in creating success, though. Internal analysis identifies exactly which assets bring the most value to the firm.

The Value Chain

Before examining the role of resources and capabilities in firm success, let's take a look at the importance of how a firm uses those factors in its operations. A firm's **value chain** is the progression of activities it undertakes to create a product or service that consumers will pay for. A firm should be adding value at each of the chain of steps it follows to create its product. The goal is for the firm to add enough value so that its customers will believe that the product is worth buying for a price that is higher than the costs the firm incurs in making it. As an example, Figure 5.5 illustrates a hypothetical value chain for some of Walmart's activities.

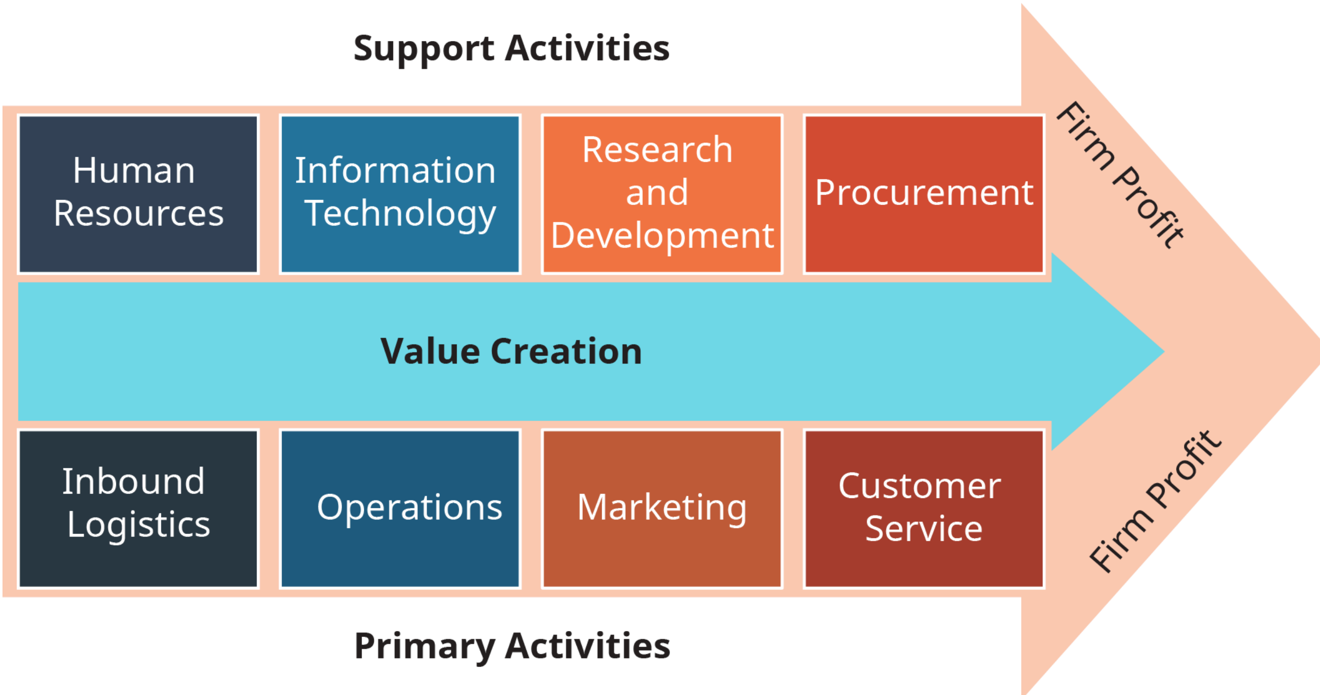

Fig. 5.5 A Value Chain Example

In this example, note that value increases from left to right as Walmart performs more activities. If it adds enough value through its efforts, it will profit when it finally sells its services to customers. By working with product suppliers (procurement), getting those products to store locations efficiently (inbound logistics), and automatically keeping track of sales and inventory (information technology), Walmart is able to offer its customers a wide variety of products in one store at low prices, a service customers value. **Primary activities**, the ones across the bottom half of the diagram, are the actions a firm takes to directly provide a product or service to customers. **Support activities**, the ones across the top of the diagram, are actions required to sustain the firm that are not directly part of product or service creation.

Using Resources and Capabilities to Build an Advantage over Rivals

A firm's resources and capabilities are not just a list of equipment and things it can do. Instead, resources and capabilities are the distinctive assets and activities that separate firms from each other. Firms that can amass critical resources and develop superior capabilities will succeed in competition over rivals in their industry. Strategists evaluate firm resources and capabilities to determine if they are sufficiently special to help the firm succeed in a competitive industry.

Using VRIO

The analytical tool used to assess resources and capabilities is called **VRIO**. As usual, this is an acronym developed to remind managers of the questions to ask when evaluating their firms' resources and capabilities. The four questions of VRIO, which focus on **v**alue, **r**arity, **i**mitation, and **o**rganization, are illustrated in Figure 5.6.

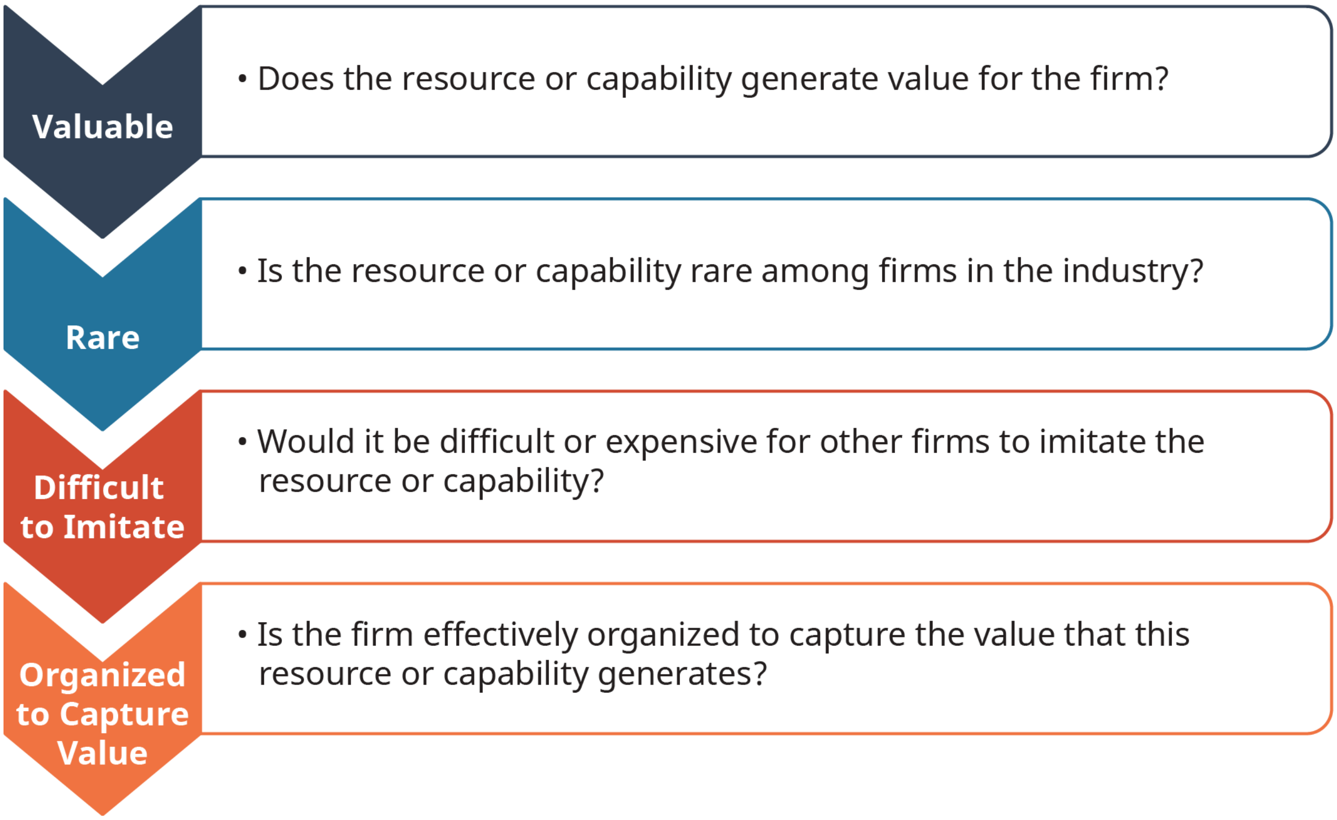

Fig. 5.6 VRIO, a Tool for Evaluating Firm Resources and Capabilities

If each question can be answered with a "yes," then the resource or capability being evaluated can be the source of a competitive advantage for the firm. An example will help you better understand the VRIO process.

Imagine that you are a top manager for Starbucks and you want to understand why you are able to be successful against rivals in the coffee industry. You make a list of some of Starbucks' resources and capabilities and use VRIO to determine which ones are key to your success. These are shown in Table 5.2.

Table 5.2 – © Rice University & OpenStax, CC BY 4.0 license

Starbucks' Resources and Capabilities	
Resources	**Capabilities**
Brand name	Making quality coffee drinks
Thousands of locations worldwide	Delivering excellent customer service
Cash	Training excellent staff
Loyal customers	Paying above-average wages
Well-trained employees	Retaining quality employees

You look at your list and decide to pick a few of the entries to evaluate with VRIO (**Table 5.3**):

Table 5.3: – © Rice University & OpenStax, CC BY 4.0

Evaluating Starbucks' VRIO					
Resource/Capability	**Is it valuable?**	**Is it rare?**	**Is it difficult to imitate?**	**Is Starbucks organized to capture its value?**	**Can it be a basis for competitive advantage?**
Brand name	Yes	Yes	Yes	Yes	Yes
Delivering excellent customer service	Yes	Yes	Yes	Yes	Yes
Thousands of locations worldwide	Yes	No	No	Yes	No

According to the evaluation above, Starbucks' brand helps it compete and succeed against rivals, as does its excellent customer service. However, simply having a lot of locations globally isn't enough to beat rivals—McDonald's and Subway also have thousands of worldwide locations, and both serve coffee. Starbucks succeeds against them because of their brand and customer service.

Case: Uber, Lyft, and the Self-Driving Car

Although the ride-sharing industry is still relatively new, it has seen explosive growth, and its two main rivals, Uber and Lyft, are looking for ways to increase their capacity to serve riders. Both firms, and rivals like them, operate in basically the same way. A person needing a ride uses a smartphone app to alert a nearby person with a car of their location. The driver, usually an independent contractor for the service (meaning they are just a person with a car that has signed up to provide rides in exchange for a portion of the fare the customer pays), picks up the customer and drives them to their destination.

The popularity of ride-sharing services has soared, and both companies are constantly recruiting more drivers. However, both companies have also explored alternatives to independent drivers: self-driving cars. Uber and Lyft have taken different paths to develop this capability. Uber has worked to internally develop its own software technology and self-driving car technology, while Lyft has focused on software interfaces that can accommodate other companies' self-driving cars (Bensinger, 2017). Lyft's partnerships with firms such as Google and GM that are already developing self-driving cars has put it ahead of Uber in the race to get driverless vehicles into its ride-sharing network, and it was able to test self-driving cars in Boston by partnering with NuTonomy in 2017 (Edelstein, 2017). Lyft offered a demonstration to journalists at the Consumer Electronics Show in Las Vegas in 2018, offering rides in self-driving cars developed by Aptiv (O'Kane, 2018). Uber had been testing similar technology in Pittsburgh but suspended its self-driving car program after a fatal pedestrian accident in Arizona (Korosec, 2018).

Critical Thinking Questions

1. What resource or capability challenges have Uber and Lyft faced because their fast company growth?
2. What PESTEL factors do you think are contributing to the popularity of ride-sharing services?
3. What industry challenges (think of Porter's Five Forces) does the use of self-driving cars address?

5.6 COMPETITION, STRATEGY, AND COMPETITIVE ADVANTAGE

Now that you understand more about the environment that businesses operate in, let's take a deeper look at exactly how they operate. Businesses exist to make profits by offering goods and services in the marketplace at prices that are higher than the costs they incurred creating those goods and services. Businesses rarely exist alone in an industry; **competition** is a usually a key part of any marketplace. This means that businesses must find ways to attract customers to their products and away from competitors' products. **Strategy** is the process of planning and implementing actions that will lead to success in competition.

The analytical tools we discuss here are part of the strategic planning process. Managers cannot successfully plan to compete in an industry if they don't understand its competitive landscape. It is also unlikely that a firm planning to launch a new product they are not equipped to make will be successful.

Competition

Porter's Five Forces model is centred around rivalry, a synonym for competition. In any industry, multiple firms compete against each other for customers by offering better or cheaper products than their rivals. Firms use PESTEL to understand what consumers are interested in and use VRIO to evaluate their own resources and capabilities so that they can figure out how to offer products and services that match those consumer interests and that are better in quality and price than the products offered by their competitors.

A firm is described as having a **competitive advantage** when it successfully attracts more customers, earns more profit, or returns more value to its shareholders than rival firms do. A firm achieves a competitive advantage by adding value to its products and services or reducing its own costs more effectively than its rivals in the industry.

Generic Business-Level Competitive Strategies

When discussing business strategy, a business is a firm or a unit of a firm that centres its activities around one primary type of product or service line. Business-level strategy is the general way that a business organizes its activities to compete against rivals in its product's industry. Michael Porter (the same Harvard professor who developed the Five Forces Model) defined three **generic business-level strategies** that outline the basic methods of organizing to compete in a product market. He called the strategies "generic" because these ways of organizing can be used by any firm in any industry.

Cost Leadership

When pursuing a **cost-leadership strategy**, a firm offers customers its product or service at a lower price than its rivals can. To achieve a competitive advantage over rivals in the industry, the successful cost leader tightly controls costs throughout its value chain activities. Supplier relationships are managed to guarantee the lowest prices for parts, manufacturing is conducted in the least expensive labour markets, and operations may be automated for maximum efficiency. A cost leader must spend as little as possible producing a product or providing a service so that it will still be profitable when selling that product or service at the lowest price. Walmart is the master of cost leadership, offering a wide variety of products at lower prices than competitors because it does not spend money on fancy stores, it extracts low prices from its suppliers, and its pays its employees relatively low wages.

Differentiation

Not all products or services in the marketplace are offered at low prices, of course. A **differentiation strategy** is exactly the opposite of a cost-leadership strategy. While firms do not look to spend as much as possible to produce their output, firms that differentiate try to add value to their products and services so they can attract customers who are willing to pay a higher price. At each step in the value chain, the differentiator increases the quality, features, and overall attractiveness of its products or services. Research and development efforts focus on innovation, customer service is excellent, and marketing bolsters the value of the firm brand. These efforts guarantee that the successful differentiator can still profit even though its production costs are higher than a cost leader's. Starbucks is a good example of a differentiator: it makes coffee, but its customers are willing to pay premium prices for a cup of Starbucks coffee because they value the restaurant atmosphere, customer service, product quality, and brand.

Porter's typology assumes that firms can succeed through either cost leadership or differentiation. Trying to combine these two, Porter suggests, can lead to a firm being stuck in the middle.

Focus

Porter's third generic competitive strategy, **focus**, is a little different from the other two. A firm that focuses still must choose one of the other strategies to organize its activities. It will still strive to lower costs or add value. The difference here is that a firm choosing to implement a focused strategy will concentrate its marketing and selling efforts on a smaller market than a broad cost leader or differentiator. A firm following a focus-differentiation strategy, for example, will add value to its product or service that a few customers will value highly, either because the product is specifically suited to a particular use or because it is a luxury product that few can afford. For example, Flux is a company that offers custom-made bindings for your snowboard. Flux is a focus differentiator because it makes a specialized product that is valued by a small market of customers who are willing to pay premium prices for high-quality, customized snowboarding equipment.

Strategic Groups

When managers analyze their competitive environment and examine rivalry within their industry, they are not confronted by an infinite variety of competitors. Although there are millions of businesses of all sizes around the globe, a single business usually competes mainly against other businesses offering similar products or services and following the same generic competitive strategy. Groups of businesses that follow similar strategies in the same industry are called **strategic groups**, and it is important that a manager know the other firms in their strategic group. Rivalry is fiercest within a strategic group, and the actions of one firm in a group will elicit responses from other group members, who don't want to lose market share in the industry. Take a look at Figure 5.7: although all of the firms shown are in the retail industry, they don't all compete directly against one another.

Fig. 5.7 Strategic Groups in the Retail Industry
Image © Rice University & OpenStax, CC BY 4.0

Although some cross competition can occur (for example, you could buy a Kate Spade wallet at Nordstrom), firms in different strategic groups tend to compete more with each other than against firms outside their group. Although Walmart and Neiman Marcus both offer a wide variety of products, the two firms do not cater to the same customers, and their managers do not lose sleep at night wondering what each might do next. On the other hand, a Walmart manager would be concerned with the products or prices offered at Target; if laundry detergent is on sale at Target, the Walmart manager might lose sales from customers who buy it at Target instead, and so the Walmart manager might respond to Target's sale price by discounting the same detergent at Walmart.

5.7 STRATEGIC POSITIONING

Photo by Pixabay, CC0 1.0.

A manager who has done all of the analysis described so far in this chapter has some decisions to make based on all of the information the analysis has revealed. A firm's decisions on how to serve customers and compete against rivals is called **strategic positioning**. In order to develop its position, a firm combines its understanding of the competitive environment, including the firm's own resources and capabilities, its industry situation, and facts about the macro environment. A strategic position includes a choice of generic competitive strategy, which a firm selects based on its own capabilities and in response to the positions already staked out by its industry rivals. The firm also determines which customers to serve and what those customers are willing to pay for. A strategic position also includes decisions about what geographic markets to participate in.

Most importantly, a firm's strategic position should try to be unique in some way that competitors cannot imitate quickly or easily. Competitive advantage is achieved when a firm attracts more customers or makes more profit than rivals. This cannot happen unless the firm organizes its activities to provide customers with better value than rivals.

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5.9 KEY TERMS

Key Terms

Barriers To Entry: Factors that prevent new firms from successfully competing in the industry. 5.4

Buyer Power: Which refers to the balance of power in the relationship between a firm and its customers. 5.4

Capabilities Are things a firm can do, such as deliver good customer service or develop innovative products to create value. 5.5

Competition Business: Actions a firm undertakes to attract customers to its products and away from competitors' products. 5.6

Competitive Advantage: When it successfully attracts more customers, earns more profit, or returns more value to its shareholders than rival firms do. 5.6

Competitive Environment: Factors and situations both inside the firm and outside the firm that has the potential to impact its operations and success. 5.1

Cost-Leadership Strategy: A generic business-level strategy in which a firm tightly controls costs throughout its value chain activities in order to offer customers low-priced goods and services at a profit. 5.6

Demographics: A subset of this category, includes facts about income, education levels, age groups, and the ethnic and racial composition of a population. All of these facts present market challenges and possibilities. 5.3

Differentiation Strategy: A generic business-level strategy in which firms add value to their products and services in order to attract customers who are willing to pay a higher price. 5.6

Economic Factors: PESTEL category that includes facts (such as unemployment rates, interest rates, and commodity prices) about the state of the local, national, or global economy. 5.3

External Factors: PESTEL category examines a firm's external situation with respect to the natural environment, including pollution, natural resource availability and preservation, and alternative energy. 5.1

Environmental Scanning: the systematic and intentional analysis of both a firm's internal state and its external, competitive environment. From a local coffee shop to an international corporation, firms of all sizes benefit from strategic analysis 5.1

External Environment for Businesses: A firm must confront, adapt to, take advantage of, and defend itself against what is happening in the world around it to succeed. To make gathering and interpreting information about the external environment easier, strategic analysts have defined several general categories of activities and groups that managers should examine and understand. 5.3

External Factors: Things in the world or industry environments that may impact a firm's operations or success, such as the economy, government actions, or supplier power. Strategic decisions can be made in response to these things but normally cannot directly influence or change them. 5.3

Focus: A firm that focuses still must choose one of the other strategies to organize its activities. It will still strive to lower costs or add value. The difference here is that a firm choosing to implement a focused strategy will concentrate its marketing and selling efforts on a smaller market than a broad cost leader or differentiator. 5.6

Focus Strategy: A generic business-level competitive strategy that firms use in combination with either a cost-leadership or differentiation strategy in order to target a smaller demographic or geographic market with specialized products or services. 5.6

Generic Business-Level Strategies: Basic methods of organizing firm value chain activities to compete in a product market that can be used by any sized firm in any industry. 5.6

Industry: a group of firms all making similar products or offering similar services, for example, automobile manufacturers or airlines. 5.4

Internal Environment: Consists of members of the firm itself, investors in the firm, and the assets a firm has. Employees and managers are good examples; they are firm members who have skills and knowledge that are valuable assets to their firms. 5.5

Internal Factors: Are characteristics of the firm itself. To plan to compete against other firms, a firm needs to understand what physical, financial, and human resources it has, what it is good at, and how it is organized. 5.1

Legal Factors: In PESTEL, the laws impacting business, such as those governing contracts and intellectual property rights and illegal activities, such as online piracy. 5.3

Macro Environment: The outermost layer of elements in a firm's external environment that can impact a business but are generally beyond the firm's direct control, such as the economy and political activity. 5.3

Micro Environment: The middle layer of elements in a firm's external environment, primarily concerned with a firm's industry situation. 5.3

New Entrants: One of Porter's Five Forces, the threat of new entrants assesses the potential that a new firm will start operations in an industry. 5.4

Opportunity: This is a potential situation that a firm is equipped to take advantage of. 5.2

PESTEL: A strategic analysis tool that examines several distinct categories in the macro-environment: political, economic, sociocultural, technological, environmental, and legal. 5.3

Political Factors: PESTEL factor that identifies political activities in the macro-environment that may be relevant to a firm's operations. 5.3

Porter's Five Forces: Evaluate the interconnected relationships between various actors in the industry, including competing firms, their suppliers, and their customers, by examining five forces: industry rivalry, the threat of new entrants, the threat of substitutes, supplier power, and buyer power. 5.4

Primary Activities: Firm activities on the value chain that are directly responsible for creating, selling, or servicing a product or service, such as manufacturing and marketing. 5.5

Resources: These are things a firm has to work with, such as equipment, facilities, raw materials, employees, and cash. 5.5

Sociocultural Factors: PESTEL category that identifies trends, facts, and changes in society's composition, tastes, and behaviours, including demographics. 5.3

Strategic Analysis: This is the process that firms use to study and understand the many different layers and aspects of their competitive environment. 5.1

Strategic Groups: Businesses offering similar products or services and following the same generic competitive strategy. 5.6

Strategic Positioning: A firm's decisions on how to serve customers and compete against rivals 5.6

Strategy: This is the process of planning and implementing actions that will lead to success in competition. 5.6

Strengths: Are, to put it simply, what it is good at. 5.2

Substitute: One of Porter's Five Forces; is products or services outside a firm's industry that can satisfy the same customer needs as industry products or services can. 5.4

Supplier Power: One of Porter's Five Forces; describes the balance of power in the relationship between firms in an industry and their suppliers. 5.4

Support Activities: Value chain activities that a firm performs to sustain itself; do not directly create a product or service but are necessary to support the firm's existence, such as accounting and human resources. 5.5

Switching Costs: Penalty, financial or otherwise, that a consumer bears when giving up the use of a product currently being used to select a competing product or service. 5.4

SWOT: is an acronym for strengths, weaknesses, opportunities, and threats. Firms use SWOT analysis to get a general understanding of what they are good or bad at and what factors outside their doors might present chances for success or difficulty. 5.2

Technological Factors: PESTEL category includes factors such as the Internet, social media, automation, and other innovations that impact how businesses compete or how they manufacture, market, or sell their goods or services. 5.3

Threat: Anything in the competitive environment that would make it harder for a firm to be successful. 5.2

Value Chain: Sequence of activities that firms perform to turn inputs (parts or supplies) into outputs (goods or services). 5.5

VRIO: An analytical tool that evaluates a firm's resources and capabilities to determine whether or not it can support an advantage for the firm in the competitive environment: value, rarity, imitation, and organization. 5.5

Weaknesses: Things that a firm does not have good capabilities to perform or gaps in firm resources. 5.2

CHAPTER 6: GLOBAL MARKET ENTRY MODES

Chapter Outline

6.0 Introduction

6.1 International Entry Modes

6.2 Exporting

6.3 Licensing

6.4 Franchising

6.5 Contract Manufacturing

6.6 Joint Ventures

6.7 Chapter References

6.8 Key Terms

6.0 INTRODUCTION

Learning Objectives

After reading this section, students should be able to:

1. Define and describe the five common international-expansion entry modes.
2. Discuss the advantages and disadvantages of each entry mode.
3. Explain why companies would select each mode of entry.

Companies that wish to move beyond exporting and importing can avail themselves of a wide range of alternative market entry strategies. Each alternative has distinct advantages and disadvantages associated with it; the alternatives can be ranked on a continuum representing increasing levels of investment, commitment, and risk. Licensing can generate revenue flow with little new investment; it can be a good choice for a company that possesses advanced technology, a strong brand image, or valuable intellectual property. Contract manufacturing and franchising are two specialized forms of licensing that are widely used in global marketing.

A higher level of involvement outside the home country may involve foreign direct investment. This can take many forms. Joint ventures offer two or more companies the opportunity to share risk and combine value chain strengths. Companies considering joint ventures must plan carefully and communicate with partners to avoid "divorce." Foreign direct investment can also be used to establish company operations outside the home country through greenfield investment, acquisition of a minority or majority equity stake in a foreign business, or taking full ownership of an existing business entity through merger or outright acquisition.

Cooperative alliances known as strategic alliances, strategic international alliances, and global strategic partnerships (GSPs) represent an important market entry strategy in the twenty-first century. GSPs are ambitious, reciprocal, cross-border alliances that may involve business partners in a number of different country markets. GSPs are particularly well suited to emerging markets in Central and Eastern Europe, Asia, and Latin America. Western businesspeople should also be aware of two special forms of cooperation found in Asia, namely Japan's keiretsu and South Korea's chaebol.

6.1 INTERNATIONAL ENTRY MODES

The Five Common International-Expansion Entry Modes

Fig 6.1 "5 Common International expansion entry modes" by Alyssa Giles, CC BY-NC-SA 4.0.

What is the best way to enter a new market? Should a company first establish an export base or license its products to gain experience in a newly targeted country or region? Or does the potential associated with first-mover status justify a bolder move such as entering an alliance, making an acquisition, or even starting a new subsidiary? Many companies move from exporting to licensing to a higher investment strategy, in effect treating these choices as a learning curve. Each has distinct advantages and disadvantages. In this section, we will explore the traditional international-expansion entry modes. Beyond importing, international expansion is achieved through exporting, licensing arrangements, partnering and strategic alliances, acquisitions, and establishing new, wholly owned subsidiaries, also known as greenfield ventures. These modes of entering international markets and their characteristics are shown in Table 6.1 "International-Expansion Entry Modes" (Zahra et al., 2000). Each mode of market entry has advantages and disadvantages. Firms need to evaluate their options to choose the entry mode that best suits their strategy and goals.

Table 6.1 International-Expansion Entry Modes

Type of Entry	Advantages	Disadvantages
Exporting	Fast-entry, low financial risk, diversified revenue source	Low control, low local knowledge, potential negative environmental impact of transportation, cultural and language barriers, transportation costs and complexities
Licensing and Franchising	Fast-entry, low-cost, low-risk, shared marketing costs, potential for rapid global expansion	Less control, licensee may become a competitor, legal and regulatory environment (IP and contract law) must be sound, quality/brand control challenges, royalty and franchise fees
Partnering and Strategic Alliance	Shared costs reduce investment needed, reduced risk, seen as local entity, access to new markets and customers, rapid market entry	Higher cost than exporting, licensing, or franchising; integration problems between two corporate cultures, risk of sharing sensitive information, lack of full control
Acquisition	Fast entry into a new market, established operations, access to local distribution channels	High upfront cost, integration issues with home office, cultural differences
Greenfield Venture (Launch of a new, wholly owned subsidiary)	Gain local market knowledge; can be seen as an insider who employs locals; maximum control	High initial investment, high risk due to unknowns, longer time to establish operations, lack of local market knowledge

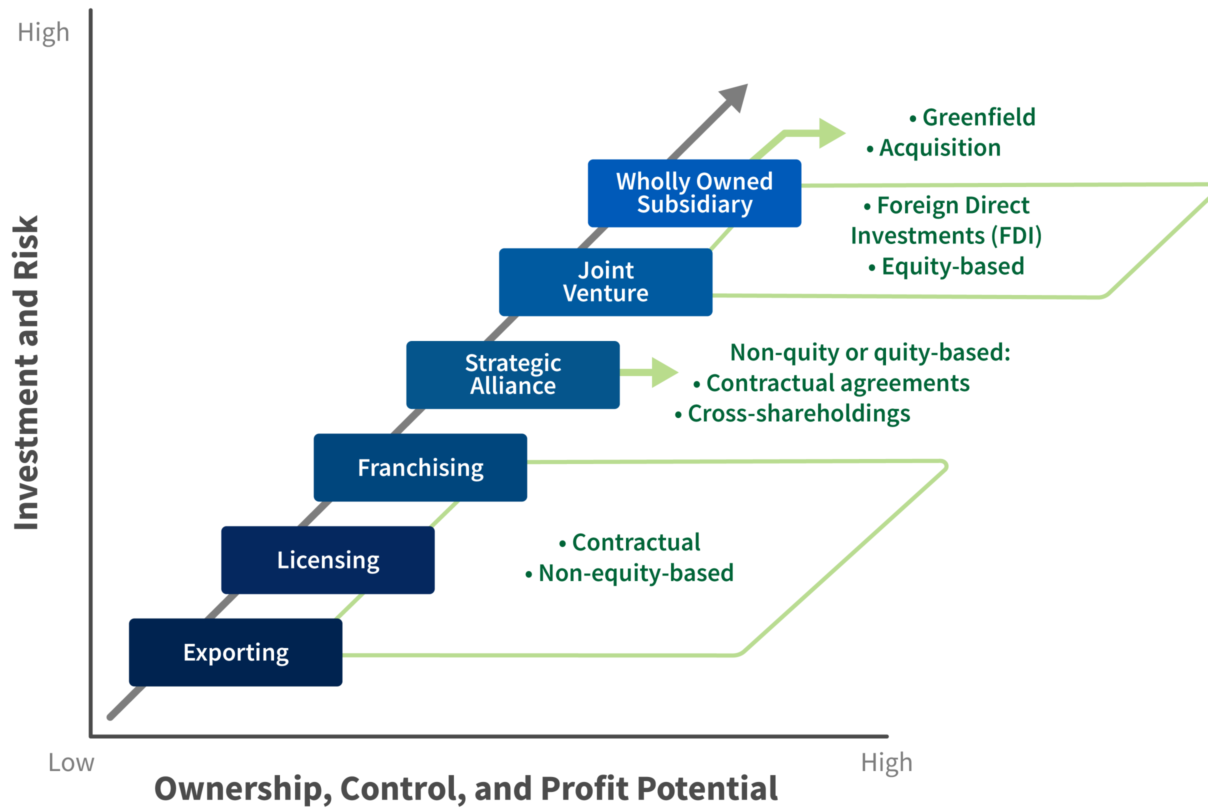

Fig 6.2 Entering International Markets adapted from original: Colour change

Exporting

Exporting is the marketing and direct sale of domestically produced goods in another country. Exporting is a traditional and well-established method of reaching foreign markets. Since it does not require that the goods be produced in the target country, no investment in foreign production facilities is required. Most of the costs associated with exporting take the form of marketing expenses.

While relatively low risk, exporting entails substantial costs and limited control. Exporters typically have little control over the marketing and distribution of their products, face high transportation charges and possible tariffs, and must pay distributors for a variety of services. What is more, exporting does not give a company firsthand experience in staking out a competitive position abroad, and it makes it difficult to customize products and services to local tastes and preferences.

Exporting is a typically the easiest way to enter an international market, and therefore most firms begin their international expansion using this model of entry. Exporting is the sale of products and services in foreign countries that are sourced from the home country. The advantage of this mode of entry is that firms avoid the expense of establishing operations in the new country. Firms must, however, have a way to distribute and market their products in the new country, which they typically do through contractual agreements with a local company or distributor. When exporting, the firm must give thought to labelling, packaging, and pricing the offering appropriately for the market. In terms of marketing and promotion, the firm will need to let potential buyers know of its offerings, be it through advertising, trade shows, or a local sales force.

Amusing Anecdotes

One common factor in exporting is the need to translate something about a product or service into the language of the target country. This requirement may be driven by local regulations or by the company's wish to market the product or service in a locally friendly fashion. While this may seem to be a simple task, it's often a source of embarrassment for the company and humour for competitors. David Ricks's book on international business blunders relates the following anecdote for US companies doing business in the neighbouring French-speaking Canadian province of Quebec. A company boasted of *lait frais usage*, which translates to "used fresh milk," when it meant to brag of *lait frais employé*, or "fresh milk used." The "terrific" pens sold by another company were instead promoted as *terrifiantes*, or terrifying. In another example, a company intending to say that its appliance could use "any kind of electrical current," actually stated that the appliance "wore out any kind of liquid." And imagine how one company felt when its product to "reduce heartburn" was advertised as one that reduced "the warmth of heart" (Ricks, 1999).

Among the disadvantages of exporting are the costs of transporting goods to the country, which can be high and can have a negative impact on the environment. In addition, some countries impose tariffs on incoming goods, which will impact the firm's profits. In addition, firms that market and distribute products through a contractual agreement have less control over those operations and, naturally, must pay their distribution partner a fee for those services.

Ethics in Action

Companies are starting to consider the environmental impact of where they locate their manufacturing facilities. For example, Olam International, a cashew producer, originally shipped nuts grown in Africa to Asia for processing. Now, however, Olam has opened processing plants in Tanzania, Mozambique, and Nigeria. These locations are close to where the nuts are grown. The result? Olam has lowered its processing and shipping costs by 25 percent while greatly reducing carbon emissions (Kramer, 2011).

Likewise, when Walmart enters a new market, it seeks to source produce for its food sections from local farms that are near its warehouses. Walmart has learned that the savings it gets from lower transportation costs and the benefit of being able to restock in smaller quantities more than offset the lower prices it was getting from industrial farms located farther away. This practice is also a win-win for locals, who have the opportunity to sell to Walmart, which can increase their profits and let them grow and hire more people and pay better wages. This, in turn, helps all the businesses in the local community (Kramer, 2011).

Firms export mostly to countries that are close to their facilities because of the lower transportation costs and the often greater similarity between geographic neighbours. For example, Mexico accounts for 40 percent of the goods exported from Texas (Cassey, 2011).

The Internet has also made exporting easier. Even small firms can access critical information about foreign markets, examine a target market, research the competition, and create lists of potential customers. Even applying for export and import licenses is becoming easier as more governments use the Internet to facilitate these processes.

Because the cost of exporting is lower than that of the other entry modes, entrepreneurs and small businesses are most likely to use exporting as a way to get their products into markets around the globe. Even with exporting, firms still face the challenges of currency exchange rates. While larger firms have specialists that manage the exchange rates, small businesses rarely have this expertise. One factor that has helped reduce the number of currencies that firms must deal with was the formation of the European Union (EU) and the move to a single currency, the euro, for the first time. As of 2011, seventeen of the twenty-seven EU members use the euro, giving businesses access to 331 million people with that single currency (The Euro, 2011).

Licensing and Franchising

A company that wants to get into an international market quickly while taking only limited financial and legal risks might consider licensing agreements with foreign companies.

An international licensing agreement allows a foreign company (the *licensee*) to sell the products of a producer (the *licensor*) or to use its intellectual property (such as patents, trademarks, copyrights) in exchange for royalty fees. Here's how it works: You own a company in the United States that sells coffee-flavoured popcorn. You're sure that your product would be a big hit in Japan, but you don't have the resources to set up a factory or sales office in that country. You can't make the popcorn here and ship it to Japan because it would get stale. So you enter into a licensing agreement with a Japanese company that allows your licensee to manufacture coffee-flavoured popcorn using your special process and to sell it in Japan under your brand name. In exchange, the Japanese licensee would pay you a royalty fee.

Licensing essentially permits a company in the target country to use the property of the licensor. Such property is usually intangible, such as trademarks, patents, and production techniques. The licensee pays a fee in exchange for the rights to use the intangible property and possibly for technical assistance as well.

Because little investment on the part of the licensor is required, licensing has the potential to provide a very large return on investment. However, because the licensee produces and markets the product, potential returns from manufacturing and marketing activities may be lost. Thus, licensing reduces cost and involves limited risk. However, it does not mitigate the substantial disadvantages associated with operating from a distance. As a rule, licensing strategies inhibit control and produce only moderate returns.

Another popular way to expand overseas is to sell franchises. Under an international franchise agreement, a company (the *franchiser*) grants a foreign company (the *franchisee*) the right to use its brand name and to sell its products or services. The franchisee is responsible for all operations but agrees to operate according to a business model established by the franchiser. In turn, the franchiser usually provides advertising, training, and new-product assistance. Franchising is a natural form of global expansion for companies that operate domestically according to a franchise model, including restaurant chains, such as McDonald's and Kentucky Fried Chicken, and hotel chains, such as Holiday Inn and Best Western.

Contract Manufacturing and Outsourcing

Because of high domestic labour costs, many U.S. companies manufacture their products in countries where labour costs are lower. This arrangement is called international contract manufacturing or outsourcing. A U.S. company might contract with a local company in a foreign country to manufacture one of its products. It will, however, retain control of product design and development and put its own label on the finished product. Contract manufacturing is quite common in the U.S. apparel business, with most American brands being made in a number of Asian countries, including China, Vietnam, Indonesia, and India (Gereffi & Frederick, 2010).

Thanks to twenty-first-century information technology, nonmanufacturing functions can also be outsourced to nations with lower labour costs. U.S. companies increasingly draw on a vast supply of relatively inexpensive skilled labour to perform various business services, such as software development, accounting, and claims processing. For years, American insurance companies have processed much of their claims-related paperwork in Ireland. With a large, well-educated population with English language skills, India has become a centre for software development and customer-call centres for American companies. In the case of India, the attraction is not only a large pool of knowledge workers but also significantly lower wages.

Partnerships and Strategic Alliances

Another way to enter a new market is through a strategic alliance with a local partner. A strategic alliance involves a contractual agreement between two or more enterprises stipulating that the involved parties will cooperate in a certain way for a certain time to achieve a common purpose. To determine if the alliance approach is suitable for the firm, the firm must decide what value the partner could bring to the venture in terms of both tangible and intangible aspects. The advantages of partnering with a local firm are that the local firm likely understands the local culture, market, and ways of doing business better than an outside firm. Partners are especially valuable if they have a recognized, reputable brand name in the country or have existing relationships with customers that the firm might want to access. For example, Cisco formed a strategic alliance with Fujitsu to develop routers for Japan. In the alliance, Cisco decided to co-brand with the Fujitsu name so that it could leverage Fujitsu's reputation in Japan for IT equipment and solutions while still retaining the Cisco name to benefit from Cisco's global reputation for switches and routers (Steinhilber, 2008). Similarly, Xerox launched signed strategic alliances to grow sales in emerging markets such as Central and Eastern Europe, India, and Brazil (Association for Strategic Alliance Professionals, 2010).

Strategic alliances and joint ventures have become increasingly popular in recent years. They allow companies to share the risks and resources required to enter international markets. And although returns also may have to be shared, they give a company a degree of flexibility not afforded by going it alone through direct investment.

There are several motivations for companies to consider a partnership as they expand globally, including (a) facilitating market entry, (b) risk and reward sharing, (c) technology sharing, (d) joint product development, and (e) conforming to government regulations. Other benefits include political connections and distribution channel access that may depend on relationships.

Such alliances often are favourable when (a) the partners' strategic goals converge while their competitive goals diverge; (b) the partners' size, market power, and resources are small compared to the industry leaders; and (c) partners are able to learn from one another while limiting access to their own proprietary skills.

What if a company wants to do business in a foreign country but lacks the expertise or resources? Or what if the target nation's government doesn't allow foreign companies to operate within its borders unless it has a local partner? In these cases, a firm might enter into a strategic alliance with a local company or even with the government itself. A strategic alliance is an agreement between two companies (or a company and a nation) to pool resources in order to achieve business goals that benefit both partners. For example, Viacom (a leading global media company) has a strategic alliance with Beijing Television to produce Chinese-language music and entertainment programming (Viacom International, 2004).

An alliance can serve a number of purposes:

- Enhancing marketing efforts
- Building sales and market share
- Improving products
- Reducing production and distribution costs
- Sharing technology

Strategic alliances are also advantageous for small entrepreneurial firms that may be too small to make the needed investments to enter the new market themselves. In addition, some countries require foreign-owned companies to partner with a local firm if they want to enter the market. For example, in Saudi Arabia, non-Saudi companies looking to do business in the country are required by law to have a Saudi partner. This requirement is common in many Middle Eastern countries. Even without this type of regulation, a local partner often helps foreign firms bridge the differences that otherwise make doing business locally impossible. Walmart, for example, failed several times over nearly a decade to effectively grow its business in Mexico, until it found a strong domestic partner with similar business values.

The disadvantages of partnering, on the other hand, are lack of direct control and the possibility that the partner's goals differ from the firm's goals. David Ricks, who has written a book on blunders in international business, describes the case of a US company eager to enter the Indian market: "It quickly negotiated terms and completed arrangements with its local partners. Certain required documents, however, such as the industrial license, foreign collaboration agreements, capital issues permit, import licenses for machinery and equipment, etc., were slow in being issued. Trying to expedite governmental approval of these items, the US firm agreed to accept a lower royalty fee than originally stipulated. Despite all of this extra effort, the project was not greatly expedited, and the lower royalty fee reduced the firm's profit by approximately half a million dollars over the life of the agreement (Ricks, 1999)." Failing to consider the values or reliability of a potential partner can be costly, if not disastrous.

To avoid these missteps, Cisco created one globally integrated team to oversee its alliances in emerging markets. Having a dedicated team allows Cisco to invest in training the managers how to manage the complex relationships involved in alliances. The team follows a consistent model, using and sharing best practices for the benefit of all its alliances (Steinhilber, 2008).

The key issues to consider in a joint venture are ownership, control, length of agreement, pricing, technology transfer, local firm capabilities and resources, and government intentions. Potential problems include (a) conflict over asymmetric new investments, (b) mistrust over proprietary knowledge, (c) performance ambiguity, that is, how to "split the pie," (d) lack of parent firm support, (e) cultural clashes, and (f) if, how, and when to terminate the relationship.

Ultimately, most companies will aim at building their own presence through company-owned facilities in important international markets. *Acquisitions* or greenfield start-ups represent this ultimate commitment. Acquisition is faster, but starting a new, wholly owned subsidiary might be the preferred option if no suitable acquisition candidates can be found.

Acquisitions

An acquisition is a transaction in which a firm gains control of another firm by purchasing its stock, exchanging the stock for its own, or, in the case of a private firm, paying the owners a purchase price. In our increasingly flat world, cross-border acquisitions have risen dramatically. In recent years, cross-border acquisitions have made up over 60 percent of all acquisitions completed worldwide. Acquisitions are appealing because they give the company quick, established access to a new market. However, they are expensive, which in the past had put them out of reach as a strategy for companies in the undeveloped world to pursue. What has changed over the years is the strength of different currencies. The higher interest rates in developing nations has strengthened their currencies relative to the dollar or euro. If the acquiring firm is in a country with a strong currency, the acquisition is comparatively cheaper to make. As Wharton professor Lawrence G. Hrebiniak explains, "Mergers fail because people pay too much of a premium. If your currency is strong, you can get a bargain (Knowledge at Wharton, 2010)."

When deciding whether to pursue an acquisition strategy, firms examine the laws in the target country. China has many restrictions on foreign ownership, for example, but even a developed-world country like the United States has laws addressing acquisitions. For example, you must be an American citizen to own a TV station in the United States. Likewise, a foreign firm is not allowed to own more than 25 percent of a US airline (Knowledge at Wharton, 2010).

Acquisition is a good entry strategy to choose when scale is needed, which is particularly the case in certain industries (e.g., wireless telecommunications). Acquisition is also a good strategy when an industry is consolidating. Nonetheless, acquisitions are risky. Many studies have shown that between 40 percent and 60 percent of all acquisitions fail to increase the market value of the acquired company by more than the amount invested (Knowlege at Wharton, 2010).

Foreign Direct Investment and Subsidiaries

Many of the approaches to global expansion that we've discussed so far allow companies to participate in international markets without investing in foreign plants and facilities. As markets expand, however, a firm might decide to enhance its competitive advantage by making a direct investment in operations conducted in another country.

Also known as foreign direct investment (FDI), acquisitions and greenfield start-ups involve the direct ownership of facilities in the target country and, therefore, the transfer of resources including capital, technology, and personnel. Direct ownership provides a high degree of control in the operations and the ability to better know the consumers and competitive environment. However, it requires a high level of resources and a high degree of commitment (Mandel, 2007).

Foreign direct investment refers to the formal establishment of business operations on foreign soil—the building of factories, sales offices, and distribution networks to serve local markets in a nation other than the company's home country. On the other hand offshoring occurs when the facilities set up in the foreign country replace U.S. manufacturing facilities and are used to produce goods that will be sent back to the United States for sale. Shifting production to low-wage countries is often criticized as it results in the loss of jobs for U.S. workers.

FDI is generally the most expensive commitment that a firm can make to an overseas market, and it's typically driven by the size and attractiveness of the target market. For example, German and Japanese automakers, such as BMW, Mercedes, Toyota, and Honda, have made serious commitments to the U.S. market: most of the cars and trucks that they build in plants in the South and Midwest are destined for sale in the United States.

A common form of FDI is the foreign subsidiary: an independent company owned by a foreign firm (called the *parent*). This approach to going international not only gives the parent company full access to local markets but also exempts it from any laws or regulations that may hamper the activities of foreign firms. The parent company has tight control over the operations of a subsidiary, but while senior managers from the parent company often oversee operations, many managers and employees are citizens of the host country. Not surprisingly, most very large firms have foreign subsidiaries. IBM and Coca-Cola, for example, have both had success in the Japanese market through their foreign subsidiaries (IBM-Japan and Coca-Cola–Japan). FDI goes in the other direction, too, and many companies operating in the United States are in fact subsidiaries of foreign firms. Gerber Products, for example, is a subsidiary of the Swiss company Novartis, while Stop & Shop and Giant Food Stores belong to the Dutch company Royal Ahold.

All these strategies have been successful in the arena of global business. But success in international business involves more than merely finding the best way to reach international markets. Doing global business is a complex, risky endeavour. As many companies have learned the hard way, people and organizations don't do things the same way abroad as they do at home. What differences make global business so tricky? That's the question that we'll turn to next.

Wholly Owned Subsidiaries

Firms may want to have a direct operating presence in the foreign country, completely under their control. To achieve this, the company can establish a new, wholly owned subsidiary (i.e., a greenfield venture) from scratch, or it can purchase an existing company in that country. Some companies purchase their resellers or early partners (as Vitrac Egypt did when it bought out the shares that its partner, Vitrac, owned in the equity joint venture). Other companies may purchase a local supplier for direct control of the supply. This is known as vertical integration.

Establishing or purchasing a wholly owned subsidiary requires the highest commitment on the part of the international firm because the firm must assume all of the risk—financial, currency, economic, and political.

The process of establishing a new, wholly owned subsidiary is often complex and potentially costly, but it affords the firm maximum control and has the most potential to provide above-average returns. The costs and risks are high given the costs of establishing a new business operation in a new country. The firm may have to acquire the knowledge and expertise of the existing market by hiring either host-country nationals—possibly from competitive firms—or costly consultants. An advantage is that the firm retains control of all its operations.

Case: Aritzia – Wholly Owned Subsidiaries

Photo by bargainmoose, CC BY 2.0

Aritzia is a women's fashion retailer founded in Vancouver, BC, and is a great example of a Canadian company that has expanded into the United States by establishing its own wholly-owned subsidiaries. New wholly owned subsidiaries, i.e., greenfield ventures, allow companies to have a direct operating presence in the foreign market they are expanding into. Though this requires more money and may require more time to do adequate market research, this preserves complete control of the company while in a foreign market.

Since its inception in 1984 Aritzia has made a name for itself, establishing a strong brand presence and cult following across Canada (Market Research #12: Aritzia, 2019). With 68 locations across Canada and 33 across the States as of 2021, they are a Canadian retail success story (Number of Aritzia Stores by Country 2021, 2021). Their strength in the e-commerce world and across social media has helped significantly with driving brand awareness across international borders, giving them the recognition and demand necessary for lowering risks associated with establishing new business operations outside of Canada.

Bernice Chan, March 2023

Cautions When Purchasing an Existing Foreign Enterprise

As we've seen, some companies opt to purchase an existing company in a foreign country outright as a way to get into a foreign market quickly. When making an acquisition, due diligence is important—not only on the financial side but also on the side of the country's culture and business practices. The annual disposable income in Russia, for example, exceeds that of all the other BRIC countries (i.e., Brazil, India, and China). For many major companies, Russia is too big and too rich to ignore as a market. However, Russia also has a reputation for corruption and red tape that even its highest-ranking officials admit. In a *BusinessWeek* article, presidential economic advisor Arkady Dvorkovich (whose office in the Kremlin was once occupied by Soviet leader Leonid Brezhnev), for example, advises, "Investors should choose wisely" which regions of Russia they locate their business in, warning that some areas are more corrupt than others. Corruption makes the world less flat precisely because it undermines the viability of legal vehicles, such as licensing, which otherwise lead to a flatter world (Matlack, 2009).

The culture of corruption is even embedded into some Russian company structures. In the 1990s, laws inadvertently encouraged Russian firms to establish legal headquarters in offshore tax havens, like Cyprus. A tax haven is a country that has very advantageous (low) corporate income taxes.

Businesses registered in these offshore tax havens to avoid certain Russian taxes. Even though companies could obtain a refund on these taxes from the Russian government, "the procedure is so complicated you never actually get a refund," said Andrey Pozdnyakov, cofounder of Siberian-based Elecard, in the same *BusinessWeek* article (Matlack, 2009).

Building Long-Term Relationships

Developing a good relationship with regulators in target countries helps with the long-term entry strategy. Building these relationships may include keeping people in the countries long enough to form good ties, since a deal negotiated with one person may fall apart if that person returns too quickly to headquarters.

Case: Coca-Cola and Illy Caffé

In March 2008, the Coca-Cola company and Illy Caffé Spa finalized a joint venture and launched a premium ready-to-drink espresso-based coffee beverage. The joint venture, Ilko Coffee International, was created to bring three ready-to-drink coffee products—Caffè, an Italian chilled espresso-based coffee; Cappuccino, an intense espresso, blended with milk and dark cacao; and Latte Macchiato, a smooth espresso, swirled with milk—to consumers in 10 European countries. The products will be available in stylish, premium cans (150 ml for Caffè and 200 ml for the milk variants). All three offerings will be available in 10 European Coca-Cola Hellenic markets including Austria, Croatia, Greece, and Ukraine. Additional countries in Europe, Asia, North America, Eurasia, and the Pacific were slated for expansion into 2009.

The Coca-Cola Company is the world's largest beverage company. Along with Coca-Cola, recognized as the world's most valuable brand, the company markets four of the world's top five nonalcoholic sparkling brands, including Diet Coke, Fanta, Sprite, and a wide range of other beverages, including diet and light beverages, waters, juices and juice drinks, teas, coffees, and energy and sports drinks. Through the world's largest beverage distribution system, consumers in more than 200 countries enjoy the company's beverages at a rate of 1.5 billion servings each day.

Based in Trieste, Italy, Illy Caffé produces and markets a unique blend of espresso coffee under a single brand leader in quality. Over 6 million cups of Illy espresso coffee are enjoyed every day. Illy is sold in over 140 countries around the world and is available in more than 50,000 of the best restaurants and coffee bars. Illy buys green coffee directly from the growers of the highest quality Arabica through partnerships based on the mutual creation of value. The Trieste-based company fosters long-term collaborations with the world's best coffee growers—in Brazil, Central America, India, and Africa—providing know-how and technology and offering above-market prices.

(The Coca-Cola Company, n.d.)

In summary, when deciding which mode of entry to choose, companies should ask themselves two key questions:

1. How much of our resources are we willing to commit? The fewer the resources (i.e., money, time, and expertise) the company wants (or can afford) to devote, the better it is for the company to enter the

foreign market on a contractual basis—through licensing, franchising, management contracts, or turnkey projects.

2. How much control do we wish to retain? The more control a company wants, the better off it is establishing or buying a wholly owned subsidiary or, at least, entering via a joint venture with carefully delineated responsibilities and accountabilities between the partner companies.

Regardless of which entry strategy a company chooses, several factors are always important.

- **Cultural and linguistic differences.** These affect all relationships and interactions inside the company, with customers, and with the government. Understanding the local business culture is critical to success.
- **Quality and training of local contacts and/or employees.** Evaluating skill sets and then determining if the local staff is qualified is a key factor for success.
- **Political and economic issues.** Policy can change frequently, and companies need to determine what level of investment they're willing to make, what's required to make this investment, and how much of their earnings they can repatriate.
- **Experience of the partner company.** Assessing the experience of the partner company in the market—with the product and in dealing with foreign companies—is essential in selecting the right local partner.

6.2 EXPORTING

Exporting is defined as the sale of products and services in foreign countries that are sourced or made in the home country. Importing is the flipside of exporting. Importing refers to buying goods and services from foreign sources and bringing them back into the home country.

Importing is also known as global sourcing.

Importing: Heritage Link Brands

Selena Cuffe started her wine import company, Heritage Link Brands, in 2005. Importing wine isn't new, but Cuffe did it with a twist: she focused on importing wine produced by black South Africans. Cuffe got the idea after attending a wine festival in Soweto, where she saw more than five hundred wines from eighty-six producers showcased. Cuffe did some market research and learned of the $3 billion wine industry in Africa. She also saw a gap in the existing market related to wine produced by indigenous African vintners and decided to fill it. She started her company with $70,000, financed through her savings and credit cards. In the first year, sales were only $100,000 but then jumped to $1 million in the second year, when Cuffe sold to more than one thousand restaurants, retailers, and grocery stores. Even better, American Airlines began carrying Cuffe's imported wines on flights, thus providing a steady flow of business amid the more uncertain restaurant market. Cuffe has attributed her success to passion as well as to patience for meeting the multiple regulations required when running an import business.

Exporting is an effective entry strategy for companies that are just beginning to enter a new foreign market. It's a low-cost, low-risk option compared to the other strategies. These same reasons make exporting a good strategy for small and midsize companies that can't or won't make significant financial investment in the international market.

Companies can sell into a foreign country either through a local distributor or through their own salespeople. Many government export-trade offices can help a company find a local distributor. Increasingly, the Internet has provided a more efficient way for foreign companies to find local distributors and enter into commercial transactions.

Distributors are export intermediaries who represent the company in the foreign market. Often, distributors represent many companies, acting as the "face" of the company in that country, selling products, providing customer service, and receiving payments. In many cases, the distributors take title to the goods and then resell them. Companies use distributors because distributors know the local market and are a cost-effective way to enter that market.

However, using distributors to help with export can have its own challenges. For example, some companies find that if they have a dedicated salesperson who travels frequently to the country, they're likely to get more sales than by relying solely on the distributor. Often, that's because distributors sell multiple products and sometimes even competing ones. Making sure that the distributor favours one firm's product over another product can be hard to monitor. In countries like China, some companies find that—culturally—Chinese consumers may be more likely to buy a product from a foreign company than from a local distributor, particularly in the case of a complicated, high-tech product. Simply put, the Chinese are more likely to trust that the overseas salesperson knows their product better.

Why Do Companies Export?

Companies export because it's the easiest way to participate in global trade, it's a less costly investment than the other entry strategies, and it's much easier to simply stop exporting than it is to extricate oneself from the other entry modes. An export partner in the form of either a distributor or an export management company can facilitate this process. An export management company (EMC) is an independent company that performs the duties that a firm's own export department would execute. The EMC handles the necessary documentation, finds buyers for the export, and takes title of the goods for direct export. In return, the EMC charges a fee or commission for its services. Because an EMC performs all the functions that a firm's export department would, the firm doesn't have to develop these internal capabilities. Most of all, exporting gives a company quick access to new markets.

Benefits of Exporting: Vitrac

Egyptian company Vitrac was founded by Mounir Fakhry Abdel Nour to take advantage of Egypt's surplus fruit products. At its inception, Vitrac sourced local fruit, made it into jam, and exported it worldwide. Vitrac has acquired money, market, and manufacturing advantages from exporting.

- **Market.** The company has access to a new market, which has brought added revenues.
- **Money.** Not only has Vitrac earned more revenue, but it has also gained access to foreign currency, which benefits companies located in certain regions of the world, such as in Vitrac's home country of Egypt.
- **Manufacturing.** The cost to manufacture a given unit decreased because Vitrac has been able to manufacture at higher volumes and buy source materials in higher volumes, thus benefiting from volume discounts.

Risks of Exporting

There are risks in relying on the export option. If you merely export to a country, the distributor or buyer might switch to or at least threaten to switch to a cheaper supplier in order to get a better price. Or someone might start making the product locally and take the market from you. Also, local buyers sometimes believe that a company which only exports to them isn't very committed to providing long-term service and support once a sale is complete. Thus, they may prefer to buy from someone who's producing directly within the country. At this point, many companies begin to reconsider having a local presence, which moves them toward one of the other entry options.

Ethics in Action: Different Countries, Different Food and Drug Rule

Particular products, especially foods and drugs, are often subject to local laws regarding safety, purity, packaging, labelling, and so on. Companies that want to make a product that can be sold in multiple countries must comply with the highest common denominator of all the laws of all the target markets. Complying with the highest standard could increase the overall cost of the product. As a result, some companies opt to stay out of markets where compliance with the regulation would be more costly. Is it ethical to be selling a product in one country that another country deems substandard?

Exporting is a easy way to enter an international market. In addition to exporting, companies can choose to pursue more specialized modes of entry—namely, contracautal modes or investment modes. Contractual modes involve the use of contracts rather than investment. Let's look at the two main contractual entry modes, licensing and franchising.

6.3 LICENSING

Licensing gives a licensee certain rights or resources to manufacture and/or market a certain product in a host country.

Licensing

Licensing is a business arrangement in which one company gives another company permission to manufacture its product for a specified payment. Licensing is defined as the granting of permission by the licenser to the licensee to use intellectual property rights, such as trademarks, patents, brand names, or technology, under defined conditions. The possibility of licensing makes for a flatter world, because it creates a legal vehicle for taking a product or service delivered in one country and providing a nearly identical version of that product or service in another country. Under a licensing agreement, the multinational firm grants rights on its intangible property to a foreign company for a specified period of time. The licenser is normally paid a royalty on each unit produced and sold. Although the multinational firm usually has no ownership interests, it often provides ongoing support and advice. Most companies consider this market-entry option of licensing to be a low-risk option because there's typically no up-front investment.

For a multinational firm, the advantage of licensing is that the company's products will be manufactured and made available for sale in the foreign country (or countries) where the product or service is licensed. The multinational firm doesn't have to expend its own resources to manufacture, market, or distribute the goods. This low cost, of course, is coupled with lower potential returns, because the revenues are shared between the parties.

Licensing generally involves allowing another company to use patents, trademarks, copyrights, designs, and other intellectual in exchange for a percentage of revenue or a fee. It's a fast way to generate income and grow a business, as there is no manufacturing or sales involved. Instead, licensing usually means taking advantage of an existing company's pipeline and infrastructure in exchange for a small percentage of revenue.

An international licensing agreement allows foreign firms, either exclusively or non-exclusively, to manufacture a proprietor's product for a fixed term in a specific market.

To summarize, in this foreign market entry mode, a licensor in the home country makes limited rights or resources available to the licensee in the host country. The rights or resources may include patents, trademarks, managerial skills, technology, and others that can make it possible for the licensee to manufacture and sell in the host country a similar product to the one the licensor has already been producing and selling in the home country without requiring the licensor to open a new operation overseas. The licensor's earnings usually take the form of one-time payments, technical fees, and royalty payments, usually calculated as a percentage of sales.

Advantages

As in this mode of entry the transference of knowledge between the parental company and the licensee is strongly present, the decision of making an international license agreement depend on the respect the host government shows for intellectual property and on the ability of the licensor to choose the right partners and avoid having them compete in each other's market. Licensing is a relatively flexible work agreement that can be customized to fit the needs and interests of both licensor and licensee. The following are the main advantages and reasons to use international licensing for expanding internationally:

- Obtain extra income for technical know-how and services.
- Reach new markets not accessible by export from existing facilities.
- Quickly expand without much risk and large capital investment.
- Pave the way for future investments in the market.
- Retain established markets closed by trade restrictions.
- Political risk is minimized as the licensee is usually 100% locally owned.

Disadvantages

This is highly attractive for companies that are new in international business. On the other hand, international licensing is a foreign market entry mode that presents some disadvantages and reasons why companies should not use it because there is:

- Lower income than in other entry modes
- Loss of control of the licensee manufacture and marketing operations and practices leading to loss of quality
- Risk of having the trademark and reputation ruined by an incompetent partner
- The foreign partner also can become a competitor by selling its products in places where the parental company has a presence

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6.4 FRANCHISING

Franchising is the practice of licensing another firm's business model as an operator.

Franchising is the practice of using another firm's successful business model. For the franchiser, the franchise is an alternative to building "chain stores" to distribute goods that avoids the investments and liability of a chain. The franchiser's success depends on the success of the franchisees. The franchisee is said to have a greater incentive than a direct employee because he or she has a direct stake in the business. Essentially, and in terms of distribution, the franchiser is a supplier who allows an operator, or a franchisee, to use the supplier's trademark and distribute the supplier's goods. In return, the operator pays the supplier a fee.

Similar to a licensing agreement, under a franchising agreement, the multinational firm grants rights on its intangible property, like technology or a brand name, to a foreign company for a specified period of time and receives a royalty in return. The difference is that the franchiser provides a bundle of services and products to the franchisee. For example, McDonald's expands overseas through franchises. Each franchise pays McDonald's a franchisee fee and a percentage of its sales and is required to purchase certain products from the franchiser. In return, the franchisee gets access to all of McDonald's products, systems, services, and management expertise.

In short, in terms of distribution, the franchiser is a supplier who allows an operator, or a franchisee, to use the supplier's trademark and distribute the supplier's goods. In return, the operator pays the supplier a fee.

Each party to a franchise has several interests to protect. The franchiser is involved in securing protection for the trademark, controlling the business concept, and securing know how. The franchisee is obligated to carry out the services for which the trademark has been made prominent or famous. There is a great deal of standardization required. The place of service has to bear the franchiser's signs, logos, and trademark in a prominent place. The uniforms worn by the staff of the franchisee have to be of a particular design and colour. The service has to be in accordance with the pattern followed by the franchiser in the successful franchise operations. Thus, franchisees are not in full control of the business, as they would be in retailing.

A service can be successful if equipment and supplies are purchased at a fair price from the franchiser or sources recommended by the franchiser. A coffee brew, for example, can be readily identified by the trademark if its raw materials come from a particular supplier. If the franchiser requires purchase from his stores, it may come under anti-trust legislation or equivalent laws of other countries. So too the purchase of uniforms of personnel, signs, etc., as well as the franchise sites, if they are owned or controlled by the franchiser.

Franchise agreements carry no guarantees or warranties, and the franchisee has little or no recourse to legal intervention in the event of a dispute. Franchise contracts tend to be unilateral contracts in favour of the franchiser, who is generally protected from lawsuits from their franchisees because of the non-negotiable contracts that require franchisees to acknowledge, in effect, that they are buying the franchise knowing that there is risk, and that they have not been promised success or profits by the franchiser. Contracts are renewable at the sole option of the franchiser. Most franchisers require franchisees to sign agreements that mandate where and under what law any dispute would be litigated.

Case: Global Market Entry Modes

Photo by Beris Creatives, Unsplash Licence

Global market entry modes refer to the various strategies that businesses can use to enter international markets (Cateora, Gilly, & Graham, 2021). These include exporting, licensing, joint ventures, franchising, and wholly-owned subsidiaries. Each mode has its own advantages and disadvantages, so businesses need to evaluate various factors before selecting the best expansion mode. For instance, exporting might be a suitable mode for small businesses with limited resources, while joint ventures or wholly-owned subsidiaries might be a better option for larger firms with more capital and expertise.

Tim Hortons is a Canadian company that has successfully used these entry modes (The Canadian Encyclopedia, 2020). The fast-food chain has expanded to several countries, including the United States, Mexico, and the United Arab Emirates, through franchise agreements. Franchising has allowed Tim Hortons to leverage local knowledge and expertise while maintaining its brand standards and control over operations.

Moreover, Tim Hortons has used joint ventures to expand into the Chinese market as it partnered with Cartesian Capital Group, to open over 1,500 stores in China in the next decade (Tim Hortons, 2018). The joint venture model has enabled the company to access local knowledge, overcome regulatory hurdles, and reduce operational costs.

In conclusion, global market entry modes are crucial for businesses seeking to expand their operations beyond their home country. Hence, choosing the right mode requires careful evaluation of various factors, and there is no one-size-fits-all approach.

Diksha Dutta, March 2023

6.5 CONTRACT MANUFACTURING

In **contract manufacturing,** a hiring firm makes an agreement with the contract manufacturer to produce and ship the hiring firm's goods.

A contract manufacturer ("CM") is a manufacturer that enters into a contract with a firm to produce components or products for that firm . It is a form of outsourcing. In a contract manufacturing business model, the hiring firm approaches the contract manufacturer with a design or formula. The contract manufacturer will quote the parts based on processes, labour, tooling, and material costs. Typically a hiring firm will request quotes from multiple CMs. After the bidding process is complete, the hiring firm will select a source, and then, for the agreed-upon price, the CM acts as the hiring firm's factory, producing and shipping units of the design on behalf of the hiring firm.

Benefits

Contract manufacturing offers a number of benefits:

- *Cost Savings*: Companies save on their capital costs because they do not have to pay for a facility and the equipment needed for production. They can also save on labour costs such as wages, training, and benefits. Some companies may look to contract manufacture in low-cost countries, such as China, to benefit from the low cost of labour.
- *Mutual Benefit to Contract Site*: A contract between the manufacturer and the company it is producing for may last several years. The manufacturer will know that it will have a steady flow of business at least until that contract expires.
- *Advanced Skills*: Companies can take advantage of skills that they may not possess, but the contract manufacturer does. The contract manufacturer is likely to have relationships formed with raw material suppliers or methods of efficiency within their production.
- *Quality*: Contract Manufacturers are likely to have their own methods of quality control in place that help them to detect counterfeit or damaged materials early.
- *Focus:* Companies can focus on their core competencies better if they can hand off base production to an outside company.

- *Economies of Scale:* Contract Manufacturers have multiple customers that they produce for. Because they are servicing multiple customers, they can offer reduced costs in acquiring raw materials by benefiting from economies of scale. The more units there are in one shipment, the less expensive the price per unit will be.

Risks

Balanced against the above benefits of contract manufacturing are a number of risks:

- *Lack of Control*: When a company signs the contract allowing another company to produce their product, they lose a significant amount of control over that product. They can only suggest strategies to the contract manufacturer; they cannot force them to implement those strategies.
- *Relationships*: It is imperative that the company forms a good relationship with its contract manufacturer. The company must keep in mind that the manufacturer has other customers. They cannot force them to produce their product before a competitor's. Most companies mitigate this risk by working cohesively with the manufacturer and awarding good performance with additional business.
- *Quality*: When entering into a contract, companies must make sure that the manufacturer's standards are congruent with their own. They should evaluate the methods in which they test products to make sure they are of good quality. The company has to ensure the contract manufacturer has suppliers that also meet these standards.
- *Intellectual Property Loss*: When entering into a contract, a company is divulging their formulas or technologies. This is why it is important that a company not give out any of its core competencies to contract manufacturers. It is very easy for an employee to download such information from a computer and steal it. The recent increase in intellectual property loss has corporate and government officials struggling to improve security. Usually, it comes down to the integrity of the employees.
- *Outsourcing Risks*: Although outsourcing to low-cost countries has become very popular, it does bring along risks such as language barriers, cultural differences, and long lead times. This could make the management of contract manufacturers more difficult, expensive, and time-consuming.
- *Capacity Constraints:* If a company does not make up a large portion of the contract manufacturer's business, they may find that they are de-prioritized over other companies during high production periods. Thus, they may not obtain the product they need when they need it.
- *Loss of Flexibility and Responsiveness*: Without direct control over the manufacturing facility, the company will lose some of its ability to respond to disruptions in the supply chain. It may also hurt their ability to respond to demand fluctuations, risking their customer service levels

6.6 JOINT VENTURES

In a **joint venture** business model, two or more parties agree to invest time, equity, and effort for the development of a new shared project.

Joint Ventures

A joint venture is a business agreement in which parties agree to develop a new entity and new assets by contributing equity. They exercise control over the enterprise and consequently share revenues, expenses and assets.

When two or more persons come together to form a partnership for the purpose of carrying out a project, this is called a joint venture. In this scenario, both parties are equally invested in the project in terms of money, time and effort to build on the original concept. While joint ventures are generally small projects, major corporations use this method to diversify. A joint venture can ensure the success of smaller projects for those that are just starting in the business world or for established corporations. Since the cost of starting new projects is generally high, a joint venture allows both parties to share the burden of the project as well as the resulting profits. Since money is involved in a joint venture, it is necessary to have a strategic plan in place. In short, both parties must be committed to focusing on the future of the partnership rather than just the immediate returns. Ultimately, short term and long term successes are both important. To achieve this success, honesty, integrity and communication within the joint venture are necessary.

A consortium JV (also known as a cooperative agreement) is formed when one party seeks technological expertise, franchise and brand-use agreements, management contracts, and rental agreements for one-time contracts. The JV is dissolved when that goal is reached. Some major joint ventures include Dow Corning, Miller Coors, Sony Ericsson, Penske Truck Leasing, Norampac, and Owens-Corning.

An equity joint venture is a contractual, strategic partnership between two or more separate business entities to pursue a business opportunity together. The partners in an equity joint venture each contribute capital and resources in exchange for an equity stake and share in any resulting profits. (In a nonentity joint venture, there is no contribution of capital to form a new entity.)

To see how an equity joint venture works, let's return to the example of Egyptian company, Vitrac. Mounir Fakhry Abdel Nour founded his jam company to take advantage of Egypt's surplus fruit products. Abdel Nour initially approached the French jam company, Vitrac, to enter into a joint venture with his newly founded company, VitracEgypt. Abdel Nour supplied the fruit and the markets, while his French partner supplied the technology and know-how for producing jams.

In addition to exporting to Australia, the United States, and the Middle East, Vitrac began exporting to Japan. Sales results from Japan indicated a high demand for blueberry jam. To meet this demand—in an interesting twist, given Vitrac's origin—Vitrac had to import blueberries from Canada. Vitrac thus was importing blueberries from Canada, manufacturing the jam in Egypt, and exporting it to Japan (JETRO, 2010).

Using French Vitrac's manufacturing know-how, Abdel Nour had found a new supply and the opportunity to enter new markets with it, thus expanding his partner's reach. The partnership fit was good. The two companies' joint venture continued for three years, until the French company sold its shares to Abdel Nour, making Vitrac a 100 percent owned and operated Egyptian company. Abdel Nour's company reached $22 million in sales and was the Egyptian jam-market leader before being bought by a larger Swiss company, Hero.

Risks of Joint Ventures

Equity joint ventures pose both opportunities and challenges for the companies involved.

- First and foremost is the challenge of finding the right partner—not just in terms of business focus but also in terms of compatible cultural perspectives and management practices.
- Second, the local partner may gain the know-how to produce its own competitive product or service to rival the multinational firm. This is what's currently happening in China. To manufacture cars in China, non-Chinese companies must set up joint ventures with Chinese automakers and share technology with them. Once the contract ends, however, the local company may take the knowledge it gained from the joint venture to compete with its former partner. For example, Shanghai Automotive Industry (Group) Corporation, which worked with General Motors (GM) to build Chevrolets, has pursued plans to increase sales of its own vehicles tenfold to 300,000 in five years and to compete directly with its former partner (Rowley, 2009).

Did You Know: Joint Ventures in China

In the past, joint ventures were the only relationship foreign companies could form with Chinese companies. In fact, prior to 1986, foreign companies could not wholly own a local subsidiary. The Chinese government began to allow equity joint ventures in 1979, which marked the beginning of the Open Door Policy, an economic liberalization initiative. The Chinese government strongly encouraged equity joint ventures as a way to gain access to the technology, capital, equipment, and know-how of foreign companies. The risk to the foreign company was that if the venture soured, the Chinese company could end up keeping all of these assets. Often, Chinese companies only contributed things like land or tax concessions that foreign companies couldn't keep if the venture ended. As of 2010, equity joint ventures between a Chinese company and a foreign partner require a minimum equity investment by the foreign partner of at least 33 to 70 percent of the equity, but there's no minimum investment set for the Chinese partner.

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6.8 KEY TERMS

Key Terms

Acquisition: Is a transaction in which a firm gains control of another firm by purchasing its stock, exchanging the stock for its own, or, in the case of a private firm, paying the owners a purchase price. 6.1

Contract Manufacturing: A hiring firm makes an agreement with the contract manufacturer to produce and ship the hiring firm's goods. 6.5

Cultural And Linguistic Differences: These affect all relationships and interactions inside the company, with customers, and with the government. Understanding the local business culture is critical to success. 6.1

Experience of The Partner Company: Assessing the experience of the partner company in the market—with the product and in dealing with foreign companies—is essential in selecting the right local partner. 6.1

Exporting: Is defined as the sale of products and services in foreign countries that are sourced or made in the home country. Importing is the flipside of exporting. Importing refers to buying goods and services from foreign sources and bringing them back into the home country. 6.2

Franchising: Is the practice of licensing another firm's business model as an operator. 6.4

Importing: Is also known as global sourcing. 6.2

Joint Venture: Business model, two or more parties agree to invest time, equity, and effort for the development of a new shared project. 6.6

Licensing: Gives a licensee certain rights or resources to manufacture and/or market a certain product in a host country. 6.3

Manufacturing: The cost to manufacture a given unit decreased because Vitrac has been able to manufacture at higher volumes and buy source materials in higher volumes, thus benefiting from volume discounts. 6.2

Market: The company has access to a new market, which has brought added revenues. 6.2

Money: Not only has Vitrac earned more revenue, but it has also gained access to foreign currency, which benefits companies located in certain regions of the world, such as in Vitrac's home country of Egypt. 6.2

Political and Economic Issues: Policy can change frequently, and companies need to determine what level of investment they're willing to make, what's required to make this investment, and how much of their earnings they can repatriate. 6.1

Quality and Training of Local Contacts and/or Employees: Evaluating skill sets and then determining if the local staff is qualified is a key factor for success. 6.1

CHAPTER 7: GLOBAL PRODUCTS

Chapter Outline

7.0 INTRODUCTION

Learning Objectives

After reading this section, students should be able to:

1. Describe common consumer product categories.
2. Describe the product life cycle.
3. Explain marketing considerations through the product life cycle.
4. Explain the stages of the new-product development process.
5. Outline the trade-offs between standardized versus customized products.
6. List the dimensions of value proposition adaptation.
7. List the major drivers behind value proposition adaptation.
8. Outline the significant advantages of a global innovation strategy.
9. List the steps in the global innovation strategy of a firm.
10. Outline the nature and size of BOP markets.
11. Provide examples of firms pursuing BOP strategies.

The product is the most important element of a company's marketing program. Global marketers face the challenge of formulating coherent product and brand strategies on a worldwide basis. A **product** can be viewed as a collection of tangible and intangible attributes that collectively provide benefits to a buyer or user. **A brand** is a complex bundle of images and experiences in the mind of the customer. In most countries, local brands compete with international brands and global brands. A local product is available in a single country; a global product meets the wants and needs of a global market.

Product and communications strategies can be viewed within a framework that allows for combinations of three strategies: extension strategy, adaptation strategy, and creation strategy. Five strategic alternatives are open to companies pursuing geographic expansion: product-communication extension; product extension-communication adaptation; product adaptation-communication extension; product-communication adaptation; and product invention (innovation). The strategic alternative(s) that a particular company chooses will depend on the product and the need it serves, customer preferences and purchasing power, and the costs of adaptation versus standardization. Product transformation occurs when a product that has been introduced into new country markets serves a different function or is used differently than originally intended. When choosing a strategy, management should consciously strive to avoid the "not invented here" syndrome.

Global competition has put pressure on companies to excel at developing standardized product platforms that can serve as a foundation for cost-efficient adaptation. New products can be classified as discontinuous, dynamically continuous, or continuous innovations. A successful product launch requires an understanding of how markets develop: sequentially over time or simultaneously. Today, many new products are launched in multiple national markets as product development cycles shorten and product development costs soar.

7.1 OVERVIEW OF PRODUCTS

Often when we hear the word *marketing,* we think about promotion or perhaps only advertising, but product is the core of the marketing mix. Product defines what will be priced, promoted, and distributed. If you are able to create and deliver a product that provides exceptional value to your target customer, the rest of the marketing mix is easier to manage. A successful product makes every aspect of a marketer's job easier—and more fun.

Consumer Product Categories

A **product** is a bundle of attributes (features, functions, benefits, and uses) that a person receives in an exchange. In essence, the term "product" refers to anything offered by a firm to provide customer satisfaction, tangible or intangible. Thus, a product may be an idea (recycling), a physical good (a pair of sneakers), a service (banking), or any combination of the three (Marketing Accountability Standards Board, 2020).

Broadly speaking, products fall into one of two categories: consumer products and business products (also called industrial products and B2B products). **Consumer products** are purchased by the final consumer. **Business products** are purchased by other companies. Some products, like computers, for instance, may be both consumer products and business products, depending on who purchases and uses them.

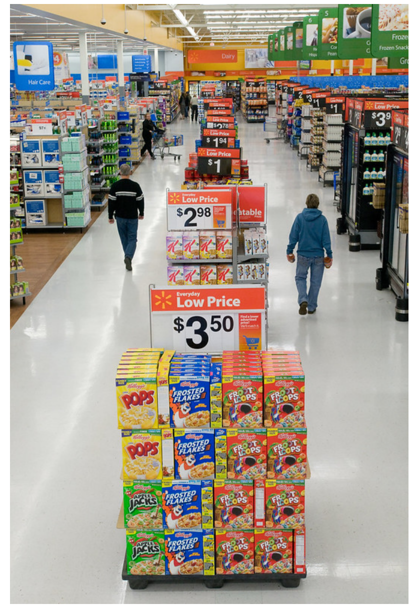
The product fills an important role in the marketing mix because it is the core of the exchange. Does the product provide the features, functions, benefits, and uses that the target customer expects and desires? Throughout our discussion of product we will focus on the target customer. Often companies become excited about their capabilities, technologies, and ideas and forget the perspective of the customer. This leads to investments in product enhancements or new products that don't provide value to the customer—and, as a result, are unsuccessful.

Consumer products are often classified into four groups related to different kinds of buying decisions: convenience, shopping, specialty, and unsought products. These are described below.

Convenience Products

A **convenience product** is an inexpensive product that requires a minimum amount of effort on the part of the consumer in order to select and purchase it. Examples of convenience products are bread, soft drinks, pain reliever, and coffee. They also include headphones, power cords, and other items that are easily misplaced.

From the consumer's perspective, little time, planning, or effort go into buying convenience products. Often product purchases are made on impulse, so availability is important. Consumers have come to expect a wide variety of products to be conveniently located at their local supermarkets. They also expect easy online purchase options and low-cost, quick shipping for those purchases. Convenience items are also found in vending machines and kiosks.



Walmart's "Action Alley" in Gladstone, MO
Photo by Walmart, CC BY 2.0

For convenience products, the primary marketing strategy is extensive distribution. The product must be available in every conceivable outlet and must be easily accessible in these outlets. These products are usually of low unit value, and they are highly standardized. Marketers must establish a high level of brand awareness and recognition. This is accomplished through extensive mass advertising, sales promotion devices such as coupons and point-of-purchase displays, and effective packaging. Yet, the key is to convince resellers (wholesalers and retailers) to carry the product. If the product is not available when, where, and in a form the consumer desires, the convenience product will fail.

Shopping Products

In contrast, consumers want to be able to compare products categorized as shopping products. **Shopping products** are usually more expensive and are purchased occasionally. The consumer is more likely to compare a number of options to assess quality, cost, and features.

Although many shopping goods are nationally advertised, in the marketing strategy it is often the ability of the retailer to differentiate itself that generates the sale. If you decide to buy a TV at BestBuy, then you are more likely to evaluate the range of options and prices that BestBuy has to offer. It becomes important for BestBuy to provide a knowledgeable and effective sales person and have the right pricing discounts to offer you a competitive deal. BestBuy might also offer you an extended warranty package or in-store service options. While shopping in BestBuy, consumers can easily check prices and options for online retailers, which places even greater pressure on BestBuy to provide the best total value to the shopper. If the retailer can't make the sale, product turnover is slower, and the retailer will have a great deal of their capital tied up in inventory.

There is a distinction between heterogeneous and homogeneous shopping products. Heterogeneous shopping products are unique. Think about shopping for clothing or furniture. There are many stylistic differences, and the shopper is trying to find the best stylistic match at the right price. The purchase decision with heterogeneous shopping products is more likely to be based on finding the right fit than on price alone.

In contrast, homogeneous shopping products are very similar. Take, for example, refrigerators. Each model has certain features that are available at different price points, but the basic functions of all of the models are very similar. A typical shopper will look for the lowest price available for the features that they desire.

Specialty Products

Specialty goods represent the third product classification. From the consumer's perspective, these products are so unique that it's worth it to go to great lengths to find and purchase them. Almost without exception, price is not the principle factor affecting the sales of specialty goods. Although these products may be custom-made or one-of-a-kind, it is also possible that the marketer has been very successful in differentiating the product in the mind of the consumer.

For example, some consumers feel a strong attachment to their hair stylist or barber. They are more likely to wait for an appointment than schedule time with a different stylist.

It is generally desirable for a marketer to lift her product from the shopping to the specialty class—and keep it there. With the exception of price-cutting, the entire range of marketing activities is needed to accomplish this.

Unsought Products

Unsought products are those the consumer never plans or hopes to buy. These are either products that the customer is unaware of or products the consumer hopes not to need. For example, most consumers hope never to purchase pest control services and try to avoid purchasing funeral plots. Unsought products have a tendency to draw aggressive sales techniques, as it is difficult to get the attention of a buyer who is not seeking the product.

7.2 PRODUCT LIFE CYCLE

Stages of the Product Life Cycle

A company has to be good at both developing new products and managing them in the face of changing tastes, technologies, and competition. Products generally go through a life cycle with predictable sales and profits. Marketers use the product life cycle to follow this progression and identify strategies to influence it. The **product life cycle (PLC)** starts with the product's development and introduction, then moves toward maturity, withdrawal and eventual decline. This progression is shown in the graph, below.

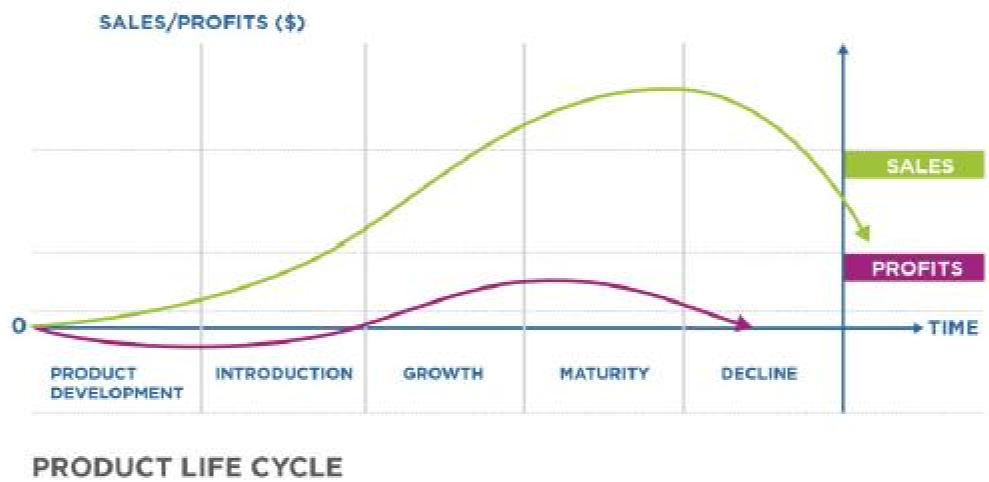


Fig 7.1 Product Life Cycle

The five stages of the PLC are:

1. Product development
2. Market introduction
3. Growth
4. Maturity
5. Decline

The table below shows common characteristics of each stage.

	Common Characteristics
0. **Product development stage**	1. investment is made 2. sales have not begun 3. new product ideas are generated, operationalized, and tested
1. **Market introduction stage**	1. costs are very high 2. slow sales volumes to start 3. little or no competition 4. demand has to be created 5. customers have to be prompted to try the product 6. makes little money at this stage
2. **Growth stage**	1. costs reduced due to economies of scale 2. sales volume increases significantly 3. profitability begins to rise 4. public awareness increases 5. competition begins to increase with a few new players in establishing market 6. increased competition leads to price decreases
3. **Maturity stage**	1. costs are lowered as a result of increasing production volumes and experience curve effects 2. sales volume peaks and market saturation is reached 3. new competitors enter the market 4. prices tend to drop due to the proliferation of competing products 5. brand differentiation and feature diversification is emphasized to maintain or increase market share 6. profits decline
4. **Decline stage**	1. costs increase due to some loss of economies of scale 2. sales volume declines 3. prices and profitability diminish 4. profit becomes more a challenge of production/distribution efficiency than increased sales

Using the Product Life Cycle

The product life cycle can be a useful tool in planning for the life of the product, but it has a number of limitations.

Not all products follow a smooth and predictable growth path. Some products are tied to specific business cycles or have seasonal factors that impact growth. For example, enrolment in higher education tracks closely with economic trends. When there is an economic downturn, more people lose jobs and enrol in college to improve their job prospects. When the economy improves and more people are fully employed, college enrolments drop. This does not necessarily mean that education is in decline, only that it is in a down cycle.

Furthermore, evidence suggests that the PLC framework holds true for industry segments but not necessarily for individual brands or projects, which are likely to experience greater variability (Mullor-Sebastion, 1983).

Of course, changes in other elements of the marketing mix can also affect the performance of the product during its life cycle. Change in the competitive situation during each of these stages may have a much greater impact on the marketing approach than the PLC itself. An effective promotional program or a dramatic lowering of price may improve the sales picture in the decline period, at least temporarily. Usually the improvements brought about by non-product tactics are relatively short-lived, and basic alterations to product offerings provide longer benefits.

Whether one accepts the S-shaped curve as a valid sales pattern or as a pattern that holds only for some products (but not for others), the PLC concept can still be very useful. It offers a framework for dealing systematically with product marketing issues and activities. The marketer needs to be aware of the characteristics that apply to a given product as it moves through the various stages.

Marketing through the Product Cycle

There are some common marketing considerations associated with each stage of the PLC. How marketers think about the marketing mix and the blend of promotional activities–also known as the promotion mix–should reflect a product's life-cycle stage and progress toward market adoption. These considerations cannot be used as a formula to guarantee success, but they can function as guidelines for thinking about budget, objectives, strategies, tactics, and potential opportunities and threats.

Keep in mind that we will discuss the new-product development process next, so it is not covered here.

Market Introduction Stage

Think of the market introduction stage as the product launch. This phase of the PLC requires a significant marketing budget. The market is not yet aware of the product or its benefits. Introducing a product involves convincing consumers that they have a problem or need which the new offering can uniquely address. At its core, messaging should convey, "This product is a great idea! You want this!" Usually a promotional budget is needed to create broad awareness and educate the market about the new product. To achieve these goals, often a product launch includes promotional elements such as a new Web site (or significant update to the existing site), a social media campaign, print or broadcast advertising, a press release and press campaign.

There is also a need to invest in the development of the distribution channels and related marketing support. For a B2B product, this often requires training the sales force and developing sales tools and materials for direct and personal selling. In a B2C market, it might include training and incentivizing retail partners to stock and promote the product.

Pricing strategies in the introduction phase are generally set fairly high, as there are fewer competitors in the market. This is often offset by early discounts and promotional pricing.

It is worth noting that the launch will look different depending on how new the product is. If the product is a completely new innovation that the market has not seen before, then there is a need to both educate the market about the new offering and build awareness of it. In 2013 when Google launched Google Glass—an optical head-mounted computer display—it had not only to get the word out about the product but also help prospective buyers understand what it was and how it might be used. Google initially targeted tech-savvy audiences most interested in novelty and innovation (more about them later when we discuss *diffusion of innovation*). By offering the new product with a lot of media fanfare and limited availability, Google's promotional strategy ignited demand among these segments. Tech bloggers and insiders blogged and tweeted about their Google Glass adventures, and word-of-mouth sharing about the new product spread rapidly. You can imagine that this was very different from the launch of Wheat Thins Spicy Buffalo crackers, an extension of an existing product line, targeting a different audiences (retailers, consumers) with promotional activities that fit the product's marketing and distribution channels. The Google Glass situation was also different from the launch of Tesla's home battery. In that case Tesla offered a new line of home products from a company that had previously only offered automobiles. Breaking into new product categories and markets is challenging even for a well-regarded company like Tesla. As you might expect, the greater the difference in new products from a company's existing offerings, the greater the complexity and expense of the introduction stage.

One other consideration is the maturity of the product itself. Sometimes marketers will choose to be conservative during the marketing introduction stage when the product is not yet fully developed or proven, or when the distribution channels are not well established. This might mean initially introducing the product to only one segment of the market, doing less promotion, or limiting distribution (as with Google Glass). This approach allows for early customer feedback but reduces the risk of product issues during the launch.

While we often think of an introduction or launch as a single event, this phase can last several years. Generally a product moves out of the introduction stage when it begins to see rapid growth, though what counts as "rapid growth" varies significantly based on the product and the market.

Growth Stage

Once rapid growth begins, the product or industry has entered the growth stage. When a product category begins to demonstrate significant growth, the market usually responds: new competitors enter the market, and larger companies acquire high-growth companies and products.

These emerging competitive threats drive new marketing tactics. Marketers who have been seeking to build broad market awareness through the introduction phase must now differentiate their products from competitors, emphasizing unique features that appeal to target customers. The central thrust of market messaging and promotion during this stage is "This brand is the best!" Pricing also becomes more competitive and must be adjusted to align with the differentiation strategy.

Often in the growth phase the marketer must pay significant attention to distribution. With a growing number of customers seeking the product, more distribution channels are needed. Mass marketing and other promotional strategies to reach more customers and segments start to make sense for consumer-focused markets during the growth stage. In business-to-business markets, personal selling and sales promotions often help open doors to broader growth. Marketers often must develop and support new distribution channels to meet demand. Through the growth phase, distribution partners will become more experienced selling the product and may require less support over time.

The primary challenges during the growth phase are to identify a differentiated position in the market that allows the product to capture a significant portion of the demand and to manage distribution to meet the demand.

Maturity Stage

When growth begins to plateau, the product has reached the maturity phase. In order to achieve strong business results through the maturity stage, the company must take advantage of economies of scale. This is usually a period in which marketers manage budget carefully, often redirecting resources toward products that are earlier in their life cycle and have higher revenue potential.

At this stage, organizations are trying to extract as much value from an established product as they can, typically in a very competitive field. Marketing messages and promotions seek to remind customers about a great product, differentiate from competitors, and reinforce brand loyalty: "Remember why this brand is the best." As mentioned in the previous section, this late in the life cycle, promotional tactics and pricing discounts are likely to provide only short-term benefits. Changes to product have a better chance of yielding more sustained results.

In the maturity stage, marketers often focus on niche markets, using promotional strategies, messaging, and tactics designed to capture new share in these markets. Since there is no new growth, the emphasis shifts from drawing new customers to the market to winning more of the existing market. The company may extend a product line, adding new models that have greater appeal to a smaller segment of the market.

Often, distribution partners will reduce their emphasis on mature products. A sales force will shift its focus to new products with more growth potential. A retailer will reallocate shelf space. When this happens the manufacturer may need to take on a stronger role in driving demand.

We have repeatedly seen this tactic in the soft drink industry. As the market has matured, the number of different flavors of large brands like Coke and Pepsi has grown significantly. We will look at other product tactics to extend the growth phase and manage the maturity phase in the next section.

Decline Stage

Once a product or industry has entered decline, the focus shifts almost entirely to minimizing costs. Marketing spend is reduced for products in this life stage, because the marketing investment is better spent on other priorities. For goods, distributors will seek to eliminate inventory by cutting prices. For services, companies will reallocate staff to ensure that delivery costs are in check. Where possible, companies may initiate a planned obsolescence process. Commonly technology companies will announce to customers that they will not continue to support a product after a set obsolescence date.

Often a primary focus for marketers during this stage is to transition customers to newer products that are earlier in the product life cycle and have more favorable economics. Promotional activities and marketing communications typically focus on making this transition successful among brand-loyal segments who still want the old product. A typical theme of marketing activity is “This familiar brand is still here, but now there’s something even better.”

The New-Product Development Process

There are probably as many varieties of new-product development systems as there are types of companies, but most of them share the same basic steps or stages—they are just executed in different ways. Below, we have divided the process into eight stages, grouped into three phases. Many of the activities are performed repeatedly throughout the process, but they become more concrete as the product idea is refined and additional data are gathered. For example, at each stage of the process, the product team is asking, “Is this a viable product concept?” but the answers change as the product is refined and more market perspectives can be added to the evaluation.

Phase I: Generating and Screening Ideas	**Phase II: Developing New Products**	**Phase III: Commercializing New Products**
Stage 1: Generating New Product Ideas	Stage 4: Business Case Analysis	Stage 6: Test Marketing
Stage 2: Screening Product Ideas	Stage 5: Technical and Marketing Development	Stage 7: Launch
Stage 3: Concept Development and Testing		

Stage 1: Generating New Product Ideas

Generating new product ideas is a creative task that requires a particular way of thinking. Coming up with ideas is easy, but generating *good* ideas is another story. Companies use a range of internal and external sources to identify new product ideas. A SWOT analysis might suggest strengths in existing products that could be the basis for new products or market opportunities. Research might identify market and customer trends. A competitive analysis might expose a hole in the company's product portfolio. Customer focus groups or the sales team might identify unmet customer needs. Many amazing products are also the result of lucky mistakes—product experiments that don't meet the intended goal but have an unintended and interesting application. For example, 3M scientist Dr. Spencer Silver invented Post-It Notes in a failed experiment to create a super-strong adhesive.

The key to the idea generation stage is to explore possibilities, knowing that most will not result in products that go to market.

Stage 2: Screening Product Ideas

The second stage of the product development process is idea screening. This is the first of many screening points. At this early stage much is *not* known about the product and its market opportunity. Still, product ideas that do not meet the organization's overall objectives should be rejected at this stage. If a poor product idea is allowed to pass the screening stage, it wastes effort and money in later stages until it is abandoned. Even more serious is the possibility of screening out a worthwhile idea and missing a significant market opportunity. For this reason, this early screening stage allows many ideas to move forward that may not eventually go to market.

At this early stage, product ideas may simply be screened through some sort of internal rating process. Employees might rate the product ideas according to a set of criteria, for example; those with low scores are dropped and only the highest ranked products move forward.

Stage 3: Concept Development and Testing

Today, it is increasingly common for companies to run some small concept test in a real marketing setting. The *product concept* is a synthesis or a description of a product idea that reflects the core element of the proposed product. Marketing tries to have the most accurate and detailed product concept possible in order to get accurate reactions from target buyers. Those reactions can then be used to inform the final product, the marketing mix, and the business analysis.

New tools leveraging technology for product development are available that support the rapid development of prototypes which can be tested with potential buyers. When concept testing can include an actual product prototype, the early test results are much more reliable. Concept testing helps companies avoid investing in bad ideas and at the same time helps them catch and keep outstanding product ideas.

Stage 4: Business Case Analysis

Before companies make a significant investment in a product's development, they need to be sure that it will bring a sufficient return.

The company seeks to answer such questions as the following:

1. What is the market opportunity for this product?
2. What are the costs to bring the product to market?
3. What are the costs through the stages of the product life cycle?
4. Where does the product fit in the product portfolio and how will it impact existing product sales?
5. How does this product impact the brand?
6. How does this product impact other corporate objectives such as social responsibility?

The marketing budget and costs are one element of the business analysis, but the full scope of the analysis includes all revenues, costs, and other business impacts of the product.

Stage 5: Technical and Marketing Development

A product that has passed the screening and business analysis stages is ready for technical and marketing development. Technical development processes vary greatly according to the type of product. For a product with a complex manufacturing process, there is a lab phase to create specifications and an equally complex phase to develop the manufacturing process. For a service offering, there may be new processes requiring new employee skills or the delivery of new equipment. These are only two of many possible examples, but in every case the company must define both what the product is and how it will be delivered to many buyers.

While the technical development is under way, the marketing department is testing the early product with target customers to find the best possible marketing mix. Ideally, marketing uses product prototypes or early production models to understand and capture customer responses and to identify how best to present the product to the market. Through this process, product marketing must prepare a complete marketing plan—one that starts with a statement of objectives and ends with a coherent picture of product distribution, promotion, and pricing integrated into a plan of marketing action.

Stage 6: Test Marketing and Validation

Test marketing is the final stage before commercialization; the objective is to test all the variables in the marketing plan including elements of the product. Test marketing represents an actual launching of the total marketing program, done on a limited basis.

Initial product testing and test marketing are not the same. Product testing is totally initiated by the producer: he or she selects the sample of people, provides the consumer with the test product, and offers the consumer some sort of incentive to participate.

Test marketing, on the other hand, is distinguished by the fact that the test group *represents* the full market, the consumer must make a purchase decision and pay for the product, and the test product must compete with the existing products in the actual marketing environment. For these and other reasons, a market test is an accurate simulation of the broader market and serves as a method for reducing risk. It should enhance the new product's probability of success and allow for final adjustment in the marketing mix before the product is introduced on a large scale.

Stage 7: Launch

Finally, the product arrives at the commercial launch stage. The marketing mix comes together to introduce the product to the market. This stage marks the beginning of the product life cycle.

Stage 8: Evaluation

The launch does not in any way signal the end of the marketing role for the product. To the contrary, after launch the marketer finally has real market data about how the product performs in the wild, outside the test environment. These market data initiate a new cycle of idea generation about improvements and adjustments that can be made to all elements of the marketing mix.

7.3 GLOBAL PRODUCTS AND SERVICES

Straight Product Extension

Companies deciding to market their products in different countries typically have a choice of three common strategies to pursue. The first is the straight **product extension**. This means taking the company's current products and selling them in other countries without making changes to the product. The advantages of this strategy are that the company doesn't need to invest in new research, development, or manufacturing. Changes may be made in packaging and labelling, but these are driven by local regulatory requirements. The disadvantages, however, are that its products may not be well suited to local needs and that the products may be more costly due to higher manufacturing and labour costs in the United States.

Product Adaptation

The second strategy is **product adaptation** and refers to modifying the company's existing product in a way that makes it fit better with local needs. For example, when Procter & Gamble (P&G) introduced Tide laundry detergent in emerging markets like India, it changed the formulation to remove softeners. The reformulated Tide cost less than the original Tide. This change was important because price was an important factor in India where income levels were lower. Indian consumers were more able to afford the reformulated Tide.

Another way to localize a product is through packaging. Locally appropriate packaging doesn't just mean using the country's language. It also means creating packaging sizes that suit the country. For example, a company wanting to make its products more economical to less-wealthy countries may be tempted to sell larger, economy-sized packaging. But emerging-market consumers often prefer smaller package sizes, even if that increases the cost-per-use. They tend to buy sachets of shampoo rather than economy-size bottles. These smaller sizes are also easier to transport to local villages or to store in smaller-sized homes.

Mobile-phone maker Nokia went a step further in localizing its phones to different markets. The company uses local designers to create mobile-phone handset models that are specifically appropriate for each country. For example, the handsets designed in India are dust resistant and have a built-in flashlight. The models designed in China have a touchscreen, stylus, and Chinese character recognition.

Local designers are more likely to understand the needs of the local population than headquarters-located designers do.

The examples of Tide and Nokia show how companies can create a version of their existing product tailored to specific countries.

Product Invention

The third strategy, **product invention**, is creating an entirely new product for the target market. In this strategy, companies go back to the drawing board and rethink how best to design a product for that country.

The first step in inventing a product for a new country market is to understand the key product characteristics needed to succeed in that market. For example, when P&G wanted to sell diapers in BRIC countries (i.e., Brazil, Russia, India, and China), it started from square one. Rather than merely modifying the existing design, P&G engaged local knowledge and reconsidered all the key features of the design in the context of the needs of the emerging markets.

A major issue was price. To make the diaper affordable, P&G settled on an aggressive price target—each diaper should cost as much as one egg. But the company also wanted a diaper that could uphold the P&G brand name. At first, the designers thought that the lower-cost product needed to do everything that the current developed-world product did. But further discussions refined and narrowed the definition so that P&G could meet the cost target without damaging the brand.

P&G designers debated features such as absorbency, colour, fit, and packaging to find a design that was acceptable on cost targets, acceptable to emerging-market consumers, and acceptable as a P&G-branded product. The designers considered materials and how they could avoid using high-paid, specialized suppliers. Some characteristics, such as packaging, could be adjusted to meet local cost standards. In other cases, a characteristic was nonnegotiable—such as corporate social-responsibility issues. For example, P&G wanted to ensure that none of the suppliers to its diaper business used child labour. In the end, P&G succeeded by understanding both the critical elements of the brand and the emerging-market customers' expectations.

Nuances of Product Extension, Adaptation, and Invention

The product-adaptation strategy is easier for firms to execute than product invention. Nonetheless, even product adaptation requires understanding the local market well. Consider Ford Motor Company's missteps in adapting its mid-priced car model to the Indian market. Ford realized that it needed to lower the cost of its car to make it more affordable to Indian consumers. Ford brought a team of designers together in Detroit and tasked them with figuring out how to reduce the cost of the car. The designers looked at removing nonessential elements. The first feature to go was air conditioning. Next, the team decided to remove power windows in the back, keeping them only in the front. These and other such tweaks brought the total cost of the car down from $20,000 to $15,000. Reducing the cost by 25 percent is notable, but unfortunately the design team lacked vital local knowledge about India. First, even though the price of the car was lower, the $15,000 price point in India is still way above what the middle class can afford. The Indians who can afford a $15,000 car are the very rich. Second, the very rich in India who can afford to pay $15,000 for a car can also afford (and will have) a chauffeur. Remember the clever idea of removing the air conditioning and the power windows in the back? The consequence is that the chauffeur is the only one who gets a breeze. Given the sweltering summer temperatures and traffic congestion in Indian cities, you can guess that the Ford car didn't sell well (Govindarajan, 2009).

Country-of-Origin Effect

The country-of-origin effect refers to consumers using the country where the product was made as a barometer for evaluating the product. Their perceptions of the country influence whether they will perceive the product favourably or unfavourably. That perception influences consumers' purchasing decisions. For example, France is known for its wines and luxury goods. Wines from Chile may be just as good and more affordably priced, but consumers may perceive French wines to be better due to the country-of-origin effect. In the 1960s, "Made in Japan" was a signal of low quality, but over time Japan has changed that perception through a dedicated focus on high quality. Specifically, Japan adopted Total Quality Management (TQM) which is a set of management practices initially introduced to Japan by W. Edwards Deming. The focus of TQM is increasing quality and reducing errors in production or service delivery. TQM consists of systematic processes, planning, measurement, continuous improvement, and customer satisfaction. These days, "made in Japan" is viewed positively, but "made in China" faces more of a stigma. Likewise, consumers in Colombia don't want products that are made in Colombia. A similar problem happens with Mercedes-Benz—Mercedes-Benz cars assembled in Egypt have much lower resale value than those assembled in Germany. In these cases, local assembly in Egypt might be taken as a sign of inferior quality.

Reverse Innovation: How Designing for Emerging Economies Brings Benefits Back Home

Increasingly, marketing and innovation are directly linked. **Reverse innovation** means designing a product for a developing country and bringing that innovation back to the home country. Creating new products and services for developing countries requires radical innovation and opens new opportunities in developed-world markets as well.

To learn more about reverse innovations, view this article: 20 Inspirational Reverse Innovation Examples In Business.

7.4 PRODUCT ADAPTATION DECISIONS

Value proposition adaptation deals with a whole range of issues, ranging from the quality and appearance of products to materials, processing, production equipment, packaging, and style. A product may have to be adapted to meet the physical, social, or mandatory requirements of a new market. It may have to be modified to conform to government regulations or to operate effectively in country-specific geographic and climatic conditions. Or it may be redesigned or repackaged to meet the diverse buyer preferences or standard-of-living conditions. A product's size and packaging may also have to be modified to facilitate shipment or to conform to possible differences in engineering or design standards in a country or in regional markets. Other dimensions of value proposition adaptation include changes in brand name, colour, size, taste, design, style, features, materials, warranties, after-sale service, technological sophistication, and performance.

The need for some changes, such as accommodating different electricity requirements, will be obvious. Others may require in-depth analysis of societal customs and cultures, the local economy, technological sophistication of people living in the country, customers' purchasing power, and purchasing behaviour. Legal, economic, political, technological, and climatic requirements of a country market may all dictate some level of localization or adaptation.

As tariff barriers (tariffs, duties, and quotas) are gradually reduced around the world in accordance with World Trade Organization (WTO) rules, other *nontariff barriers*, such as *product standards*, are proliferating. For example, consider regulations for food additives. Many of the United States' "generally recognized as safe" (GRAS) additives are banned today in foreign countries. In marketing abroad, documentation is important not only for the amount of additive but also for its source, and often additives must be listed on the label of ingredients. As a result, product labelling and packaging must often be adapted to comply with another country's legal and environmental requirements.

Many products must be adapted to local *geographic and climatic* conditions. Factors such as topography, humidity, and energy costs can affect the performance of a product or even define its use in a foreign market. The cost of petroleum products, along with a country's infrastructure, for example, may mandate the need to develop products with a greater level of energy efficiency. Hot, dusty climates of countries in the Middle East and other emerging markets may force automakers to adapt automobiles with different types of filters and clutch systems than those used in North America, Japan, and European countries. Even shampoo and cosmetic product makers have to chemically reformulate their products to make them more suited for people living in hot, humid climates.

The availability, performance, and level of sophistication of a *commercial infrastructure* will also warrant a need for adaptation or localization of products. For example, a company may decide not to market its line of frozen food items in countries where retailers do not have adequate freezer space. Instead, it may choose to develop dehydrated products for such markets. Size of packaging, material used in packaging, before- and after-sale service, and warranties may have to be adapted in view of the scope and level of service provided by the distribution structure in the country markets targeted. In the event that postsale servicing facilities are conspicuous by their absence, companies may need to offer simpler, more robust products in overseas markets to reduce the need for maintenance and repairs.

Differences in *buyer preferences* are also major drivers behind value proposition adaptation. Local customs, such as religion or the use of leisure time, may affect market acceptance. The sensory impact of a product, such as taste or its visual impression, may also be a critical factor. The Japanese consumer's desire for beautiful packaging, for example, has led many U.S. companies to redesign cartons and packages specifically for this market. At the same time, to make purchasing mass-marketed consumer products more affordable in lesser developed countries, makers of products such as razor blades, cigarettes, chewing gum, ball-point pens, and candy bars repackage them in small, single units rather than multiple units prevalent in the developed and more advanced economies.

As a general rule, *packaging design* should be based on customer needs. For industrial products, packaging is primarily functional and should reflect needs for storage, transportation, protection, preservation, reuse, and so on. For consumer products, packaging has additional functionality and should be protective, informative, appealing, conform to legal requirements, and reflect buying habits.

In analyzing adaptation requirements, careful attention to *cultural differences* between the target customers in the home country (country of origin) and those in the host country is extremely important. The greater the cultural differences between the two target markets, the greater the need for adaptation. Cultural considerations and customs may influence branding, labelling, and package considerations. Certain colours used on labels and packages may be found unattractive or offensive. Red, for example, stands for good luck and fortune in China and parts of Africa; aggression, danger, or warning in Europe, America, Australia, and New Zealand; masculinity in parts of Europe; mourning (dark red) in the Ivory Coast; and death in Turkey. Blue denotes immortality in Iran, while purple denotes mourning in Brazil and is a symbol of expense in some Asian cultures. Green is associated with high tech in Japan, luck in the Middle East, connotes death in South America and countries with dense jungle areas, and is a forbidden colour in Indonesia. Yellow is associated with femininity in the United States and many other countries but denotes mourning in Mexico and strength and reliability in Saudi Arabia. Finally, black is used to signal mourning, as well as style and elegance, in most Western nations, but it stands for trust and quality in China, while white—the symbol for cleanliness and purity in the West—denotes mourning in Japan and some other Far Eastern nations.

A country's *standard of living* and the *target market's purchasing power* can also determine whether a company needs to modify its value proposition. The level of income, the level of education, and the availability of energy are all factors that help predict the acceptance of a product in a foreign market. In countries with a lower level of purchasing power, a manufacturer may find a market for less-sophisticated product models or products that are obsolete in developed nations. Certain high-technology products are inappropriate in some countries, not only because of their cost but also because of their function. For example, a computerized, industrial washing machine might replace workers in a country where employment is a high priority. In addition, these products may need a level of servicing that is unavailable in some countries.

When potential customers have limited purchasing power, companies may need to develop an entirely new product designed to address the market opportunity at a price point that is within the reach of a potential target market. Conversely, companies in lesser-developed countries that have achieved local success may find it necessary to adopt an "up-market strategy" whereby the product may have to be designed to meet world-class standards.

Mini Case: Kraft Reformulates Oreo Cookies in China

Kraft's Oreo has long been the top-selling cookie in the U.S. market, but the company had to reinvent it to make it sell in China. Unlike their American counterparts, Oreo cookies sold in China are long, thin, four-layered, and coated in chocolate.

Oreos were first introduced in 1912 in the United States, but it was not until 1996 that Kraft introduced Oreos to Chinese consumers. After more than 5 years of flat sales, the company embarked on a complete makeover. Research had shown, among other findings, that traditional Oreos were too sweet for Chinese tastes and that packages of 14 Oreos priced at 72 cents were too expensive. In response, Kraft developed and tested 20 prototypes of reduced-sugar Oreos with Chinese consumers before settling on a new formula; it also introduced packages containing fewer Oreos for just 29 cents.

But Kraft did not stop there. The research team had also picked up on China's growing thirst for milk, which Kraft had not considered before. It noted that increased milk demand in China and other developing markets was a contributing factor to higher milk prices around the world. This put pressure on food manufacturers like Kraft, whose biggest business is cheese, but it also spelled opportunity.

Kraft began a grassroots marketing campaign to educate Chinese consumers about the American tradition of pairing milk with cookies. The company created an Oreo apprentice program at 30 Chinese universities that drew 6,000 student applications. Three hundred were accepted and trained as Oreo-brand ambassadors. Some of them rode around Beijing on bicycles, outfitted with wheel covers resembling Oreos, and handed out cookies to more than 300,000 consumers. Others organized Oreo-themed basketball games to reinforce the idea of dunking cookies in milk. Television commercials showed kids twisting apart Oreo cookies, licking the cream centre, and dipping the chocolate cookie halves into glasses of milk.

Still, Kraft realized it needed to do more than just tweak its recipe to capture a bigger share of the Chinese biscuit market. China's cookie-wafer segment was growing faster than the traditional biscuit-like cookie segment, and Kraft needed to catch up to rival Nestlé SA, the world's largest food company, which had introduced chocolate-covered wafers there in 1998.

So Kraft decided this market opportunity was big enough to justify a complete remake of the Oreo itself and, departing from longstanding corporate policy for the first time, created an Oreo that looked almost nothing like the original. The new Chinese Oreo consisted of four layers of crispy wafer filled with vanilla and chocolate cream, coated in chocolate. To ensure that the chocolate product could be shipped across the country, could withstand the cold climate in the north and the hot, humid weather in the south, and would still melt in the mouth, the company had to develop a new proprietary handling process.

Kraft's adaptation efforts paid off. In 2006, Oreo wafer sticks became the best-selling biscuit in China, outpacing HaoChiDian, a biscuit brand made by the Chinese company Dali. The new Oreos also outsell traditional (round) Oreos in China. They also have created opportunities for further aggregation and product innovation. Kraft now sells the wafers elsewhere in Asia, as well as in Australia and Canada, and the company has introduced another new product in China: wafer rolls, a tube-shaped wafer lined with cream. The hollow cookie can be used as a straw through which to drink milk.

This success encouraged Kraft to empower managers in other businesses around the globe. For example, to take advantage of the European preference for dark chocolate, Kraft introduced dark chocolate in Germany under its Milka brand. Research showed that Russian consumers like premium instant coffee, so Kraft positioned its Carte Noire freeze-dried coffee as an upscale brand. And in the Philippines, where iced tea is popular, Kraft launched iced-tea-flavoured Tang.

As Kraft's experience shows, successful global marketing and branding is rooted in a careful blend of aggregation, adaptation, and arbitrage strategies that is tailored to the specific needs and preferences of a particular region or country.

(Jargon, 2008)

7.5 GLOBAL INNOVATION

Many companies now have global supply chains and product development processes, but few have developed effective global innovation capabilities (Santos et al., 2004). Increasingly, however, technology access and innovation are becoming key global strategic drivers. This move from cost to growth and innovation is likely to continue as the centre of gravity of economic activity shifts further to the East.

A core competency in global innovation—the ability to leverage new ideas all around the world—has become a major source of global competitive advantage, as companies such as Nokia, Airbus, SAP, and Starbucks demonstrate. They realize that the principal constraint on innovation "performance" is knowledge. Accessing a diverse set of sources of knowledge is, therefore, a key challenge and is critical to successful differentiation. Companies whose knowledge pool is the same as that of its competitors will likely develop uninspired "me, too" products; access to a diversity of knowledge allows a company to move beyond incremental innovation to attention-grabbing designs and breakthrough solutions.

There is an interesting relationship between *geography* and *knowledge* diversity. In Finland, for example, the high cost of installing and maintaining fixed telephone lines in isolated places has spurred advances in radio telephony. In Germany, cultural and political factors have encouraged the growth of a strong "green movement," which in turn has generated a distinctive market and technical knowledge in recycling and renewable energy. Just-in-time production systems were pioneered in part because of high land costs there. Recognition of the role played by geography in innovation has prompted many companies to globalize their perspective on the innovation process. For example, pharmaceutical companies such as Novartis AG and GlaxoSmithKline plc now realize that the knowledge they need extends far beyond traditional chemistry and therapeutics to include biotechnology and genetics. What is more, much of this new knowledge comes from sources other than the companies' traditional R&D labs in Basel, Bristol, and in New Jersey, from places such as California, Tel Aviv, Cuba, or Singapore. For these companies, globalization of innovation processes is no longer optional—it has become imperative.

Companies that globalize their supply chains by accessing raw materials, components, or services from around the world are typically able to reduce the overall costs of their operations. Similarly, a side benefit of global innovation is cost reduction. Consider, for example, how companies are now leveraging software programmers in Bangalore, India, aerospace technologists in Russia, or chipset designers in China to cut the costs of their innovation processes.

To reap the benefits of global innovation, companies must do three things:

1. *Prospect* (find the relevant pockets of knowledge from around the world)
2. *Assess* (decide on the optimal "footprint" for a particular innovation)
3. *Mobilize* (use cost-effective mechanisms to move distant knowledge without degrading (Santos et al., 2004).

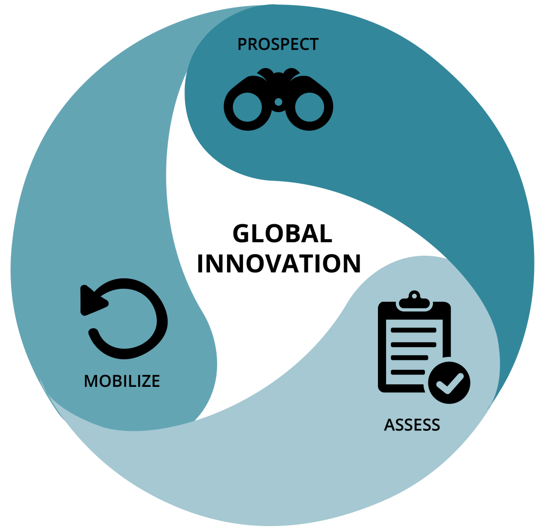


Fig 7.2 "Ways to get the benefits of global innovation" by Alyssa Giles, CC BY-NC-SA 4.0.

Prospecting—that is, finding valuable new pockets of knowledge to spur innovation—may well be the most challenging task. The process involves knowing what to look for, where to look for it, and how to tap into a promising source. Santos et al. (2004) cite the efforts of the cosmetics maker Shiseido Co., Ltd., in entering the market for fragrance products. Based in Japan, a country with a very limited tradition of perfume use, Shiseido was initially unsure of the precise knowledge it needed to enter the fragrance business. But the company did know where to look for it. So it bought two exclusive beauty boutique chains in Paris, mainly as a way to experience, firsthand, the personal care demands of the most sophisticated customers of such products. It also hired the marketing manager of Yves Saint Laurent Parfums and built a plant in Gien, a town located in the French perfume "cluster." France's leadership in that industry made the *where* fairly obvious to Shiseido. The *how* had also become painfully clear because the company had previously flopped in its efforts to develop perfumes in Japan. Those failures convinced Shiseido executives that to access such complex knowledge—deeply rooted in local culture and combining customer information, aesthetics, and technology—the company had to immerse itself in the French environment and learn by doing. Having figured out the *where* and *how*, Shiseido would gradually learn *what* knowledge it needed to succeed in the perfume business.

Assessing new sources of innovation, that is, incorporating new knowledge into and optimizing an existing innovation network, is the second important challenge companies face. If a semiconductor manufacturer is developing a new chipset for mobile phones, for example, should it access technical and market knowledge from Silicon Valley, Austin, Hinschu, Seoul, Bangalore, Haifa, Helsinki, and Grenoble? Or should it restrict itself to just some of those sites? At first glance, determining the best footprint for innovation does not seem fundamentally different from the trade-offs companies face in optimizing their global supply chains: adding a new source might reduce the price or improve the quality of a required component, but more locations may also mean additional complexity and cost. Similarly, every time a company adds a source of knowledge to the innovation process, it might improve its chances of developing a novel product, but it also increases costs.

Determining an optimal innovation footprint is more complicated, however, because the direct and indirect cost relationships are far more imprecise.

Mobilizing the footprint, that is, integrating knowledge from different sources into a virtual melting pot from which new products or technologies can emerge, is the third challenge. To accomplish this, companies must bring the various pieces of (technical) knowledge that are scattered around the world together and provide a suitable organizational form for innovation efforts to flourish. More importantly, they would have to add the more complex, contextual (market) knowledge to integrate the different pieces into an overall innovation blueprint.

Case: P&G's Success in Trickle-Up Innovation: Vicks Cough Syrup With Honey

A new over-the-counter medicine from Vicks that has recently become popular in Switzerland is not as new as it seems. The product, Vicks Cough Syrup with Honey, is really just the latest incarnation of a product that Vicks parent company, Procter & Gamble (P&G), initially created for lower-income consumers in Mexico and then "trickled up" to more affluent markets.

The term "trickle up" refers to a strategy of creating products for consumers in emerging markets and then repackaging them for developed-world customers. Until recently, affluent consumers in the United States and Western Europe could afford the latest and greatest in everything. Now, with purchasing power dramatically reduced because of the global recession, budget items once again make up a growing portion of total sales in many product categories.

P&G is not the only multinational company using this strategy. Other practitioners of trickle-up innovation include General Electric (GE), Nestlé, and Nokia. In early 2008, GE Healthcare launched the MAC 400, GE's first portable Electrocardiograph (ECG) that was designed in India for the fast-growing local market there. The company simplified elements of its earlier, 65-lb devices made for U.S. hospitals by shrinking its case to the size of a fax machine and removing features such as the keyboard and screen. The smaller MAC 400 costs only $1,500, versus $15,000 for its U.S. predecessor. This trickle-down innovation trickled back up again when GE Healthcare decided to sell the unit in Germany as well.

Nestlé offers inexpensive instant noodles in India and Pakistan under its Maggi brand. The line includes dried noodles that are engineered to taste as if they were fried, while they have a whole-wheat flavor that is popular in South Asia. And Nokia researches how people in emerging nations share phones, such as the best-selling 1100 series of devices created for developing-world consumers. The company then uses the information as inspiration for new features for developed-world users.

But what is unique about P&G's Honey Cough, as it is also called, is that it has moved around the globe in more than one direction. Honey Cough originated in 2003 in P&G's labs in Caracas, Venezuela, which creates products for all of Latin America. Market research revealed that Latin American shoppers tended to prefer homeopathic remedies for coughs and colds, so P&G set out to create a medicine using natural honey rather than the artificial flavors typically used. The company first introduced the syrup in Mexico, under the label VickMiel, and then in other Latin American markets, including Brazil.

P&G deduced that the product would appeal to parts of the United States that have large Hispanic populations. In 2005, the company rebranded it as Vicks Casero for sale in California and Texas, at a price slightly less than Vicks' mainstay product, Vicks Formula 44. Within the first year of its release, the company boosted distribution to 27% more outlets.

Figuring that natural ingredients could appeal to even wider groups, P&G took the product to other markets where research indicated that homeopathic cold medicines are popular. In the past 2 years, the company has been marketing the product in Britain, France, Germany, and Italy, as well as Switzerland, and plans to add other Western European countries to the roster.

And Western Europe is not the last destination for iterations of Honey Cough. If P&G's current market research in the greater United States shows that mainstream American shoppers will buy Honey Cough, P&G will repackage it and market it nationwide, not just as Vicks Casero in Latino markets.

Developing and marketing a new product for each nation or ethnic group can take half a decade. Trickle-up innovation can reduce this time by several years, which explains its appeal. In each rollout, P&G has needed to do little more than make adjustments for each nation's health regulations.

At a time when companies are looking to speed product offerings while dealing with shrinking budgets and cash-strapped consumers, P&G's experience with its Honey Cough line shows how an international product portfolio can be tapped quickly and cheaply—that is, if American companies learn how to go against the flow.

(Jana, 2009).

7.6 GLOBAL INNOVATION AT THE BOP

Contemporary View of BOP

In 1998, Professors C. K. Prahalad and Stuart L. Hart defined the bottom of the pyramid (BOP) as the billions of people living on less than $2 per day. Both men expanded this definition of BOP in their subsequent writing (Prahalad, 2004; Hart, 2005). The BOP is estimated to comprise between four billion and five billion people.

Too Good to Be True?

Professor Aneel Karnani at the University of Michigan argues that the BOP proposition is indeed too good to be true. "It is seductively appealing, but it is riddled with fallacies. There is neither glory nor fortune at the bottom of the pyramid—it is all a mirage" (Karnani, 2006). He argues that the BOP proposition is logically flawed and is not supported by empirical evidence. He proposes an alternative approach for the private sector to alleviate poverty by viewing the poor as producers, not consumers. This shift in view, Karnani argues, is the way to alleviate poverty by raising the incomes of the poor.

In Prahalad and Hart's view, companies that understand the potential for commercial consumption at the BOP can open a new, potentially lucrative market that benefits the business as well as BOP consumers. By innovating to meet the needs of BOP customers, a company treats them with dignity and respect that previously was afforded only to the wealthy, Prahalad and Hart say.

Twelve Principles of BOP Innovation

Addressing the bottom of the pyramid requires a fresh managerial mind-set, summarized below in Prahalad's "12 Principles of BOP Innovation"—which are innovations themselves (Prahalad, 2004). In developed markets, Prahalad suggests that one may take the availability of electricity, telephones, credit, refrigeration, and other such amenities for granted. At the BOP, the infrastructure is much spottier and more hostile. Consumers may have to cope with frequent electric-power blackouts and brownouts. Credit may be extremely costly. Refrigeration may be unavailable. Products marketed to the bottom of the pyramid must be able to withstand such an environment.

Below are Prahalad's "12 Principles of BOP Innovation," along with examples of each.

1. **Focus on value and on delivering performance for the price.** The BOP consumer isn't interested merely in cheap prices but in getting the greatest possible performance for the price paid. It's extraordinary how low a price can be and still be highly profitable, if the seller is organized to deliver value. For example, doctors at India's Aravind Eye Care System, the world's largest eye-care business, perform hundreds of thousands of cataract surgeries each year. The prices range from $50 to $300 per surgery, including the hospital stay. Aravind is quite profitable, although 60 percent of its patients pay nothing.
2. **Innovate.** Old technologies can't solve the problems of BOP consumers, and products aimed at the BOP market can't simply be watered-down versions of developed-world products. Instead, products must be rethought to bring radically lower cost while at the same time having features that meet the BOP's highest needs. For example, Hindustan Unilever Limited (HUL), a Unilever subsidiary, developed a new molecular encapsulation technology to prevent iodized salt from losing its iodine before consumption. To test the efficacy of the technology, the researchers used radioactive tracing techniques pioneered by the Indian Atomic Energy Commission.
3. **Make the solution scalable.** When delivering high performance at affordable prices, profits must be generated through volume sales. The product itself must be low cost, but with four billion to five billion BOP customers across the world, scaling the operation is what will make the venture sustainable. Solutions should be scalable across borders.
4. **Aim to conserve resources.** BOP consumers cannot afford to waste resources. Per capita water consumption in the United States is almost 2,000 cubic meters per year, compared to less than 500 in China and less than 700 in India. The developed world's high standard of living is a water- and waste-intensive lifestyle. Innovations should emphasize conserving resources, recycling materials, and eliminating waste. Creating products for five billion people means designing the products in ways that can be environmentally sustainable. China's focus on electric cars rather than gasoline-powered cars reflects the reality that it's unlikely China could obtain the oil it would need for that many cars and that its extremely polluted cities could handle the additional exhaust fumes.
5. **Identify functionality.** BOP customers likely require different functionality than high-end consumers. For example, prosthetic legs developed for India's BOP consumers needed to meet some special requirements: consumers needed to be able to squat, sit cross-legged, and walk on rough ground. Dr. Pramod Karan Sethi and Ram Chandra developed the Jaipur Foot prosthetic for this purpose. The charity Bhagwan Mahaveer Viklang Sahayata Samiti, which is based in Jaipur, India, made them available for less than $30 (Mcgirk, 1997).
6. **Think in terms of process innovations.** One way to bring costs down dramatically is to standardize

processes. That's how Aravind is able to bring down the costs of cataract surgery so dramatically. Aravind made the process highly standardized and trained young village women to prepare patients and handle postoperative care. Thus doctors focus exclusively on surgery and perform only cataract surgery—nothing else. This focused process lets one doctor and two technicians perform fifty surgeries per day.

7. **Reduce the skills required to do the job.** Design products and services suitable to people without skills. Voxiva, a Peruvian start-up, developed a system enabling health-care workers to diagnose illnesses such as smallpox by comparing a patient's lesions to a picture of a similar lesion. With this simplified diagnostic process, health-care workers don't require great skills to know when to call a doctor.
8. **Educate consumers in the use of products.** This may require collaborating with nongovernmental organizations (NGOs), governments, and others. HUL launched a program in some of India's village schools to promote the washing of hands with soap as a way to prevent the childhood diarrhea that kills two million children per year. HUL educated the children, who in turn educated their parents.
9. **Design products and services to operate in very tough infrastructure environments.**For example, when Indian conglomerate ITC built a network connecting Indian villages, it had to provide personal computers that could handle wide voltage fluctuations. ITC included surge suppressors and solar panels to give the system adequate, reliable electricity.
10. **Make the interface simple and the learning curve short.** In Mexico, the chain retailer Elektra uses automated teller machines (ATMs) with a fingerprint identification system so BOP consumers don't have to remember lengthy identification codes.
11. **Innovate in distribution.** Avon has built a Brazilian direct-sales business that delivers revenues of $1.7 billion annually.
12. **Challenge assumptions.** The Jaipur Foot and Aravind Eye Care System hospitals defy conventional wisdom about how (and at what price) it's possible to deliver health care to the poor.

Ethics in Action

NextBillion.net began as an initiative of the World Resources Institute's Markets and Enterprise Program. The name refers to the next billion people to rise from the bottom of the pyramid into the middle class and connotes the next billion in profits that companies can make serving this market. The purpose of the site is to provide a source for news, analysis, research and discussion on development through enterprise and BOP ideas. In addition, the NextBillion.net website has a career centre that posts jobs (consulting projects as well as full-time jobs and academic appointments). As the site states, its mission is to "highlight the development and implementation of business strategies that open opportunities and improve the lives of the world's approximately 4 billion low-income producers and consumers" (NextBillion, n.d.).

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7.8 KEY TERMS

Key Terms

Brand is a bundle of images and experiences in the mind of the customer. 7.0

Business products are purchased by other companies. Some products, like computers, for instance, may be both consumer products and business products, depending on who purchases and uses them. 7.1

Consumer products are purchased by the final consumer. 7.1

Convenience products: The product is an inexpensive product that requires a minimum amount of effort on the part of the consumer in order to select and purchase it. 7.1

Product: can be viewed as a collection of tangible and intangible attributes (features, functions, benefits, and uses) that collectively provide benefits to a buyer. 7.0/7.1

Product adaptation and refers to modifying the company's existing product in a way that makes it fit better with local needs. 7.3

Product extension. This means taking the company's current products and selling them in other countries without making changes to the product. 7.3

Product invention, is creating an entirely new product for the target market. 7.3

Product life cycle (PLC) is a model marketers use to identify the phases of a product's development to help identify strategies to influence it. 7.2

Prospecting—that is, finding valuable new pockets of knowledge to spur innovation. 7.5

Reverse innovation means designing a product for a developing country and bringing that innovation back to the home country. 7.3

Shopping products are usually more expensive and are purchased occasionally. 7.1

Specialty products are so unique that it's worth it for buyers to go to great lengths to find and purchase them. 7.1

Unsought products are those the consumer never plans or hopes to buy. 7.1

CHAPTER 8: GLOBAL PRICING

Chapter Outline

8.0 INTRODUCTION

Learning Objectives

After reading this section, students should be able to:

1. Explain pricing from the customer's viewpoint.
2. Describe the objectives businesses hope to achieve with product pricing.
3. Explain the methods businesses use for discounts and allowances.
4. Apply the basics of pricing to global pricing decisions.
5. Discuss the global marketer's view of price.
6. List the alternative approaches to determining global prices.
7. Discuss penetration and skimming in global pricing.
8. Explain the role of currency fluctuations and global pricing.

Pricing decisions are a critical element of the marketing mix that must reflect costs, competitive factors, and customer perceptions regarding value of the product. In a true global market, the law of one price would prevail. Pricing strategies include market skimming, market penetration, and market holding. Novice exporters frequently use cost-plus pricing. International terms of a sale such as ex-works, F.A.S., F.O.B., and C.I.F. are known as Incoterms and specify which party to a transaction is responsible for covering various costs. These and other costs lead to export price escalation, the accumulation of costs that occurs when products are shipped from one country to another.

Expectations regarding currency fluctuations, inflation, government controls, and the competitive situation must also be factored into pricing decisions. The introduction of the euro has impacted price strategies in the EU because of improved price transparency. Global companies can maintain competitive prices in world markets by shifting production sources as business conditions change. Overall, a company's pricing policies can be categorized as ethnocentric, polycentric, or geocentric.

Several additional pricing issues are related to global marketing. The issue of gray market goods arises because price variations between different countries lead to parallel imports. Dumping is another contentious issue that can result in strained relations between trading partners. Price fixing among companies is anticompetitive and illegal.

Transfer pricing is an issue because of the sheer monetary volume of intra-corporate sales and because country governments are anxious to generate as much tax revenue as possible. Various forms of countertrade play an important role in today's global environment. Barter, counter purchase, offset, compensation trading, and switch trading are the main countertrade options.

8.1 OVERVIEW OF PRICE

In this section you'll learn about some very specific, yet standard pricing strategies that organizations use to meet their objectives and address consumer perceptions of value.

Case: Rent the Runway

Rent the Runway is a company that lets customers borrow expensive designer dresses for a short time at a low price—to wear on a special occasion—and then send them back. A customer can rent a Theia gown that retails for $995 for four days for the price of $150. Or, she can rent a gown from Laundry by Shelli Segal that retails for $325 for the price of $100. The company offers a 20 percent discount to first-time buyers and offers a "free second size" option to ensure that customers get the right fit.

Photo by Ajay Suresh, CC BY 2.0

Do the customers get a bargain when they are able to wear a designer dress for a special occasion at 15 percent of the retail price? Does the retail price matter to customers in determining value, or are they only considering the style and price they will pay for the rental?

What does value really mean in the pricing equation?

The Customer's View of Price

Whether a customer is the ultimate user of the finished product or a business that purchases components of the finished product, the customer seeks to satisfy a need through the purchase of a particular product. The customer uses several criteria to decide how much she is willing to spend in order to satisfy that need. Her preference is to pay as little as possible.

PRICE-VALUE EQUATION

VALUE = PERCEIVED BENEFITS - PERCEIVED COSTS

In order to increase value, the business can either increase the perceived benefits or reduce the perceived costs. Both are important aspects of price. If you buy a Louis Vuitton bag for $600, in return for this high price you perceive that you are getting a beautifully designed, well-made bag that will last for decades—in other words, the value is high enough for you that it can offset the cost. On the other hand, when you buy a parking pass to park in a campus lot, you are buying the convenience of a parking place close to your classes. Both of these purchases provide value at some cost. The perceived benefits are directly related to the price-value equation; some of the possible benefits are status, convenience, the deal, brand, quality, choice, and so forth. Some of these benefits tend to go hand in hand. For instance, a Mercedes Benz E750 is a very high-status brand name, and buyers expect superb quality to be part of the value equation (which makes it worth the $100,000 price tag). In other cases, there are tradeoffs between benefits. Someone living in an isolated mountain community might prefer to pay a lot more for groceries at a local store than drive sixty miles to the nearest Safeway. That person is willing to sacrifice the benefit of choice for the benefit of greater convenience.

When we talk about increasing perceived benefits, we refer to this as increasing the "value added." Identifying and increasing the value-added elements of a product are an important marketing strategy. In our initial example, Rent the Runway is providing dresses for special occasions. The price for the dress is reduced because the customer must give it back, but there are many value-added elements that keep the price relatively high, such as the broad selection of current styles and the option of trying a second size at no additional cost. In a very competitive marketplace, the value-added elements become increasingly important, as marketers use them to differentiate the product from other similar offerings.

Perceived costs include the actual dollar amount printed on the price tag, plus a host of additional factors. If you learn that a gas station is selling gas for 25 cents less per gallon than your local station, will you automatically buy from the lower-priced gas station? That depends. You will consider a range of other issues. How far do you have to drive to get there? Is it an easy drive or a drive through traffic? Are there long lines that will increase the time it takes to fill your tank? Is the low-cost fuel the grade or brand that you prefer? Inconvenience, poor service, and limited choice are all possible perceived costs. Other common perceived costs are the risk of making a mistake, related costs, lost opportunity, and unexpected consequences, to name but a few.

Viewing price from the customer's point of view pays off in many ways. Most notably, it helps define value–the most important basis for creating a competitive advantage.

Pricing Objectives

Companies set the prices of their products in order to achieve specific objectives. Consider the following examples.

Nike

In 2014 Nike initiated a new pricing strategy. The company determined from a market analysis that its customers appreciated the value that the brand provided, which meant that it could charge a higher price for its products. Nike began to raise its prices 4–5 percent a year. *Footwear News* reported on the impact of their strategy:

> "The ability to raise prices is a key long-term advantage in the branded apparel and footwear industry—we are particularly encouraged that Nike is able to drive pricing while most U.S. apparel names are calling for elevated promotional [and] markdown levels in the near-term," said UBS analyst Michael Binetti. Binetti said Nike's new strategy is an emerging competitive advantage (Jordan, 2014).

Nike's understanding of customer value enabled it to raise prices and achieve company growth objectives, increasing U.S. athletic footwear sales by $168 million in one year.

Southwest Airlines

In 2015 the U.S. airline industry lost $12 billion in value in one day because of concerns about potential price wars. When Southwest Airlines announced that it was increasing its capacity by 1 percent, the CEO of American Airlines—the world's largest airline—responded that American would not lose customers to price competition and would match lower fares. *Forbes* magazine reported on the consequences:
This induced panic among investors, as they feared that this would trigger a price war among the

airlines. The investors believe that competing on prices would undermine the airline's ability to charge profitable fares, pull down their profits, and push them back into the shackles of heavy losses. Thus, the worried investors sold off stocks of major airlines, wiping out nearly $12 billion of market value of the airline industry in a single trading day (Trefis Team, 2015).

Common Pricing Objectives

Not surprising, product pricing has a big effect on company objectives. (You'll recall that objectives are essentially a company's business goals.) Pricing can be used strategically to adjust performance to meet revenue or profit objectives, as in the Nike example above. Or, as the airline-industry example shows, pricing can also have unintended or adverse effects on a company's objectives. Product pricing will impact each of the objectives below:

Profit objective	For example, "Increase net profit in 2016 by 5 percent"
Competitive objective	For example, "Capture 30 percent market share in the product category"
Customer objective	For example, "Increase customer retention"

Of course, over the long run, no company can really say, "We don't care about profits. We are pricing to beat competitors." Nor can the company focus only on profits and ignore how it delivers customer value. For this reason, marketers talk about a company's "orientation" in pricing. Orientation describes the relative importance of one factor compared to the others. All companies must consider customer value in pricing, but some have an orientation toward profit. We would call this profit-oriented pricing.

Profit-Oriented Pricing

Profit-oriented pricing places an emphasis on the finances of the product and business. A business's profit is the money left after all costs are covered. In other words, profit = revenue – costs. In profit-oriented pricing, the price per product is set higher than the total cost of producing and selling each product to ensure that the company makes a profit on each sale.

The benefit of profit-oriented pricing is obvious: the company is guaranteed a profit on every sale. There are real risks to this strategy, though. If a competitor has lower costs, then it can easily undercut the pricing and steal market share. Even if a competitor does not have lower costs, it might choose a more aggressive pricing strategy to gain momentum in the market.

Also, customers don't really care about the company's costs. Price is a component of the value equation, but if the product fails to deliver value, it will be difficult to generate sales.

Finally, profit-oriented pricing is often a difficult strategy for marketers to succeed with, because it limits flexibility. If the price is too high, then the marketer has to adjust other aspects of the marketing mix to create more value. If the marketer invests in the other three Ps—by, say, making improvements to the product, increasing promotion, or adding distribution channels—that investment will probably require additional budget, which will further raise the price.

It's fairly standard for retailers to use some profit-oriented pricing—applying a standard mark-up over wholesale prices for products, for instance—but that's rarely their only strategy. Successful retailers will also adjust pricing for some or all products in order to increase the value they provide to customers.

Competitor-Oriented Pricing

Sometimes prices are set almost completely according to competitor prices. A company simply copies the competitor's pricing strategy or seeks to use price as one of the features that differentiates the product. That could mean either pricing the product higher than competitive products, to indicate that the firm believes it to provide greater value, or lower than competitive products in order to be a low-price solution.

This is a fairly simple way to price, especially with products whose pricing information is easily collected and compared. Like profit-oriented pricing, it carries some risks, though. Competitor-oriented pricing doesn't fully take into account the value of the product to the customer vis-à-vis the value of competitive products. As a result, the product might be priced too low for the value it provides, or too high.

As the airline example illustrates, competitor-oriented pricing can contribute to a difficult market dynamic. If players in a market compete exclusively on price, they will erode their profits and, over time, limit their ability to add value to products.

Customer-Oriented Pricing

PRICE-VALUE EQUATION

VALUE = PERCEIVED BENEFITS - PERCEIVED COSTS

Customer-oriented pricing is also referred to as value-oriented pricing. Given the centrality of the customer in a marketing orientation (and this marketing course!), it will come as no surprise that customer-oriented pricing is the recommended pricing approach because its focus is on providing value to the customer. Customer-oriented pricing looks at the full price-value equation (above) and establishes the price that balances the value. The company seeks to charge the highest price *that supports the value received* by the customer.

Customer-oriented pricing requires an analysis of the customer and the market. The company must understand the buyer persona, the value that the buyer is seeking, and the degree to which the product meets the customer need. The market analysis shows competitive pricing but also pricing for substitutes.

In an attempt to bring the customer voice into pricing decisions, many companies conduct primary market research with target customers. Crafting questions to get at the value perceptions of the customer is difficult, though, so marketers often turn to something called the Van Westerndorp price-sensitivity meter. This method uses the following four questions to understand customer perceptions of pricing:

1. At what price would you consider the product to be so expensive that you would not consider buying it? (Too expensive)
2. At what price would you consider the product to be priced so low that you would feel the quality couldn't be very good? (Too cheap)
3. At what price would you consider the product starting to get expensive, such that it's not out of the question, but you would have to give some thought to buying it? (Expensive/High side)
4. At what price would you consider the product to be a bargain—a great buy for the money? (Cheap/Good value)

Each of these questions asks about the customer's perspective on the product value, with price as one component of the value equation.

Cost-Plus Pricing Method

Cost-plus pricing, sometimes called *gross margin pricing*, is perhaps the most widely used pricing method. The manager selects as a goal a particular gross margin that will produce a desirable profit level. Gross margin is the difference between how much the goods cost and the actual price for which it sells. This gross margin is designated by a percent of net sales. The percent chosen varies among types of merchandise. That means that one product may have a goal of 48 percent gross margin while another has a target of 33.5 percent or 2 percent.

A primary reason that the cost-plus method is attractive to marketers is that they don't have to forecast general business conditions or customer demand. If sales volume projections are reasonably accurate, profits will be on target. Consumers may also view this method as fair, since the price they pay is related to the cost of producing the item. Likewise, the marketer is sure that costs are covered.

A major disadvantage of cost-plus pricing is its inherent inflexibility. For example, department stores often find it hard to meet (and beat) competition from discount stores, catalogue retailers, and furniture warehouses because of their commitment to cost-plus pricing. Another disadvantage is that it doesn't take into account consumers' perceptions of a product's value. Finally, a company's costs may fluctuate, and constant price changing is not a viable strategy.

Markups

Markup is the calculation of the difference between the cost and selling price of merchandise in stock, for a particular department, or for an individual item. The difference may be expressed in dollars or as a percentage. For example, if a man's tie costs $14.50 and is sold for $30 in a Department store, the dollar markup would be $15.50 ($30.00 – $14.50 = $15.50). Markup is most commonly expressed as a percent of the selling price of the merchandise. In this example, the markup of the neckwear is 51.7% ($30.00 – $14.50 ÷ $30.00). A can of soup in a supermarket may cost $.79 and retail for $1.00 which would be a markup of 21% (gross margins of supermarkets is significantly lower than that of department stores).

Given a specific gross margin, you can easily calculate the retail price of a product by dividing the cost of a product by 1 minus the gross margin. For example, if you have a 45% gross margin on a product that costs $20 to produce, it would have a retail price of $36.50:

100% – 45% = 55% or .55

$20.00 ÷ .55 = $36.50

Cost-Oriented Pricing of New Products

Certainly costs are an important component of pricing. No firm can make a profit until it covers its costs. However, the process of determining costs and setting a price based on costs does not take into account what the customer is willing to pay in the marketplace. This strategy is a bit of a trap for companies that develop products and continually add features to them, thus adding cost. Their cost-based approach leads them to add a percentage to the cost, which they pass on to customers in the form of a new, higher price. Then they may be disappointed if their customers do not see sufficient value in the cost-based price.

Discounting Strategies

In addition to deciding about the base price of products and services, marketing managers must also set policies regarding the use of discounts and allowances. There are many different types of price reductions–each designed to accomplish a specific purpose. The major types are described below.

Quantity discounts are reductions in base price given as the result of a buyer purchasing some predetermined quantity of merchandise. In a B2B environment, a noncumulative quantity discount applies to each purchase and is intended to encourage buyers to make larger purchases. This means that the buyer holds the excess merchandise until it is used, possibly cutting the inventory cost of the seller and preventing the buyer from switching to a competitor at least until the stock is used. A cumulative quantity discount applies to the total bought over a period of time. The buyer adds to the potential discount with each additional purchase. Such a policy helps to build repeat purchases.

Both Home Depot and Lowe's offer a contractor discount to customers who buy more than $5,000 worth of goods. Home Depot has a tiered discount for painters, who can save as much as 20 percent off of retail once they spend $7,500 (Home Depot, n.d.)

B2C examples of quantity discounts are everywhere: "two-fors" (buy one for $2.00 or buy two for $3.00), "BOGO" (Buy One Get One free), etc. There are as many quantity discount deals as there are products to price.

- **Seasonal discounts** are price reductions given for out-of-season merchandise—snowmobiles discounted during the summer, for example. The intention of such discounts is to spread demand over the year, which can allow fuller use of production facilities and improved cash flow during the year.
- Seasonal discounts are not always straightforward. It seems logical that gas grills are discounted in September when the summer grilling season is over, and hot tubs are discounted in January when the weather is bad and consumers spend less freely. However, the biggest discounts on large-screen televisions are offered during the weeks before the Super Bowl when demand is greatest. This strategy aims to drive impulse purchases of the large-ticket item, rather than spurring sales during the off-season.
- **Cash discounts** are reductions on base price given to customers for paying cash or within some short time period. For example, a 2 percent discount on bills paid within 10 days is a cash discount. The purpose is generally to accelerate the cash flow of the organization and to reduce transaction costs.
- Generally cash discounts are offered in a B2B transaction where the buyer is negotiating a range of pricing terms, including payment terms. You can imagine that if you offered to pay cash immediately instead of using a credit card at a department store, you wouldn't receive a discount.
- **Trade discounts** are price reductions given to middlemen (e.g., wholesalers, industrial distributors, retailers) to encourage them to stock and give preferred treatment to an organization's products. For example, a consumer goods company might give a retailer a 20 percent discount to place a larger order for soap. Such a discount might also be used to gain shelf space or a preferred position in the store.
- Calico Corners offers a 15 percent discount on fabrics to interior designers who are creating designs or products for their customers. They have paired this with a quantity-discounts program that offers gift certificates for buyers who purchase more than $10,000 in a year.
- **Personal allowances** are similar strategies aimed at middlemen. Their purpose is to encourage middlemen to aggressively promote the organization's products. For example, a furniture manufacturer may offer to pay some specified amount toward a retailer's advertising expenses if the retailer agrees to include the manufacturer's brand name in the ads.

Some manufacturers or wholesalers also give retailers prize money called "***spiffs***," which can be passed on to the retailer's sales clerks as a reward for aggressively selling certain items. This is especially common in the electronics and clothing industries, where spiffs are used primarily with new products, slow movers, or high-margin items.

When employees in electronics stores recommend a specific brand or product to a buyer they may receive compensation from the manufacturer on top of their wages and commissions from the store.

- **Trade-in allowances** also reduce the base price of a product or service. These are often used to help the seller negotiate the best price with a buyer. The trade-in may, of course, be of value if it can be resold. Accepting trade-ins is necessary in marketing many types of products. A construction company with a used grader worth $70,000 probably wouldn't buy a new model from an equipment company that did not accept trade-ins, particularly when other companies do accept them.
- **Price bundling** is a very popular pricing strategy. The marketer groups similar or complementary products and charges a total price that is lower than if they were sold separately. Comcast and Direct TV both follow this strategy by combining different products and services for a set price. Similarly, Microsoft bundles Microsoft Word, Excel, Powerpoint, OneNote, and Outlook in the Microsoft Office Suite. The underlying assumption of this pricing strategy is that the increased sales generated will more than compensate for a lower profit margin. It may also be a way of selling a less popular product—like Microsoft OneNote—by combining it with popular ones. Industries such as financial services, telecommunications, and software companies make very effective use of this strategy.

8.2 GLOBAL PRICING

At its basic level, pricing is the process of determining what a company will receive in exchange for its products. As one of the four "Ps" in the marketing mix, pricing is the only revenue generating element. Several factors affect the global pricing of a product, e.g., manufacturing cost, market place, competition, market condition, and quality of product, distribution channels, country factors and company factors (Alon & Jaffe, 2013). According to Clarke and Wilson (2009), international pricing decisions also need to take account of tariffs, quotas, local taxes, subsidies, grants, currency exchange, rates, local purchasing power, local business and consumer characteristics. Figure 8. 1 shows the drivers of international pricing.

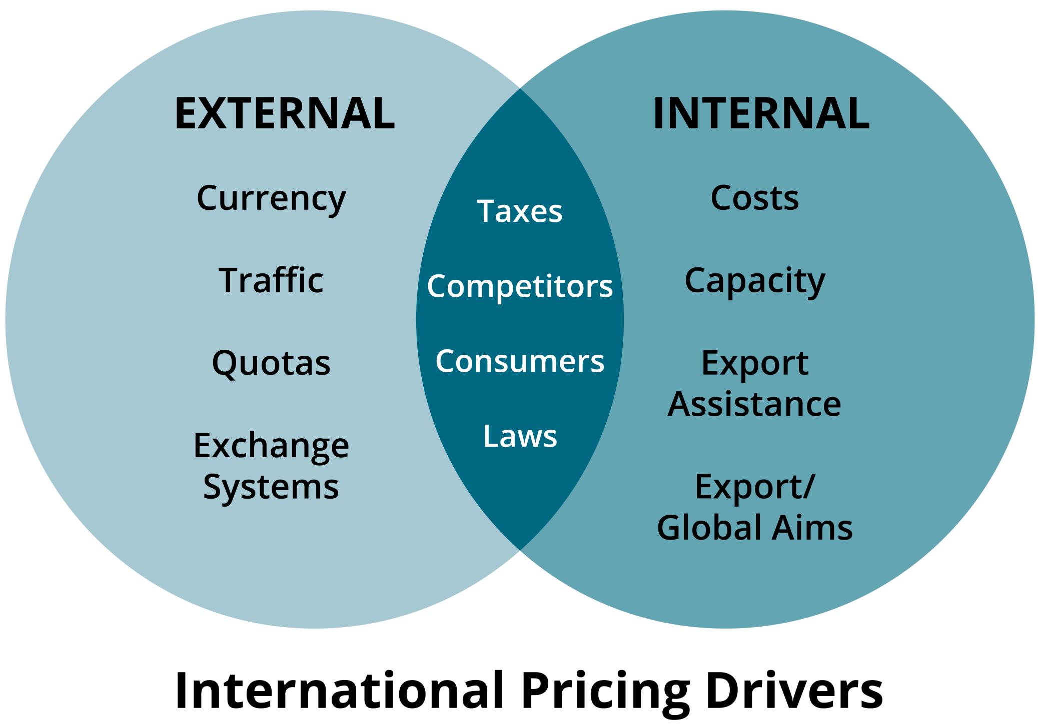


Fig 8.1 International Pricing Drivers. Adapted from Clarke and Wilson (2009) under fair dealing for educational purposes.

Prices can be used both to set values and provide signals in international markets (Eden & Rodriguez, 2004). From a customer's point of view, value is the sole justification for price. Many times customers lack an understanding of the cost of materials and other costs that go into the making of a product. But those customers can understand what that product does for them in the way of providing value. It is on this basis that customers make decisions about the purchase of a product.

Effective pricing meets the needs of consumers and facilitates the exchange process. It requires that marketers understand that not all buyers want to pay the same price for products, just as they do not all want the same product, the same distribution outlets, or the same promotional messages. Therefore, in order to effectively price products, markets must distinguish among various market segments. The key to effective pricing is the same as the key to effective product, distribution, and promotion strategies. Marketers must understand buyers and price their products according to buyer needs if exchanges are to occur. However, one cannot overlook the fact that the price must be sufficient to support the plans of the organization, including satisfying stockholders. Price charged remains the primary source of revenue for most businesses.

Although making the global pricing decision is usually a marketing decision, making it correctly requires an understanding of both the customer and society's view of price as well. In some respects, price setting is the most important decision made by a business. A price set too low may result in a deficiency in revenues and the demise of the business. A price set too high may result in poor response from customers and, unsurprisingly, the demise of the business. The consequences of a poor pricing decision, therefore, can be dire. We begin our discussion of pricing by considering the perspective of the customer.

Price From a Customer's Perspective

A customer can be either the ultimate user of the finished product or a business that purchases components of the finished product. It is the customer that seeks to satisfy a need or set of needs through the purchase of a particular product or set of products. Consequently, the customer uses several criteria to determine how much they are willing to expend in order to satisfy these needs. Ideally, the customer would like to pay as little as possible to satisfy these needs. Therefore, for the business to increase value (i.e. create the competitive advantage), it can either increase the perceived benefits or reduce the perceived costs. Both of these elements should be considered elements of price. To a certain extent, perceived benefits are the mirror image of perceived costs. For example, paying a premium price (e.g. USD 650 for a piece of Lalique crystal) is compensated for by having this exquisite work of art displayed in one's home. Other possible perceived benefits directly related to the price-value equation are status, convenience, the deal, brand, quality, choice, and so forth. Many of these benefits tend to overlap. Thus, providing value-added elements to the product has become a popular strategic alternative. Computer manufacturers now compete on value-added components such as free delivery setup, training, a 24-hour help line, trade-in, and upgrades.

Student Perspective: Sherwin-Williams

A great example of this concept is Sherwin-Williams. Our contractor segment (residential painters) wants the best product to use on their projects, yet they want to pay as little as possible. There are cases when they will use higher quality products if their customers want the best finish possible, however, once more everything comes down to cost. When the sales representative sets prices for individual contractors, they are not always the lowest. Whether a contractor purchases a low-grade, mid-grade, or high-grade product, we (store employees) try to add value to their purchase by providing exceptional services. This can range from many things such as carrying all of their paint out to their vehicles and loading it for them while having a small conversation; to reminding them about future sales; providing quick delivery services; and accepting orders by phone; or simply providing free-coffee all day. Expressing our appreciation by having cook-outs every few months also helps the contractors feel more at home with us, which is great because it helps build loyalty to our brand which is one of the main reasons why we have over 70% of the total paint and coatings market share in the world.

Silviano Espana Silva

Class of 2020

Perceived costs include the actual dollar amount printed on the product, plus a host of additional factors. As noted, these perceived costs are the mirror-opposite of the benefits. When finding a gas station that is selling its highest grade for USD 0.06 less per gallon, the customer must consider the 16 mile (25.75 kilometre) drive to get there, the long line, the fact that the middle grade is not available, and heavy traffic. Therefore, inconvenience, limited choice, and poor service are possible perceived costs. Other common perceived costs include risk of making a mistake, related costs, lost opportunity, and unexpected consequences, to name but a few. A new cruise traveller discovers he or she really does not enjoy that venue for several reasons–e.g. he or she is given a bill for incidentals when she leaves the ship, has used up her vacation time and money, and receives unwanted materials from this company for years to come. In the end, viewing price from the customer's perspective pays off in many ways. Most notably, it helps define value–the most important basis for creating a competitive advantage.

Price From a Societal Perspective

Price, at least in dollars and cents, has been the historical view of value. Derived from a bartering system (exchanging goods of equal value), the monetary system of each society provides a more convenient way to purchase goods and accumulate wealth. Price has also become a variable society employs to control its economic health. Price can be inclusive or exclusive. In many countries, such as Russia, China, and South Africa, high prices for products such as food, health care, housing, and automobiles, means that most of the population is excluded from purchase. In contrast, countries such as Denmark, Germany, and Great Britain charge little for health care and consequently make it available to all.

Price From a Global Marketer's Perspective

Price is important to global marketing, because it represents marketers' assessment of the value customers see in the product or service and are willing to pay for a product or service. A number of factors have changed the way marketers undertake the pricing of their products and services.

- Local competition puts pressure on the global firms' pricing strategies. Many local-made products are high in quality and compete in global markets on the basis of lower price for good value.
- Local competitors often try to gain market share by reducing their prices. The price reduction is intended to increase demand from customers who are judged to be sensitive to changes in price.
- New products are far more prevalent today than in the past. Pricing a new product can represent a challenge, as there is often no historical basis for pricing new products. If a new product is priced incorrectly, the marketplace will react unfavourably and the "wrong" price can do long-term damage to a product's chances for marketplace success.
- Technology has led to existing products having shorter marketplace lives. New products are introduced to the market more frequently, reducing the "shelf life" of existing products. As a result, marketers face pressures to price products to recover costs more quickly. Prices must be set for early successes including fast sales growth, quick market penetration, and fast recovery of research and development costs.

8.3 GLOBAL PRICING APPROACHES

Global pricing decisions can be based on a number of factors, including cost, demand, competition, value, or some combination of factors. However, while many marketers are aware that they should consider these factors, pricing remains somewhat of an art. For purposes of discussion, we categorize the alternative approaches to determining price as follows:

1. cost-oriented pricing;
2. demand-oriented pricing; and
3. value-based approaches.

Cost-oriented pricing: cost-plus and mark-ups

The cost-plus method, sometimes called gross margin pricing, is perhaps most widely used by marketers to set price. The manager selects as a goal a particular gross margin that will produce a desirable profit level. Gross margin is the difference between how much the goods cost and the actual price for which it sells. This gross margin is designated by a per cent of net sales. The per cent selected varies among types of merchandise. That means that one product may have a goal of 48 per cent gross margin while another has a target of 33.5 per cent or 2 per cent.

A primary reason that the cost-plus method is attractive to marketers is that they do not have to forecast general business conditions or customer demand. If sales volume projections are reasonably accurate, profits will be on target. Consumers may also view this method as fair, since the price they pay is related to the cost of producing the item. Likewise, the marketer is sure that costs are covered.

A major disadvantage of cost-plus pricing is its inherent inflexibility. For example, department stores have often found difficulty in meeting competition from discount stores, catalogue retailers, or furniture warehouses because of their commitment to cost-plus pricing. Another disadvantage is that it does not take into account consumers' perceptions of a product's value. Finally, a company's costs may fluctuate so constant price changing is not a viable strategy.

When middlemen use the term mark-up, they are referring to the difference between the average cost and price of all merchandise in stock, for a particular department, or for an individual item. The difference may be expressed in dollars or as a percentage.

For example, a man's tie costs USD 4.60 and is sold for USD 8. The dollar mark-up is USD 3.40. The mark-up may be designated as a per cent of selling price 0r as a per cent of cost of the merchandise. In this example, the mark-up is 74 per cent of cost (USD 3.40/USD 4.60) or 42.5 per cent of the retail price (USD 3.40/USD 8).

There are several reasons why expressing mark-up as a percentage of selling price is preferred to expressing it as a percentage of cost. One is that many other ratios are expressed as a percentage of sales. For instance, selling expenses are expressed as a percentage of sales. If selling costs are 8 per cent, this means that for each USD 100,000 in net sales, the cost of selling the merchandise is USD 8,000. Advertising expenses, operating expenses, and other types of expenses are quoted in the same way. Thus, there is a consistency when making comparisons in expressing all expenses and costs, including mark-up, as a percentage of sales (selling price).

Middlemen receive merchandise daily and make sales daily. As new shipments are received, the goods are marked and put into stock. Cumulative mark-up is the term applied to the difference between total dollar delivered cost of all merchandise and the total dollar price of the goods put into stock for a specified period of time. The original mark-up at which individual items are put into stock is referred to as the initial mark-up.

Maintained mark-up is another important concept. The maintained mark-up percentage is an essential figure in estimating operating profits. It also provides an indication of efficiency. Maintained mark-up, sometimes called gross cost of goods, is the difference between the actual price for which all of the merchandise is sold and the total dollar delivered cost of the goods exclusive of deductions. The maintained mark-up is typically less than the initial mark-up due to mark-downs and stock shrinkages from theft, breakage, and the like. Maintained mark-up is particularly important for seasonal merchandise that will likely be marked-down substantially at the end of the season.

Although this pricing approach may seem overly simplified, it has definite merit. The problem facing managers of certain types of businesses such as retail food stores is that they must price a very large number of items and change many of those prices frequently. The standard mark-up usually reflects historically profitable margins and provides a good guideline for pricing.

Certainly costs are an important component of pricing. No firm can make a profit until it covers its costs. However, the process of determining costs and then setting a price based on costs does not take into consideration what the customer is willing to pay at the marketplace. As a result, many companies that have set out to develop a product have fallen victim to the desire to continuously add features to the product, thus adding cost. When the product is finished, these companies add some percentage to the cost and expect customers to pay the resulting price. These companies are often disappointed, as customers are not willing to pay this cost-based price.

Break-even analysis

A somewhat more sophisticated approach to cost-based pricing is the break-even analysis. The information required for the formula for break-even analysis is available from the accounting records in most firms. The break even price is the price that will produce enough revenue to cover all costs at a given level of production. Total cost can be divided into fixed and variable **(total cost = fixed cost + variable cost)**. Recall that fixed cost does not change as the level of production goes up or down. The rent paid for the building to house the operation might be an example. No cost is fixed in the long run, but in the short run, many expenses cannot realistically be changed. Variable cost does change as production is increased or decreased. For example, the cost of raw material to make the product will vary with production.

A second shortcoming of break-even analysis is it assumes that variable costs are constant. However, wages will increase with overtime and shipping discounts will be obtained. Third, break-even assumes that all costs can be neatly categorized as fixed or variable. Where advertising expenses are entered, break-even analysis will have a significant impact on the resulting break-even price and volume.

Target rates of return

Break-even pricing is a reasonable approach when there is a limit on the quantity which a firm can provide and particularly when a target return objective is sought. Assume, for example, that the firm with the costs illustrated in the previous example determines that it can provide no more than 10,000 units of the product in the next period of operation. Furthermore, the firm has set a target for profit of 20 per cent above total costs. Referring again to internal accounting records and the changing cost of production at near capacity levels, a new total cost curve is calculated. From the cost curve profile, management sets the desirable level of production at 80 per cent of capacity or 8,000 units. From the total cost curve, it is determined that the cost for producing 8,000 units is USD 18,000. 20 per cent of USD 18,000 is USD 3,600. Adding this to the total cost at 8,000 units yields the point at that quantity through which the total revenue curve must pass. Finally, USD 21,600 divided by 8,000 units yields the price of USD 2.70 per unit; here the USD 3,600 in profit would be realized. The obvious shortcoming of the target return approach to pricing is the absence of any information concerning the demand for the product at the desired price. It is assumed that all of the units will be sold at the price which provides the desired return.

It would be necessary, therefore, to determine whether the desired price is in fact attractive to potential customers in the marketplace. If break-even pricing is to be used, it should be supplemented by additional information concerning customer perceptions of the relevant range of prices for the product. The source of this information would most commonly be survey research, as well as a thorough review of pricing practices by competitors in the industry. In spite of their shortcomings, break-even pricing and target return pricing are very common business practices.

Demand-oriented pricing

Demand-oriented pricing focuses on the nature of the demand curve for the product or service being priced. The nature of the demand curve is influenced largely by the structure of the industry in which a firm competes. That is, if a firm operates in an industry that is extremely competitive, price may be used to some strategic advantage in acquiring and maintaining market share. On the other hand, if the firm operates in an environment with a few dominant players, the range in which price can vary may be minimal.

Value-based pricing

If we consider the three approaches to setting price, cost-based is focused entirely on the perspective of the company with very little concern for the customer; demand-based is focused on the customer, but only as a predictor of sales; and value-based pricing focuses entirely on the customer as a determinant of the total price/value package. Marketers who employ value-based pricing might use the following definition: "It is what you think your product is worth to that customer at that time." Moreover, it acknowledges several marketing/price truths:

- To the customer, price is the only unpleasant part of buying.
- Price is the easiest marketing tool to copy.
- Price represents everything about the product

Still, value-based pricing is not altruistic. It asks and answers two questions : (a) what is the highest price I can charge and still make the sale? and (b) am I willing to sell at that price? The first question must take two primary factors into account: customers and competitors. The second question is influenced by two more: costs and constraints. Let us discuss each briefly.

Many customer-related factors are important in value-based pricing. For example, it is critical to understand the customer buying process. How important is price? When is it considered? How is it used? Another factor is the cost of switching. Have you ever watched the television program "The Price is Right"? If you have, you know that most consumers have poor price knowledge. Moreover, their knowledge of comparable prices within a product category —e.g. ketchup—is typically worse. So price knowledge is a relevant factor. Finally, the marketer must assess the customers' price expectations. How much do you expect to pay for a large pizza? Colour TV? DVD? Newspaper? Swimming pool? These expectations create a phenomenon called "sticker shock" as exhibited by gasoline, automobiles, and ATM fees.

A second factor influencing value-based pricing is competitors. As noted in earlier chapters, defining competition is not always easy. Of course there are like-category competitors such as Toyota and Nissan. We have already discussed the notion of pricing above, below, and at the same level of these direct competitors. However, there are also indirect competitors that consumers may use to base price comparisons. For instance, we may use the price of a vacation as a basis for buying vacation clothes. The cost of eating out is compared to the cost of groceries. There are also instances when a competitor, especially a market leader, dictates the price for everyone else. Weyerhauser determines the price for lumber. Kellogg establishes the price for cereal.

If you are building a picnic table, it is fairly easy to add up your receipts and calculate costs. For a global corporation, determining costs is a great deal more complex. For example, calculating incremental costs and identifying avoidable costs are valuable tasks. Incremental cost is the cost of producing each additional unit. If the incremental cost begins to exceed the incremental revenue, it is a clear sign to quit producing. Avoidable costs are those that are unnecessary or can be passed onto some other institution in the marketing channel. Adding costly features to a product that the customer cannot use is an example of the former. As to the latter, the banking industry has been passing certain costs onto customers.

Another consideration is opportunity costs. Because the company spent money on store remodelling, they are not able to take advantage of a discounted product purchase. Finally, costs vary from market-to-market as well as quantities sold. Research should be conducted to assess these differences.

Although it would be nice to assume that a business has the freedom to set any price it chooses, this is not always the case. There are a variety of constraints that prohibit such freedom. Some constraints are formal, such as government restrictions in respect to strategies like collusion and price-fixing. This occurs when two or more companies agree to charge the same or very similar prices. Other constraints tend to be informal. Examples include matching the price of competitors, a traditional price charged for a particular product, and charging a price that covers expected costs.

Ultimately, value-based pricing offers the following three tactical recommendations:

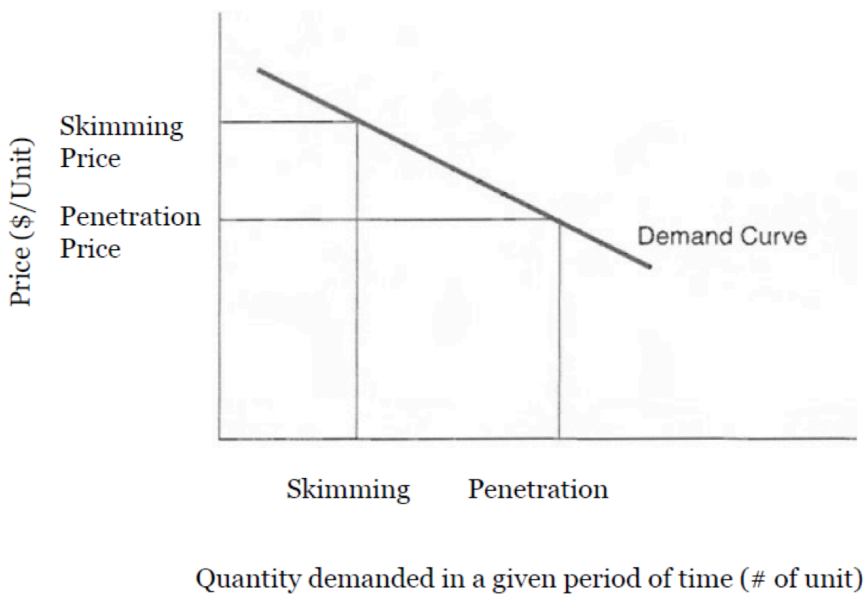
- Employ a segmented approach toward price, based on such criteria as customer type, location, and order size.
- Establish highest possible price level and justify it with comparable value.
- Use price as a basis for establishing strong customer relationships

Penetration and Skimming Pricing

Penetration pricing is usually used in the introductory stage of a new product's life cycle, and involves accepting a lower profit margin and to price relatively low. Such a strategy should generate greater sales and establish the new product in the market more quickly. Price skimming involves the top part of the demand curve. Price is set relatively high to generate a high profit margin and sales are limited to those buyers willing to pay a premium to get the new product (see Figure).

Penetration pricing can be used to achieve market share as a competitive strategy to achieve market leadership. Other times, it can also be used to increase market and sales growth. For example, Sony needed to sell the Walkman at a retail price of ¥50,000 ($249) to achieve breakeven, but a price of ¥35,000 ($170) was needed to attract the youth market segment. Through a long process of cost cutting, a breakeven price of ¥40,000 was achieved. Then Chairman Akio Morita insisted on a retail price of ¥33,000 ($165) to commemorate Sony's 33rd anniversary. Sony also used this approach when its camcorder market became very competitive with price competition from Samsung, Hitachi and Panasonic. Another example is Google's penetration pricing strategy, where they offered their Google Checkout service at a break-even price or at a loss, trying to gain market share against Paypal.

Which strategy is best depends on a number of factors. A penetration strategy would generally be supported by the following conditions: price-sensitive consumers, opportunity to keep costs low, the anticipation of quick market entry by competitors, a high likelihood for rapid acceptance by potential buyers, and an adequate resource base for the firm to meet the new demand and sales.



Skimming generates a higher profit margin while penetration generates greater volume.

Fig 8.2 : Penetration and skimming: pricing strategies as they relate to the demand curve.

A skimming strategy is most appropriate when the opposite conditions exist. A premium product generally supports a skimming strategy. In this case, "premium" does not just denote high cost of production and materials; it also suggests that the product may be rare or that the demand is unusually high. An example would be a USD 500 ticket for the World Series or an USD 80,000 price tag for a limited-production sports car. Having legal protection via a patent or copyright may also allow for an excessively high price. Intel and their Pentium chip possessed this advantage for a long period of time. In most cases, the initial high price is gradually reduced to match new competition and allow new customers access to the product.

Several electronic products that were very innovative during their introduction, such as DVRs, CR payers, Flat Screen TVs, were priced very high during the initial introduction phase; then the prices dropped steeply. According to Cateora, Graham and Gilly (2016), this strategy can also be used when their markets have only two income levels: the super-rich and the very poor, as when Johnson & Johnson priced their diapers in Brazil before the arrival of P&G. As the company's cost structure will not allow the setting of a low enough price for the low income segment, the company will cater to the wealthier segment using a premium price.

8.4 CURRENCY FLUCTUATIONS AND GLOBAL PRICING

Briefly, **currency** is any form of money in general circulation in a country. What exactly is a foreign exchange? In essence, **foreign exchange** is money denominated in the currency of another country or—now with the euro—a group of countries. Simply put, an exchange rate is defined as the rate at which the market converts one currency into another.

Any company operating globally must deal in foreign currencies. It has to pay suppliers in other countries with a currency different from its home country's currency. The home country is where a company is headquartered. The firm is likely to be paid or have profits in a different currency and will want to exchange it for its home currency. Even if a company expects to be paid in its own currency, it must assess the risk that the buyer may not be able to pay the full amount due to currency fluctuations.

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If you have traveled outside of your home country, you may have experienced the currency market—for example, when you tried to determine your hotel bill or tried to determine if an item was cheaper in one country versus another. In fact, when you land at an airport in another country, you're likely to see boards indicating the foreign exchange rates for major currencies.

Exchange Rate

For example, imagine you're on vacation in Thailand and the exchange rate board indicates that the Bangkok Bank is willing to exchange currencies at the following rates (see the following table). GBP refers to the British pound; JPY refers to the Japanese yen; and HKD refers to the Hong Kong dollar.

Because there are several countries that use the dollar as part or whole of their name, this chapter clearly states "US dollar" or uses US$ or USD when referring to American currency.

Foreign Exchange Rates: Bangkok Bank

Currency/Baht	Banknotes Buy	Banknotes Sell
USD	31.67	32.32
GPB	50.19	51.80
EURO	41.74	43.00
JOY	36.56	39.01
HKD	4.03	4.22

This chart tells us that when you land in Thailand, you can use 1 US dollar to buy 31.67 Thai baht. However, when you leave Thailand and decide that you do not need to take all your baht back to the United States, you then convert baht back to US dollars. We then have to use more baht—32.32 according to the preceding table—to buy 1 US dollar. The spread between these numbers, 0.65 baht, is the profit that the bank makes for each US dollar bought and sold. The bank charges a fee because it performed a service—facilitating the currency exchange. When you walk through the airport, you'll see more boards for different banks with different buy and sell rates. While the difference may be very small, around 0.1 baht, these numbers add up if you are a global company engaged in large foreign exchange transactions.

Companies, investors, and governments want to be able to convert one currency into another. A company's primary purposes for wanting or needing to convert currencies is to pay or receive money for goods or services. Imagine you have a business in the United States that imports wines from around the world. You'll need to pay the French winemakers in euros, your Australian wine suppliers in Australian dollars, and your Chilean vineyards in pesos. Obviously, you are not going to access these currencies physically. Rather, you'll instruct your bank to pay each of these suppliers in their local currencies. Your bank will convert the currencies for you and debit your account for the US dollar equivalent based on the exact exchange rate at the time of the exchange.

Quote a Currency

There are several ways to quote currency, but let's keep it simple. In general, when we quote currencies, we are indicating how much of one currency it takes to buy another currency. This quote requires two components: the base currency and the quoted currency. The quoted currency is the currency with which another currency is to be purchased. In an exchange rate quote, the quoted currency is typically the numerator. The base currency is the currency that is to be purchased with another currency, and it is noted in the denominator. For example, if we are quoting the number of Hong Kong dollars required to purchase 1 US dollar, then we note HKD 8 / USD 1. (Note that 8 reflects the general exchange rate average in this example.) In this case, the Hong Kong dollar is the quoted currency and is noted in the numerator. The US dollar is the base currency and is noted in the denominator. We read this quote as "8 Hong Kong dollars are required to purchase 1 US dollar." If you get confused while reviewing exchanging rates, remember the currency that you want to buy or sell. If you want to sell 1 US dollar, you can buy 8 Hong Kong dollars, using the example in this paragraph.

Direct Currency Quote and Indirect Currency Quote

Additionally, there are two methods—the American terms and the European terms—for noting the base and quoted currency. These two methods, which are also known as direct and indirect quotes, are opposite based on each reference point. Let's understand what this means exactly.

The American terms, also known as US terms, are from the point of view of someone in the United States. In this approach, foreign exchange rates are expressed in terms of how many US dollars can be exchanged for one unit of another currency (the non-US currency is the *base currency*). For example, a dollar-pound quote in American terms is USD/GP (US$/£) equals 1.56. This is read as "1.56 US dollars are required to buy 1 pound sterling." This is also called a direct quote, which states the domestic currency price of one unit of foreign currency. If you think about this logically, a business that needs to buy a foreign currency needs to know how many US dollars must be sold in order to buy one unit of the foreign currency. In a direct quote, the domestic currency is a variable amount and the foreign currency is fixed at one unit.

Conversely, the European terms are the other approach for quoting rates. In this approach, foreign exchange rates are expressed in terms of how many currency units can be exchanged for a US dollar (the US dollar is the base currency). For example, the pound-dollar quote in European terms is £0.64/US$1 (£/US$1). While this is a direct quote for someone in Europe, it is an indirect quote in the United States. An indirect quote states the price of the domestic currency in foreign currency terms. In an indirect quote, the foreign currency is a variable amount and the domestic currency is fixed at one unit.

A direct and an indirect quote are simply reverse quotes of each other. If you have either one, you can easily calculate the other using this simple formula:

direct quote = 1 / indirect quote.

To illustrate, let's use our dollar-pound example. The direct quote is US$1.56 = 1/£0.64 (the indirect quote). This can be read as

1 divided by 0.64 equals 1.56.

In this example, the direct currency quote is written as US$/£ = 1.56.

While you are performing the calculations, it is important to keep track of which currency is in the numerator and which is in the denominator, or you might end up stating the quote backward. The direct quote is the rate at which you buy a currency. In this example, you need US$1.56 to buy a British pound.

Tip: Many international business professionals become experienced over their careers and are able to correct themselves in the event of a mix-up between currencies. To illustrate using the example mentioned previously, the seasoned global professional knows that the British pound is historically higher in value than the US dollar. This means that it takes more US dollars to buy a pound than the other way around. When we say "higher in value," we mean that the value of the British pound buys you more US dollars. Using this logic, we can then deduce that 1.56 US dollars are required to buy 1 British pound. As an international businessperson, we would know instinctively that it cannot be less—that is, only 0.64 US dollars to buy a British pound. This would imply that the dollar value was higher in value. While major currencies have changed significantly in value vis-à-vis each other, it tends to happen over long periods of time. As a result, this self-test is a good way to use logic to keep track of tricky exchange rates. It works best with major currencies that do not fluctuate greatly vis-à-vis others.

Exchange fluctuations and global prices

The strengthening or weakening of a home (exporting) country's currency vis-à-vis that of the host (foreign) country, can have far-reaching effects on the price setting in the foreign country, as well as other elements of the global marketer's marketing strategy. For example, if the value of the U.S. dollar relative to the euro was U.S.$1 to 1.8315 euros in 2001, and U.S.$1 to 0.8499 euros in 2003, then the exchange rate U.S.$1 to 1.8315 euros is said to be stronger for the US dollar, and the exchange rate U.S.$1 to 0.8499 euros is said to be weaker for the US dollar. Similarly, if the value of the U.S. dollar relative to the Indian Rupee was U.S.$1 to INR 50 in 2001, and U.S.$1 to INR 70 in 2018, then the exchange rate U.S.$1 to INR 50 is said to be weaker for the US dollar than the exchange rate U.S.$1 to INR 70. A weaker exchange rate (e.g., U.S.$1 to 0.8499 euros and U.S.$1 to INR 50) will fetch lesser money in terms of the foreign currency, while a stronger exchange rate will fetch more money in terms of the foreign currency.

When the home currency of the global marketer weakens, the exchange rates are supposed be favourable to the global marketer, because the home currency will fetch lesser in terms of the foreign currency, and hence the prices of the exported product in the foreign country's currency will come down. Therefore, the global marketer can cut prices in the foreign country, and hence, increase market share. On the other hand, the global marketer can also decide to maintain the higher prices, in which case the global marketer will see windfall revenue, and increased margins. Thus if the exchange rate of the US dollar relative to the Japanese Yen weakens (lesser Yen for each dollar), then it is good for US companies manufacturing their products in the US and selling them in Japan (e.g. Boeing, Caterpillar, GE). On the other hand, it is not a good pricing scenario for Japanese companies (e.g. Canon and Olympus) who manufacture and sell in Japan against their US competitors. This context is also unfavourable to American tourists who are shopping for cameras, because they would be paying in Yen, and their US dollars would get lesser Yen, relative to what it would have fetched if the US dollar was stronger.

When the domestic (home) currency of the US global marketer strengthens (e.g., U.S.$1 to 1.8315 euros and U.S.$1 to INR 70), where the US dollar will fetch more money in terms of the foreign currency, then this price situation is said to be bad for global marketers who manufacture their products in the US and sell them in the foreign (host) country, priced in the foreign currency. Although each dollar gets more in terms of the foreign currency, what it really means is that the US company will now get lesser dollars after conversion into the US dollar, for the same amount of foreign currency, after the exchange rate strengthening. Thus, the US company may not be able to cover its costs which are specified in US dollars. One strategy to overcome this effect is to manufacture or source their products in the host country, and maximize all expenditures in the local currency (remember, each dollar gets more local currency!).

Since the strengthening of the home (domestic) currency results in more foreign currency, this conversion results in higher prices, which are specified in the local currency. This is usually not a problem if the demand for a product is inelastic. Otherwise, the global marketer has to cut costs in his home country, or improve quality and service to make up for the increased price levels. A drastic strategy to counter this situation would be to absorb some of the costs, which will result in a reduced margin.

Exchange fluctuations and global prices

WHEN HOME CURRENCY IS WEAK	WHEN HOME CURRENCY IS STRONG
(Global marketer is from the US and the US dollar is weak, e.g. U.S.$1 to INR 50) 1. Stress price benefits. 2. Expand product line and add more costly features. 3. Shift sourcing to domestic market. 4. Exploit market opportunities in all markets. 5. Use full-costing approach, but employ marginal-cost pricing to penetrate new or competitive markets. 6. Speed repatriation of foreign-earned income and collections. 7. minimize expenditures in local (host-country) currency. 8. Buy advertising, insurance, transportation and other services in domestic market. 9. Bill foreign customers in their own currency.	(Global marketer is from the US and the US dollar is strong. e.g., U.S.$1 to INR 70) 1. Engage in nonprice competition by improving quality, delivery, and after-sale service. 2. Improve productivity and engage in cost reduction. 3. Shift sourcing outside home county. 4. Give priority to exports to countries with stronger currencies. 5. Trim profit margins and use marginal-cost pricing. 6. Keep the foreign-earned income in host county; slow down collections. 7. Maximize expenditures in local (host-country) currency. 8. Buy needed services abroad an pay for them in local currencies. 9. Bill foreign customers in the domestic currency.

Adapted from: Keegan and Green (2011)

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8.6 KEY TERMS

Key Terms

Cash Discounts: These are reductions on the base price given to customers for paying cash or within some short time period. 8.1

Currency: Is any form of money in general circulation in a country. 8.4

Customer-Oriented Pricing: Is also referred to as value-oriented pricing. Given the centrality of the customer in a marketing orientation (and this marketing course!), it will come as no surprise that customer-oriented pricing is the recommended pricing approach because its focus is on providing value to the customer. Customer-oriented pricing looks at the full price-value equation (above) and establishes the price that balances the value. 8.1

Foreign Exchange: Is money denominated in the currency of another country or—now with the euro—a group of countries. Simply put, an exchange rate is defined as the rate at which the market converts one currency into another. 8.4

Personal Allowances: Are similar strategies aimed at middlemen. Their purpose is to encourage middlemen to aggressively promote the organization's products. 8.1

Profit-Oriented: Pricing places an emphasis on the finances of the product and business. A business's profit is the money left after all costs are covered. In other words, profit = revenue – costs. In profit-oriented pricing, the price per product is set higher than the total cost of producing and selling each product to ensure that the company makes a profit on each sale 8.1

Quantity Discounts: Are reductions in base price given as the result of a buyer purchasing some predetermined quantity of merchandise. 8.1

Seasonal Discounts: are price reductions given for out-of-season merchandise—snowmobiles discounted during the summer 8.1

Trade Discounts: Are price reductions given to middlemen (e.g., wholesalers, industrial distributors, retailers) to encourage them to stock and give preferred treatment to an organization's products. 8.1

CHAPTER 9: GLOBAL DISTRIBUTION

Chapter Outline

9.0 INTRODUCTION

Learning Objectives

After reading this section, students should be able to:

1. List the characteristics and flows of a distribution channel.
2. Describe the channel partners that support distribution channels.
3. Explain the role of wholesale intermediaries.
4. Describe the different types of retailers businesses use to distribute products.
5. Differentiate between supply chains and distributions channels.
6. Outline the advantages of global sourcing.
7. List the pros and cons of sole-sourcing and multisourcing.
8. Describe the distribution-management choices companies have when entering new international markets.

In today's global competitive environment, individual companies no longer compete as autonomous entities but as supply-chain networks. Instead of brand versus brand or company versus company, then network is increasingly suppliers-brand-company versus suppliers-brand-company.

Top-performing supply chains have three distinct qualities. First, they are agile enough to react readily to sudden changes in demand or supply. Second, they adapt over time as market structures and environmental conditions change. And third, they align the interests of all members of the supply-chain network in order to optimize performance.

Driven by e-commerce's capabilities to empower clients, most companies have moved from the traditional "push" business model—where manufacturers, suppliers, distributors, and marketers have most of the power—to a customer-driven "pull" model.

Supply-chain management (SCM) has three principal components: (a) creating the supply-chain network structure, (b) developing supply-chain business processes, and (c) managing the supply-chain activities. The supply-chain network structure consists of the member firms and the links between these firms. Business processes are the activities that produce a specific output of value to the customer. The management function integrates the business processes across the supply chain.

The best companies create supply chains that can respond to sudden and unexpected changes in markets. Agility—the ability to respond quickly and cost-effectively to unexpected change—is critical because in most industries, both demand and supply fluctuate more rapidly and widely than they used to. Key to increasing agility and resilience is building flexibility into the supply-chain structure, processes, and management.

Global companies must be able to adapt their supply networks when markets or strategies change. Companies that compete primarily on the basis of operational effectiveness typically focus on creating supply chains that deliver goods and services to consumers as quickly and inexpensively as possible. They invest in state-of-the-art technologies and employ metrics and reward systems aimed at boosting supply-chain performance. For companies competing on the basis of customer intimacy or product leadership, a focus on efficiency is not enough; agility is a key factor. Customer-intimate companies must be able to add and delete products and services as customer needs change; product leadership companies must be able to adapt their supply chains to changes in technology and to capitalize on new ideas.

Leading companies take care to align the interests of all the firms in their supply chain with their own. This is important because every supply-chain partner firm—whether a supplier, an assembler, a distributor, or a retailer—will focus on its own interests. If any company's interests differ from those of the other organizations in the supply chain, its actions will not maximize the chain's performance.

9.1 CHANNELS OF DISTRIBUTION

Distribution channels—which is “place” in the four Ps—cover all the activities needed to transfer the ownership of goods and move them from the point of production to the point of consumption. In this section you’ll learn more about distribution channels and some of the common strategies companies use to take advantage of them.

Evolution of Channels of Distribution

As consumers, we take for granted that when we go to a supermarket the shelves will be filled with the products we want; when we are thirsty there will be a Coke machine or bar around the corner, and we count on being able to get online and find any product available for purchase and quick delivery. Of course, if we give it some thought, we realize that this magic is not a given and that hundreds of thousands of people plan, organize, and labor long hours to make this convenience available. It has not always been this way, and it is still not this way in many other parts of the world.

Looking back over time, the channel structure in primitive culture was virtually nonexistent. The family or tribal group was almost entirely self-sufficient. The group was composed of individuals who were both communal producers and consumers of whatever goods and services could be made available. As economies evolved, people began to specialize in some aspect of economic activity. They engaged in farming, hunting, or fishing, or some other basic craft. Eventually this specialized skill produced excess products, which they exchanged or traded for needed goods that had been produced by others. This exchange process or barter marked the beginning of formal channels of distribution. These early channels involved a series of exchanges between two parties who were producers of one product and consumers of the other.

With the growth of specialization, particularly industrial specialization, and with improvements in methods of transportation and communication, channels of distribution have become longer and more complex. Thus, corn grown in Illinois may be processed into corn chips in West Texas, which are then distributed throughout the United States. Or, turkeys raised in Virginia are sent to New York so that they can be shipped to supermarkets in Virginia. Channels do not always make sense.

The channel mechanism also operates for service products. In the case of medical care, the channel mechanism may consist of a local physician, specialists, hospitals, ambulances, laboratories, insurance companies, physical therapists, home care professionals, and so on. All of these individuals are interdependent and could not operate successfully without the cooperation and capabilities of all the others.

Based on this relationship, we define a **channel of distribution**, also called a marketing channel, as sets of interdependent organizations involved in the process of making a product or service available for use or consumption, as well as providing a payment mechanism for the provider.

This definition implies several important characteristics of the channel.

1. The channel consists of *organizations*, some under the control of the producer and some outside the producer's control. Yet all must be recognized, selected, and integrated into an efficient channel arrangement.
2. The channel management *process* is continuous and requires continuous monitoring and reappraisal. The channel operates twenty-four hours a day and exists in an environment where change is the norm.
3. Channels should have certain distribution objectives guiding their activities. The structure and management of the marketing channel is thus, in part, a function of a firm's distribution objective. It's also a part of the marketing objectives, especially the need to make an acceptable profit. Channels usually represent the largest costs in marketing a product.

Channel Flows

One traditional framework that has been used to express the channel mechanism is the concept of flow. These flows reflect the many linkages that tie channel members and other agencies together in the distribution of goods and services. From the perspective of the channel manager, there are five important flows.

1. **Product flow**: the movement of the physical product from the manufacturer through all the parties who take physical possession of the product until it reaches the ultimate consumer
2. **Negotiation flow**: the institutions that are associated with the actual exchange processes
3. **Ownership flow**: the movement of title through the channel
4. **Information flow**: the individuals who participate in the flow of information either up or down the channel
5. **Promotion flow**: the flow of persuasive communication in the form of advertising, personal selling, sales promotion, and public relations

Monster Channel Flow

The figure below maps the channel flows for the Monster Energy drink (and many other energy drink brands). Why is Monster's relationship with Coca-Cola so valuable? Every single flow passes through bottlers and distributors in order to arrive in supermarkets where the product will be available to consumers.

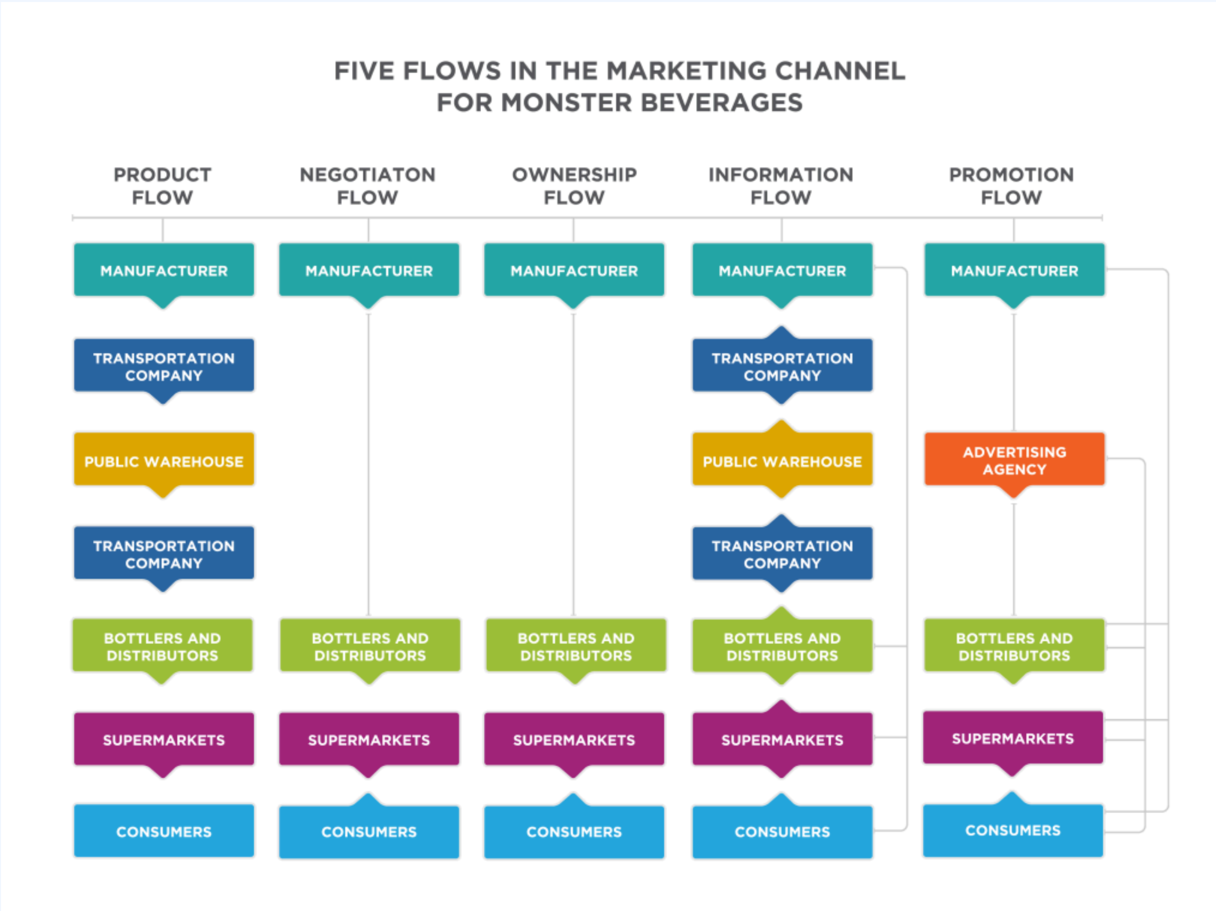

Fig 9.1 Five Flows in the Marketing Channel for Monster Beverages

Coca-Cola explains the importance of the bottlers in the distribution network:

> While many view our Company as simply "Coca-Cola," our system operates through multiple local channels. Our Company manufactures and sells concentrates, beverage bases and syrups to bottling operations, owns the brands and is responsible for consumer brand marketing initiatives. Our bottling partners manufacture, package, merchandise and distribute the final branded beverages to our customers and vending partners, who then sell our products to consumers.
>
> All bottling partners work closely with customers — grocery stores, restaurants, street vendors, convenience stores, movie theatres and amusement parks, among many others — to execute localized strategies developed in partnership with our Company. Customers then sell our products to consumers at a rate of more than 1.9 billion servings a day.

Revisiting the channel flows we find that the bottlers and distributors play a role in each flow. Examples of the flows are listed below. Remember, while the consumer is the individual who eventually consumes the drink, the supermarkets, restaurants, and other outlets are Coca-Cola's customers.

- Product flow: the bottlers receive and process the bases and syrups
- Negotiation flow: the bottlers buy concentrate, sell product and collect revenue from customers
- Ownership flow: distributors acquire the title of the syrups and own the product until it's sold to supermarkets
- Information flow: bottlers communicate product options to customers and communicate demand and needs to Coca-Cola
- Promotion flow: bottlers communicate benefits and provide promotional materials to customers
  (The Coca-Cola Company, n.d.)

9.2 CHANNEL PARTNERS

While channels can be very complex, there is a common set of channel structures that can be identified in most transactions. Each channel structure includes different organizations. Generally, the organizations that collectively support the distribution channel are referred to as **channel partners**.

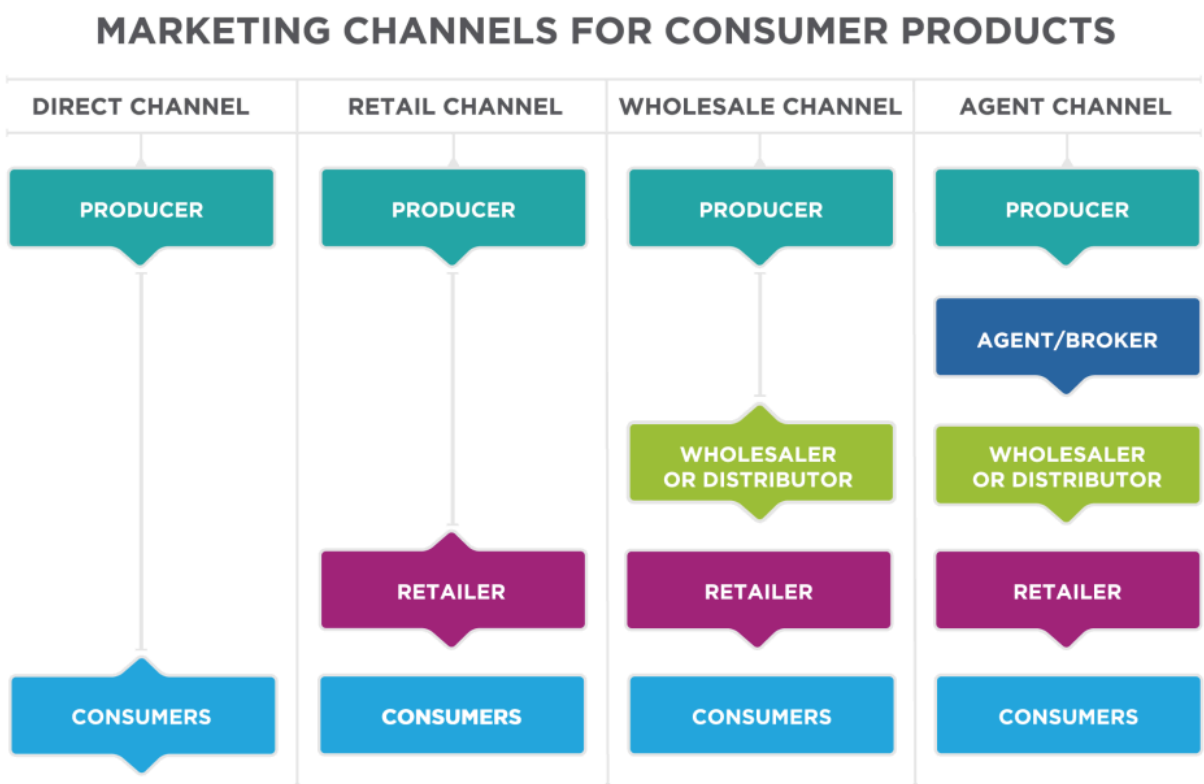

Fig 9.2 Marketing Channels for Consumer Products

Direct Channel

The **direct channel** is the simplest channel. In this case, the producer sells directly to the consumer. The most straightforward examples are producers who sell in small quantities. If you visit a farmer's market, you can purchase goods directly from the farmer or craftsman. There are also examples of very large corporations who use the direct channel effectively, especially for B2B transactions. Services may also be sold through direct channels, and the same principle applies: an individual buys a service directly from the provider who delivers the service.

Examples of the direct channel include:

- Etsy.com online marketplace
- Farmer's markets
- Oracle's personal sales team that sells software systems to businesses
- A bake sale

Retail Channel

Retailers are companies in the channel that focuses on selling directly to consumers. You are likely to participate in the **retail channel** almost every day. The retail channel is different from the direct channel in that the retailer doesn't produce the product. The retailer markets and sells the goods on behalf of the producer. For consumers, retailers provide tremendous contact efficiency by creating one location where many products can be purchased. Retailers may sell products in a store, online, in a kiosk, or on your doorstep. The emphasis is not the specific location but on selling directly to the consumer.

Examples of retailers include:

- Walmart discount stores
- Amazon online store
- Nordstrom department store
- Dairy Queen restaurant

Wholesale Channel

From a consumer's perspective, the **wholesale channel** looks very similar to the retail channel, but it also involves a wholesaler. A wholesaler is primarily engaged in buying and usually storing and physically handling goods in large quantities, which are then resold (usually in smaller quantities) to retailers or to industrial or business users. The vast majority of goods produced in an advanced economy have wholesaling involved in their distribution. Wholesale channels also include manufacturers who operate sales offices to perform wholesale functions, and retailers who operate warehouses or otherwise engage in wholesale activities.

Examples of wholesalers include:

- Christmas-tree wholesalers who buy from growers and sell to retail outlets
- Restaurant food suppliers
- Clothing wholesalers who sell to retailers

Agent Channel

The broker or **agent channel** includes one additional intermediary. Agents and brokers are different from wholesalers in that they *do not take title* to the merchandise. In other words, they do not own the merchandise because they neither buy nor sell. Instead, brokers bring buyers and sellers together and negotiate the terms of the transaction: agents represent either the buyer or seller, usually on a permanent basis; brokers bring parties together on a temporary basis. Think about a real-estate agent. They do not buy your home and sell it to someone else; they market and arrange the sale of the home. Agents and brokers match up buyers and sellers, or add expertise to create a more efficient channel.

Examples of brokers include:

- An insurance broker, who sells insurance products from many companies to businesses and individuals
- A literary agent, who represents writers and their written works to publishers, theatrical producers, and film producers
- An export broker, who negotiates and manages transportation requirements, shipping, and customs clearance on behalf of a purchaser or producer

It's important to note that the larger and more complex the flow of materials from the initial design through purchase, the more likely it is that multiple channel partners may be involved, because each channel partner will bring unique expertise that increases the efficiency of the process. If an intermediary is not adding value, they will likely be removed over time, because the cost of managing and coordinating with each intermediary is significant.

9.3 ROLE OF WHOLESALE INTERMEDIARIES

While we are probably most familiar with the retail channel, wholesalers play an important role as intermediaries. Intermediaries act as a link in the distribution process, but the roles they fill are broader than simply connecting the different channel partners. Wholesalers, often called "merchant wholesalers," help move goods between producers and retailers.

For example, McLane Company Inc. is among the largest wholesalers in the United States. The breadth of its operations is described on the company Web site:

> McLane Company, Inc. is one of the largest supply chain services leaders, providing grocery and foodservice supply chain solutions for convenience stores, mass merchants, drug stores and chain restaurants throughout the United States. McLane, through McLane Grocery and McLane Foodservice, operates over 80 distribution centers across the U.S. and one of the nation's largest private fleets. The company buys, sells and delivers more than 50,000 different consumer products to nearly 110,000 locations across the U.S. In addition, McLane provides alcoholic beverage distribution through its wholly owned subsidiary, Empire Distributors, Inc. McLane is a wholly owned unit of Berkshire Hathaway Inc. (NYSE: BRK) and employs more than 20,000 teammates (McLane Company, Inc., n.d.)

Let's look at each of the functions that a merchant wholesaler fulfills.

Purchasing

Wholesalers purchase very large quantities of goods directly from producers or from other wholesalers. By purchasing large quantities or volumes, wholesalers are able to secure significantly lower prices.

Imagine a situation in which a farmer grows a very large crop of potatoes. If he sells all of the potatoes to a single wholesaler, he will negotiate one price and make one sale. Because this is an efficient process that allows him to focus on farming (rather than searching for additional buyers), he will likely be willing to negotiate a lower price. Even more important, because the wholesaler has such strong buying power, the wholesaler is able to force a lower price on every farmer who is selling potatoes.

The same is true for almost all mass-produced goods. When a producer creates a large quantity of goods, it is most efficient to sell all of them to one wholesaler, rather than negotiating prices and making sales with many retailers or an even larger number of consumers. Also, the bigger the wholesaler is, the more likely it will have significant power to set attractive prices.

Warehousing and Transportation

Once the wholesaler has purchased a mass quantity of goods, it needs to get them to a place where they can be purchased by consumers. This is a complex and expensive process. McLane Company operates 22 modern distribution centres around the country. It relies on its own vast trucking fleet of over 1,600 tractors and 2,700 multi-temperature trailers to handle the transportation of product (McLane Company Inc., n.d.).

Grading and Packaging

Wholesalers buy a very large quantity of goods that they then break down into smaller lots. The process of breaking large quantities into smaller lots to be resold is called "bulk breaking". Often this includes physically sorting, grading, and assembling the goods. Returning to our potato example, the wholesaler would determine which potatoes are of a size and quality to sell individually and which are to be packaged for sale in five-pound bags.

Risk Bearing

Wholesalers either take title to the goods they purchase, or they *own* the goods they purchase. There are two primary consequences of this, both of which are both very important to the distribution channel. First, it means that the wholesaler finances the purchase of the goods and carries the cost of the goods in inventory until they are sold. Because this is a tremendous expense, it drives wholesalers to be accurate and efficient in their purchasing, warehousing, and transportation processes.

Second, wholesalers also bear the risk for the products until they are delivered. If goods are damaged in transport and cannot be sold, then the wholesaler is left with the goods and the cost. If there is a significant change in the value of the products between the time of the purchase from the producer and the sale to the retailer, the wholesaler will absorb that profit or loss.

Marketing

Often, the wholesaler will fill a role in the promotion of the products that it distributes. This might include creating displays for the wholesaler's products and providing the display to retailers to increase sales. The wholesaler may advertise its products that are carried by many retailers.

Wholesalers also influence which products the retailer offers. For example, McLane Company was a winner of the 2016 Convenience Store News Category Captains, in recognition for its innovations in providing the right products to its customers. McLane created unique packaging and products featuring movie themes, college football themes, and other special-occasion branding that were designed to appeal to impulse buyers.

They also shifted the transportation and delivery strategy to get the right products in front of consumers at the time they were most likely to buy. Its convenience store customers are seeing sales growth, as is the wholesaler (Durtschi, 2016).

Distribution

As distribution channels have evolved, some retailers, such as Walmart and Target, have grown so large that they have taken over aspects of the wholesale function. Still, it is unlikely that wholesalers will ever go away. Most retailers rely on wholesalers to fulfill the functions that we have discussed, and they simply do not have the capability or expertise to manage the full distribution process. Plus, many of the functions that wholesalers provide are performed most efficiently at scale. Wholesalers are able to focus on creating efficiencies for their retail channel partners that are very difficult to replicate on a small scale.

Retailers that Distribute Products

Retailing involves all activities required to market consumer goods and services to ultimate consumers who are purchasing for individual or family needs.

By definition, B2B purchases are not included in the retail channel since they are not made for individual or family needs. In practice this can be confusing because many retail outlets do serve both consumers and business customers—like Home Depot, which has a program for selling directly to builders and contractors. Generally, retailers that have a significant B2B or wholesale business report those numbers separately in their financial statements, acknowledging that they are separate lines of business within the same company. Those with a pure retail emphasis do not seek to exclude business purchasers. They simply focus their offering to appeal to individual consumers, knowing that some businesses may also choose to purchase from them.

We typically think of a store when we think of a retail sale, even though retail sales occur in other places and settings. For instance, they can be made by a Pampered Chef salesperson in someone's home. Retail sales also happen online, through catalogues, by automatic vending machines, and in hotels and restaurants. Nonetheless, despite tremendous growth in both nontraditional retail outlets and online sales, a large portion of retail sales still take place in brick-and-mortar stores.

Beyond the distinction in the products they provide, there are structural differences among retailers that influence their strategies and results. One of the reasons the retail industry is so large and powerful is its diversity. For example, stores vary in size, in the kinds of services that are provided, in the assortment of merchandise they carry, and in their ownership and management structures.

Department Stores

Department stores are characterized by their very wide product mixes. That is, they carry many different types of merchandise, which may include hardware, clothing, and appliances. Each type of merchandise is typically displayed in a different section or department within the store. The depth of the product mix depends on the store, but department stores' primary distinction is the ability to provide a wide range of products within a single store. For example, people shopping at Macy's can buy clothing for a woman, a man, and children, as well as housewares such as dishes and luggage.

Chain Stores

The 1920s saw the evolution of the chain store movement. Because chain store businesses were so large, they were able to buy a wide variety of merchandise at discounted prices. The discounts substantially lowered their cost compared to costs of single-unit retailers. As a result, they could set retail prices that were lower than those of their small competitors and thereby increase their share of the market. Furthermore, chains were able to attract many customers because of their convenient locations, made possible by their financial resources and expertise in selecting locations.

Supermarkets

Supermarkets are large, self-service stores with central checkout facilities. They carry an extensive line of food items and often nonfood products. Supermarkets' entire approach to the distribution of food and household cleaning and maintenance products is to offer large assortments these goods at each store at a minimal price.

Discount Retailers

Discount retailers are characterized by a focus on price as their main sales appeal. Merchandise assortments are generally broad and include both hard and soft goods, but assortments are typically limited to the most popular items, colours, and sizes. Traditional stores are usually large, self-service operations with long hours, free parking, and relatively simple fixtures. Online retailers such as Overstock.com have aggregated products and offered them at deep discounts. Generally, customers sacrifice having a stable assortment of products to receive deep discounts on the available products.

Warehouse Retailers

Warehouse retailers provide a bare-bones shopping experience at very low prices. Costco is the dominant warehouse retailer. Warehouse retailers streamline all operational aspects of their business and pass on the efficiency savings to customers. Costco generally uses a cost-plus pricing structure and provides goods in wholesale quantities.

Franchises

The franchise approach brings together national chains and local ownership. An owner purchases a franchise which gives her the right to use the firm's business model and brand for a set period of time. Often, the franchise agreement includes well-defined guidance for the owner including training and on-going support. The owner, or franchisee, builds and manages the local business. *Entrepreneur* magazine posts a list each year of the 500 top franchises according to an evaluation of financial strength and stability, growth rate, and size. The 2022 list is led by Taco Bell.

Malls and Shopping Centres

Malls and shopping centres are successful because they provide customers with a wide assortment of products across many stores. If you want to buy a suit or a dress, a mall provides many alternatives in one location. *Malls* are larger centres that typically have one or more department stores as major tenants or anchors. *Strip malls* are a common string of stores along major traffic routes, while isolated locations are freestanding sites not necessarily in heavy traffic areas. Stores in isolated locations must use promotion or some other aspect of their marketing mix to attract shoppers.

Online Retailing

Online retailing is unquestionably a dominant force in the retail industry, but today it accounts for only a small percentage of total retail sales. Companies like Amazon and Overstock.com complete all or most of their sales online. Many other online sales result from online sales from traditional retailers, such as purchases made at Nordstrom.com. Online marketing plays a significant role in preparing the buyers who shop in stores. In a similar integrated approach, catalogues that are mailed to customers' homes drive online orders. In a survey on its website, Land's End found that 75 percent of customers who were making purchases had reviewed the catalogue first (Ruiz, 2015).

Catalogue Retailing

Catalogues have long been used as a marketing device to drive phone and in-store sales. As online retailing began to grow, it had a significant impact on catalogue sales. Many retailers who depended on catalogue sales—Sears, Land's End, and J.C. Penney, to name a few—suffered as online retailers and online sales from traditional retailers pulled convenience shoppers away from catalogue sales. Catalogue mailings peaked in 2009 and saw a significant decrease through 2012. In 2013, there was a small increase in catalogue mailings. Industry experts note that catalogues are changing, as is their role in the retail marketing process. Despite significant declines, U.S. households still receive 11.9 billion catalogues each year (Geller, 2012).

Non-store Retailing

Beyond those mentioned in the categories above, there's a wide range of traditional and innovative retailing approaches. Although the Avon lady largely disappeared at the end of the last century, there are still in-home sales from Arbonne facial products, cabi women's clothing, WineShop at Home, and others. Many of these models are based on the idea of a woman using her personal network to sell products to her friends and their friends, often in a party setting.

Vending machines and point-of-sale kiosks have long been a popular retail device. Today they are becoming more targeted, such as companies selling easily forgotten items—such as small electronics devices and makeup items—to travellers in airports.

Each of these retailing approaches can be customized to meet the needs of the target buyer or combined to span a range of needs.

9.4 SUPPLY CHAINS AND DISTRIBUTION CHANNELS

What Is a Supply Chain?

We have discussed the channel partners, the roles they fill, and the structures they create. Marketers have long recognized the importance of managing distribution channel partners. As channels have become more complex and the flow of business has become more global, organizations have recognized that they need to manage more than just the channel partners. They need to manage the full chain of organizations and transactions from raw materials through final delivery to the customer—in other words, *the supply chain*.

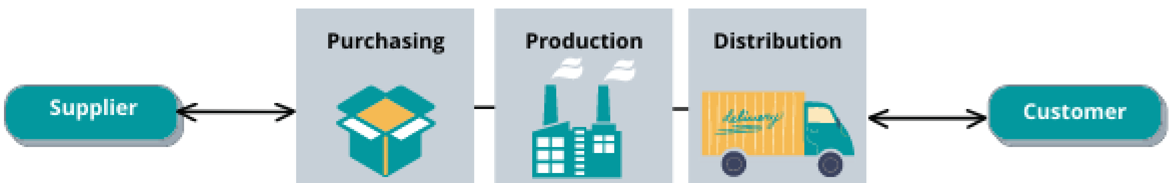

Fig 9.3 "Supply Chain Management System" by Fanshawe College, CC BY-NC-SA 4.0

A supply chain is the system through which an organization acquires raw material, produces products, and delivers the products and services to its customers. Figure 9.3 illustrates a typical supply chain. Supply chain management helps increase the efficiency of logistics service by minimizing inventory and moving goods efficiently from producers to the ultimate users.

On their way from producers to end users and consumers, products pass through a series of marketing entities known as a **distribution channel**.

The Functions of Distribution Channels

Why do distribution channels exist? Why can't every firm sell its products directly to the end user or consumer? Why are go-betweens needed? Channels serve a number of functions.

Channels Reduce the Number of Transactions

Channels make distribution simpler by reducing the number of transactions required to get a product from the manufacturer to the consumer. For example, if there are four students in a course and a professor requires five textbooks (each from a different publisher), a total of 20 transactions would be necessary to accomplish the sale of the books. If the bookstore serves as a go-between, the number of transactions is reduced to nine. Each publisher sells to one bookstore rather than to four students. Each student buys from one bookstore instead of from five publishers (see Figure 9.4).

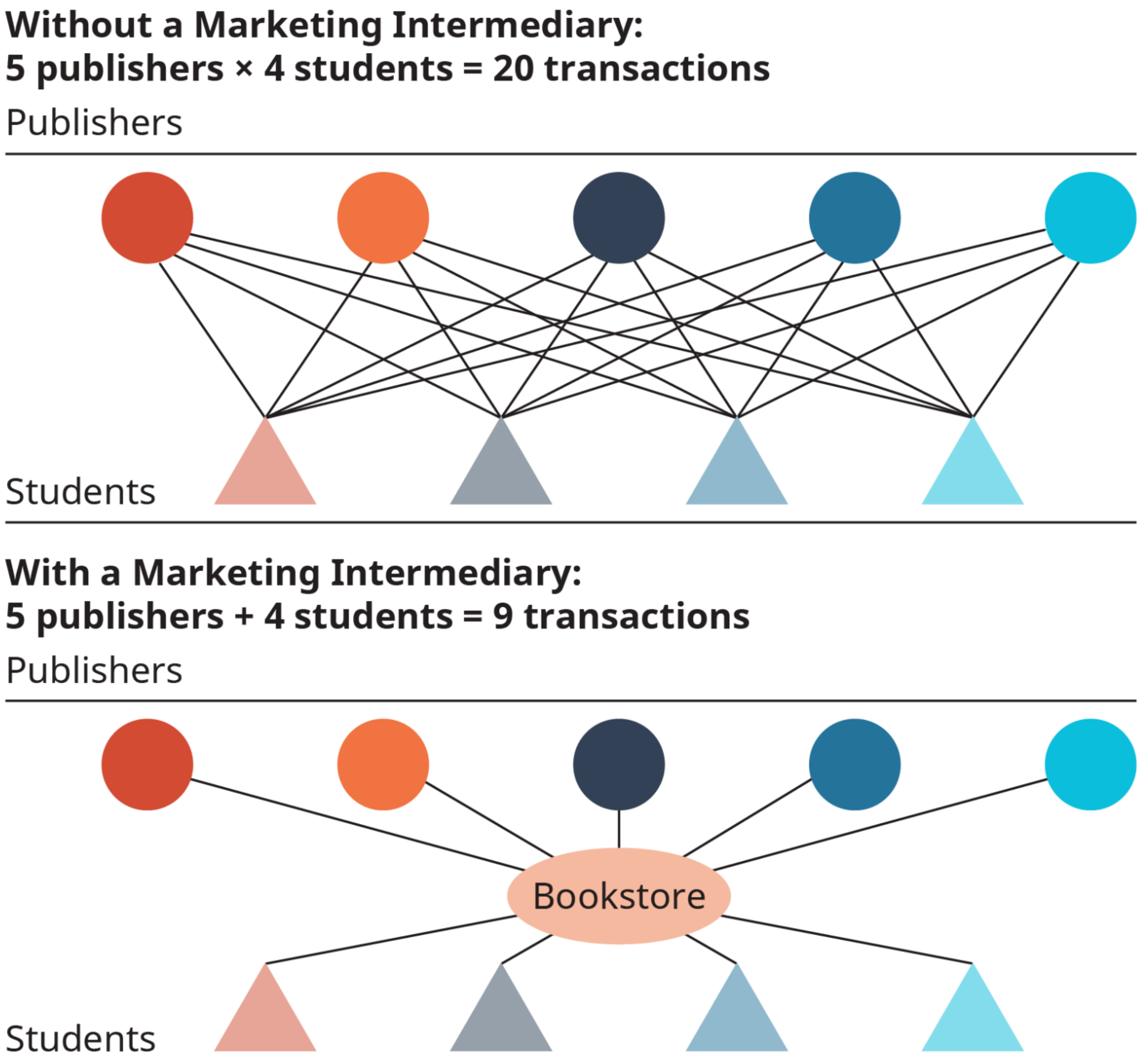

Fig 9.4 Image © Rice University & OpenStax, CC BY 4.0

Dealing with channel intermediaries frees producers from many of the details of distribution activity. Producers are traditionally not as efficient or as enthusiastic about selling products directly to end users as are channel members. First, producers may wish to focus on production. They may feel that they cannot both produce and distribute in a competitive way. On the other hand, manufacturers are eager to deal directly with giant retailers, such as Walmart, which offer huge sales opportunities to producers.

Channels Ease the Flow of Goods

Channels make distribution easier in several ways. The first is by *sorting,* which consists of the following:

- ***Sorting out:*** Breaking many different items into separate stocks that are similar. Eggs, for instance, are sorted by grade and size. Another example would be different lines of women's dresses—designer, moderate, and economy lines.
- ***Accumulating:*** Bringing similar stocks together into a larger quantity. Twelve large Grade A eggs could be placed in some cartons and 12 medium Grade B eggs in other cartons. Another example would be to merge several lines of women's dresses from different designers together.
- ***Allocating****:* Breaking similar products into smaller and smaller lots (allocating at the wholesale level is called **breaking bulk**.) For instance, a tank-car load of milk could be broken down into gallon jugs. The process of allocating generally is done when the goods are dispersed by region and as ownership of the goods changes.

Without the sorting, accumulating, and allocating processes, our modern consumer society would not exist. Instead, there would be home-based industries providing custom or semicustom products to local markets. In short, society would return to a much lower level of consumption.

A second way channels ease the flow of goods is by locating buyers for merchandise. A wholesaler must find the right retailers to sell a profitable volume of merchandise. A sporting-goods wholesaler, for instance, must find the retailers who are most likely to reach sporting-goods consumers. Retailers have to understand the buying habits of consumers and put stores where consumers want and expect to find the merchandise. Every member of a distribution channel must locate buyers for the products it is trying to sell.

Channel members also store merchandise so that goods are available when consumers want to buy them. The high cost of retail space often means many goods are stored by the wholesaler or manufacturer.

Supply Chain vs. Marketing Channels

The supply chain and marketing channels can be differentiated in the following ways:

1. **The supply chain is broader than marketing channels.** It begins with raw materials and delves deeply into production processes and inventory management. Marketing channels are focused on bringing together the partners who can most efficiently deliver the right marketing mix to the customer in order to maximize value. Marketing channels provide a more narrow focus within the supply chain.
2. **Marketing channels are purely customer facing.** Supply chain management seeks to optimize how products are supplied, which adds a number of financial and efficiency objectives that are more internally focused. Marketing channels emphasize a stronger market view of the customer expectations

and competitive dynamics in the marketplace.

3. **Marketing channels are part of the marketing mix.** Supply chain professionals are specialists in the delivery of goods. Marketers view distribution as one element of the marketing mix, in conjunction with product, price, and promotion. Supply chain management is more likely to identify the most efficient delivery partner. A marketer is more likely to balance the merits of a channel partner against the value offered to the customer. For instance, it might make sense to keep a channel partner who is less efficient but provides important benefit in promotional strategy. Successful organizations develop effective, respectful partnerships between the marketing and supply chain teams. When the supply chain team understands market dynamics and the points of flexibility in product and pricing, they are better able to optimize the distribution process. When marketing has the benefit of effective supply chain management—which is analyzing and optimizing distribution within and beyond the marketing channels—greater value is delivered to customers.

9.5 GLOBAL SOURCING AND DISTRIBUTION

Global sourcing refers to buying the raw materials or components that go into a company's products from around the world, not just from the headquarters' country. For example, Starbucks buys its coffee from locations like Colombia and Guatemala. The advantages of global sourcing are quality and lower cost. Global sourcing is possible to the extent that the world is flat—for example, buying the highest-quality cocoa beans for making chocolate or buying aluminum from Iceland, where it's cheaper because it's made using free geothermal energy.

When making global-sourcing decisions, firms face a choice of whether to sole-source (i.e., use one supplier exclusively) or to multisource (i.e., use multiple suppliers). The advantage of sole-sourcing is that the company will often get a lower price by giving all of its volume to one supplier. If the company gives the supplier a lot of business, the company may have more influence over the supplier for preferential treatment. For example, during a time of shortage or strained capacity, the supplier may give higher quantities to that company rather than to a competitor as a way of rewarding the company's loyalty.

On the other hand, using multiple suppliers gives a company more flexibility. For instance, if there's a natural disaster or other disruption at one of their suppliers, the company can turn to its other suppliers to meet its needs. For example, when Hurricane Mitch hit Honduras with 180-mile-per-hour winds, 70 to 80 percent of Honduras's infrastructure was damaged and 80 percent of its banana crop was lost. Both Dole Food Company and Chiquita bought bananas from Honduras, but Dole relied more heavily on bananas from Honduras than from other countries. As a result, Dole lost 25 percent of its global banana supply, but Chiquita lost only 15 percent (Sheffi, 2005).

Sole-Sourcing Advantages	Sole-Sourcing Disadvantages
• Price discounts based on higher volume • Rewards for loyalty during tough times • Exclusivity brings differentiation • Greater influence with a supplier	• Higher risk of disruption • Supplier has more negotiating power on price

Multisourcing Advantages	Multisourcing Disadvantages
• More flexibility in times of disruption • Negotiating lower rates by pitting one supplier against another	• Quality across suppliers may be less uniform • Less influence with each supplier • Higher coordination and management costs

Whichever sourcing strategy a company chooses, it can reduce risk by visiting its suppliers regularly to ensure the quality of products and processes, the financial health of each supplier, and the supplier's adherence to laws, safety regulations, and ethics.

The Case of Global Sourcing

While there is little systematic research on questions related to ethics and global sourcing, one recent survey in the context of clothing manufacturers identified the following most encountered issues according to Pretious and Love (2006):

- **Child labour.** Forty-three percent of the respondents had encountered factories where child labour was being used. India, China, Thailand, and Bangladesh were cited as the worst offenders in this regard, partly because of the absence or unreliability of birth certificates, but also because of the difficulty that Westerners have in assessing the age of workers in these countries. Buyers relied on the management of the factory to check on documents supplied by the employee.
- **Dangerous working conditions and health and safety issues.** Forty-three percent of the respondents had encountered dangerous working conditions in factories. These included unsafe machinery (e.g., machine guards having been removed to speed up production), workers failing to use safety equipment such as cutting gloves, and the use and storage of hazardous chemicals (e.g., those used for dyeing and printing). Fire regulations were also sometimes inadequate, both in factories and in the dormitory accommodation often provided for workers who live away from their home regions. Sometimes fire exits were locked, and fire extinguishers were missing.
- **Bribery and corruption.** Thirty-one percent of respondents said that they had experienced bribery and corruption. One blatantly fraudulent practice mentioned was for suppliers to mislead the buyer over the true source of production. Many suppliers claim that goods are made in one factory, then transfer the production elsewhere, making it difficult for the retailer to audit.
- **Exploitation of the workforce.** Twenty-five percent of respondents mention some aspect of exploitation of the workforce, encompassing the issues of child labour and health and safety. However, it can also cover low wages being paid to workers and excessive overtime being expected by employers. Respondents specifically mentioned that they had encountered worker exploitation. Many spoke of long working hours in factories, especially at peak periods, with employees often working over seventy hours

per week.

Distribution Management

Selling internationally means considering how your company will distribute its goods in the market. Developed countries have good infrastructure—passable roads that can accommodate trucks, retailers who display and sell products, and reliable communications infrastructure and media choices. Emerging markets, on the other hand, often have very fragmented distribution networks, limited logistics, and much smaller retailer outlets. Hole-in-the-wall shops, door-to-door peddlers, and street vendors play a much larger role in emerging-market countries. In the emerging countries of Africa, for example, books might be sold from the back of a moped.

In addition, the standards of living in emerging countries vary widely. Most of the middle class lives in cities, but the percentage of the population that lives in rural areas varies by country. Rural logistics are especially problematic. Narrow dirt roads, weight-limited bridges, and mud during the rainy season hamper the movement of goods.

Distribution-Management Choices: Partner, Acquire, or Build from Scratch

There are typically three distribution strategies for entering a new market. First, companies can do a joint-venture or partnership with a local company. This is the strategy Walmart used when entering Mexico. A second strategy is to acquire a local company to have immediate access to large-scale distribution. The Home Depot pursued this strategy in China when it acquired a partner with whom it had been working for quite some time. Third, a company can to build its own distribution from scratch. Retailer Carrefour chose this route in China years ago, because it knew China would offer a big opportunity, and Carrefour wanted to develop its own local capabilities. Which strategy the company chooses depends on its timetable for volume in the market, local foreign-ownership laws, and the availability of suitable partners or acquisition targets.

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9.7 KEY TERMS

Key Terms

Accumulating: Bringing similar stocks together into a larger quantity. Twelve large Grade A eggs could be placed in some cartons and 12 medium Grade B eggs in other cartons. Another example would be to merge several lines of women's dresses from different designers together. 9.4

Allocating: Breaking similar products into smaller and smaller lots (allocating at the wholesale level is called breaking bulk.) For instance, a tank-car load of milk could be broken down into gallon jugs. The process of allocating generally is done when the goods are dispersed by region and as ownership of the goods changes. 9.4

Broker or Agent Channel: Includes one additional intermediary. Agents and brokers are different from wholesalers in that they do not take title to the merchandise. In other words, they do not own the merchandise because they neither buy nor sell. 9.2

Channel of Distribution: also called a marketing channel, a set of interdependent organizations involved in the process of making a product or service available for use or consumption, as well as providing a payment mechanism for the provider. 9.1

Direct Channel: Is the simplest channel. In this case, the producer sells directly to the consumer. 9.2

Distribution Channel: On their way from producers to end users and consumers, products pass through a series of marketing entities 9.4

Grading and Packaging: Wholesalers buy a very large quantity of goods that they then break down into smaller lots. The process of breaking large quantities into smaller lots to be resold is called "bulk breaking". Often this includes physically sorting, grading, and assembling the goods. 9.3

Information Flow: The individuals who participate in the flow of information either up or down the channel. 9.1

Negotiation Flow: The institutions that are associated with the actual exchange processes. 9.1

Ownership Flow: The movement of title through the channel. 9.1

Product Flow: The movement of the physical product from the manufacturer through all the parties who take physical possession of the product until it reaches the ultimate consume. 9.1

Promotion Flow: The flow of persuasive communication in the form of advertising, personal selling, sales promotion, and public relations. 9.1

Purchasing: Wholesalers purchase very large quantities of goods directly from producers or from other wholesalers. By purchasing large quantities or volumes, wholesalers are able to secure significantly lower prices. 9.3

Retail Channel: Is different from the direct channel in that the retailer doesn't produce the product. The retailer markets and sells the goods on behalf of the producer 9.2

Risk Bearing: Wholesalers either take title to the goods they purchase, or they own the goods they purchase. 9.3

Sorting Out: Breaking many different items into separate stocks that are similar. Eggs, for instance, are sorted by grade and size. Another example would be different lines of women's dresses—designer, moderate, and economy lines. 9.4

Wholesaler: Is primarily engaged in buying and usually storing and physically handling goods in large quantities, which are then resold (usually in smaller quantities) to retailers or to industrial or business users. 9.2

Wholesale Channel: Looks very similar to the retail channel, but it also involves a wholesaler. 9.2

CHAPTER 10: GLOBAL PROMOTION

Chapter Outline

10.0 INTRODUCTION

Learning Objectives

After reading this section, students should be able to:

1. Explain integrated marketing communication (IMC).
2. Explain the promotion mix.
3. Describe common marketing communication methods, including their advantages and disadvantages.
4. Explain how organizations use IMC to support their marketing strategies.
5. List driving factors in global promotion decisions.
6. Outline the steps in changing the global promotional mix.

Marketing communications—the promotion P of the marketing mix—includes advertising, public relations, sales promotion, and personal selling. When a company embraces integrated marketing communications (IMC), it recognizes that the various elements of a company's communication strategy must be carefully coordinated. Advertising is a sponsored, paid message that is communicated through nonpersonal channels. Global advertising consists of the same advertising appeals, messages, artwork, and copy in campaigns around the world. The effort required to create a global campaign forces a company to determine whether or not a global market exists for its product. The trade-off between standardized and adapted advertising is often accomplished by means of pattern advertising, which can be used to create localized global advertising. Many advertising agencies are part of larger advertising organizations. Advertisers may place a single global agency in charge of worldwide advertising; it is also possible to use one or more agencies on a regional or local basis.

The starting point in ad development is the creative strategy, a statement of what the message will say. The people who create ads often seek a big idea that can serve as the basis for memorable, effective messages. The advertising appeal is the communication approach—rational or emotional—that best relates to buyer motives. Rational appeals speak to the mind: emotional appeals speak to the heart. The selling proposition is the promise that captures the reason for buying the product. The creative execution is the way an appeal or proposition is presented. Art direction and copy must be created with cultural considerations in mind. Perceptions of humour, male-female relationships, and sexual imagery vary in different parts of the world. Media availability varies considerably from country to country. When selecting media, marketers are sometimes as constrained by laws and regulations as by literacy rates.

A company utilizes public relations (PR) to foster goodwill and understanding among constituents both inside and outside the company. In particular, the PR department attempts to generate favourable publicity about the company and its products and brands. The PR department must also manage corporate communications when responding to negative publicity. The most important PR tools are press releases, media kits, interviews, and tours. Many global companies make use of various types of corporate advertising, including image advertising and advocacy advertising. Public relations is also responsible for providing accurate, timely information, especially in the event of a crisis.

10.1 INTEGRATED MARKETING COMMUNICATION

Making an Impact

Having a great product available to your customers at a great price does absolutely nothing for you if your customers don't know about it. That's where promotion enters the picture: it does the job of connecting with your target audiences and communicating what you can offer them.

In today's marketing environment, promotion involves **integrated marketing communication (IMC)**. In a nutshell, IMC involves bringing together a variety of different communication tools to deliver a common message and make a desired impact on customers' perceptions and behaviour. As an experienced consumer in the English-speaking world, you have almost certainly been the target of IMC activities (practically every time you "like" a TV show, article, or a meme on Facebook, you are participating in an IMC effort!).

What Is Marketing Communication?

Defining marketing communication is tricky because, in a real sense, everything an organization does has communication potential. The price placed on a product communicates something very specific about the product. A company that chooses to distribute its products strictly through discount stores sends a distinct message to the market. A business that follows strict environmental practices says much about the organization.

Marketing communication refers to activities deliberately focused on promoting an offering among target audiences. The following definition helps to clarify this term:

> **Marketing communication** includes all the messages, media, and activities used by an organization to communicate with the market and help persuade target audiences to accept its messages and take action accordingly.

Integrated marketing communication is the the process of coordinating all this activity across different communication methods. Note that a central theme of this definition is *persuasion*: persuading people to believe something, to desire something, and/or to do something. Effective marketing communication is goal directed, and it is aligned with an organization's marketing strategy. It aims to deliver a particular message to a specific audience with a targeted purpose of altering perceptions and/or behaviour. Integrated marketing communication (IMC) makes marketing activity more efficient and effective because it relies on multiple communication methods and customer touch points to deliver a consistent message in multiple means and in more compelling ways.

The Promotion Mix: Marketing Communication Methods

The ***promotion mix*** refers to how marketers combine a range of marketing communication methods to execute their marketing activities. Different methods of marketing communication have distinct advantages and complexities, and it requires skill and experience to deploy them effectively. Not surprisingly, marketing communication methods evolve over time as new communication tools and capabilities become available to marketers and the people they target.

Fig 10.1 The Promotion Mix: Marketing Communication Methods.

Seven common methods of marketing communication are described below:

- **Advertising:** Any paid form of presenting ideas, goods, or services by an identified sponsor.

Historically, advertising messages have been tailored to a group and employ mass media such as radio, television, newspaper, and magazines. Advertising may also target individuals according to their profile characteristics or behaviour; examples are the weekly ads mailed by supermarkets to local residents or online banner ads targeted to individuals based on the sites they visit or their Internet search terms.

- **Public relations (PR):** The purpose of public relations is to create goodwill between an organization (or the things it promotes) and the "public" or target segments it is trying to reach. This happens through unpaid or earned promotional opportunities: articles, press and media coverage, winning awards, giving presentations at conferences and events, and otherwise getting favourable attention through vehicles not paid for by the sponsor. Although organizations earn rather than pay for the PR attention they receive, they may spend significant resources on the activities, events, and people who generate this attention.
- **Personal selling:** Personal selling uses people to develop relationships with target audiences for the purpose of selling products and services. Personal selling puts an emphasis on face-to-face interaction, understanding the customer's needs, and demonstrating how the product or service provides value.
- **Sales promotion:** Sales promotions are marketing activities that aim to temporarily boost sales of a product or service by adding to the basic value offered, such as "buy one get one free" offers to consumers or "buy twelve cases and get a 10 percent discount" to wholesalers, retailers, or distributors.
- **Direct marketing:** This method aims to sell products or services directly to consumers rather than going through retailers. Catalogues, telemarketing, mailed brochures, or promotional materials and television home shopping channels are all common traditional direct marketing tools. Email and mobile marketing are two next-generation direct marketing channels.
- **Digital marketing:** Digital marketing covers a lot of ground, from Web sites to search-engine, content, and social media marketing. Digital marketing tools and techniques evolve rapidly with technological advances, but this umbrella term covers all of the ways in which digital technologies are used to market and sell organizations, products, services, ideas, and experiences.
- **Guerrilla marketing:** This newer category of marketing communication involves unconventional, innovative, and usually low-cost marketing tactics to engage consumers in the marketing activity, generate attention and achieve maximum exposure for an organization, its products, and/or services. Generally guerrilla marketing is experiential: it creates a novel situation or memorable experience consumers connect to a product or brand.

Most marketing initiatives today incorporate multiple methods: hence the need for IMC.

The Objectives of Marketing Communication

The basic objectives of all marketing communication methods are (1) to communicate, (2) to compete, and (3) to convince. In order to be effective, organizations should ensure that whatever information they communicate is clear, accurate, truthful, and useful to the stakeholders involved. In fact, being truthful and accurate in marketing communications is more than a matter of integrity; it's also a matter of legality, since fraudulent marketing communications can end in lawsuits and even the criminal justice system.

Marketing communication is key to competing effectively, particularly in markets where competitors sell essentially the same product at the same price in the same outlets. Only through marketing communications may an organization find ways to appeal to certain segments, differentiate its product, and create enduring brand loyalty. Remaining more appealing or convincing than competitors' messages is an ongoing challenge.

Ideally, marketing communication is convincing: it should present ideas, products, or services in such a compelling way that target segments are led to take a desired action. The ability to persuade and convince is essential to winning new business, but it may also be necessary to re-convince and retain many consumers and customers. Just because a customer buys a particular brand once or a dozen times, or even for a dozen years, there is no guarantee that the person will stick with the original product. That is why marketers want to make sure he or she is constantly reminded of the product's unique benefits.

Case: Fashion Nova IMC Strategy

Often when we think about IMC, it comes off as either so many activities to be done or an expensive mode of marketing, especially during the market entry stage for brands. Understanding and carefully selecting what IMC tools to put together for a brand is key to a brand's success, regardless of what market entry stage the brand might be in. While these methods might seem expensive for new brands, Fashion Nova is an example of a new brand that has been able to scale up using this method successfully.

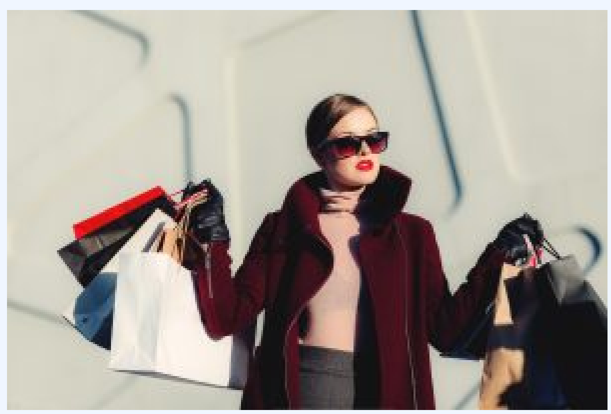

Photo by freestocks, Unsplash Licence

At first glance, it looks like this brand uses influencer marketing as its only marketing tactic, harnessing social media marketing with looks on influencers of all shapes and sizes. However, the clothing e-commerce company has exploded with a unique retention marketing strategy that includes public relations (event sponsorship), direct response, email marketing, ambassador marketing, and sales promotions. Their impeccable merge of these marketing methods has kept users coming back for more, as the brand made $4.3M in revenue as of 2021 (Fashion Nova Revenue: Annual, Historic, and Financials – Zippia, 2022)

Aderoju Bankole, October 2022

10.2 COMMON MARKETING COMMUNICATION METHODS

In a successfully operated campaign, all activities will be well-coordinated to build on one another to increase the overall impact. For example, a single campaign might include:

- **Advertising:** A series of related, well-timed, carefully placed television ads coupled with print advertising in selected magazines and newspapers.
- **Direct marketing:** Direct-to-consumer mail pieces sent to target segments in selected geographic areas, reinforcing the messages from the ads.
- **Personal selling:** Preparation and training for customer sales representatives about the campaign to equip them to explain and demonstrate the product benefits stressed in advertising.
- **Sales promotion:** In-store display materials reflecting the same messages and design as the ads, emphasizing point-of-sale impact.
- **Digital marketing:** Promotional information on the organization's Web site that reflects the same messages, design, and offers reflected in the ads; ads themselves may be posted on the Website, YouTube, Facebook, and shared in other social media.
- **Public relations:** A press release announcing something newsworthy in connection to the campaign focus, objectives, and target segment(s).

Advertising

Advertising is probably the first thing you think of when you think of marketing. Advertising is any paid form of communication from an identified sponsor or source that draws attention to ideas, goods, services or the sponsor itself- essentially commercials and ads (whether digital or print). Most advertising is directed toward groups rather than individuals, and advertising is usually delivered through media such as television, radio, newspapers and, increasingly, the internet. Ads are often measured in *impressions* (the number of times a consumer is exposed to an advertisement).

Advantages and Disadvantages of Advertising

As a method of marketing communication, advertising has both advantages and disadvantages. In terms of advantages, advertising creates a sense of credibility or legitimacy when an organization invests in presenting itself and its products in a public forum. Ads can convey a sense of quality and permanence, the idea that a company isn't some fly-by-night venture. Advertising allows marketers to repeat a message at intervals selected strategically. Repetition makes it more likely that the target audience will see and recall a message, which improves awareness-building results. Advertising can generate drama and human interest by featuring people and situations that are exciting or engaging. Finally, advertising is an excellent vehicle for brand building, as it can create rational and emotional connections with a company or offering that translate into goodwill.

The primary disadvantage of advertising is cost. Marketers question whether this communication method is really cost-effective at reaching large groups. Of course, costs vary depending on the medium, with television ads being very expensive to produce and place. In contrast, print and digital ads tend to be much less expensive. Along with cost is the question of how many people an advertisement actually reaches. Ads are easily tuned out in today's crowded media marketplace. Even ads that initially grab attention can grow stale over time. Because advertising is a one-way medium, there is usually little direct opportunity for consumer feedback and interaction, particularly from consumers who often feel overwhelmed by competing market messages.

Direct Marketing

Direct marketing activities bypass any intermediaries and communicate directly with the individual consumer. Direct mail is personalized to the individual consumer, based on whatever a company knows about that person's needs, interests, behaviours, and preferences. Traditional direct marketing activities include mail, catalogues, and telemarketing. The thousands of "junk mail" offers from credit card companies, bankers, and charitable organizations that flood mailboxes every year are artifacts of direct marketing. Telemarketing contacts prospective customers via the telephone to pitch offers and collect information. Today, direct marketing overlaps heavily with digital marketing, as marketers rely on email and, increasingly, mobile communications to reach and interact with consumers.

If you've ever paid off an auto loan, you may have noticed a torrent of mail offers from car dealerships right around the five-year mark. They know, from your credit history, that you're nearly done paying off your car and you've had the vehicle for several years, so you might be interested in trading up for a newer model. Based on your geography and any voter registration information, you may be targeted during election season to participate via telephone in political polls and to receive "robocalls" from candidates and parties stumping for your vote. Moving into the digital world, virtually any time you share an email address with an organization, it becomes part of a database to be used for future marketing.

Advantages and Disadvantages of Direct Marketing

Direct marketing can offer significant value to consumers by tailoring their experience in the market to things that most align with their needs and interests. If you're going to have a baby (and you don't mind people knowing about it), wouldn't you rather have Target send you special offers on baby products than on men's shoes or home improvement goods? Additionally, direct marketing can be a powerful tool for anticipating and predicting customer needs and behaviours. Over time, as companies use consumer data to understand their target audiences and market dynamics, they can develop more effective campaigns and offers.

Among the leading disadvantages of direct marketing are, not surprisingly, customer concerns about privacy and information security. Data-driven direct marketing might seem a little creepy or even nefarious, and certainly it can be when marketers are insensitive or unethical in their use of consumer data. Direct marketing also takes place in a crowded, saturated market in which people are only too willing to toss junk mail and unsolicited email into trash bins without a second glance. Electronic spam filters screen out many email messages, so people may never even see email messages from many of the organizations that send them.

Heavy reliance on data also leads to the challenge of keeping databases and contact information up to date and complete, a perennial problem for many organizations. Finally, direct marketing implies a direct-to-customer business model that inevitably requires companies to provide an acceptable level of customer service and interaction to win new customers and retain their business.

Personal Selling

Personal selling uses in-person interaction to sell products and services. This type of communication is carried out by sales representatives, who are the personal connection between a buyer and a company or a company's products or services. In addition to enhancing customer relationships, this type of marketing communications tool can be a powerful source of customer feedback, as well.

Effective personal selling addresses the buyer's needs and preferences without making him or her feel pressured. Good salespeople offer advice, information, and recommendations, and they can help buyers save money and time during the decision process. The seller should give honest responses to any questions or objections the buyer has and show that the company cares more about meeting the buyer's needs than making the sale. Attending to these aspects of personal selling contributes to a strong, trusting relationship between buyer and seller (Merchant, 2019).

Advantages and Disadvantages of Personal Selling

The most significant strength of personal selling is its flexibility. Salespeople can tailor their presentations to fit the needs, motives, and behaviour of individual customers. A salesperson can gauge the customer's reaction to a sales approach and immediately adjust the message to facilitate better understanding. A salesperson is also in an excellent position to encourage the customer to act. The one-on-one interaction of personal selling means that a salesperson can effectively respond to and overcome objections—e.g., concerns or reservations about the product—so that the customer is more likely to buy. Salespeople can also offer many customized reasons that might spur a customer to buy, whereas an advertisement offers a limited set of reasons that may not persuade everyone in the target audience.

Personal selling also minimizes wasted effort. Advertisers can spend a lot of time and money on a mass-marketing message that reaches many people outside the target market (but doesn't result in additional sales). In personal selling, the sales force pinpoints the target market, makes a contact, and focuses effort that has a strong probability of leading to a sale.

High cost is the primary disadvantage of personal selling. With increased competition, higher travel and lodging costs, and higher salaries, the cost per sales contract continues to rise. Many companies try to control sales costs by compensating sales representatives through commissions or by using complementary techniques, such as telemarketing, direct mail, toll-free numbers for interested customers, and online communication with qualified prospects. Another weakness of personal selling is message inconsistency. Many salespeople view themselves as independent from the organization, so they design their own sales techniques, use their own messaging strategies, and engage in questionable ploys to generate sales (you'll recall our discussion in the ethics module about the unique challenges that B2B salespeople face.) As a result, it can be difficult to find a unified company or product message within a sales force or between the sales force and the rest of the marketing mix.

Sales Promotions

Sales promotions are a marketing communication tool for stimulating revenue or providing incentives or extra value to distributers, sales staff, or customers over a short time period. Sales promotion activities include special offers, displays, demonstrations, and other nonrecurring selling efforts that aren't part of the ordinary routine. As an additional incentive to buy, these tools can be directed at consumers, retailers and other distribution partners, or the manufacturer's own sales force.

Companies use many different forms of media to communicate sales promotions, such as printed materials like posters, coupons, direct mail pieces and billboards, radio and television ads, digital media (like text messages), email, websites, social media, and so forth. Most consumers are familiar with common sales promotion techniques including samples, coupons, point-of-purchase displays, premiums, contents, loyalty programs, and rebates.

Advantages and Disadvantages of Sales Promotions

In addition to their primary purpose of boosting sales in the near term, companies can use consumer sales promotions to help them understand price sensitivity. Coupons and rebates provide useful information about how pricing influences consumers' buying behaviour. Sales promotions can also be a valuable–and sometimes sneaky–way to acquire contact information for current and prospective customers. Many of these offers require consumers to provide their names and other information in order to participate. Electronicallyscanned coupons can be linked to other purchasing data, to inform organizations about buying habits. All this information can be used for future marketing research, campaigns and outreach.

Consumer sales promotions can generate loyalty and enthusiasm for a brand, product, or service. Frequent flyer programs, for example, motivate travellers to fly on a preferred airline even if the ticket prices are somewhat higher. If sales have slowed, a promotion such as a sweepstakes or contest can spur customer excitement and renew interest in the company's offering. Sales promotions are a good way of energizing and inspiring customer action.

Trade promotions offer distribution channel partners financial incentives that encourage them to support and promote a company's products. Offering incentives like prime shelf space at a retailer's store in exchange for discounts on products has the potential to build and enhance business relationships with important distributors or businesses. Improving these relationships can lead to higher sales, stocking of other product lines, preferred business terms and other benefits.

Sales promotions can be a two-edged sword: if a company is continually handing out product samples and coupons, it can risk tarnishing the company's brand. Offering too many freebies can signal to customers that they are not purchasing a prestigious or "limited" product. Another risk with too-frequent promotions is that savvy customers will hold off purchasing until the next promotion, thus depressing sales.

Often businesses rush to grow quickly by offering sales promotions, only to see these promotions fail to reach their sales goals and target customers. The temporary boost in short term sales may be attributed to highly price-sensitive consumers looking for a deal, rather than the long-term loyal customers a company wants to cultivate. Sales promotions need to be thought through, designed, and promoted carefully. They also need to align well with the company's larger business strategy. Failure to do so can be costly in terms of dollars, profitability and reputation.

If businesses become overly reliant on sales growth through promotions, they can get trapped in short-term marketing thinking and forget to focus on long-term goals. If, after each sales dip, a business offers another sales promotion, it can be damaging to the long-term value of its brand.

(Edward Lowe Foundation, n.d.)

Digital Marketing

Digital marketing is an umbrella term for using digital tools to promote and market products, services, organizations and brands. As consumers and businesses become more reliant on digital communications, the power and importance of digital marketing have increased. There are several essential tools in the digital marketing tool kit: email, mobile marketing, websites, content marketing and search-engine optimization (SEO), and social media marketing. For now, we'll focus on websites and social media.

Websites represent an all-in-one storefront, a display counter, and a megaphone for organizations to communicate in the digital world. For digital and brick-and-mortar businesses, websites are a primary channel for communicating with current and prospective customers as well as other audiences. A good website provides evidence that an organization is real, credible, and legitimate.

Social media are distinctive for their networking capabilities: they allow people to reach and interact with one another through interconnected networks. This "social" phenomenon changes the power dynamic in marketing: no longer is the marketer the central gatekeeper for all communication about a product, service, brand, or organization. Social media allows for organic dialogue and activity to happen directly between individuals, unmediated by a company. Companies can (and should) listen, learn, and find ways to participate authentically.

Advantages and Disadvantages of Digital Marketing

Websites have so many advantages that there is almost no excuse for a business not to have one. Effective website marketing declares to the world that an organization exists, what value it offers, and how it does business. Websites can be an engine for generating customer data and new business leads. An electronic storefront is often dramatically less expensive than a physical storefront, and it can serve customers virtually anywhere in the world with internet access. Websites are very flexible and easy to alter. Organizations can try out new strategies, content and tactics at relatively low cost to see what works and where changes pay off.

The advantages and benefits of social media marketing focus heavily on the two-way and even multidirectional communication between customers, prospects, and advocates for your company or brand. By listening and engaging in social media, organizations are better equipped to understand and respond to market sentiment. Social media helps organizations identify and cultivate advocates for its products, services, and brand, including the emergence of customers who can become highly credible, trusted voices to help promote the brand.

At the same time, digital marketing strategies carry costs and risks. Websites require some investment of time and money to set up and maintain. Organizations should make wise, well-researched decisions about information infrastructure and website hosting, to ensure their sites remain operational with good performance and uptime. Companies that capture and maintain customer data through their websites must be vigilant about information security to prevent hackers from stealing sensitive customer data.

Social media also carry a number of inherent challenges. Social media are dynamic environments that requires significant effort to monitor and stay current. It is also difficult to continually create "share-worthy" content. The variety of social media tools makes it a challenge to understand which platforms to use for which target audiences and calls to action. Crisis communications can be difficult, too, particularly in the public environment of social media, in which it is difficult to contain or control communication. This means it can be difficult to mitigate the impact of a crisis on the brand. One of the biggest challenges facing organizations is determining who in the organization should "own" the social media platforms for the organization. Too few hands to help means the burden of content creation is high on a single individual. However, too many people often results in duplication of efforts or conflicting content.

Public Relations

Public relations (PR) is the process of maintaining a favourable image and building beneficial relationships between an organization and the public communities, groups, and people it serves. Unlike advertising, which tries to create favourable impressions through paid messages, public relations does not pay for attention and publicity. Instead, PR strives to earn a favourable image by drawing attention to newsworthy and attention-worthy activities of the organization and its customers. For this reason, PR is often referred to as "free advertising."

In fact, PR is a costless form of promotion. It requires salaries to be paid to people who oversee and execute PR strategy. It also involves expenses associated with events, sponsorships and other PR-related activities.

In 2021, Emirates Airlines took their advertising campaign to new heights when they filmed their ad on top of Burj Khalifa. Sitting 828 meters above the ground, this Dubai landmark is the tallest building in the world. Watch the video: We're on top of the world by Emirates Airline [:33]

Video: We're on top of the world by Emirates Airline [:33] is licensed under the Standard YouTube License. Transcription

This "We Are On Top Of The World" video advertisement was a creative PR strategy to announce that Dubai was taken off the UK's red list – a covid-related restriction that banned travel between the two countries (Godinho, 2021). This unconventional video ad quickly went viral and attracted massive media attention across the world.

Then, only a few months after Emirates created a buzz with this viral video, they released a second video promoting the 2020 Dubai Expo. This time, with an A380 flying in the background. With over 12M views to date (May 2022), the second video has already outperformed the original. Watch the video: We did it again by Emirates [1:15].

Video: We did it again by Emirates [1:15] is licensed under the Standard YouTube License. Transcript

"We always look to challenge the norm and push boundaries at Emirates. We do it every day through our innovative services, our best in class product and of course through our advertising. The calm and confidence of the cabin crew you see in the ad is an embodiment of our frontline team, serving travellers and ensuring their safety. We're proud to be among a privileged few who have been allowed to film at the top of the Burj Khalifa by Emaar; and even prouder that we get to showcase our beautiful city, Dubai," said Sir Tim Clark, President Emirates Airline (The Emirates Group, 2021).

Advantages and Disadvantages of Public Relations

Because PR activity is earned rather than paid, it tends to carry more credibility and weight. For example, when a news story profiles a customer's successful experience with a company and its products, people tend to view this type of article as less biased (and therefore more credible) than a paid advertisement. The news story comes from an objective reporter who feels the story is worth telling. Meanwhile, an advertisement on a similar topic would be viewed with skepticism because it is a paid placement from a biased source: the ad sponsor.

Using IMC to Support Marketing Strategies

Determining which marketing communication methods and tools to use and how best to combine them is a challenge for any marketer planning a promotional strategy. To aid the planning process, marketing managers often use a campaign approach. A *campaign* is a planned, coordinated series of marketing communication efforts built around a single theme or idea and designed to reach a particular goal. For years, the term "campaign" has been used in connection with advertising, and this term applies equally well to the entire IMC program.

Walt Disney Company (Disney)

The Walt Disney Company (Disney) was a pioneer and "wrote the book" on IMC techniques. For example, when Disney released a new movie property they would unleash a marketing juggernaut across their business empire. Ads and trailers for the new movie would be run on Disney T.V. channels and Disney movies currently in theatres. Posters and merchandise would populate Disney theme parks- even new rides would be constructed with the new property theme. Videos would be run in Disney retail stores with posters and merchandise available for purchase. Disney licensees would partner with large national retailers to coordinate the movie release with in-store promotions and displays. Utilizing T.V., movies, retail stores, theme parks, and national retail promotion, it is easy to see why the Walt Disney Company has been so successful with its marketing efforts.

Organizations may conduct many types of IMC campaigns, and several may be run concurrently. Geographically, a firm may have a local, regional, or national campaign, depending upon the available funds, objectives, and market scope. One campaign may be aimed at consumers and another at wholesalers and retailers. Different marketing campaigns might target different segments simultaneously, delivering messages and using communication tools tailored to each segment. Marketers use a marketing plan (sometimes called an IMC plan) to track and execute a set of campaigns over a given period of time.

A campaign revolves around a theme, a central idea, focal point, or purpose. This theme permeates all IMC efforts and works to unify the campaign. The theme may refer to the campaign's goals—for example, KCRW "Capital Campaign" launched by the popular Los Angeles-based public radio station KCRW to raise $48 million to build a new state-of-the-art media facility for its operations. The theme may also refer to the shift in customer attitudes or behaviour that a campaign focuses on—such as new-member campaigns launched by numerous member organizations, from professional associations to school parent-teacher organizations. A theme might take the form of a slogan, such as Coca-Cola's "Taste the Feeling" campaign or DeBeers' "A diamond is forever."

The IMC approach takes a central theme and pushes that message through appropriate communication channels. LinkedIn recently staged a campaign using "In it together" as their theme. The company produced a number of black and white, documentary-style videos featuring highly-motivated individuals demonstrating their inspiration for their hard work. The company used outdoor ads, social media, and their website to leverage the inspirational videos and their message.

Clear Channel in Switzerland

Clear Channel is a marketing company that specializes in outdoor advertising. For their latest advertising campaign in Switzerland, they created a slogan-based theme, "Where Brands Meet People," and asked their clients to participate in dramatizing it. Dozens of Swiss companies gave their logo to be used as individual "tiles" in three colourful mosaic portraits. These mosaics appeared on the web and on the streets of Switzerland (Tsevis, n.d.).

- A high-resolution version of the image that reveals all the brands that make up the mosaics.

Some of the billboards appeared in animated form, as below:

Video: Where Brands Meet People by Clear Channel [0:10] is licensed under the Standard YouTube License. on-screen text only

Marketing campaigns may also adopt themes that refer to a stage in the product life cycle, such as McDonald's 2015 "All-Day Breakfast" rollout campaign. Some organizations use the same theme for several campaigns; others develop a different theme for each new campaign.

10.3 CHANGES IN PROMOTION

Before a company decides to become global, it must consider a multitude of factors unique to the international marketing environment. These factors are social, cultural, political, legal, competitive, economic, and even technological in nature. Ultimately, at the global marketing level, a company trying to speak with one voice is faced with many challenges when creating a worldwide marketing plan. Unless a company holds the same position against its competition in all markets (market leader, low cost, etc.), it is impossible to launch identical marketing plans worldwide. Thus, global companies must be nimble enough to adapt to changing local market trends, tastes, and needs.

Global Promotion

Language is usually one element that is customized in a global promotional mix.

For global advertisers, there are four potentially competing business objectives that must be balanced when developing worldwide advertising: building a brand while speaking with one voice, developing economies of scale in the creative process, maximizing local effectiveness of advertisements, and increasing the company's speed of implementation. Global marketers can use the following approaches when executing global promotional programs: exporting executions, producing local executions, and importing ideas that travel.

Factors in Global Promotion

To successfully implement these approaches, brands must ensure their promotional campaigns take into how consumer behaviour is shaped by internal conditions (e.g., demographics, knowledge, attitude, beliefs) and external influences (e.g., culture, ethnicity, family, lifestyle) in local markets.

Fig 10.2 "Factors in global promotion" by Alyssa Giles CC BY-NC-SA 4.0.

- **Language**– The importance of language differences is extremely crucial in global marketing, as there are almost 3,000 languages in the world. Language differences have caused many problems for marketers in designing advertising campaigns and product labels. Language becomes even more significant if a country's population speaks several languages.
- **Colours**– Colours also have different meanings in different cultures. For example, in Egypt, the country's national colour of green is considered unacceptable for packaging because religious leaders once wore it. In Japan, black and white are colours of mourning and should not be used on a product's package. Similarly, purple is unacceptable in Hispanic nations because it is associated with death.
- **Values**– An individual's values arise from his or her moral or religious beliefs and are learned through experiences. For example, Americans place a very high value on material well-being and are much more likely to purchase status symbols than people in India. In India, the Hindu religion forbids the consumption of beef.
- **Business norms**– The norms of conducting business also vary from one country to the next. For example, in France, wholesalers do not like to promote products. They are mainly interested in supplying retailers with the products they need.
- **Religious beliefs**– A person's religious beliefs can affect shopping patterns and products purchased in addition to his or her values. In the United States and other Christian nations, Christmas time tends to be a major sales period. In other religions, significant religious holidays may or may not serve as popular times for purchasing products.

There are many other factors, including a country's political or legal environment, monetary circumstances, and technological environment that can impact a brand's promotional mix. Companies have to be ready to quickly respond and adapt to these challenges as they evolve and fluctuate in the market of each country.

Changing the Global Promotional Mix

When launching global advertising, public relations or sales campaigns, global companies test promotional ideas using marketing research systems that provide results comparable across countries. The ability to identify the elements or moments of an advertisement that contribute to the success of a product launch or expansion is how economies of scale are maximized in marketing communications. Market research measures such as flow of attention, flow of emotion, and branding moments provide insight into what is working in an advertisement in one or many countries. These measures can be particularly helpful for marketers since they are based on visual, not verbal, elements of the promotion.

Considering these measures along with conducting extensive market research is essential to determining the success of promotional tactics in any country or region. Once brands discover what works (and what does not) in their promotional mix, those ideas can be imported by any other market. Likewise, companies can use this intelligence to modify various elements in their promotional mix that are receiving minimal or unfavourable response from global audiences.

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10.5 KEY TERMS

Key Terms

Advertising: Any paid form of presenting ideas, goods, or services by an identified sponsor. Historically, advertising messages have been tailored to a group and employ mass media such as radio, television, newspaper, and magazines. 10.1

Business Norms: The norms of conducting business also vary from one country to the next. For example, in France, wholesalers do not like to promote products. They are mainly interested in supplying retailers with the products they need. 10.3

Colours: Colours also have different meanings in different cultures. For example, in Egypt, the country's national colour of green is considered unacceptable for packaging because religious leaders once wore it. In Japan, black and white are colours of mourning and should not be used on a product's package. Similarly, purple is unacceptable in Hispanic nations because it is associated with death. 10.3

Digital Marketing: Digital marketing covers a lot of ground, from Web sites to search-engine, content, and social media marketing. Digital marketing tools and techniques evolve rapidly with technological advances, but this umbrella term covers all of the ways in which digital technologies are used to market and sell organizations, products, services, ideas, and experiences. 10.1

Direct Marketing: This method aims to sell products or services directly to consumers rather than going through retailers. Catalogues, telemarketing, mailed brochures, or promotional materials and television home shopping channels are all common traditional direct marketing tools. 10.1

Guerrilla Marketing: This newer category of marketing communication involves unconventional, innovative, and usually low-cost marketing tactics to engage consumers in the marketing activity, generate attention and achieve maximum exposure for an organization, its products, and/or services. Generally guerrilla marketing is experiential. 10.1

Integrated Marketing Communication (IMC): In a nutshell, IMC involves bringing together a variety of different communication tools to deliver a common message and make a desired impact on customers' perceptions and behaviour. 10.1

Language: The importance of language differences is extremely crucial in global marketing, as there are almost 3,000 languages in the world. Language differences have caused many problems for marketers in designing advertising campaigns and product labels. Language becomes even more significant if a country's population speaks several languages. 10.3

Marketing Communication: Includes all the messages, media, and activities used by an organization to communicate with the market and help persuade target audiences to accept its messages and take action accordingly. 10.1

Personal Selling: Personal selling uses people to develop relationships with target audiences for the purpose of selling products and services. Personal selling puts an emphasis on face-to-face interaction, understanding the customer's needs, and demonstrating how the product or service provides value. 10.1

Promotion Mix: Refers to how marketers combine a range of marketing communication methods to execute their marketing activities. 10.1

Public Relations (PR): The purpose of public relations is to create goodwill between an organization (or the things it promotes) and the "public" or target segments it is trying to reach. 10.1

Religious Beliefs: A person's religious beliefs can affect shopping patterns and products purchased in addition to his or her values. In the United States and other Christian nations, Christmas time tends to be a major sales period. In other religions, significant religious holidays may or may not serve as popular times for purchasing products. 10.3

Sales Promotion: Sales promotions are marketing activities that aim to temporarily boost sales of a product or service by adding to the basic value offered, such as "buy one get one free" offers to consumers or "buy twelve cases and get a 10 percent discount" to wholesalers, retailers, or distributors. 10.1

Values: An individual's values arise from his or her moral or religious beliefs and are learned through experiences. For example, Americans place a very high value on material well-being and are much more likely to purchase status symbols than people in India. In India, the Hindu religion forbids the consumption of beef. 10.3

CHAPTER 11: THE GLOBAL MARKETING PLAN

Chapter Outline

11.0 INTRODUCTION

Learning Objectives

After reading this section, students should be able to:

1. Explain how the marketing plan is used to track progress, evaluate impact, and adjust course where needed.
2. Explain why and how to update the marketing plan.
3. Outline the decision sequence in international marketing.
4. Explain how the marketing mix elements are integrated in the international marketing plan.
5. Explain how the basic principles of marketing apply to global marketing.

11.1 THE MARKETING PLAN


THE MARKETING PLANNING PROCESS
CORPORATE MISSION
SITUATIONAL ANALYSIS
INTERNAL FACTORS
Strengths & Weaknesses
EXTERNAL FACTORS
Opportunities & Threats
CORPORATE STRATEGY
Objectives & Tactics
MARKETING STRATEGY
Objectives & Tactics
PRODUCT
PRICE
TARGET MARKET
PROMOTION
PLACE
IMPLEMENTATION & EVALUATION

Fig 11.1 The Marketing Planning Process

The **marketing plan** captures the outputs from the marketing planning process in one cohesive document. If the plan is done well, it puts a plan in place that aligns the marketing strategy, objectives, and tactics with the corporate mission. It also supports the corporate objectives and strategy, which creates alignment with other functions across the company.

While this alignment is assumed, the presentation and formalization of the marketing plan often surfaces misalignment. Perhaps the finance team had assumed that the promotion strategy was not central to the plan and had reduced the budget. Perhaps the supply chain team had not recognized how aggressive the new product plans were and is not staffed to support them. While it it frustrating to identify points of confusion and misalignment, it is always best to do that in the planning process before it has impact on customers and on the market.

The marketing plan acts as a mechanism to communicate with other functions and to check for alignment.

Clarifying the Action Plan

There are many reasons why organizations fail to execute effectively, but many can be traced back to communication. When a large marketing organization begins to execute a plan, it's important that everyone understands what the goals are, but it's equally important to know which analysis supports (or possibly undermines) the plan. If a marketer is not fully aware of competitive threats that have been identified, then he may unknowingly make trade-offs that fail to address the competitive risk. If a product marketer is deeply focus on defining a new product and bringing it to market, she might not be aware of significant dependencies on the supply chain and distribution channels.

Similarly, in small organizations, there is a tendency to jump over the analysis and simply do what needs to be done. The marketing plan requires a greater level of rigour and serves to communicate that rigour to the rest of the team. The marketing plan is also a requirement of most funders (banks and investors alike), because it forces a degree of discipline on small businesses, which they may not already have.

The marketing plan is an important tool to communicate detailed plans within the marketing function.

Informing Adjustments and New Strategies

As soon as the first activity identified in the plan is executed, the marketing plan begins to be outdated. The more successful the plan is, the more quickly it will require a significant revision. If you are able to identify and implement a strategy that results in tremendous success, that will change the competitive dynamics and cause other companies to adjust their strategy and tactics.

Moreover, each action will generate new market data about what works and what doesn't work. This creates opportunities for new analysis and better strategies.

Sometimes an organization can get away with small quarterly updates to the marketing plan and major annual revisions. Other times, the market has shifted enough by the end of one quarter that a completely new approach is warranted—or a more aggressive implementation of the current approach. Either way, a regular update to the marketing plan allows for new analysis informed by new market experience, opportunities to realign plans with other functions, and the chance to inform others within the marketing function so that the team can learn and evolve together.

11.2 WRITING THE GLOBAL MARKETING PLAN

It should be apparent by now that companies and organizations planning to compete effectively in world markets need a clear and well-focused international marketing plan that is based on a thorough understanding of the markets in which the company is introducing its products. The challenge, then, of international marketing is to ensure that any international strategy has the discipline of thorough research, and an understanding and accurate evaluation of what is required to achieve the competitive advantage. As such, the decision sequence in international marketing is much larger than that of domestic markets.

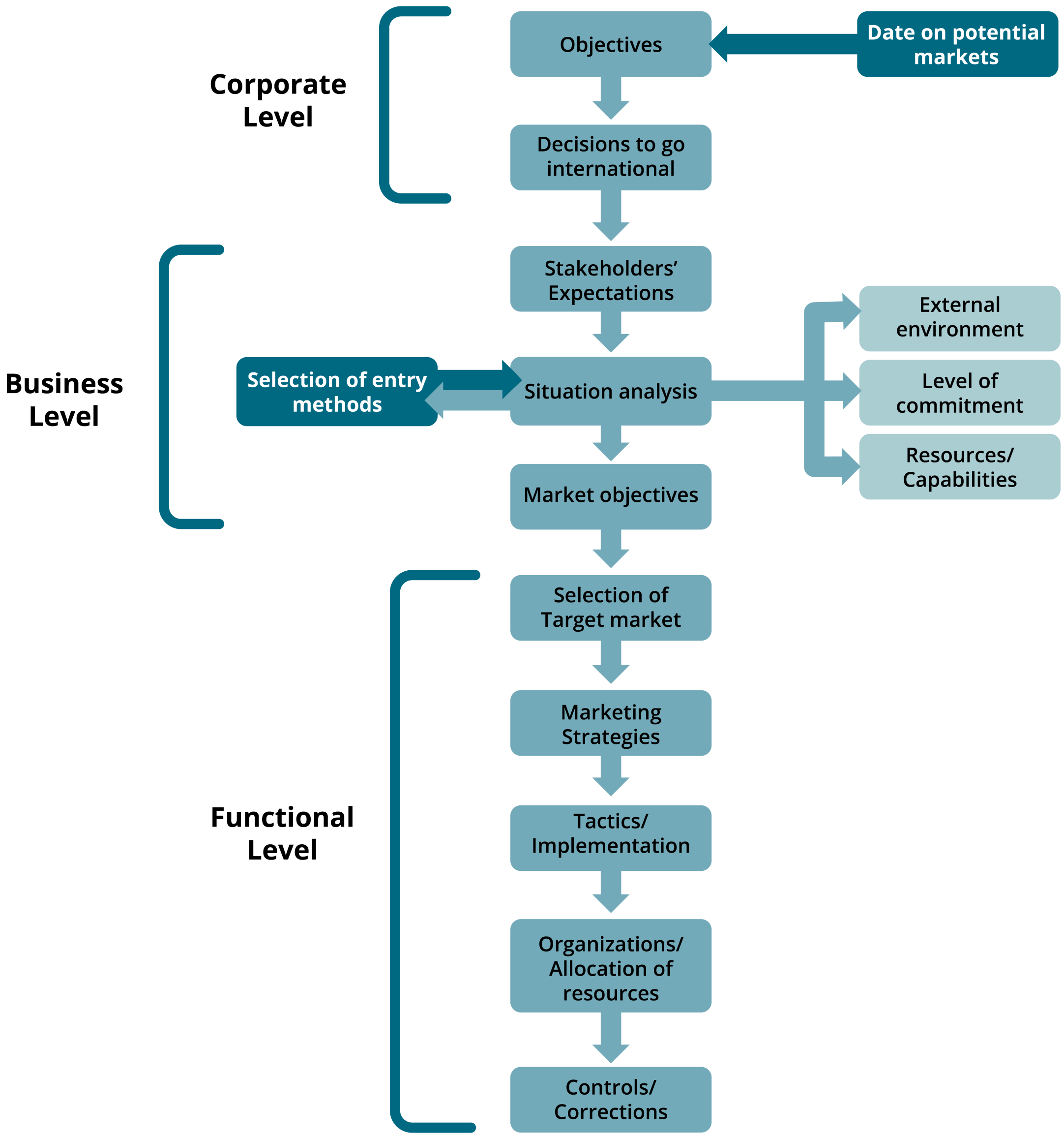

Fig 11.2 "The decision sequence in international marketing", adapted by Alissa Giles (colour change), CC BY-NC-SA 4.0

The Corporate Level

We begin at the corporate level, where firms decide whether to become involved in international markets and determine the resources they are willing to commit. Thus, this stage is primarily concerned with the analysis of international markets. Decisions here will be dependent on matching the results of that analysis with the company's objectives. These objectives, in turn, will be determined by the many motivating factors we have discussed in the earlier sections. The level of resources that the company is willing to commit should be determined by the strategy that is needed to achieve the objectives that have been set.

The Business Level

Business-level considerations begin with the assessment of the stakeholders involved in the business. It is important to clearly identify the different stakeholder groups, understand their expectations, and evaluate their power, because the stakeholders provide the broad guidelines within which the firm operates. In the case of international marketing, it is particularly important to address the concerns of the stakeholders in the host company.

The situation analysis concerns a thorough examination of the factors that influence the businesses' ability to successfully market a product or service. The results lead to a realistic set of objectives. Conducting a situation analysis in an international setting is a bit more extensive. It not only includes the normal assessment of *external environmental* factors and *resources /capabilities*, it also includes a determination of the *level of commitment* exhibited by the business, as well as possible methods of entry. These last two factors are interrelated in that a company's level of commitment to international markets will directly influence whether they employ exporting, a joint venture, or some other method of entry.

In turn, level of commitment and method of entry are influenced by the evaluation of environmental factors as well as resources and capabilities. The latter audits not only the weaknesses of the company, but also the strengths of the company, which are often taken for granted. This is particularly important in international markets; for example, customer brand loyalty may be much stronger in certain markets than others, and products may be at the end of their life in the domestic market but may be ideal for less sophisticated markets. It is important, too, to evaluate the capacity of the firm to be flexible, adaptable, and proactive, as these are the attributes necessary, for success in a highly competitive and rapidly changing world.

Undoubtedly, environmental factors have received the most attention from marketers considering international markets.

The Functional Level

Having set the objectives for the company, both at the corporate level and the business level, the company can now develop a detailed program of functional activities to achieve the objectives. Following the integrated approach employed throughout this text, each of the functional elements (e.g. finance, human resources, research) must be considered jointly. The best international marketing strategy is doomed to failure if human resources can not find and train the appropriate employees, or research cannot modify the product so that it is acceptable to consumers in another country. Ultimately, this coordination between business functions is contingent on the market entry strategy employed as well as the degree of standardization or customization deemed.

Having integrated at the function level, we next consider integration of the marketing mix elements.

11.3 THE MARKETING MIX IN GLOBAL MARKETING

The same marketing principles that lead to marketing success in domestic marketing can also apply to global marketing. With the rapidly growing force of globalization, the distinction between marketing within an organization's home country and marketing within external markets is disappearing very quickly. With this in mind, organizations are modifying their marketing strategies to meet the challenges of the global marketplace while trying to sustain their competitiveness within home markets. These changes have also prompted brands to customize their global marketing mix for different markets, based on local languages, needs, wants, and values.

The **four Ps of marketing**—product, price, placement, and promotion—are all affected as a company moves through the different phases to become and maintain dominance as a global company.

Global Marketing Mix: Product Plus Promotion

For multinational corporations (MNCs), the interplay between product and promotion is important because it can enable a company to make minor adjustments to a single product and its promotion strategy rather than totally revamping the product and promotion for different markets. Coca-Cola is a strong example of this principle. The beverage brand uses two formulas (one with sugar and one with corn syrup) for all markets. The product packaging in every country incorporates Coca-Cola's contour bottle design and signature ribbon in some shape or form. However, the bottle can also include the country's native language and appear in identical sizes as other beverage bottles or cans in that country's market.

Before launching promotional programs, global companies must first define their target markets and determine the products that will resonate most with those consumers and businesses. This research can help inform marketing leaders about what course to take—localization versus standardization strategy—as they learn more about the target market's receptivity to their goods and services. In addition to pinpointing which price point and distribution channels would best serve a country's markets, global marketers must decide whether and how to customize their products. Product introductions are also important. Promotional tactics for global audiences can range from television commercials to social-media marketing on Facebook or

YouTube. It is the job of global marketers to create and place promotional efforts in settings where local consumers will be most receptive to receiving and acting on those messages. Consumers in each target market have different media habits and preferences, and understanding these behaviours is important for selecting the right promotional mix.

After product research, development, and creation, promotion is generally the largest line item in a global company's marketing budget. Using integrated marketing communications can significantly increase efficiency and reduce promotional costs, as messages across multiple channels reinforce and amplify one another. For organizations that pursue a standardized approach to promoting products and building brands, promotion is the crucial component of the mix that enables a global company to send the same message worldwide using relevant, engaging, and cost-effective techniques.

While a standardized global promotion strategy enables global brands to engage in uniform marketing practices and promote a consistent brand and image, marketers must also be prepared for the challenge of responding to differences in consumer response to marketing mix elements. Marketers must also fend off the full spectrum of local and global competitors, using promotional strategies, branding, and product development to full competitive effect.

Global Marketing Mix: Promotion

Before a company decides to become global, it must consider social, cultural, economic, political, competitive, and other factors relative to the global expansion it is considering. Creating a worldwide marketing plan is no simple task. It is virtually impossible for a company to communicate one identical message in a unified voice to global markets unless a company holds the same position against its competition in all markets (e.g., market leader, low cost, etc.). This is rarely the case, so most global companies must be open to some level of localization and be nimble enough to adapt to changing local market trends, tastes, and needs.

Global marketers must balance four potentially competing business objectives when developing worldwide advertising:

1. building a brand while speaking with one voice
2. developing economies of scale in the creative process
3. maximizing local effectiveness of advertisements
4. increasing the company's speed of implementation

Global marketers can use several approaches when executing global promotional programs: exporting executions, producing local executions, and importing ideas that travel.

To successfully implement these approaches, marketers must ensure that their promotional campaigns take into account how consumer behaviour is shaped by internal conditions (e.g., demographics, knowledge, attitude, beliefs) and external influences (e.g., culture, ethnicity, family, lifestyle) in local markets. Areas for attention include:

Language: Language differences are crucial in global marketing. There are nearly 3,000 languages in the world. Language differences have caused many problems for marketers in designing advertising campaigns and product labels. There are numerous examples of brand names that work well in some languages but have offensive or unfortunate meanings in other languages. Even countries that use the same language have words with different meanings. Consider the British terms "flat" (*apartment* in U.S. English), "pants" (*underwear* in U.S. English), and "lift" (*elevator* in U.S. English). Marketing messaging and materials could easily go wrong if they are not adjusted to fit in-country dialect and usage. Language becomes even more significant if a country's population speaks several languages. An additional language consideration for marketers is literacy rates. Depending on the target audience and market, literacy may be a significant issue.

Colours: Colours may have different meanings in different cultures. This highlights the importance of careful testing of packaging and other visual elements intended for global audiences. For example, green is a sacred colour in the Muslim faith, and it is not considered appropriate for packaging and branding purposes in Middle Eastern countries. In Japan, black and white are colours of mourning and should be avoided on product packaging. Purple is associated with death in some Hispanic nations.

Values: An individual's values arise from his or her education, moral or religious beliefs and are learned through experiences. For example, as a consumer market, Americans place a very high value on material well-being and are much more likely to purchase status symbols than people in India. Chinese consumers highly value the sense of honour, dignity, and pride, and in some situations they will pay price premiums to "save face" by spending what is perceived to be an appropriate amount to preserve their honour. In Canada, our values, based on the UWaterloo's Well-Being Index include: fairness, inclusion, safety, sustainability, and diversity.

Business norms: The norms of conducting business also vary from one country to the next. In France, for example, wholesalers do not like to promote products. They are mainly interested in supplying retailers with the products they need.

Religious beliefs and holidays: In addition to affecting their values, a person's religious beliefs can affect shopping patterns and products purchased. In the United States and other Christian nations, the Christmas holiday season is a major sales period. In China, the Chinese New Year brings out the shoppers. In India, a string of Hindu festivals including Dussehra and Diwali mark a holiday season that extends over multiple months.

Many other factors, including a country's political or legal environment, economic status, and technological environment, can impact a brand's promotional mix. Companies should monitor dynamics in their target markets and be ready to quickly respond and adapt to consumer needs and preferences.

Recommendations for Adjusting the Promotional Mix

When launching global advertising, public relations, or sales campaigns, global companies test promotional ideas using marketing research systems that provide results comparable across countries. These systems help marketers achieve economies of scale in marketing communications, since they reveal which messaging or creative elements contribute to a product's market success. Marketing-research measures of nonverbal factors such as flow of attention, flow of emotion, and branding moments can provide insight into what is working in an advertisement or other marketing communication piece across multiple countries and languages.

The same recommendations about how to research and understand a target market in domestic settings apply to global settings. Marketing research is essential for marketers to build their understanding of which promotional tactics will be successful in any country or region. Informed experimentation and trial and error are also good teachers. Once marketers and brand managers discover what works (and what doesn't) in the promotional mix, they can import this knowledge to infuse creative ideas into other markets. Likewise, companies can use this intelligence to modify various elements in their promotional mix that are receiving minimal or unfavourable response from global audiences.

Global Marketing Mix: Price

Pricing is the process of determining what a company will receive in exchange for its products. Many pricing considerations in global marketing are similar to domestic marketing. As marketers develop pricing strategy, they should keep the following goals in mind:

- Achieving the financial goals of the company and generating profits
- Matching the realities of the marketplace and consumer buying trends
- Supporting the designated positioning for a product, making it consistent with other elements of the marketing mix, product, promotion and placement

Walmart: Placement, product, and promotion work in concert with pricing in the global marketing mix. Photo by Daniel Case, CC BY-SA 3.0

Similar to domestic marketing, in the global marketing mix, factors that affect pricing include manufacturing cost, distribution channels, marketplace, competition, market conditions, and quality of product. For instance, if distribution is exclusive to one channel partner, then prices are likely to be higher. High prices are required to cover high costs of manufacturing, shipping, extensive advertising, and promotional campaigns. If manufacturing costs go up due to the rise in price of some raw material, then prices will need to rise as well.

Global Pricing Considerations

Pricing considerations become more complicated in the global context when it comes to factors affecting global trade. Multinational companies must operate with different currencies, exchange rates, and interest rates. Pricing needs to account for risk associated with fluctuations in the relative value of different currencies in the markets where businesses operate. When the dollar is strong against a foreign currency, for example, imported American goods are more expensive relative to the local competition, so local sales may decrease. When a weak dollar makes product imports more expensive, the final good must carry a higher price tag to cover production costs.

Pricing can be affected by the cost of production (locally or internationally), natural resources (product ingredients or components), and the cost of delivery (e.g., the availability of fuel). For instance, if a country imposes a minimum wage law that forces the company to pay more to its workers, the price of the product is likely to rise to cover some of that cost. Natural resources, such as oil, may also fluctuate in price, changing the price of the final good. Pricing may be affected by government policy, such as trade tariffs and taxes, or costs associated with regulatory compliance and adherence to administrative or legal criteria of specific jurisdictions.

Global marketers must be also prepared to deal with other localized factors affecting pricing. Cultural expectations may dictate what consumers are willing to pay for some products and brands. A product's positioning in relation to the local competition influences the brand's ultimate profit margin. Global marketers must carefully consider how to position their products in global markets and decide whether their products are considered high-end, economical, or something in between according to cultural norms.

Global Marketing Mix: Place (Distribution)

Although other elements of the marketing mix are often more visible during the marketing process, place, or distribution, is essential in getting the product distributed to customers. Placement determines the channels used to distribute a product across different countries, taking in factors such as competition and they way similar brands are being offered to the target market. Regardless of its size or visibility, a global brand must adjust its country strategies to take into account placement and distribution in the marketing mix.

Global marketing presents more challenges around distribution, compared to domestic or local marketing. Consequently, brands competing in the global marketplace often conduct extensive research to accurately define the market, as well as the environments where consumers will find, buy, and use the product. A country's transportation and economic infrastructure, customs, marketplace conditions, and the competitive landscape can all factor into strategic decisions around distribution. For example, not all cultures use or have access to vending machines to distribute beverages. In the Canada, beverages are sold by the pallet via warehouse stores. But warehouse stores do not exist in all markets.

Placement decisions must also consider the product's positioning in the marketplace. A global luxury brand would not want to be distributed via a discount chain in Canada. Buying a Gucci scarf at the Dollar Store is unlikely. Conversely, low-end shoemakers would likely be ignored by shoppers browsing in an Italian boutique store. Global marketers must also consider how their products will be distributed across the different shopping venues unique to a particular country or market. Customizing these placement strategies for national and local markets while retaining a strong and consistent brand image can help companies gain significant competitive advantages.

Video: "Kleenex Video Case Study"[10:58] by Ruben Osorio is licensed under the Standard YouTube License. Captions and transcripts are available on YouTube.

Introduction to Marketing II (MKTG 2005) Marketing Principles in Global Environments by NSCC and

11.4 LULULEMON MARKETING STRATEGY AND PLAN

Having taken an entire course and developed your own global marketing plan, you're well on your way to being an expert student of marketing. While the experience of developing and presenting a marketing plan for a class may seem far removed from the "real thing," rest assured that the key elements, structure, and basic layout of your plan aren't contrived at all. Below is an example of a real marketing plan so you can see what one looks like for Lululemon.

Introduction and Executive Summary

This report proposes a marketing strategy and plan for Lululemon Athletica, focusing on their Wunder Under product line. In summary, this report concludes that Lululemon should undertake several initiatives to strengthen its position in the market. This report includes a situation analysis, a look at Lululemon's strategy, tactics, implementation, and financials.

Photo by Raysonho, CC0 1.0

Lululemon Overview, Vision, Mission, and Plan Scope

Lululemon sells yoga and exercise apparel and they have found success in marketing a lifestyle rather than a product. Lululemon's mission statement is "to elevate the world from mediocrity to greatness." The mission statement comprises of these components: improving lives, improving health, and exceeding expectations. Lululemon is passionate when it comes to initiating long-lasting changes in everyone that uses their products. Lululemon's vision statement is "to be the experimental brand that ignites a community of people living the sweat life through sweat, grow and connect." The statement consists of the following components: exceptional brand, ignite communities through sweat, and create connections. Lululemon prioritizes quality over quantity to provide value to their customers (Mission Statement Academy, 2019).

The scope of this plan includes a look at Wunder Under, a legging product line. Wunder Unders are leggings that are meant to make you feel empowered while having a snug waistline, lots of support and they offer them in many lengths (Lululemon Athletica, 2020). They sell their products in 440 company- owned stores in 15 countries. They also sell online and via mobile apps where they offer many products and services (Dun & Bradstreet, 2019). Most of their stores operate in North America. Lululemon is focused on international expansion, especially in the Asia-Pacific region. They are hoping to introduce Wunder Unders into the Chinese Market.

Lululemon Goals, Strategies and Budget

Lululemon has many goals they hope to achieve. These include:

- Identify retail locations to open new stores and attract new customers.
- Provide customers with new products.
- Sustain their brand image.
- Achieve growth and maintain cash flow.
- Increase sales of current stores.
- Operate efficiently in all departments.
- Keep their dedicated and experienced staff (Ghani, 2015)

Lululemon's strategy allows them to become one of the major players in athletic apparel. To achieve its goals, Lululemon uses three main strategies.

1. Innovation forever- they have a very active Research and Development department and are always looking to get new and improved products to their customers.
2. Interactive digital marketing- they portray their brand as essential for athletic teams, fitness facilities and yoga studios.
3. Expanding the market by launching new product lines in different regions – while Lululemon has been very successful in North America, they hope to expand their marketing to China (Business Strategy Hub, 2019).

Lululemon had a total revenue of $3.29 billion in 2018. Of that, 65% of it came from their own stores. Lululemon's sales have jumped with the rising popularity of yoga and their improved brand awareness. They have almost doubled from $1.8 billion in 2014 to $3.3 billion in 2018 and net income has had a similar outcome (Dun & Bradstreet, 2019).

Strategic Analysis

The following selection describes the market, the competition, a SWOT analysis of Lululemon, Lululemon's' customers, as well as its products and services.

Lululemon Market Analysis

Lululemon's leggings operate in the technical athletic wear market made up of women ages 20-40 across the world. Currently, 70% of Lululemon's sales revenue comes from the USA, 15% comes from Canada and Australia, and the rest are dispersed between European and Asia-Pacific countries(Dun & Bradstreet, 2019). Out of its 440 stores worldwide, 235 locations are in the USA alone, 64 in Canada and only 22 stores operate in China (Dun & Bradstreet, 2019). The rest are in Europe and other Asian-Pacific counties. We estimate the total addressable market to be worth **$197.35 billion** in revenue worldwide. We further estimate the market penetration to be **59.8%**. We further estimate that Lululemon's market share is **2.7%.**

We further defined the market for the following categories

1. *Qualified customers not buying anything.* China is an untapped market for Lululemon, and it currently makes up less than a percent of their total revenue. This number reflects the potential revenue in this market based on the average amount spent / year by Lululemon consumers **($200)** multiplied by 25% of the Chinese population **(348 250 000)** which is **$69.65 billion** in sales revenue.
2. Lululemon's current customer base **$3.2 billion** in sale revenue.
3. Customers buying from Lululemon and all competitors **$118 billion** in sales revenue.
4. Customers buying exclusively from direct competitors Adidas, NIKE and Under Armour **$6.5 billion** in sales revenue.

Lululemon Competitive Analysis

Lululemon's healthy lifestyle inspired athletic apparel and accessories are marketed under the Lululemon brand. They offer a comprehensive line of apparel and accessories for women and men. Their apparel assortment includes items such as pants, shorts, tops, and leggings designed for a healthy lifestyle including activities such as yoga, running, training, and other sweaty pursuits. They also offer fitness- related accessories. Through their vertical retail strategy and direct connection with guests, we can collect feedback and incorporate unique performance and fashion needs into the design process. This way, they can solve problems for their guests. Advance product lines differentiate them from the competition. Lululemon benefits from the growing number of people that participate in yoga, they believe the percentage of their products sold for other activities will continue to increase as they broaden product range (Farooq, 2018).

Lululemon SWOT analysis

We have undertaken a SWOT analysis for Lululemon in the context of our scope and discovered the following:

Strengths

Product Quality

Lululemon focuses on producing the highest quality of all the products in the market. They have designed their products to last for years. Lululemon has patented 45 materials and has trademarked their products and fabric names to protect them from being copied from competitors (Quiroz, 2018).

Price Point

Lululemon focuses on ensuring that they have made a superior quality product (CPG, FMCG & Retail, 2019). This means that Lululemon has higher pricing points than their competitors. Although in some countries this fact may seem like a weakness, when relating it to the Chinese market it is a strength. In China, people are willing to pay more for "luxury products" with "superior quality" so Lululemon's price point is a great fit.

Weaknesses

Brand Presence

In North America, Lululemon has a strong presence and relies a lot on customer loyalty, word of mouth, and their trained sales associates to sell their products. However, in China Lululemon doesn't have a strong brand presence, and cannot rely on it for marketing. Instead, Lululemon needs to adapt and become more focused on digital and mobile marketing to tailor itself towards Chinese consumers.

Lack of Customer Base

Lululemon has not expanded into China enough to engage with the customers the way they do in the US. This results in a lack of customer base and customer loyalty.

Opportunities

Global Expansion

Lululemon currently has many retail stores, only a few of them operate outside of North America though. This leaves Lululemon with a lot of room to expand and grow in markets like Europe, and Asia. Although Lululemon has an e-commerce site and an ability to sell their products to those countries already, Lululemon sees more revenue when there is a store in place. This means that expanding the number of retail stores in foreign markets could increase their opportunities for sales.

E-Commerce Expansion

Lululemon currently runs an e-commerce website where you can buy many of their products online, however, most of Lululemon's revenues come from their retail locations. Lululemon could invest in more services for their website to grow online sales in China and give their guests an omnichannel experience by creating content on platforms exclusive to China.

Growing Industry

Mintel, an international marketing agency has estimated that the value of the sportswear industry in China will reach up to 2200 billion before 2020. The quality of life in China is also advancing, and they are continuing to see a growth in health and fitness consumers. This makes it a very good time for Lululemon to continue expanding into the Chinese market (Who Knows China, 2020).

Threats

Competition

When it comes to Lululemon's Wunder Under leggings there is a lot of competition in the market. For example, Nike has a line of leggings called the "one tight" these leggings closely resemble that of Lululemon. Under Armour, Gymshark and Adidas are also some brands that have made similar leggings to Lululemon. Although their competitors leggings are high-priced, Lululemon has the highest price out of all of them (Lululemon Athletica, 2020).

Counterfeit Product

With Lululemon's high price-point and overall brand image, many people have started to try to create "dupe leggings" and sell them at much lower prices than Lululemon does. For example, brands like Queenieke, and

Occffy, sell their leggings directly through Amazon for $29.99, and claim they are exactly like Lululemon's leggings (Amazon, n.d.).

Lululemon Target Customer Description

Lululemon's primary and largest customer group is made up of women. This is the typical ideal customer of North America is a 32-year-old professional single woman named Ocean, who makes $100,000 a year. Ocean is also engaged, has her condo, is travelling, fashionable, has an hour and a half to work out a day. The woman is so aspirational because "If you're 20 years old or you're graduating from university, you can't wait to be that woman," Wilson said. "If you're 42 years old with a couple of children, you wish you had that time back (Lutz, 2015).

Lululemon Typical Customer

Based on the cultural values in China, we have created a persona for the typical customer for the Wunder Unders.

> *Breeze is a professional in her twenties, and she is successful in her career. In her downtime, she focuses on her health and fitness. She has some extra money to spend and looks for quality products and a recognizable brand to sweat in during her favourite yoga practices.*

Lululemon Customer Buying Process

The typical Chinese consumer behaves very differently in their buying process than the North American consumer. The typical consumer starts their product search online and takes their time to research to ensure products meet their needs (Digital Crew Insights and Analysis, 2019). These are the steps taken to make a purchase:

1. **Product Search**
   Consumers search on popular Chinese platforms such as Tmall and Baidu. Tmall is a platform for local Chinese and international businesses to sell brand name goods to consumers in mainland China, Hong Kong, Macau and Taiwan. It is the world's second-largest e-commerce website and it has over 500 million monthly active users (Digital Marketing to China, 2019). This website is a great platform for Lululemon to communicate the features and benefits of their product, showcase product video content, and list where the products can be found. Baidu is a search engine similar to google. It provides many of the same services as google such as mapping, AI and digital advertising. Chinese consumers will also visit

the brands' official website for additional information. The typical consumer is highly influenced by online and social media content, with 90% of consumers saying they have purchased a product based on their search (Digital Marketing to China, 2019). Currently, Lululemon has a small presence on the TMall channel and has room to grow.

2. **Product Testing**
   Although the typical consumer does their research online, they will go to showrooms and brick and mortar stores to test the product. Lululemon has 38 stores operating in China for consumers to test product quality.
3. **Product Comparison**
   Consumers are likely to shop in showrooms and online looking for the best deal, before committing to a product (Digital Crew Insights and Analysis, 2019). Lululemon is exclusive to its stores and has trademarked all of its material and patterns. This makes it difficult to find a comparable product quality for a lower price.
4. **Product Purchase**
   Based on the consumers' experience in the product testing they will buy the product in-store or on their mobile phone.
5. **Post Purchase Behaviour**
   If the consumer is fully content with a product, they will keep the product, and perhaps re-buy in a different style or pattern if they believe in the quality and brand after use. They will also be inclined to engage in online activities with the brand (Digital Crew Insights and Analysis, 2019). It is also important to note that there is a high rate of product return with online shopping. For those consumers who can't make it to a showroom, the behaviour tends to be a bulk purchase to test products at home, and then return most of the product (Digital Crew Insights and Analysis, 2019).

Lululemon Product and Service Analysis

The following describes the products and service analysis of Lululemon's Wunder-Under leggings and services relative to the competition brands such as Nike One Tight. Lululemon is a brand that is proud to be environmentally friendly, its distribution centres have a recycling rate of 86% and their recycling and compost program has a 70% recycling rate. When buying Lululemon 'Wunder-Under" leggings from a store you'll be given them in 25% recycled reusable bag, which is 100% disposable. 'Wunder-Under Leggings' are made of 86% nylon and 14% Lycra. These leggings were created because Chip and Shannon Wilson noticed how poorly cotton-based clothing worked while working out and doing yoga. These leggings are machine washable and the only thing Lululemon advises consumers of is to wash them in cold water to keep the colour and shape longer. Consumers love them, the only thing they don't love is how thin the material is, but that is one of the reasons they are best for yoga and working out. Lululemon also offers free tailoring or replacement of items when the seams come loose or undone (Kalpazanova, 2016).

Nike One Tights are designed for all-day wear, they are made of 83% polyester and 17% elastane with a mid-rise waistband to feel snug and secure. It's made from 50% recycled polyester fabric, which comes from plastic bottles that Nike diverted from landfills since 2010. Nike uses a Dri-fit technology to help keep the consumer dry and comfortable during their workout or everyday activities. They have a pocket located on the back of the waistband big enough to hold a phone and a small pocket in the front of the waistband to hold cash or keys (Nike, n.d.).

Nike is one of the most well-known and trusted brands around the world whereas Lululemon is still trying to create that fan base. Nike's consumers have a wide range of options to choose from, women's and men's loungewear, workout wear, shoes and so on whereas Lululemon is still only truly tailored to men's and women's workout and yoga gear.

Feature A

Where we perform the weakest relative to our competition is in the following product and services features and benefits:

Style	• Doesn't offer many colours • Smaller logos
All-Purpose	• Doesn't offer leggings designed to all activities

Feature B

Modifications to these product features will form the basis of our marketing strategy. Lululemon could add the following product features to improve their product and stand stronger against the competition:

Style	• Add a wider range of colours, focusing on bright, eye-catching colours • Add larger logos
All-Purpose	• Create leggings that can be everyday wear while also be tailored to all sports. With making these modifications Lululemon will grow to be a more successful company in the Chinese market.

Lululemon Product Service Analysis

Feature	Benefit	How Lululemon's Product Performs	How Competitor's Product Performs
Flexibility	Be able to work out in certain positions without any problems	Extremely well	Good
Durability	The longevity of the product before it needs to be replaced	Good — Lululemon offers a replacement service	Average
Style	Variety of colours, patterns and logos to fit personal styles	Average	Great – Large variety of logos, colours, and patterns offered
Price	Is it expensive/inexpensive	Higher end brand, higher cost	higher end brand but not as expensive as Lululemon
Fit	Feeling comfortable in leggings that fit all body types	Wonderful – sized to fit all body and focused on length	Good – multiple options

Lululemon Marketing Strategy

Based on our analysis to date, we propose that a great opportunity for Lululemon to increase sales in China is to target women in their 20s who are becoming more health-conscious and fit. These women would be part of the upper class with a higher household income, valuing quality and fashion. Lululemon can achieve this opportunity by adapting its product to the market, expanding its retail stores and growing its e-commerce platforms through engaging and information digital and mobile marketing strategies.

We have created the following value proposition based on our strategy:

> Lululemon provides quality, performance leggings to successful, health-conscious women by offering personalized brand engagement and an omni channel retail experience to showcase the technical performance of the Wunder Under legging.

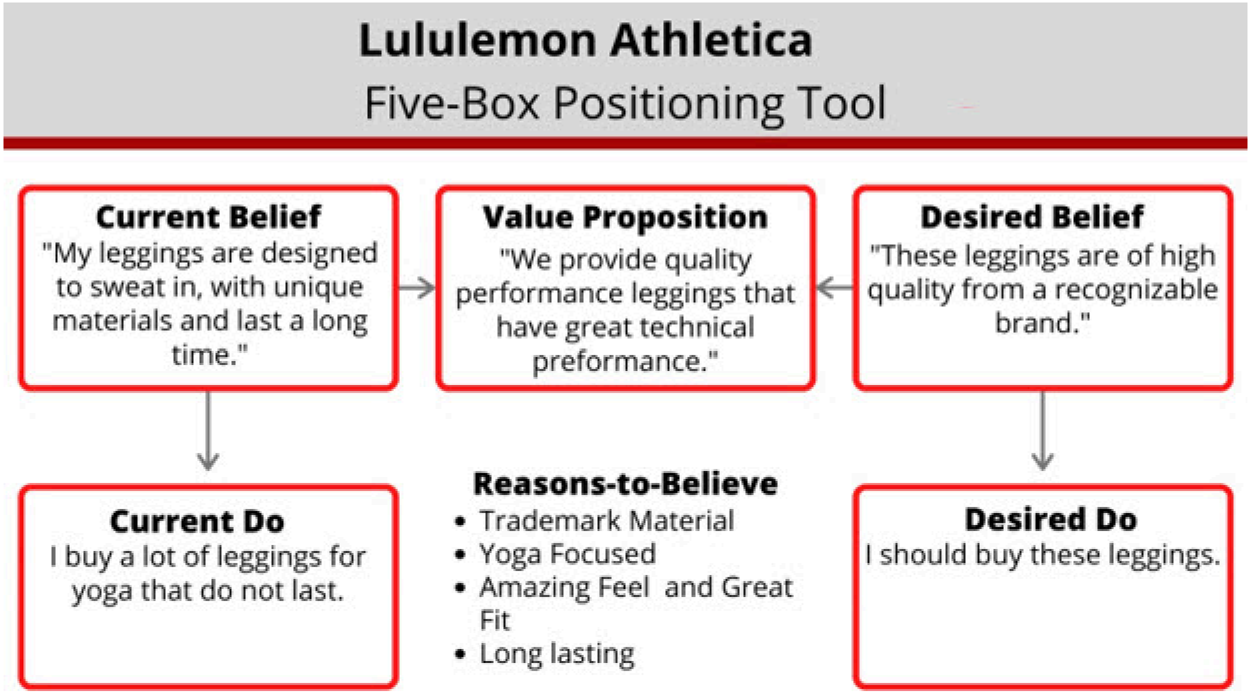

Fig 11.3 Lululemon Athletica Five Box Positioning Tool

Tactical Analysis

This section proposes more specific recommendations for Wunder Under marketing programs, pricing approach, promotion and channel design. Lululemon Product and Service. The following are the changes and improvements in Lululemon products and services proposed to address gaps and opportunities relative to their competition. Currently Lululemon tends to be neutral in their colour choices and they are tailored towards yoga. Lululemon currently offers complimentary hemming on tops and pants in store, returns done in person or by mail and within 30 days of the purchase date, and a contact section on their website with a list of accounts to reach out to through WeChat and Weibo (Lululemon Athletica, 2020).

New Colours and Loud Prints

To make Lululemon leggings work in the Chinese market, they should make them less muted, using more bright, playful colours. Lululemon should go with colourful and all-purpose leggings. Lululemon should launch a new product line to include bright coloured leggings. Including highlighter type colours that are very eye-catching and that will stand out. There will be multiple colours to pick from including neon pink, yellow, blue and lime green.

Create a Line with a Bigger Logo

When researching culture in China, it is stated they big logos are a sign of status and luxury (Pan, 2018). Lululemon should think about having a bigger logo on their leggings so that their brand becomes more known. Lululemon should create a new product line with bigger logos on leggings. They will create a legging that grabs attention and makes a strong first impression. Logos are the foundation of brand identity and it will make Lululemon more memorable while separating them from their competition.

All-purpose Leggings

In China, it seems to be becoming more popular to wear sportswear as an extension of casualwear in fashion (Rapp, 2018). Lululemon should have more leggings tailored to more sports while also focusing on the casual side of their leggings. Lululemon should design leggings to give customers more choice and enhance their workouts with leggings made for specific activities but also focusing on their comfort, casualness and stretch. They will make sure the waistband is high enough for coverage but not so high that it makes it restricts movement during sports or casual activities.

Create Chinese Lululemon App and Social Media

Lululemon should make a Chinese version of the Lululemon App. They should use their website and WeChat to encourage customers to visit their brand-owned apps, where they can get information on products, events and exclusive content including coaching tips and personalized services for Chinese members. Going more digital is a strategy that will help Lululemon do better in Chinese market. Focusing on digital platforms, Lululemon would be able to create different communities and provide various online services and offline experiences.

Women's Only Stores

Another idea is to open a women's only store. In this store, they could put on events that are designed to inspire active women. Lululemon would be able to build a more cohesive female community in China (Allison, 2020). There are major gaps in Lululemon's offered products and services compared to their competition. Lululemon should expand their services online to grow their e-commerce sales in China. Features rated high by Chinese consumers are colourful, eye catchy designs and luxury brand items. Lululemon should work with their designers to incorporate those features in their clothing lines. Lululemon should give their customers a full experience by creating content on platforms exclusive to China (Boyd, 2020).

Lululemon's Wunder Under leggings pricing strategy is a customer-value based strategy to help grow the companies brand image and luxury status in the market. Lululemon sells all functional garments at a high consistent price point because of their quality and exclusivity. Chinese consumers have a perception that high-quality products are found at a higher price point. To attract more Chinese consumers to their product, Lululemon has inflated its already high price. The high price is further justified by the larger amount of shipping cost and tax to run a business in China. Lululemon is paying a higher rate of tax in China to participate in e-commerce operations. They are also taxes on importing raw materials thought out the world to create their luxurious fabric. These factors justify the high price point in the Chinese market (Thangavelu, 2018).

Lululemon uses a strict pricing strategy to create pricing awareness and maintain their luxury status using the following tactics. Regular price Wunder Unders, which consists of four core colours retail for ¥750, ¥850 and ¥980, which is slightly more inflated than the North American pricing. They are sold year-round at this price point (Tmall, 2020). Seasonal Wunder Under colours retail at regular price for 2 seasons and then enter a discounted rate of ¥ 450-¥ 650 or 20%-30% off. These discounts keep the market happy, knowing it is possible to get a deal, while the company still maintains high profit margins.

This pricing strategy is consistent across all Lululemon stores globally. Pricing is communicated consistently across online platforms and in retail stores. Customers are educated on the product quality first before the price is revealed (Policella, 2019).

Although Lululemon doesn't typically participate in large discount events, they have adapted to the Chinese culture by participating in International Singles day, a sale event that occurs every year, on November 11. During the sale, Lululemon has incorporated lottery pricing and dollars off purchases over certain purchase value. This is a valuable sale to participate in because it is the largest spending day in China, and it's a good opportunity to engage new customers who may be skeptical of the regular price point. The discount rate will not drop any further than the regular discount rate of 20%-30% off regular price items to maintain luxury status while still being perceived as a deal (Who Knows China, 2020).

The following is the proposed promotion plan for our target audience including the promotional tools to be used and the key messages to be delivered. We will be applying integrated marketing communication using a mix of digital and traditional channels to communicate with our customers. Our communication channel will focus on leveraging social media platforms to create an online brand community, customer engagement and product awareness online to ultimately drive traffic into our stores for customers to experience the product quality and the brand lifestyle.

Social Media & Direct Mobile Marketing

We will use social media channels such as WeChat and Weibo to create an online community for young yoga enthusiasts. We will also use these channels to advertise our events and generate brand excitement at a national and local level. WeChat and Weibo will also be used as a platform to connect with the brand with any customer service issues, which has already been established.

WeChat has 1 Billion active users as of 2019, and Weibo has 500 Million active users. 70%-85% of users on each of these platforms are in their twenties, and 49.8% of them are female (Verot, 2017). To further our reach with user-generated video content to showcase our product on real people we will create yoga challenges on short video platforms DouYin. We will also be creating short video ads to release through these platforms once a week. The purpose of these ads will be to promote new products like the Wunder Unders, issue yoga challenges, and advertise our local and large-scale events. Direct mobile marketing has been described an engaging and enjoyable by the Gen Z and Gen Y and they are likely to subscribe to push notifications to get the latest information on their favourite brands (Lee, 2017).

Community Events

In the last month of each quarter we will host major gatherings in each major city to give our brand community a chance to get together and socialize, and of course a large group yoga practice. These events will be covered through social media channels as well. Lululemon has hosted large scale events like this in the past such as The Forbidden City Yoga Session is 2017, and the “Unroll Your Mat!” in 2016 To launch the new line of yoga mats (Rapp, 2017) These types of events have been successful in starting the lifestyle community, and by hosting them more frequently we hope to continue building those relationships with customers by engaging them in our lifestyle experience surrounded by their community.

Sales Promotions

In China, November 11 is International Singles Day Shopping Festival. On this day we will hold a nation-wide event in-store, on our website and on Tmall to make the sale accessible. This is the largest spending day in China, bringing in nearly $38 billion in one day in 2019. This event, mostly celebrated by young people of major cities like Beijing, Shanghai and Guangzhou, is celebrated with a lot of festivities (Marketing to China, 2017). This will be the largest discount sale of the year for Lululemon in China. Previously, the discount has been determined by lottery 25%-30% off, with every customer receiving a deal no matter what.

Lululemon Distribution Plan

Direct distribution will be through showroom stores, and we will also distribute our product indirectly through Tmall, an e-commerce selling and distribution agent. Tmall shortens the distribution chain and works as an agent. When distributing Wunder Under leggings, Lululemon would sell the product to Tmall and Tmall would then sell the product directly to the consumer, which eliminates intermediaries and makes the distribution process more efficient and effective.

Another way that Tmall helps the distribution chain is by using a B2D structure (Export China, 2018). This means that Tmall assists in helping brands and companies connect with local Chinese distributors. This process advertises brands in the current market, and allows them to choose their distributor straight from the Tmall app. Tmall is a great asset for Lululemon to continue its relationship with because it allows for direct business to consumer selling, but they also allow for business to distributor selling. Another way we plan on expanding our distribution is by opening more stores. This will be done by adding around 20 new stores to China this year. We plan on opening most of the stores in areas with a higher population, with a younger demographic.

Implementation Plan

Product and Service Adaptations

Product and service success will be evaluated throughout the year as we continue to engage the market, look at trends in design and sell through, and review product feedback to create the right product for the market. We will do this by creating two teams:

- **Product Adaptation Team** – The team will consist of representatives from market analysis, finance, sales and design departments. They will meet at the end of each product season to evaluate the strengths and weaknesses of a seasonal product with a focus on logos, colours and sizing. Based on their evaluation they will come up with a plan to improve next year's product and tailor it to our target market.
- **Service Adaptations Team** – The team will consist of representatives from market analysis, digital marketing, customer service, retail operations, e-commerce and distribution departments. They will evaluate the strengths and weaknesses in our services offered instore and online. They will meet quarterly and submit evaluations and suggestions to improve servicing our market.

Pricing Implementation

- Maintain Prices
- Prices will be determined for each season 1 month before the product goes live online and instore. Finance and marketing will determine these prices to maximize the pricing strategy.
- Follow Discounted Pattern
- Representatives from Finance, Marketing and Sales will work together monthly to determine which

product should be discounted and when the discount will roll out on a seasonal basis. Sale prices will not exceed 20%-30% off regular price.

- Special Projects Team: International Singles Day – Representatives from Marketing, Finance, Community Events, Digital Marketing, E-commerce, Distribution, Allocation and Retail Operations will dedicate Q1, Q2, planning the logistics for International singles day. They will be responsible for creating the discount structure, an allocation plan for retail stores as well as e-commerce platforms and distributors and an advertising campaign.

Promotional Implementation

The company needs to establish a social media presence on WeChat, Weibo and DouYin to create online community engagement and brand awareness to create a seamless omnichannel retail experience and two-way communication.

- Grow the Social Media Team and Create Accounts.
- Expand the social media team and divide them into National and Local levels for each major city. They will be responsible for content creation on all platforms, liaising with marketing, advertising, store manager, community events team to create consistent two-way communications. Platform Names will include: LululemonChina, LululemonShanghai, LuluLemonHangzhou, LululemonGuangzhou, LululemonChengdu, LululemonShenzhen and LululemonBeijing to target specific communities. Social Media Initiatives will be ongoing throughout the year on a consistent schedule established by the marketing and advertising departments.
- Grow the Community Events Team.
- Expand the Community events team to tailor events to urban areas such as Shanghai, Hangzhou, Guangzhou, Chengdu, Shenzhen and Beijing. The community event team will be responsible for coordinating and planning all events in their designated district and liaising with local store managers, head office and the social media team. They will also need to become product experts to create their events which will feature specific products like the Wunder Under legging.
- Invest in Mobile Marketing.

The most effective way to reach our target market is by Mobile Marketing campaigns. Marketing, Advertising, Finance and the Social Media teams will be responsible for overseeing these initiatives. The marketing and finance departments will be responsible for defining the effectiveness of our mobile marketing initiatives, while advertising, social media will create the content and execute the planned schedule.

Distribution Implementation

- **Showroom Expansion** – A New Store Opening team, which will operate under retail ops will consist of real estate, facilities, visual, and IT will be created for each major city Shanghai, Hangzhou, Guangzhou, Chengdu, Shenzhen and Beijing. We will be opening 20 new stores, 15 regular and 5 Women-only to grow interest in leggings. The goal is to open five stores per quarter.
- **E-Commerce Partnerships** – B2B partnerships will be responsible for finding another e-commerce platform to get out product on by the end of the year. They will also continue working with their current partner, Tmall to find more distribution partners to get our products to our consumers quickly and efficiently.

Budget and Forecast

After looking at Lululemon's 2018 financials we realized they had spent $1.1 billion on their selling, general and administrative expenses, which was a 23% increase from their spending in the previous year (Lululemon Athletica, 2018). We then estimated that their spending for 2019 would increase by 25%, and further determined that their spending in 2020 would be up 30% for a total budget of $1.79 billion for our implementation strategy. This budget was then allocated to, opening and operating new stores, digital marketing, product adaptation and community events. After estimating each department's spending, we determined that opening and operating new stores would receive 50% of the budget, giving the department $895 million. Digital marketing received a total budget of $447.5 million, product adaption received a total budget of $268.5 million. We then had 10% of the budget left over which we dedicated to community events, giving them a budget of $179 million.

Since China is the second-largest activewear market in the world it is a great opportunity for Lululemon to increase its revenues (Swartz, 2020). Based on our research we discovered that in 2019 Lululemon had doubled their amount of sales out of the North America region, making that share would 12% of its total sales. We believe that if Lululemon opens more retail stores in China and expands its e-commerce market that it could see an increase of 24% of total sales being from outside of the North American region.

Case: Lululemon's Marketing Strategy in Hong Kong

Photo by Tseuwonn Rekauidscoo, CC BY-SA 4.0

Lululemon's marketing plan has achieved success in Hong Kong. Over the past two years, all my friends have become aware of this brand due to its effective promotional strategies and digital marketing efforts. During the pandemic, when they could not visit gyms, many developed habits of doing yoga at home and sometimes felt lost and insecure about the intense situation.

Meanwhile, Lululemon was promoting the ideas of self-care and well-being, encouraging people to relax by doing yoga at home. Their success in building brand awareness can be attributed to the promotion on social media, holding community campaigns, connecting local athletes and yoga instructors, and even cooperating with other organizations that care about mental health and healing. My friends recognized that Lululemon matched the prevailing trend of yoga, so they followed the brand's social media account and participated in outdoor yoga events. They have now become loyal customers of their yoga leggings. Lululemon is growing at the right time because there was a growth in health and fitness concerns during the pandemic, whether physical or mental. They build a sense of belonging to a community more than only offering and selling products (Danziger, 2019). Now, it has become the top of the favourite brand of yoga leggings among all my Hong Kong friends.

Zheng Zeng, October 2022

Credits

Lululemon Marketing Strategy and Plan written by Taylor Rawding, Jantien Sneyd, Tiffani Hamilton, Saroja Venkatesha, Jodie Holman and Zoe Ciarrocco as an assignment.

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11.6 KEY TERMS

Key Terms

E-Commerce Partnerships: B2B partnerships will be responsible for finding another e-commerce platform to get out product on by the end of the year. They will also continue working with their current partner, Tmall to find more distribution partners to get our products to our consumers quickly and efficiently. 11.4

Four Ps of Marketing: Product, price, placement, and promotion—are all affected as a company moves through the different phases to become and maintain dominance as a global company. 11.3

Marketing Plan: Captures the outputs from the marketing planning process in one cohesive document. If the plan is done well, it puts a plan in place that aligns the marketing strategy, objectives, and tactics with the corporate mission. 11.1

Product Adaptation Team: The team will consist of representatives from market analysis, finance, sales and design departments. They will meet at the end of each product season to evaluate the strengths and weaknesses of a seasonal product with a focus on logos, colours and sizing. Based on their evaluation they will come up with a plan to improve next year's product and tailor it to our target market. 11.4

Service Adaptations Team: The team will consist of representatives from market analysis, digital marketing, customer service, retail operations, e-commerce and distribution departments. They will evaluate the strengths and weaknesses in our services offered instore and online. They will meet quarterly and submit evaluations and suggestions to improve servicing our market. 11.4

Showroom Expansion: A New Store Opening team, which will operate under retail ops will consist of real estate, facilities, visual, and IT will be created for each major city Shanghai, Hangzhou, Guangzhou, Chengdu, Shenzhen and Beijing. 11.5

CHAPTER 12: CREATING A GLOBAL BRAND

Chapter Outline

12.0 INTRODUCTION

Learning Objectives

After reading this section, students should be able to:

1. Outline the elements of brand architecture.
2. Explain the value of a corporate brand endorsement.
3. Outline the advantages and disadvantages of global branding.
4. Identify the trade-offs of centralized versus decentralized marketing decision making.
5. Identify the special challenges of branding decisions in emerging markets.
6. Outline the brand structures in multinational companies.
7. Outline the principles guiding brands in the global market.
8. Outline the factors shaping a company's international brand structure.
9. Explain the role of firm-based, product-market, and market dynamic characteristics in global branding.
10. List the approaches to globally manage and monitor strategic brands.
11. State the benefits of corporate branding.

A global brand has the same name and a similar image and positioning in most parts of the world. Many global companies leverage favourable brand images and high brand equity by employing combination (tiered) branding, cobranding, and brand extension strategies. Companies can create strong brands in all markets through global brand leadership. Maslow's hierarchy is a needs-based framework that offers a way of understanding opportunities to develop local and global products in different parts of the world. Some products and brands benefit from the country-of-origin effect. Product decisions must also address packaging issues such as labelling and aesthetics. Also, express warranty policies must be appropriate for each country market.

Companies invest a lot in building their brand recognition and reputation because a brand name signals trust. "Trust is what drives profit margin and share price," says Larry Light, CEO of Arcature brand consultancy and a veteran of McDonald's and BBDO Worldwide and Bates Worldwide advertising agencies. "It is what consumers are looking for and what they share with one another" (Kiley, 2009).

Many emerging markets call for lower-cost goods. But how low can a company go on quality and performance without damaging the company's brand? The challenge is to balance maintaining a global reputation for quality while serving local markets at lower cost points.

One way to resolve the challenge is to offer the product at quality levels that are the best in that country even though they would be somewhat below developed-country standards. This is the tactic Walmart has successfully used in Mexico. Walmart's flooring, lighting, and air conditioning make its Mexican stores better than any other local stores even if they might seem Spartan to US consumers.

12.1 ELEMENTS AND BENEFITS OF BRANDING

What Is a Brand?

Brands are interesting, powerful concoctions of the marketplace that create tremendous value for organizations and for individuals. Because brands serve several functions, we can define the term "brand" in the following ways:

1. A brand is an *identifier*: a name, sign, symbol, design, term, or some combination of these things that identifies an offering and helps simplify choice for the consumer.
2. A brand is a *promise*: the promise of what a company or offering will provide to the people who interact with it.
3. A brand is an *asset*: a reputation in the marketplace that can drive price premiums and customer preference for goods from a particular provider.
4. A brand is a set of *perceptions*: the sum total of everything individuals believe, think, see, know, feel, hear, and experience about a product, service, or organization.
5. A brand is "*mind share*": the unique position a company or offering holds in the customer's mind, based on their past experiences and what they expect in the future.

A **brand** consists of all the features that distinguish the goods and services of one seller from another: name, term, design, style, symbols, customer touch points, etc. Together, all elements of the brand work as a psychological trigger or stimulus that causes an association to all other thoughts one has had about this brand.

Brands are a combination of tangible and intangible elements, such as the following:

- Visual design elements (i.e., logo, colour, typography, images, tagline, packaging, etc.)
- Distinctive product features (i.e., quality, design sensibility, personality, etc.)
- Intangible aspects of customers' experience with a product or company (i.e., reputation, customer experience, etc.)

Branding–the act of creating or building a brand–may take place at multiple levels: company brands, individual product brands, or branded product lines. Any entity that works to build consumer loyalty can also be considered a brand, such as celebrities (e.g., Lady Gaga), events (e.g., Susan G. Komen Race for the Cure), and places (e.g., Las Vegas).

Brands Create Market Perceptions

A successful brand is much more than just a name or logo. As suggested in one of the definitions above, a brand is the sum of perceptions about a company or product in the minds of consumers. Effective brand building can create and sustain a strong, positive, and lasting impression that is difficult to displace. Brands provide external cues to taste, design, performance, quality, value, or other desired attributes if they are developed and managed properly. Brands convey positive or negative messages about a company, product, or service. Brand perceptions are a direct result of past advertising, promotion, product reputation, and customer experience.

A brand can convey multiple levels of meaning, including the following:

As an automobile brand, the Mercedes-Benz logo suggests high prestige.
Photo by Mikes-Photography, Pixabay License

1. **Attributes:** specific product features. The Mercedes-Benz brand, for example, suggests expensive, well-built, well-engineered, durable vehicles.
2. **Benefits:** attributes translate into functional and emotional benefits. Mercedes automobiles suggest prestige, luxury, wealth, reliability, self-esteem.
3. **Values:** company values and operational principles. The Mercedes brand evokes company values around excellence, high performance, power.
4. **Culture:** cultural elements of the company and brand. Mercedes represents German precision, discipline, efficiency, quality.
5. **Personality:** strong brands often project a distinctive personality. The Mercedes brand personality combines luxury and efficiency, precision and prestige.
6. **User:** brands may suggest the types of consumers who buy and use the product. Mercedes drivers might be perceived and classified differently than, for example, the drivers of Cadillacs, Corvettes, or BMWs.

Brands Create an Experience

Effective branding encompasses everything that shapes the perception of a company or product in the minds of customers. Names, logos, brand marks, trade characters, and trademarks are commonly associated with brand, but these are just part of the picture. Branding also addresses virtually every aspect of a customer's experience with a company or product: visual design, quality, distinctiveness, purchasing experience, customer service, and so forth. Branding requires a deep knowledge of customers and how they experience the company or product. Brand-building requires long-term investment in communicating about and delivering the unique value embodied in a company's "brand," but this effort can bring long-term rewards.

In consumer and business-to-business markets, branding can influence whether consumers will buy the product and how much they are willing to pay. Branding can also help in new product introduction by creating meaning, market perceptions, and differentiation where nothing existed previously. When companies introduce a new product using an existing brand name (a brand extension or a branded product line), they can build on consumers' positive perceptions of the established brand to create greater receptivity for the new offering.

Brands Create Value

Brands create value for consumers and organizations in a variety of ways.

Value of Branding for the Consumer

Brands help simplify consumer choices. Brands help create trust, so that a person knows what to expect from a branded company, product, or service. Effective branding enables the consumer to easily identify a desirable company or product because the features and benefits have been communicated effectively. Positive, well-established brand associations increase the likelihood that consumers will select, purchase, and consume the product. Dunkin' Donuts, for example, has an established logo and imagery familiar to many U.S. consumers. The vivid colours and image of a "DD" cup are easily recognized and distinguished from competitors, and many associate this brand with tasty donuts, good coffee, and great prices.

Value of Branding for Product and Service Providers

For companies and other organizations that produce goods, branding helps create loyalty. It decreases the risk of losing market share to the competition by establishing a competitive advantage customers can count on. Strong brands often command premium pricing from consumers who are willing to pay more for a product they know, trust, and perceive as offering good value. Branding can be a great vehicle for effectively reaching target audiences and positioning a company relative to the competition. Working in conjunction with positioning, brand is the ultimate touchstone to guide choices around messaging, visual design, packaging, marketing, communications, and product strategy.

Fig 12.1 "Brand" by Alyssa Giles, CC BY-NC-SA 4.0.

For example, Starbucks' loyal fan base values and pays premium prices for its coffee. Starbucks' choices about beverage products, neighbourhood shops, the buying experience, and corporate social responsibility all help build the Starbucks brand and communicate its value to a global customer base.

The Starbucks brand is associated with premium, high-priced coffee.
Photo by JerryUnderscore under Pixabay License

Value of Branding for the Retailer

Retailers such as Target, Safeway, and Walmart create brands of their own to create a loyal base of customers. Branding enables these retailers to differentiate themselves from one another and build customer loyalty around the unique experiences they provide. Retailer brand building may focus around the in-store or online shopping environment, product selection, prices, convenience, personal service, customer promotions, product display, etc.

Retailers also benefit from carrying the branded products customers want. Brand-marketing support from retailers or manufacturers can help attract more customers (ideally ones who normally don't frequent an establishment). For example, a customer who truly values organic brands might decide to visit a CVS store to shop for organic household cleaners that are safe to use around babies. This customer might have learned that a company called BabyGanics, which brands itself as making “safe, effective, natural household solutions,” was available at this particular retailer.

12.2 FORMULATING A GLOBAL BRAND STRATEGY

To create an effective global brand structure capable of spanning operations in different countries and product lines, companies must clearly define the importance and role of each level of branding (corporate, product division, or product brand level), as well as the interrelation or overlap of branding at each level. They should also determine the appropriate geographic scope for each level relative to the firm's current organizational structure. To be effective, such "architecture" should satisfy three key principles: parsimony, consistency, and connectivity.

Parsimony requires that the brand architecture should incorporate all existing brands, whether developed internally or acquired, and provide a framework for consolidation to reduce the number of brands and strengthen the role of individual brands. Brands that are acquired need to be melded into the existing structure, especially when these brands occupy similar market positions to those of existing brands. When the same or similar products are sold under different brand names or are positioned differently in each country, ways to harmonize these should be examined.

A second important element of brand architecture is its consistency relative to the number and diversity of products and product lines within the company. A balance needs to be struck between the extent to which brand names differentiate product lines or establish a common identity across different products. The development of strong and distinctive brand images for different product lines helps establish their separate identities. Conversely, the use of a common brand name consolidates effort and can produce synergies.

The value of corporate brand endorsement across different products and product lines and at lower levels of the brand hierarchy—a brand's connectivity—also needs to be assessed. The use of corporate brand endorsement as either a name identifier or logo connects the different product brands to the company and helps provide reassurance to customers, distributors, and other value-chain partners. Implemented well, a corporate brand endorsement can integrate and unify different brand identities across national boundaries. At the same time, corporate endorsement of a highly diverse range of product lines can result in dilution of the image. Worse, if one product brand is "damaged," corporate endorsement can spread the resulting negative effects or associations to other brands in the portfolio and create lasting effects across multiple product lines. Thus, both aspects need to be weighed in determining the role of corporate brand endorsement in brand architecture.

12.3 GLOBAL BRANDING

Photo of coke for the example of a global brand. Photo by Mae Mu, Unsplash License

A global brand is the brand name of a product that has worldwide recognition. Indeed, the world does become flatter to the extent a brand is recognized, accepted, and trusted across borders. Some of the most-recognized brands in the world include Coca-Cola, IBM, Microsoft, GE, Nokia, McDonald's, Google, Toyota, Intel, and Disney (Frampton et al., 2010).

The advantages of creating a global brand are economies of scale in production and packaging, which lower marketing costs while leveraging power and scope. The disadvantages, however, are that consumer needs differ across countries, as do legal and competitive environments. So while global branding, and consumer acceptance of such, is a flattener, significant country differences remain even when a firm has a strong global brand. Companies may decide to follow a global-brand strategy but also make adjustments to their communications strategy and marketing mix locally based on local needs.

The decision companies face is whether they should market one single brand around the world or multiple brands. Coca-Cola uses the Coke name on its cola products around the world but markets its water under the Dasani brand. Nestlé uses a local branding strategy for its 7,000 brands but also promotes the Nestlé corporate brand globally.

Acer's Multiple-Brand Strategy

PC maker Acer sells its personal computers under four different brands. Using a multi-brand strategy is a good choice when a country has a strong, positive association with a particular brand. For example, when Taiwan-based Acer bought US PC-maker Gateway, Acer kept the Gateway brand to use in the United States for midtier PCs. In Europe, however, Acer uses the Packard Bell brand. Acer also has two other brands, which are segmented by price. Acer's eMachines brand is for the lower-end consumer who is most focused on price, whereas the Acer brand is reserved for the highest-quality products aimed at technophiles. This multi-brand strategy also helps Acer's distribution. As Acer's chief marketing officer, Gianpiero Morello, says, "It's difficult to get a retailer to place 50 percent of his space with one brand. It's easier to split that same space with three brands." (Einhorn & Culpan, 2010).

Global Brand Web Strategy

Companies that are promoting their global brands successfully on the web include Google, Philips, Skype, Ericsson, Hewlett-Packard, and Cisco Systems. These companies are mindful of the cultural and language differences across countries. They have created websites in local languages and are using images and content specific to each country. At the same time, however, each country website has the same look and feel of the main corporate website to preserve the overall brand (Ballance, 2009).

Planning a Brand Strategy for Emerging Markets

Entering an emerging market with a developed-country brand poses an extra challenge. Income levels in emerging markets are lower, so companies tend to price their products as inexpensively as possible. This low-cost strategy may have consequences for the company's brand, however. For example, if a company introduces its brand as a "premium" product despite having a lower price, how will it introduce and differentiate its true "premium" brand later as consumers' incomes rise?

Centralized versus Decentralized Marketing Decisions

Who has the authority to make marketing decisions? In a centralized-marketing organizational structure, the home-country headquarters retains decision-making power. In a decentralized-marketing organizational structure, the regions are able to make decisions without headquarters' approval. The advantage of the centralized structure is speed, consistency, and economies of scale that can save costs (such as through global-marketing campaigns). The disadvantages are that the marketing isn't tied to local knowledge and doesn't reflect local tastes, so sales aren't optimized to appeal to regional differences.

12.4 GLOBAL BRAND STRUCTURES

Multinational companies typically operate with one of three brand structures: (a) a corporate-dominant, (b) a product-dominant, or (c) a hybrid structure. A corporate-dominant brand structure is most common among firms with relatively limited product or market diversity, such as Shell, Toyota, or Nike. Product-dominant structures, in contrast, are often used by (mostly industrial) companies, such as Akzo Nobel, that have multiple national or local brands or by firms such as Procter & Gamble (P&G) that have expanded internationally by leveraging their "power" brands. The most commonly used structure is a hybrid (think of Toyota Corolla cars or Cadbury Dairy Milk chocolate) consisting of a mix of global (corporate), regional, and national product-level brands or different structures for different product divisions.

In many companies, "global" branding evolves as the company enters new countries or expands product offerings within an existing country. Typically, expansion decisions are made incrementally, and often on a country-by-country, product-division, or product-line basis, without considering their implications on the overall balance or coherence of the global brand portfolio. As their global market presence evolves and becomes more closely interlinked, however, companies must pay closer attention to the coherence of their branding decisions across national markets and formulate an effective global brand strategy that transcends national boundaries. In addition, they must decide how to manage brands that span different geographic markets and product lines, who should have custody of international brands and who is responsible for coordinating their positioning in different national or regional markets, as well as making decisions about use of a given brand name on other products or services.

To make such decisions, companies must formulate a coherent set of principles to guide the effective use of brands in the global marketplace. These principles must define the company's "brand architecture," that is, provide a guide for deciding which brands should be emphasized at what levels in the organization, how brands are used and extended across product lines and countries, and the extent of brand coordination across national boundaries.

12.5 DETERMINANTS OF GLOBAL BRAND STRUCTURE

The kinds of issues a company must resolve as it tries to shape a coherent global branding strategy reflect its globalization history—how it has expanded internationally and how it has organized its international operations. At any given point, the structure of a brand portfolio reflects a company's past management decisions as well as the competitive realities the brand faces in the marketplace. Some companies, such as P&G and Coca-Cola, expanded primarily by taking domestic "power" brands to international markets. As they seek to expand further, they must decide whether to further extend their power brands or to develop brands geared to specific regional or national preferences and how to integrate the latter into their overall brand strategy. Others, such as Nestlé and Unilever, grew primarily by acquisition. As a consequence, they relied mainly on country-centred strategies, building or acquiring a mix of national and international brands. Such companies must decide how far to move toward greater harmonization of brands across countries and how to do so. This issue is particularly relevant in markets outside the United States, which often are fragmented, have small-scale distribution, and lack the potential or size to warrant the use of heavy mass-media advertising needed to develop strong brands.

Specifically, a company's international brand structure is shaped by three sets of factors: (a) firm-based characteristics, (b) product-market characteristics, and (c) underlying market dynamics (Douglas et al., 2001).

Firm-Based Characteristics

Firm-based characteristics reflect the full array of past management decisions. First, a company's administrative heritage—in particular, its organizational structure—defines the template for its brand structure. Second, a firm's international expansion strategy—acquisition or organic growth—affects how its brand structure evolves over time. What is more, the use of strategic alliances to broaden the geographic scope of the firm's operations often results in a "melding" of the brand strategies of the partners. Third and fourth, the importance of corporate identity and the diversity of the firm's product lines and product divisions also determine the range and number of brands.

An appreciation of a company's administrative heritage is critical to understanding its global brand structure (Bartlett & Ghoshal, 1989). A firm that has historically operated on a highly decentralized basis, in which country managers have substantial autonomy and control over strategy as well as day-to-day operations, is likely to have a substantial number of local brands. In some cases, the same product may be sold under different brand names in different countries. In others, a product may be sold under the same brand name but have a different positioning or formulation in different countries.

Firms with a centralized organizational structure and global product divisions, such as Panasonic or Siemens, are more likely to have global brands. Both adopted a corporate branding strategy that emphasizes quality and reliability. Product lines are typically standardized worldwide, with minor variations in styling and features for local country markets.

Firms that expand internationally by acquiring local companies, even when the primary goal is to gain access to distribution channels, often acquire local brands. If these brands have high local recognition or a strong customer or distributor franchise, the company will normally retain the brand. This is particularly likely if the brand does not occupy a similar positioning to that of another brand currently owned by the firm. Nestlé and Unilever are examples of companies following this type of expansion strategy.

Expansion is often accompanied by diversification. Between 1960 and 1990, Nestlé expanded by acquiring a number of companies in a range of different product-markets, mostly in the food and beverage segment. These acquisitions included well-known global brands such as Perrier and San Pellegrino (mineral water), confectionery companies such as Rowntree and Perugina, pet food companies and brands such as Spillers and Alpo, and grocery companies such as Buitoni, Crosse & Blackwell, and Herta. The resulting proliferation of brands created the need to consolidate and integrate company-branding structures (Douglas et al., 2001).

Firms that have expanded predominantly by extending strong domestic, so-called power brands into international markets primarily use product-level brand strategies. P&G, for instance, has rolled out several of its personal products brands, such as Camay and Pampers, into international markets. This strategy appears most effective when customer interests and desired product attributes are similar worldwide and brand image is an important cue for the consumer.

The relative importance placed by the firm on its corporate identity also influences brand structure. Companies such as General Electric (GE) and Apple place considerable emphasis on corporate identity in the communications strategies. In the case of GE, “Imagination at Work” is associated with a corporate reputation dedicated to turning innovative ideas into leading products and services that help alleviate some of the world’s toughest problems. Equally, Apple uses its apple logo to project the image of a vibrant innovator in the personal computer market. Increasingly, companies use their corporate identity as a means of reassuring customers and distributors that the company is reliable and stands behind its products. As a result, even companies with highly diverse product lines—such as Samsung—rely on the corporate brand name (and its logo) to project an image of reliability.

A fourth determinant of a company’s brand structure is the diversity, or, conversely, the interrelatedness of the product businesses in which the firm is involved. Firms that are involved in closely related product lines or businesses that share a common technology or rely on similar core competencies often emphasize corporate brands. 3M Corporation, for example, is involved in a wide array of product businesses worldwide, ranging from displays and optics to health care products to cleaners to abrasives and adhesives. All rely heavily on engineering skills and have a reputation of being cutting-edge. The use of the 3M brand provides reassurance and reinforces the firm's reputation for competency and reliable products worldwide.

Product-Market Factors

Three product-market factors play an important role in brand architecture: the nature and scope of the target market, the product's cultural associations, and the competitive market structure (Douglas et al., 2001).

When companies target a global market segment with relatively homogeneous needs and preferences worldwide, global brands provide an effective means of establishing a distinctive global identity. Luxury brands such as Godiva, Moet and Chandon, and Louis Vuitton, as well as brands such as deBeers, Benetton, and L'Oreal are all targeted to the same market segment worldwide and benefit from the cachet provided by their appeal to a global consumer group. Sometimes it is more effective to segment international markets by region and target regional segments with similar interests and purchase behaviour, such as Euro-consumers. This provides cost efficiencies when such segments are readily accessible through targeted regional media and distribution channels.

A critical factor influencing brand structure is the extent to which the product is associated with a particular culture, that is, the extent to which there are strong and deeply ingrained local preferences for specific products or product variants (think of beer) or the products are an integral part of a culture (think of bratwurst, soccer teams). The stronger the cultural association, the less likely it is that global product brands will thrive; instead, local branding may be called for.

A third product-market driver of a company's brand structure is the product's competitive market structure, defined as the relative strength of local (national) versus global competitors in a given product market. If markets are fully integrated and the same competitors compete in these markets worldwide, as in aerospace, the use of global brands helps provide competitive differentiation on a global basis. If strong local, national, or regional competitors, as well as global competitors, are present in a given national or regional market, the use of a multitier branding structure, including global corporate or product brands as well as local brands, is desirable. Coca-Cola, for example, beyond promoting its power brands, has introduced several local and regional brands that cater to specific market tastes around the world.Whether you prefer obscure imports or something mainstream, most beer brands like to invoke their country of origin. Guinness comes from Ireland, Corona is Mexican, Heineken and Amstel are Dutch, and Budweiser is a truly American brand.The use of "country of origin effects" is an essential part of beer branding. Using the country of origin as part of the brand equity is free, so companies can avoid having to build an image from scratch over decades. For a long time, Foster's used a kangaroo in its advertisements, while Lapin Kulta, from Lapland in Finland, relies heavily on its unusual provenance in its marketing. Images of Finland's stark landscapes adorn communications material and bottle labels.

Market Dynamics

Finally, while the firm's history and the product markets in which it operates shape its brand structure, market dynamics—including ongoing political and economic integration, the emergence of a global market infrastructure, and consumer mobility—shape and continually change the context in which this evolves (Douglas et al., 2001).

Increasing political and economic integration in many parts of the world has been a key factor behind the growth of international branding. As governments remove tariff and nontariff barriers to business transactions and trade with other countries, and as people and information move easily across borders, the business climate has become more favourable to the marketing of international brands. Firms are less frequently required to modify products to meet local requirements or to develop specific variants for local markets and increasingly can market standardized products with the same brand name in multiple country markets. In many cases, harmonization of product regulation across borders has further facilitated this trend.

The growth of a global market infrastructure is also a major catalyst to the spread of international brands. Global and regional media provide economical and effective vehicles for advertising international brands. At the same time, global media help lay the groundwork for consumer acceptance of, and interest in, international brands by developing awareness of these brands and the lifestyles with which they are associated in other countries. In many cases, this stimulates a desire for the brands that consumers perceive as symbolic of a coveted lifestyle.

The globalization of retailing has further facilitated and stimulated the development of international manufacturer brands. As retailers move across borders, they provide an effective channel for international brands and, at the same time, increase their power. This forces manufacturers to develop strong brands with an international appeal so that they can negotiate their shelf position more effectively and ensure placement of new products.

A final factor shaping the context for international branding is increased consumer mobility. While global media provide passive exposure to brands, increasing international travel and movement of customers across national boundaries provides active exposure to brands in different countries. Awareness of the availability and high visibility of an international brand in multiple countries enhances its value to consumers and provides reassurance of its strength and reliability. Increased exposure to, and familiarity with, new and diverse products and the lifestyles and cultures in which they are embedded also generate greater receptivity to products of foreign origin or those perceived as international rather than domestic. All these factors help create a climate more favourable to international brands.

12.6 MANAGING KEY STRATEGIC BRANDS

Companies must also think about how to globally manage and monitor key strategic brands to ensure that they build and retain their integrity, visibility, and value. This entails assigning brand custody or appointing a brand champion responsible for approving brand extensions and monitoring brand positioning.

One option is to negotiate the harmonization of specific brand positions between corporate headquarters and country managers. This is appropriate for firms with strong country management that operate in product markets where brands were historically tailored to local market characteristics.

A more proactive and increasingly popular solution is to appoint a brand champion responsible for building and managing a brand worldwide. This includes monitoring the consistency of the brand positioning in international markets as well as authorizing the use of the brand (brand extensions) on other products or other product businesses. The brand champion can be a senior manager at corporate headquarters, a country manager, or a product development group. It is critical that the brand champion report directly to top management and have clear authority to sanction or refuse brand extensions to other product lines and product businesses so as to maintain the integrity of the brand and avoid brand dilution.

A third option is to centralize control of brands within a global product division. This approach is likely to be most effective when the business is targeted to a specific global market segment, with new products or brands, when there is greater consistency in market characteristics across countries, and when the company's administrative heritage has only a limited history of strong country management.

Benefits of Corporate Branding

Fig 12.2 "Effective Corporate Brands" by Alyssa Giles CC BY-NC-SA 4.0.

Corporations around the world are increasingly becoming aware of the enhanced value that corporate branding strategies can provide. A strong corporate branding strategy can add significant value in terms of helping the entire corporation and the management team with implementing its long-term vision, creating unique positions in the marketplace for the company and its brands, and signalling a commitment to a broader set of stakeholder issues. An effective corporate branding strategy, therefore, enables the company to leverage its tangible and nontangible assets and promote excellence throughout the corporation. To be effective and meet such objectives, corporate branding requires a high level of personal attention and commitment from the CEO and the senior management. Examples of effective corporate brands include Microsoft, Intel, Singapore Airlines, Disney, CNN, Samsung, and Mercedes. In recent years, the global financial powerhouses HSBC and Citibank have both acquired a vast number of companies across the globe and have fully adopted them under their international corporate brands with great success and within a relatively short time frame. All these companies understand that a well-executed corporate branding strategy can confer significant benefits.

Corporate Brand as the "Face of the Company"

A strong corporate brand acts as the face of the company, portraying what it wants to do and what it wants to be known for in the marketplace. In other words, the corporate brand is the umbrella for the corporation's activities and encapsulates its vision, values, personality, positioning, and image, among many other dimensions. Think of HSBC. It employs the same slogan—"The world's local bank"—around the world. This creative platform enables the corporation to portray itself as a bridge between cultures.

Cost Savings

A corporate branding strategy is often more cost-efficient than a multibrand architecture. Specifically, corporate branding produces efficiencies in terms of marketing and advertising spending as the corporate brand replaces budgets for individual product marketing efforts. Even a combined corporate and product branding strategy can often enable management to reduce costs and exploit synergies from a new and more focused brand architecture. The Apple brand has established a very strong position of being a design-driven and innovative company offering many types of products and services. Their corporate brand encapsulates the body and soul of the company, and the main messages from the company use the corporate Apple brand. Various sub-brands then help to identify the individual product lines.

12.7 COMMON BRANDING STRATEGIES

Managing Brands As Strategic Assets

As organizations establish and build strong brands, they can pursue a number of strategies to continue developing them and extending their value to stakeholders (customers, retailers, supply chain and distribution partners, and of course the organization itself).

Brand Ownership

Who "owns" the brand? The legal owner of a brand is generally the individual or entity in whose name the legal registration has been filed. Operationally speaking, brand ownership should be the responsibility of an organization's management and employees. Brand ownership is about building and maintaining a brand that reflects your principles and values. Brand *building* is about effectively persuading customers to believe in and purchase your product or service. Iconic brands, such as Apple and Disney, often have a history of visionary leaders who champion the brand, evangelize about it, and build it into the organizational culture and operations.

Branding Strategies

A branding strategy helps establish a product within the market and to build a brand that will grow and mature. Making smart branding decisions up front is crucial since a company may have to live with their decisions for a long time. The following are commonly used branding strategies:

"Branded House" Strategy

A "branded house" strategy (sometimes called a "house brand") uses a strong brand—typically the company name—as the identifying brand name for a range of products (for example, Mercedes Benz or Black & Decker) or a range of subsidiary brands (such as Cadbury Dairy Milk or Cadbury Fingers). Because the primary focus and investment is in a single, dominant "house" brand, this approach can be simpler and more cost-effective in the long run when it is well aligned with broader corporate strategy.

“House of Brands” Strategy

With the “house of brands” strategy, a company invests in building out a variety of individual, product-level brands. Each of these brands has a separate name and may not be associated with the parent company name at all. These brands may even be in de facto competition with other brands from the same company. For example, Kool-Aid and Tang are two powdered beverage products, both owned by Kraft Foods. The “house of brands” strategy is well suited to companies that operate across many product categories at the same time. It allows greater flexibility to introduce a variety of different products, of differing quality, to be sold without confusing the consumer’s perception of what business the company is in or diluting brand perceptions about products that target different tiers or types of consumers within the same product category.

Private-Label or Store Branding

Also called store branding, private-label branding has become increasingly popular. In cases where the retailer has a particularly strong identity, the private label may be able to compete against even the strongest brand leaders and may outperform those products that are not otherwise strongly branded. The northeastern U.S. grocery chain Wegman’s offers many grocery products that carry the Wegman’s brand name. Meanwhile national grocery chain Safeway offers several different private label “store” brands: Safeway Select, Organics, Signature Cafe, and Primo Taglio, among others (Safeway, n.d.).

“No-Brand” Branding

A number of companies successfully pursue “no-brand” strategies by creating packaging that imitates generic-brand simplicity. “No brand” branding can be considered a type of branding since the product is made conspicuous by the absence of a brand name. “Tapa Amarilla” or “Yellow Cap” in Venezuela during the 1980s is a prime example of no-brand strategy. It was recognized simply by the colour of the cap of this cleaning products company.

Personal and Organizational Brands

Photo by Georgia Sierra Club under CC BY-NC 2.0

Personal and organizational branding are strategies for developing a brand image and marketing engine around individual people or groups. Personal branding treats persons and their careers as products to be branded and sold to target audiences. Organizational branding promotes the mission, goals, and/or work of the group being branded. The music and entertainment industries provide many examples of personal and organizational branding. From Justin Bieber to George Clooney to Kim Kardashian, virtually any celebrity today is a personal brand. Likewise, bands, orchestras, and other artistic groups typically cultivate an organizational (or group) brand. Faith branding is a variant of this brand strategy, which treats religious figures and organizations as brands seeking to increase their following. Mission-driven organizations such the Girl Scouts of America, the Sierra Club, the National Rifle Association (among millions of others) pursue organizational branding to expand their membership, resources, and impact.

Place Branding

The developing fields of place branding and nation branding work on the assumption that places compete with other places to win over people, investment, tourism, economic development, and other resources. With this in mind, public administrators, civic leaders, and business groups may team up to "brand" and promote their city, region, or nation among target audiences. Depending on the goals they are trying to achieve, targets for these marketing initiatives may be real-estate developers, employers and business investors, tourists and tour/travel operators, and so forth. While place branding may focus on any given geographic area or destination, nation branding aims to measure, build, and manage the reputation of countries.

Co-Branding

Co-branding is an arrangement in which two established brands collaborate to offer a single product or service that carries both brand names. In these relationships, generally both parties contribute something of value to the new offering that neither would have been able to achieve independently. Effective co-branding builds on the complementary strengths of the existing brands. It can also allow each brand an entry point into markets in which they would not otherwise be credible players.

The following are some examples of co-branded offerings:

- Delta Airlines and American Express offer an entire family of co-branded credit cards; other airlines offer similar co-branded cards that offer customer rewards in terms of frequent flyer points and special offers
- Home furnishings company Pottery Barn and the paint manufacturer Benjamin Moore co-brand seasonal colour palettes for home interior paints
- Fashion designer Liz Lange designs a ready-to-wear clothing line co-branded with and sold exclusively at Target stores
- Auto maker Fiat and toy maker Mattel teamed up to celebrate Barbie's fiftieth anniversary with the nail-polish-pink Fiat 500 Barbie car

Photo by Xavigivax, CC BY-SA 3.0

Co-branding is a common brand-building strategy, but it can present difficulties. There is always risk around how well the market will receive new offerings, and sometimes, despite the best-laid plans, co-branded offerings fall flat. Also, these arrangements often involve complex legal agreements that are difficult to implement. Co-branding relationships may be unevenly matched, with the partners having different visions for their collaboration, placing different priority on the importance of the co-branded venture, or one partner holding significantly more power than the other in determining how they work together. Because co-branding impacts the existing brands, the partners may struggle with how to protect their current brands while introducing something new and possibly risky.

Brand Licensing

Brand licensing is the process of leasing or renting the right to use a brand in association with a product or set of products for a defined period and within a defined market, geography, or territory. Through a licensing agreement, a firm (licensor) provides some tangible or intangible asset to another firm (licensee) and grants that firm the right to use the licensor's brand name and related brand assets in return for some payment. The licensee obtains a competitive advantage in this arrangement, while the licensor obtains inexpensive access to the market in question.

Licensing can be extremely lucrative for the owner of the brand, as other organizations pay for permission to produce products carrying a licensed name. The Walt Disney Company was an early pioneer in brand licensing, and it remains a leader in this area with its wildly popular entertainment and toy brands: Star Wars, Disney Princesses, Toy Story, Mickey Mouse, and so on. Toy manufacturers, for example, pay millions of dollars and vie for the rights to produce and sell products affiliated with these "super-brands."

Line Extensions and Brand Extensions

Organizations use line extensions and brand extensions to leverage and increase brand equity.

A company creates a ***line extension*** when it introduces a new variety of offering within the same product category. To illustrate with the food industry, a company might add new flavors, package sizes, nutritional content, or products containing special additives in line extensions. Line extensions aim to provide more variety and hopefully capture more of the market within a given category. More than half of all new products introduced each year are line extensions. For example, M&M candy varieties such as peanut, pretzel, peanut butter, and dark chocolate are all line extensions of the M&M brand. Diet Coke™ is a line extension of the parent brand Coke ™. While the products have distinct differences, they are in the same product category.

A ***brand extension*** moves an existing brand name into a new product category, with a new or somehow modified product. In this scenario, a company uses the strength of an established product to launch a product in a different category, hoping the popularity of the original brand will increase receptivity of the new product. An example of a brand extension is the offering of Jell-O pudding pops in addition to the original product, Jell-O gelatin. This strategy increases awareness of the brand name and increases profitability from offerings in more than one product category.

Line extensions and brand extensions are important tools for companies because they reduce financial risk associated with new-product development by leveraging the equity in the parent brand name to enhance consumers' perceptions and receptivity towards new products. Due to the established success of the parent brand, consumers will have instant recognition of the product name and be more likely to try the new line extension.

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12.9 KEY TERMS

Key Terms

"Branded House" Strategy: Sometimes called a "house brand" uses a strong brand—typically the company name—as the identifying brand name for a range of products. 12.7

"House of Brands" Strategy: A company invests in building out a variety of individual, product-level brands. 12.7

"No-Brand" Branding: A number of companies successfully pursue "no-brand" strategies by creating packaging that imitates generic-brand simplicity. "No brand" branding can be considered a type of branding since the product is made conspicuous by the absence of a brand name. 12.7

Attributes are specific product features. 12.1

Benefits are attributes translate into functional and emotional benefits. 12.1

Brand consists of all the features that distinguish the goods and services of one seller from another: name, term, design, style, symbols, customer touch points, etc. Together, all elements of the brand work as a psychological trigger or stimulus that causes an association to all other thoughts one has had about this brand. 12.1

Brand analysis involves a measurement of how a brand influences customer demand at the point of purchase. 12.6

Brand extension moves an existing brand name into a new product category, with a new or somehow modified product. 12.7

Brand ownership should be the responsibility of an organization's management and employees.

Brand ownership is about building and maintaining a brand that reflects your principles and values. 12.7

Branding strategy helps establish a product within the market and to build a brand that will grow and mature. Making smart branding decisions up front is crucial since a company may have to live with their decisions for a long time. 12.7

Brand Strength Score: As brands are assets, valuing them requires an assessment of their ability to secure future earnings on behalf of the businesses that own them. Brand strength is a measure of the brand's ability to secure demand, and therefore earnings, over time. 12.6

Brand's value is a financial representation of a business's earnings due to the superior demand created for its products and services through the strength of its brand. 12.6

Line extension – when it introduces a new variety of offering within the same product category. 12.7

Managing Brands As Strategic Assets: As organizations establish and build strong brands, they can pursue a number of strategies to continue developing them and extending their value to stakeholders (customers, retailers, supply chain and distribution partners, and of course the organization itself). 12.7

Personality: strong brands often project a distinctive personality. 12.1

Private-Label or Store Branding: Also called store branding, private-label branding has become increasingly popular. In cases where the retailer has a particularly strong identity, the private label may be able to compete against even the strongest brand leaders and may outperform those products that are not otherwise strongly branded. 12.7

User: brands may suggest the types of consumers who buy and use the product. 12.1

Values: company values and operational principles. 12.1

CHAPTER 13: INTRODUCTION TO E-COMMERCE

Chapter Outline

13.0 Introduction

13.1 Definitions

13.2 Advantages and Disadvantages

13.3 Online Strategy

13.4 Types of E-Commerce

13.5 E-Commerce Models

13.6 E-Commerce Technology

13.7 E-Commerce Platforms

13.8 Blockchain and Bitcoin

13.9 Trends

13.10 Chapter References

13.11 Key Terms

13.0. CHAPTER INTRODUCTION

Learning Outcomes

After reading this section, students should be able to:

1. Define e-business and e-commerce and explain the difference between them.
2. List the major categories of e-business.
3. Describe advantages and disadvantages of e-commerce.
4. Outline the business-to-consumer e-commerce cycle.
5. Summarize the major models of e-commerce.
6. Discuss the different technologies used for e-commerce.
7. Explain social commerce, and New Retail, and the reasons for its increasing popularity.

The internet has had a massive impact on the way we communicate and how businesses operate. Businesses have found new ways to reach customers, expand markets, and transact more efficiently in digital formats. Changes in technology have allowed new business models to flourish while also making it difficult for some industries to keep pace. In general, electronic business has created a revolution in business practices. However, if organizations are going to take advantage of electronic technologies, they must take a strategic perspective. Corporate strategy must align with the company's e-commerce strategy. In this chapter, we will discuss definitions of electronic business and categories of e-commerce, as well as discussing the trends in e-commerce.

13.1 DEFINITIONS

E-Business & E-Commerce

Electronic business or e-business, in a broad sense, is the use of computer networks to improve organizational performance. Increasing profitability, gaining market share, improving customer service, and delivering products faster are some of the organizational performance gains possible by doing business electronically. E-business is more than ordering goods online, it involves all aspects of an organization's electronic interactions with its stakeholders.

E-business includes activities such as establishing a web page to support investor relations or communicating electronically with employees. It involves the use of information technology to enhance communications and transactions with all of an organization's stakeholders. Such stakeholders include: customers, suppliers, government regulators, financial institutions, managers, employees, and the public at large. E-business involves several major components: business intelligence (BI), customer relationship management (CRM), supply chain management (SCM), enterprise resource planning (ERP), e-commerce, conducting electronic transactions within the firm, collaboration, and online activities among businesses.

Fig 13.1 E-business involves several major components: business intelligence (BI), customer relationship management (CRM), supply chain management (SCM), enterprise resource planning (ERP), e-commerce, conducting electronic transactions within the firm, collaboration, and online activities among businesses. Adapted from Components of E-Business by Matthew Pauley, CC BY-NC-SA 4.0

E-business and e-commerce are often used interchangeably, but they are not the same thing. E-commerce is the marketing, selling, and buying of goods and services online. It generates revenue, while e-business does not. The facilitation of commerce on a website, such as the ability for customers to order products online, to get questions answered about products, and for the company to introduce new products and ideas is considered e-commerce. E-business refers to all aspects of operating an online business while e-commerce refers specifically to the transaction of goods and services.

The history of e-commerce begins with the first ever online sale on August 11, 1994. A man sold a CD by Sting to his friend through his website NetMarket, an American retail platform. This is the first example of a consumer purchasing a product from a business through the internet. Since then, e-commerce has evolved to make products easier to discover and purchase through online retailers and marketplaces. Independent freelancers, small businesses, and large corporations have all benefited from e-commerce, which enables them to sell their goods and services at a scale that was not possible with traditional offline retail.

E-Commerce in Canada

E-commerce activity in Canada proliferated during the COVID-19 pandemic as restrictions for in-person shopping were put in place. Overall retail sales declined by about 18%, but e-commerce sales nearly doubled at 99.3%. As can be seen in the graph below, sales dramatically increased in April of 2020 at the peak of the pandemic. E-commerce grew in all retail sub-sectors, but the greatest gains were experienced in non-essential items. Many businesses had to shift their models and increase their web presence in order to support online selling (Aston, et al., 2020). To see more on Canadian's online shopping habits, see this infographic from Statistics Canada.

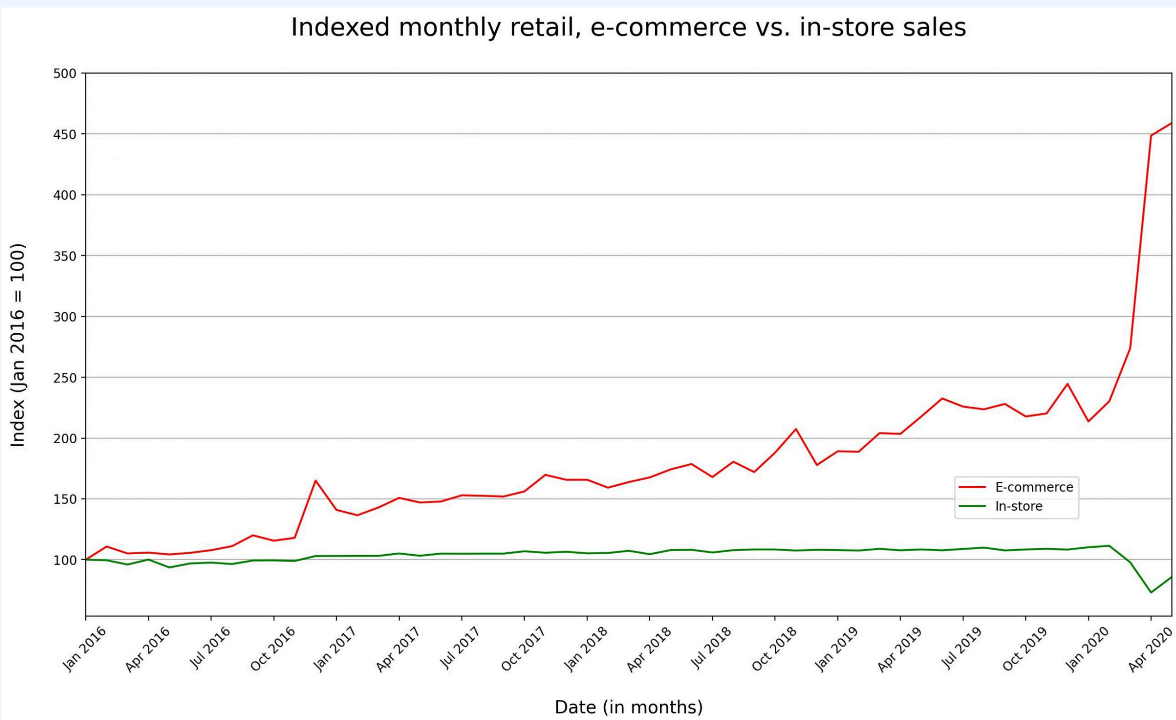


Fig 13.2 Adapted from Statistics Canada, Indexed monthly retail e-commerce sales vs. in-store sales, Canada- July 24, 2020. This does not constitute an endorsement by Statistics Canada of this product. (click to enlarge)

13.2 E-COMMERCE ADVANTAGES AND DISADVANTAGES

It is important to understand the advantages and disadvantages of this model compared to traditional brick-and-mortar businesses. Businesses need to understand their customers and their needs as well as the value of this model.

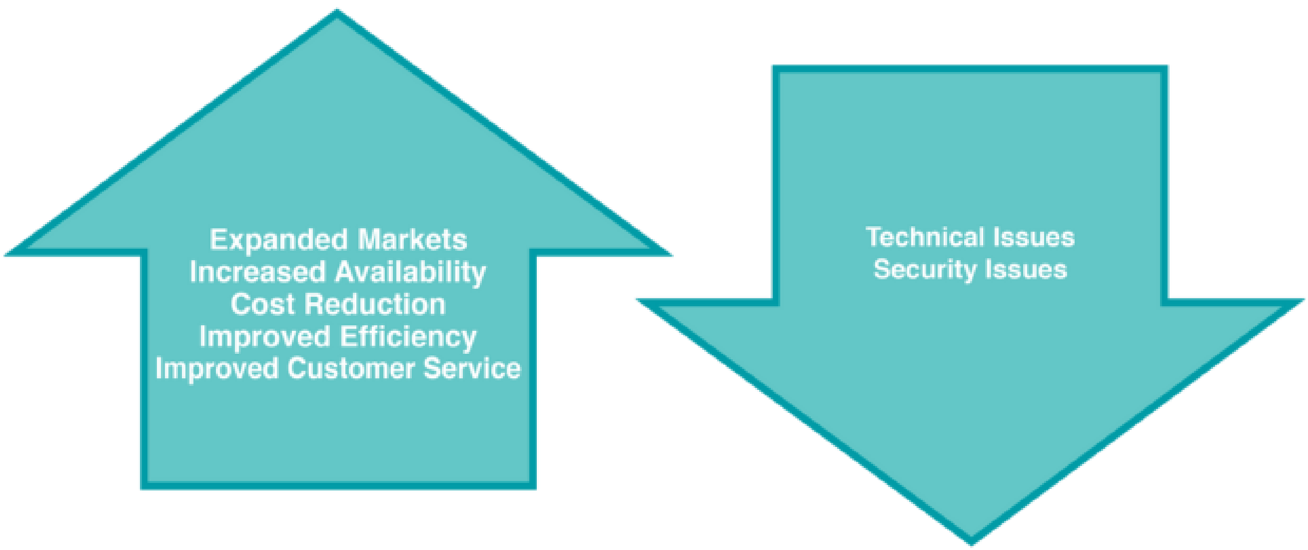


Fig 13.3 E-Commerce Advantages & Disadvantages (click to enlarge).

Advantages

Expanded Markets

Businesses with an online presence are not limited to servicing customers in their immediate geographic area only, and can broaden their market to serve customers at greater distances, even globally. The business would be limited only by shipping methods and costs and would need to consider this in their setup.

Increased Availability

Online operations allow businesses to interact and transact with customers all day every day, and are no longer limited to traditional bricks and mortar operating hours. This makes it easy for customers to make their purchases at a time that is convenient for them. As well, the automation of the online site means that a business can expand operating hours without necessarily increasing labour costs. As well, there are no limitations on shelf space making it possible to expand product offerings.

Reduce Costs

There are many ways that online technology can be utilized by businesses to reduce costs. For a traditional brick and mortar business, by moving online they can save on all of the infrastructure costs of having a physical presence, such as rent, utilities, and maintenance. As well, since online businesses are not limited to shelf space, they can provide expanded product offerings to their customers without the added costs of stocking in store. For businesses that manufacture goods they can use an online site to transact directly with their customers and remove any need for a retailer (intermediary). The elimination of an intermediary is referred to as disintermediation. An example of this is Dell Direct. As well, instead of drawing employees from their local area, organizations can now hire people from the global labour pool. This allows organizations to pay a lower labour cost for the same work based on the prevailing wage in different countries.

Improved Efficiency

When processes are done online or digitally as opposed to more traditional approaches like paper based, the business benefits through efficiency. For example, online ordering allows customers to create accounts and enter in their own information which can reduce errors and speed processes like ordering and payment. This allows the business to track their customers and their shopping habits which can benefit them in the future.

Improved Customer Service

Customers are able to connect with businesses online in different ways which can improve customer satisfaction. Some businesses even have chatbots that allow customers to ask questions and receive immediate answers based on similar questions asked before. As well, customers can leave reviews and have the opportunity to provide feedback to businesses online about their satisfaction with their products and services. Some businesses have made the online return process fairly simple by automating the process and allowing customers to print return labels and drop in the mail.

The amount of data collected digitally on customers as they are interacting with the website is extremely valuable as well. This information can be used to help encourage further purchases or to help target new customers. Many sites use algorithms to suggest similar products when purchasing online to upsell the customer.

While e-commerce provides a number of advantages there are also some disadvantages with this method of doing business.

Disadvantages

Technical & Accessibility issues

Around the world customers may still experience bandwidth issues that prevent them from being able to efficiently interact with businesses online. Bandwidth and access issues will not be a problem in the future as more infrastructure is built.

Security & Privacy Issues

Customers may still be wary about shopping online especially when large privacy breaches have been well publicized. According to the Canadian Internet Use Survey looking at the online shopping habits of Canadians in 2020, for those Canadians who don't shop online, close to a quarter stated that it is due to security and privacy reasons (Statistics Canada, 2021).

Establishing Customer Trust & Satisfaction

Trust is about believing that someone will do what they say and that they will not intentionally do something to hurt you. Trust in business is essential and it is easier to establish in the physical world as customers receive cues from the environment as well as body language from the sales staff. In the online environment, businesses can help build trust by ensuring customers have a good experience by making their online platform easy to navigate and use. Their website presentation should also be high quality and free from errors. They can also provide reviews on other customers experiences.

Fake Reviews

Customer Reviews

Since online reviews of a company's products and services have been found to generate online sales, the prevalence of fake reviews has proliferated. According to estimates, 4% of all online reviews are fake which equates to an impact on global online spending of $152 billion. Fake reviews are often created by bots which allows companies to leverage security systems to filter and remove this type of activity. Removing fake reviews is important for a company's authenticity and helps to build and maintain customer trust (Marciano, 2021).

To build trust, businesses should also make sure the product or service meets the customers expectations. Customers may be dissatisfied especially when ordering products online if the product is not reliable, or different than expected. Meaning that the display and description of the product on the website is not what they received. Online retailers should provide a complete and realistic description of the product and its benefits—with high-quality pictures and perhaps even demonstration videos if possible, appropriate, and affordable—along with product availability and likely ship dates. Customers should be notified by e-mail of order acceptance, and the anticipated delivery date with phone and e-mail contacts for any needed assistance.

13.3 ONLINE STRATEGY

Every business needs to consider the extent of their online presence. There are two key factors to be considered when considering an online strategy:

1. **How many existing or potential customers are likely to do business online?**
   If a significant portion of a company's customers are internet users, and the search cost for the product or service are reasonably, even moderately high, then an organization should have a considerable online presence; otherwise, it is missing an opportunity to inform and interact with its customers. If a company does not have a website, then there is the risk that potential customers will flow to competitors who have a web presence.
2. **What is the information intensity of the product?**
   An information-intense product is one that requires considerable information to describe it completely. The two parameters, number of customers on the web and product information intensity, can be combined to provide a straightforward model (see Figure 13.4) for determining which companies should be using the internet. Organizations falling in the top right quadrant are prime candidates because many of their customers have internet access and their products have a high information content. Firms in the other quadrants, particularly the low-low quadrant, have less need to invest in a website.

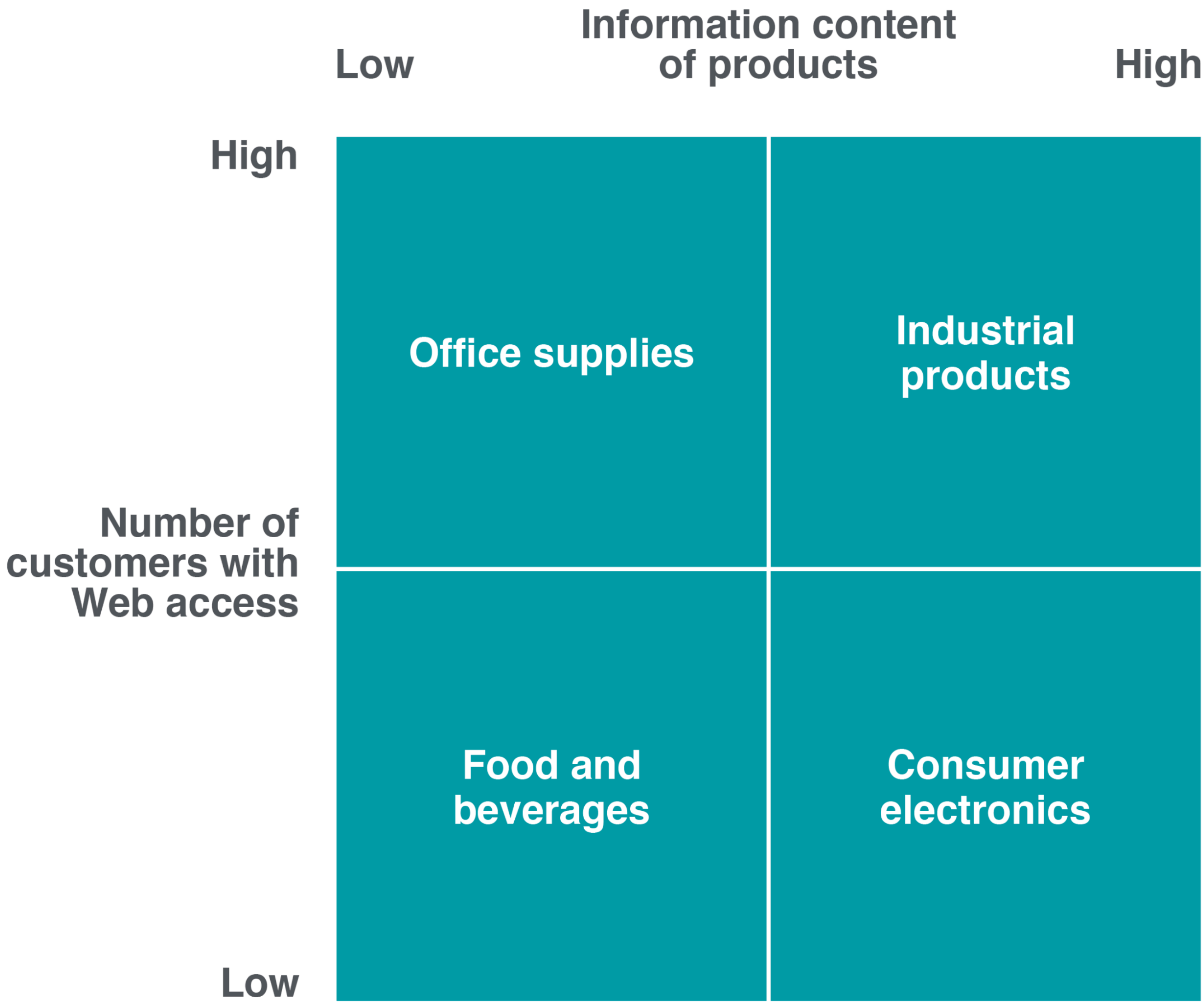


Fig 13.4 "Internet Presence Grid" (click to enlarge) adapted from Richard T. Watson, CC BY 4.0

Strategic Challenges

Now that we have explored how businesses are leveraging the internet to sell their products and services and the benefits and concerns, it is important to understand the strategic challenges of doing so. Companies often face three critical strategic challenges:

Demand Risk	Sharply changing demand or the collapse of markets poses a significant risk for many firms. The web can be used to diversify a business by taking new products to new markets.
Innovation Risk	Not being adaptable, which can lead to stagnation, and ultimately failure to remain competitive. Businesses need to be open to new ideas, and these ideas can come from customers. The internet allows communication with customers for this purpose.
Inefficiency risk	Failure to match competitors' unit costs–inefficiency risk. The internet can help reduce operating costs, such as information distribution.

13.4 TYPES OF E-COMMERCE

Every internet business is either pure-play, or brick-and-click. A **pure-play** business, such as Amazon and Well.ca, has an online presence only and uses the capabilities of the internet to create a new business. **Brick-and-click** businesses, such as Indigo and Canadian Tire, combine a physical presence with an online presence. These businesses use the Internet to supplement their existing businesses (Krishnamurthy, 2003).

There are several different types of e-commerce that can describe almost every transaction that takes place between consumers and businesses.

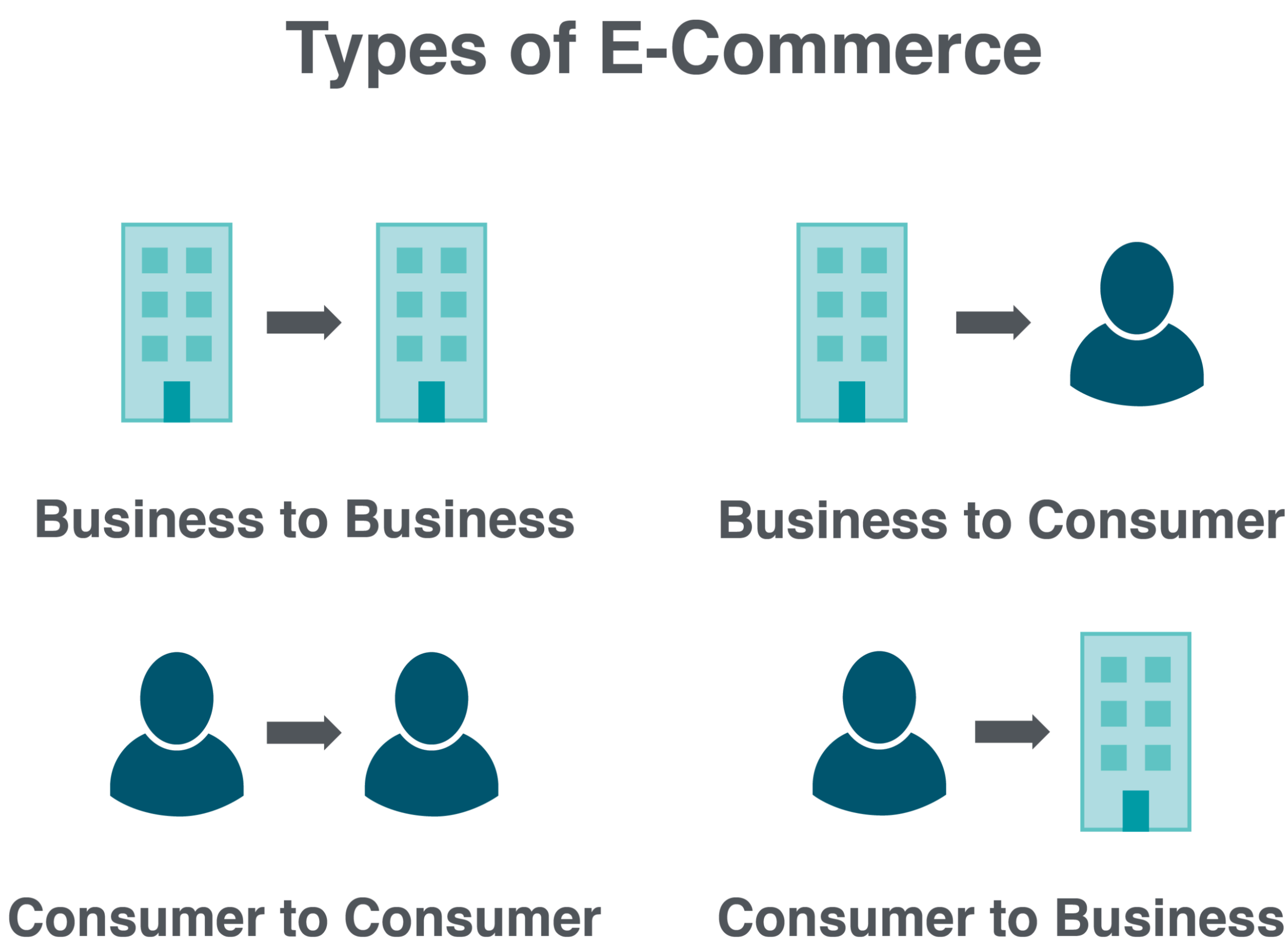


Fig 13.5 Types of e-commerce

Business to Business (B2B)	When a business sells a good or service to another business. For example, a business that sells software-as-a-service for other businesses to use, or Staples selling office supplies. This is the largest form of e-commerce.
Business to Consumer (B2C)	When a business sells a good or service to an individual consumer. For example, when you buy a pair of shoes from an online retailer like Nike.
Consumer to Consumer (C2C)	When a consumer sells a good or service to another consumer. The most well known C2C is eBay, but there are many other online market providers as well, like Kijijii or Craigslist. Peer-to-peer (P2P) are also a form of consumer to consumer. See more about P2P below.
Consumer to Business (C2B)	When a consumer sells their own products or services to a business or organization. For example, an influencer offers exposure to their online audience in exchange for a fee, or a photographer licenses their photo for a business to use.

e-Commerce can also involve the government.

Business to Government (B2G)	Defined as e-commerce transactions with the government. The internet is used for procurement, filing taxes, licensing procedures, business registrations, and other government-related operations. This is an insignificant segment of e-commerce in terms of volume, but it is growing.
Consumer to Government (C2G)	Defined as e-commerce transactions between the government and individuals. This would involve licenses and registrations, and paying taxes.

M-Commerce

Mobile e-commerce (m-commerce) refers to the purchase of goods and services through wireless technology, such as cell phones and handheld devices. M-commerce is growing fast with an estimated 73% of all e-commerce sales being done via a mobile device (Loesche & Richter, 2018). This can be attributed to the fact that many people now own smartphones, and they are using them all the time. This has made it convenient to be able to leverage this technology to shop online.

Growth in M-Commerce

M-commerce transactions continue to grow as a result of the following:

- The **number of global mobile users is steadily increasing** every year, resulting in an increased demand for mobile websites and applications.
- The **rapid adoption of e-commerce** means that evolving customers are looking for more options across more devices.
- **Improved technology** has given mobile devices advanced capabilities and faster internet access enabling

m-commerce to be available on even the most affordable devices.

- **Broadband technology** and **lowering data costs** mean more consumers have access to m-commerce even on affordable devices and data plans.
- Mobile users are looking for **instant gratification** online; this includes their online shopping needs. Increase in m-commerce for fast food, fresh produce and basic household items have been driven by this need for customers to get what they need when and where they want it.

Benefits of M-Commerce

Access	Gaining access to the internet through mobile is easier and more affordable than desktop options. The falling costs of data and improved internet access on mobile mean more and more users have access to the internet via mobile than any other device.
Convenience	Mobile phones are always with us and being constantly connected enhances the benefits of anytime, anywhere use with no need to plug in to or log in to computers wherever they are situated.
Costs	Mobile devices are more affordable than computers and offer multiple uses reducing the need for an additional computer. Calls, messaging services, social media and news content are just a few of the reasons consumers would prefer to use a single device making mobile phones the obvious choice.
Ease of use	Mobile phones are relatively easy and simple to use, and there is no need for a particularly digitally skilled consumer. They allow consumers to make instant purchases with little technical skill.
Mobile Payment	Security around online payments remains the biggest barrier to e-commerce. Mobile payments allow alternative options for transactions via mobile currencies, mobile wallets and alternative mobile only payment methods. Such easy and secure payment options make mobile the preferred choice for many users.
Rich Content	Advances in mobile processing power means content can be easily accessed on mobile web browsers and mobile applications. Rich media allows brands to better demonstrate a product's key features, share testimonials, and showcase the use/look of the product or service.

Peer to Peer (P2P)

Peer-to-peer is a form of e-commerce comprised of an online platform that connects individuals looking to transact with one another. Some examples of P2P are Etsy, Uber, Airbnb and TaskRabbit.

13.5 E-COMMERCE MODELS

An **e-commerce business model** is the method that a business uses to generate revenue online. E-commerce can take on a variety of forms involving different transactional relationships between businesses and consumers.

Retail	The sale of a product by a business directly to a customer without any intermediary.
Wholesale	The sale of products in bulk, often to a retailer that then sells them directly to consumers.
Dropshipping	The sale of a product, which is manufactured and shipped to the consumer by a third party.
Crowdfunding	The collection of money from consumers in advance of a product being available in order to raise the startup capital necessary to bring it to market. Example: Kickstarter
Subscription	The automatic recurring purchase of a product or service on a regular basis until the subscriber chooses to cancel. Examples: newspaper subscriptions, music streaming sites (Spotify)
Transaction Brokers	Companies who facilitate a transaction and take a portion of the revenue. Example AirBnb, EventBrite

As well e-commerce can involve different objects being exchanged as part of these transactions.

Physical products	Any tangible good that requires inventory to be replenished and orders to be physically shipped to customers as sales are made.
Digital products	Downloadable digital goods, templates, and courses, or media that must be purchased for consumption or licensed for use. For example, maybe you take a digital course online through LinkedIn Learning.
Services	A skill or set of skills provided in exchange for compensation. The service provider's time can be purchased for a fee.

The Business to Consumer Cycle

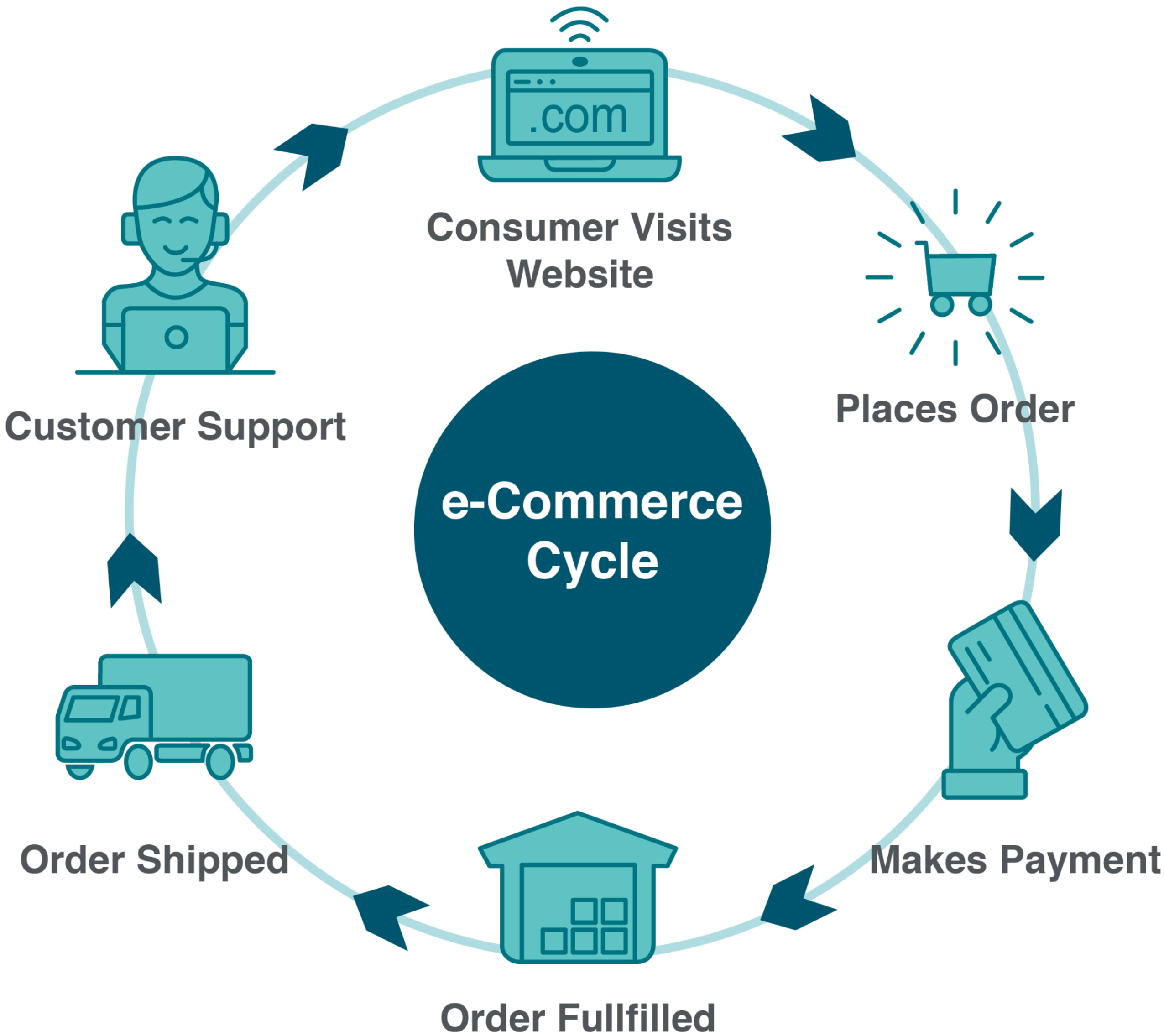


Fig 13.6 B2C e-Commerce Cycle (click to enlarge)

In the B2C e-commerce cycle a customer visits a website and peruses the products offered. They choose a product and place an order which then gets added to their online shopping cart. Once they have completed their selection, they navigate to their shopping cart and choose a shipping address and make a payment. Payment options are explored in detail later in the chapter.

On the other end, the business fulfills the order and prepares it for shipping. The order is then shipped, and the customer is notified of this step. The customer can follow up with customer service if there are any issues with the order or shipment. The customer is also sometimes asked to provide a review of the product so that future potential customers can benefit from this experience. If a customer is unhappy with their product, they can reach out to customer service and explore their options. Some companies, like Amazon, allow customers to return their orders online, and a return label is automatically created for printing. The customer simply has to package the item and return it via Canada Post or another shipping company.

Case: MEC's Online Strategy and Growth in the Canadian Market

Photo by nicpix25216, CC BY-NC-ND 2.0

E-commerce has transformed the way businesses operate, and many Canadian companies have leveraged this technology to reach a wider audience and grow their businesses. One such company is MEC (Mountain Equipment Co-op), a retail cooperative, specializing in outdoor gear and clothing. MEC operates in the business-to-consumer (B2C) e-commerce model, selling its products directly to consumers through its website (MEC, 2021).

MEC's strategy is centred on offering customers a personalized online shopping experience. Its' website features a range of tools and services, including expert advice on product selection, and user-generated reviews. MEC's e-commerce platform also offers a variety of shipping options, including free shipping, and in-store pickup for online orders.

One of the advantages of e-commerce for MEC is the ability to reach a wider audience, especially in areas where it doesn't have a physical presence. It also allows MEC to offer a more extensive selection of products and services, such as outdoor guides and courses.

One of the challenges to e-commerce for MEC, is the high competition in the online retail space, making it difficult to stand out from other retailers and significant investments in technology to support online sales, which can be costly.

Despite these challenges, MEC has been successful in growing its e-commerce business, with online sales accounting for a significant portion of its revenue. In its most recent financial report, MEC reported that online sales accounted for 19.5% of its total revenue in the fiscal year 2020 (MEC 2020).

In conclusion, e-commerce has transformed the way businesses operate and as more consumers turn to online shopping, businesses that embrace e-commerce and develop effective online strategies will be well-positioned to succeed in the modern economy.

Winifred Ofure Badaiki, March 2023

13.6 E-COMMERCE TECHNOLOGY

An **e-commerce platform** is a way to build and create an online experience that allows a company to make sales and fulfill orders. While most people think an e-commerce platform is just a tool that provides a list of products and accepts payments online, a true e-commerce platform is much more than that. It is a complete business command center that controls everything from inventory to marketing. It should support basic requirements such as custom styling, search engine optimization, credit card processing, promotions, catalog management, analytics, product browsing, checkout, and order management. Some examples of e-commerce platforms are Shopify, Wix and BigCommerce.

To make an online store accessible to the public it requires a hosting solution. **Hosting** stores information on a server, which allows internet users to visit a company's site and view all of the content. Every website is hosted somewhere, meaning it has dedicated server space from a provider. Some e-commerce platforms have hosting built in, while others require self-hosting or open-source hosting.

Hosted	Some ecommerce website builders offer a hosted platform. Building on a hosted ecommerce platform provides freedom to focus on the business, and not the technology management of the site.
Self-hosted	Self-hosted platforms require companies to use their own server space or pay to rent space from a hosting provider. This makes ongoing website management complex, as you're responsible for updates, maintenance, and bug fixes. This requires a lot of internal resources that you could otherwise allocate elsewhere. Self-hosted platforms are typically open source, and you use a third party to host your website data. Third-party sourcing options charge fees for their services, and these costs quickly add up. Many times, these hosting services use tiered pricing structures, so those on the lowest plans don't get much in the way of customer support. This can leave you hanging at really important times, like traffic boosts after unexpected press coverage.

Instead of going with an e-commerce platform, businesses can also hire a full-service web developer to provide design, programming, support, hosting, search engine optimization, and more. Any combination of the services can be selected. Having the developer perform all the services would be the most expensive alternative. The ultimate cost for a website will be a function of its size, complexity, and the level of design. No two projects will cost the same. Part of the process of building a website, however, should be conducting some research and talking with website designers. The Internet offers a variety of sources on how to determine how much a website should cost. WebFX.com offers a historical perspective on website costs, a cost calculator to find out how much a web project would cost, and examples of specific web design and website development projects with cost figures. (WebFx, 2022).

Search Engine Optimization

It is important when creating a website to consider **search engine optimization (SEO)**. Search Engine Optimization (SEO) refers to the techniques that help a website rank high in organic search results (such as on Google and other search engines). There are the two types of listings that appear when using a search engine: organic search and paid search. SEO aims to make a website more visible to people looking for specific information or a particular product or service via search engine. SEO falls under the umbrella of **Search Engine Marketing** (SEM). SEM is a form of internet marketing that involves the promotion of websites by increasing their visibility in search engine result pages primarily through paid advertising.

Payment Methods

Security, privacy, and trust are most important when considering the payment function. Without this transaction, there is no e-commerce, so it is imperative that businesses take the necessary steps to reduce customer concerns about shopping online. It is also important for merchants to offer multiple payment methods to provide flexibility and ensure customers complete their purchase. See the following types of payment methods. Credit cards are by far the most popular payment method for online transactions.

Electronic Payment

E-payment is any payment done electronically. This form of payment includes debit cards, credit cards, gift cards, e-transfers, email payments, mobile wallets, and cryptocurrency.

e-Transfers

Electronic transfer or e-transfer is the ability to send money from your bank account held at a Canadian financial institution through the Interac Corporation. With e-transfers the sender logs-on to their bank account and chooses a recipient to send money to. The recipient's email or phone number is provided for notification of the transfer. A security question can be added so that only the recipient with the correct password can process the transaction. The popularity of e-transfers is growing with 57 percent of the country's population registering for the service by the end of 2018. Most e-transfers happen on mobile phones (Interact Corporation, 2021).

E-Mail based methods (PayPal)

PayPal is a form of an email based payment method where members are able to send money to any registered person. Registration requires the user to set up an account with their e-mail address. A notification is sent to those individuals who are to receive funds but are not registered. PayPal accounts are tied to the registrants credit card or bank account. Paypal also has a mobile application that can be used for contactless payment through the use of QR codes.

Mobile Wallets

A mobile wallet is an application on your mobile device that stores your payment information to allow for contactless payments. It is like a regular wallet where you keep your credit, debit or prepaid cards. You can use your mobile wallet when shopping in-person or online. Your financial institution or the merchant may set limits on how much money you can spend using a mobile wallet. There are concerns about how financial information is stored on mobile wallets, and what happens if you were to lose your phone. To learn more about Mobile Wallets and the safety of them, go to the information page by the Financial Consumer Agency of Canada. Some examples of mobile wallets in Canada are: Apple Pay, Google Pay, Samsung Pay.

13.7 E-COMMERCE PLATFORMS

Ecommerce Platforms

There are many ecommerce platforms in the marketplace today. These platforms make it easier for businesses to deliver Ecommerce to their clients. There are also many analysts each with opinions about which platform is the best and why. The following content is drawn from *The Balance Small Business*, an organization focused on exploring and advising about alternative Ecommerce platforms. It discusses three alternatives including one which will be used in this course for a key assignment where you will develop an Ecommerce site!

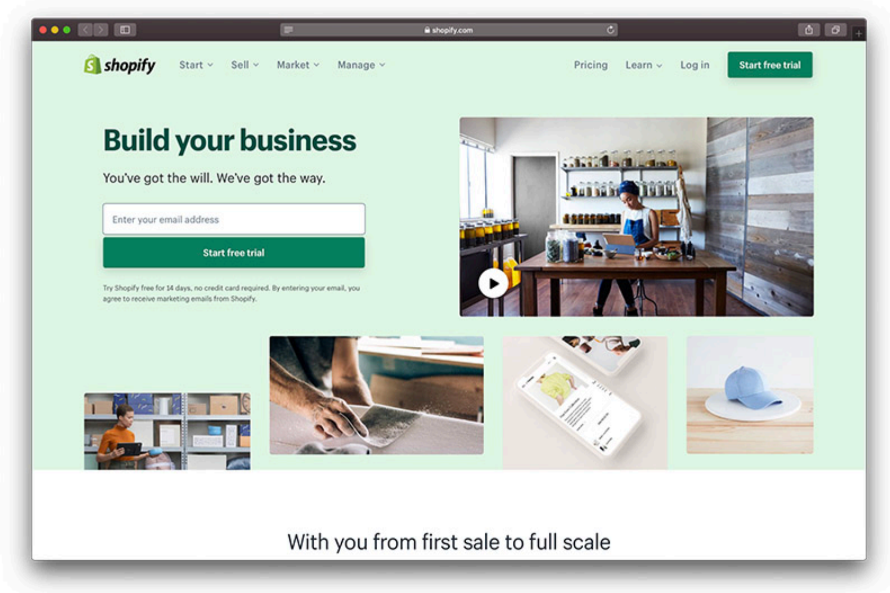
Best Ecommerce Platforms

The quest to discover the **best ecommerce platform** out there has been our ongoing goal here at ecommerce-platforms.com ever since the site was established. We invest real hours each week to test and examine each platform, all in an effort to find out how viable they are among the top ecommerce platforms in the market. We're doing all this testing so that you don't have to.

The resource you're reading right now is a summary of our findings + how to pick the perfect ecommerce solution for your individual needs!

No time to read? Here's our no.1 pick when it comes to the absolute **best ecommerce platform** in the market:

Shopify is the most flexible, feature-rich and **the most complete ecommerce platform** of the bunch. Out the box, it already offers everything you might need to run an effective store, and also lets you customize your design and add various feature extensions. You can also sell pretty much whatever you wish, including physical products, digital products and downloads, services, and even do drop-shipping.



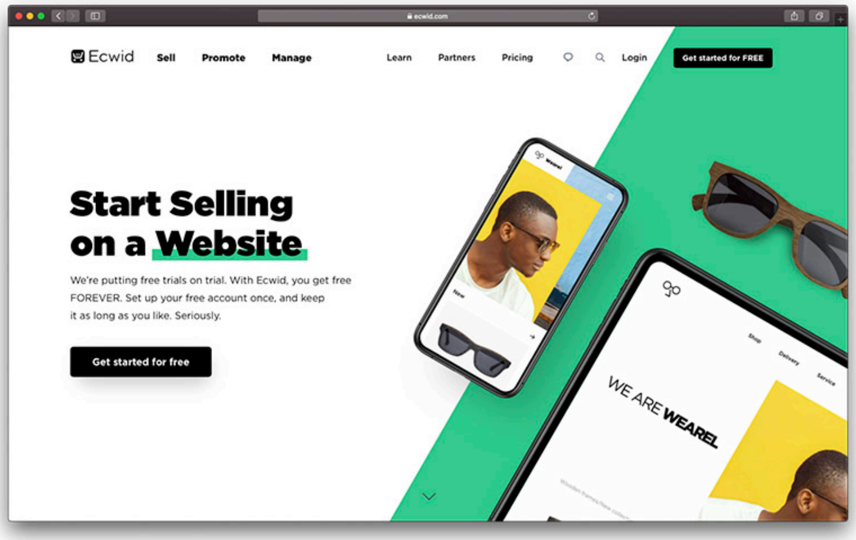
All of that starting at the price of $29 / month, or as low as $9 / month if you're okay with not having an online storefront but instead selling via social media and other channels. I wouldn't have a problem recommending this platform to anyone looking to get started in the ecommerce industry.

Overall rating: 10/10

BUDGET PICK

Ecwid

Ecwid is the only sensible free option in the market right now. Though, it's not without flaws. Chiefly, you don't get any interchangeable themes/designs for your store – you can only adjust the stock design by changing fonts, colours, etc. There's also no support on the free plan, and you can only have up to 10 products.



It might be a good place to start for some online stores. However, once your store gets off the ground and starts earning money, you're probably still better off switching to a different platform.

Overall rating: 7/10

As hard as it might be to believe, there are over 120 different shopping cart software platforms out there, and they all have their place in the market. We should know, after all, our work is to test them all out. And we've been doing that … a lot. So far, we've covered each of the top platforms in individual reviews plus created a comprehensive comparison chart looking through the most crucial traits of each platform. We've also ranked all platforms based on their SEO effectiveness.

What you're reading here is an all-in-one summary of which is the **best ecommerce platform**, plus what makes each of the contenders great. After reading this guide, **you will know exactly how to pick the right ecommerce solution for your store.**

Here are the best ecommerce platforms that we're testing

1. Shopify
2. BigCommerce
3. Ecwid
4. Volusion
5. 3dcart
6. Big Cartel

(Karol, 2020)

13.8 BLOCKCHAIN AND BITCOIN

Blockchain

Blockchain is a peer-to-peer network which provides an open, distributed record of transactions between two parties. A peer-to-peer (P2P) network is one where there is no server between the two nodes trying to communicate. Essentially, this means that each node acts as a server and a client.

Supporters see blockchain as a tool to simplify all types of transactions: payments, contracts, etc. Motivation comes from the desire to remove the middleman (lawyer, banker, broker) from transactions, making them more efficient and readily available across the internet. Blockchain is already being used to track products through supply chains. Blockchain is considered a foundational technology, potentially creating new foundations in economics and social systems. There are numerous concerns about Blockchain and its adoption. Consider the following:

- **Speed of adoption**. Initially there is a great deal of enthusiasm by a small group. However, adoption on a larger scale can take a great number of years even decades for a worldwide acceptance of a new method of doing business.
- **Governance**. The banking sector, both in individual countries (Bank of Canada and U. S. Federal Reserve System) and the world at large (the International Monetary Fund-IMF), controls financial transactions. One purpose of these organizations is an attempt to avoid banking and financial systems collapse. Blockchain will result in the governance of financial transactions shifting away from these government-controlled institutions.
- **Smart contracts**. The smart contract will re-shape how businesses interact. It is possible for blockchain to automatically send payment to a vendor the instant the product is delivered to the customer. Such "self-executing" contracts are already taking place in banking and venture capital funding (Iansiti & Lakhani, 2017).

Many are forecasting some universal form of payment or value transfer for business transactions. Blockchain and Bitcoin are being used to transform banking in various locations around the world.

Bitcoin

“Bitcoin Logo” by D. Bourgeois, CC BY-NC 4.0

Bitcoin is a form of digital currency sometimes referred to as a cryptocurrency which is a new form of money that is tradable throughout the world. It operates without the involvement of central banks or a clearinghouse and runs as a P2P network. Bitcoins can be transferred between individuals or between businesses to pay for goods and services, all without the use of a bank, so the fees for that exchange are lower. Bitcoins do have value and, as such, are subject to taxation just as with cash in your local currency. Records for transactions are recorded in the blockchain.

Advantages of Using Bitcoin

Some of the advantages of using Bitcoin over another online payment network, such as PayPal, or even your bank, are:

- It can be used in any country without the need for currency conversion;
- Sending money to a business or individual costs less per transaction;
- There are no limits to the number of transactions you can initiate each month;
- Your account cannot be frozen or suspended;
- Transactions are irreversible, unlike PayPal payments; and
- You can keep Bitcoins in a digital wallet that is accessible from your phone, tablet, or computer.

Several of these advantages exist because there is no central governing authority, as there is with a bank. Of course, that may also be a disadvantage. Bitcoin is still considered “experimental,” even by the organization itself, so be aware that there are also risks involved in accepting Bitcoins in place of cash. Bitcoin began trading in 2009.

Another potential advantage is that the fee to transfer Bitcoins from one person or business to another is unrelated to the amount being transferred. Unlike other payment networks that charge a percentage of the transaction value, Bitcoin charges based on the ability to reverse the transaction – the easier to cancel, the lower the fee.

That is, a Bitcoin transaction takes an average of 10 minutes to be resolved – 90 minutes at the most. During that process, there are confirmations that occur that the transfer of Bitcoins is occurring. The fewer the number of confirmations requested – you can request zero – the lower the fee to send coins; there is never a fee to receive Bitcoins. But you can also request as many as 36 confirmations to be absolutely sure that once the Bitcoins are in your account, they cannot leave without your permission.

This can be especially useful when selling expensive goods. On some payment networks, a buyer can claim to have an issue with an order and almost immediately receive a refund, even without your input. This would not happen with Bitcoins – once the payment is in your account, it is yours to keep.

Tanzania Bitcoin Project

A major bitcoin project is underway in Tanzania. Business transactions in this East African country are fraught with many challenges such as counterfeit currency and a 28% transaction fee on individuals who do not have a bank account. Seventy percent of the country's population fall into this category. Benjamin Fernandes, a Tanzanian and 2017 graduate of Stanford Graduate School of Business, is co-founder of NALA, a Tanzanian firm working to bring cryptocurrency to a country where 96% of the population have access to mobile devices. NALA's goal is to provide low cost transactions to all of the country's citizens through cryptocurrency (Fernandes, 2017).

13.9 TRENDS

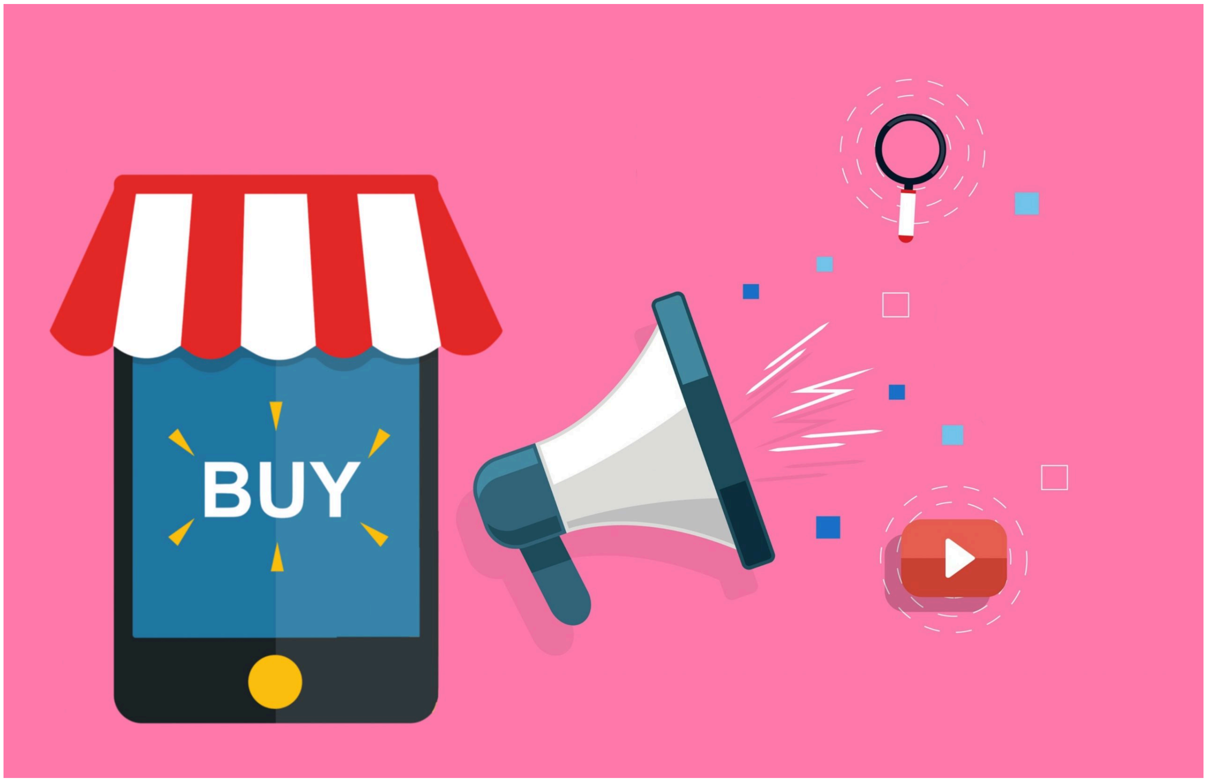


Photo by Mohamed Hassan, CCO 1.0

Social Commerce

Social factors—our attitudes, values, ethics, and lifestyles—influence what, how, where, and when people purchase products or services. However, they can be difficult to predict, define, and measure making the job of marketing more challenging. Social networks are changing that as customers are providing larges amounts of information about themselves and their preferences online for digital advertisers to mine and collect.

Online **social networks** provide a platform for people to connect with each other and share information. Facebook, Instagram, Twitter, LinkedIn and TikTok are all examples of online social networks that allow for the exchange of information. These platforms are valuable to the users, but can also be valuable for businesses. They provide insight into customer behaviour that can help direct business strategy, and also be used to market goods and services. According to Gartner, 74% of consumers rely on social networks to guide purchase decisions (Gartner UK Ltd, 2010).

This is referred to as **social commerce** where online social networks are utilized to promote the sale of goods and services. Social commerce provides a means for interactive shopping, including reviews, ratings, and social shopping websites where you can chat with merchant personnel or with friends while you are shopping.

Benefits of Social Commerce

Just like m-commerce, there are certain benefits that s-commerce has over traditional eCommerce. These include:

Audience Growth	As of January 2017, over 2.7 billion people were on social media. This is more than a third of the global population. This number is also up over 20% from 2016. A tremendous growth, with little sign of slowing down (Chaffey, 2017). One of the most important considerations for any e-commerce business is how to reach and sell to its target customer audience, and from these statistics it is safe to say that a large proportion of any brand's market is on social media.
Higher Search Ranking	Using social media for s-commerce increases traffic to your website which will influence your ranking on search engine results. It also allows your audience to engage with a product, like or share it, and to reach an even larger audience.
Authentic Engagement	The most significant benefit of using social media for s-commerce is the engagement and reach that businesses can get whenever they share content. By appearing in followers' updates or feeds on a regular basis, you're participating in a powerful branding opportunity. Operating on social media encourages users to connect with a business through two-way communication. This allows customers to not only engage with your business on a commercial level, but it also gives them the opportunity to use social media as an efficient customer service channel where it's possible to solve problems. Social media word-of-mouth (sharing/ reposting) helps with audience building, as well as increased engagement and website traffic.
Customer Loyalty	S-commerce is not purely focused on selling but uses the social platforms to help the business build relationships with potential and existing customers. Such relationships can deepen trust and loyalty between consumers and the brand. This in turn creates happy, satisfied customers, who will likely be customers who make repeat purchases, i.e. a loyal customer.
Analytics	Social media platforms make it easy to track, measure and evaluate conversions that happen through s-commerce. Facebook, Twitter, Instagram, Pinterest and LinkedIn all offer built-in analytics tools for measuring traffic, clickthrough, fans/followers, likes, sentiment and actual conversions coming via the social platform. This is a huge benefit for monitoring your ROI.

Social Media Marketing

As more and more people around the planet become connected through social media, the influence of these channels continues to grow. In response, organizations are allocating more of their promotion budgets to social media. This makes sense when social media strategies align with broader marketing strategies in support of corporate objectives.

When used effectively, social media marketing can generate a lot of buzz without a lot of expense. There are still costs associated with content creation, but the proliferation of online content creators and hungry media outlets means that on social media, content tends to be cheap. The 24-7 cycle of global social media requires eyes, brains and analytical tools to stay on top of everything happening, but never before has it been so easy to tap into, listen and learn from individuals and communities interacting with your product or brand. It is undoubtedly exciting for your brand to become a trending topic among these networks, but it is important to remember social media attention can easily veer into positive or negative territory. Absolute control of the message is virtually impossible with social media. Managing consumer perceptions requires attention and perseverance.

Because many people share immense amounts of information about themselves through social media, increasingly marketers can use this information to deliver highly targeted messages and offers. Navigational click-stream data from social media and other websites is another source of valuable information about consumer behaviour, what makes them tick, and how they do or don't choose to engage with your brand. At the same time, firms must be prepared to address increasingly complex challenges associated with cybersecurity and data privacy.

New Retail

New Retail is a term that was coined by Alibaba's Jack Ma which is defined as an "integrated retail delivery model where offline, online, logistics, and data, converge to enhance customer experience" (Medium Predict, 2021). Essentially this means that the boundary between offline and online commerce disappears. A way that an online store can create a physical presence is through a pop-up shop, or creating a partnership with other retailers where physical displays are set up. Companies can digitize their supply chain by offering the ability to buy online and pick up in store. Some companies have also explored the options of using digital ordering within physical stores for products that customers would like to see and touch. New retail is really about leveraging technology to make the process of shopping seamless whether you are instore or online.

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13.11 KEY TERMS

Key Terms

A Mobile Wallet: Is an application on your mobile device that stores your payment information to allow for contactless payments. It is like a regular wallet where you keep your credit, debit or prepaid cards. You can use your mobile wallet when shopping in person or online. 13.6

Best E-commerce Platform: Out there has been our ongoing goal here at e-commerce-platforms.com ever since the site was established. We invest real hours each week to test and examine each platform, all in an effort to find out how viable they are among the top e-commerce platforms in the market. We're doing all this testing so that you don't have to. 13.6

Bitcoin: This is a form of digital currency sometimes referred to as a cryptocurrency which is a new form of money that is tradable throughout the world. It operates without the involvement of central banks or a clearinghouse and runs as a P2P network. 13.7

Blockchain: Is a peer-to-peer network which provides an open, distributed record of transactions between two parties. A peer-to-peer (P2P) network is one where there is no server between the two nodes trying to communicate. Essentially, this means that each node acts as a server and a client. 13.7

Brick-and-Click Businesses: Such as Indigo and Canadian Tire, combine a physical presence with an online presence. These businesses use the Internet to supplement their existing businesses (Krishnamurthy, 2003). 13.4

Broadband: Technology and lowering data costs mean more consumers have access to m-commerce even on affordable devices and data plans. 13.4

Business to Business (B2B): When a business sells a good or service to another business. For example, a business that sells software-as-a-service for other businesses to use, or Staples selling office supplies. This is the largest form of e-commerce 13.4

Business to Consumer (B2C): When a business sells a good or service to an individual consumer. For example, when you buy a pair of shoes from an online retailer like Nike. 13.4

Business to Government (B2G): Defined as e-commerce transactions with the government. The internet is used for procurement, filing taxes, licensing procedures, business registrations, and other government-related operations. This is an insignificant segment of e-commerce in terms of volume, but it is growing. 13.4

Consumer to Business (C2B): When a consumer sells their own products or services to a business or organization. For example, an influencer offers exposure to their online audience in exchange for a fee, or a photographer licenses their photo for a business to use. 13.4

Consumer to Consumer (C2C): When a consumer sells a good or service to another consumer. The most well-known C2C is eBay, but there are many other online market providers as well, like Kijiji or Craigslist. Peer-to-peer (P2P) is also a form of consumer-to-consumer. See more about P2P below. 13.4

Consumer to Government (C2G): Defined as e-commerce transactions between the government and individuals. This would involve licenses and registrations, and paying taxes. 13.4

Crowdfunding: The collection of money from consumers in advance of a product being available in order to raise the startup capital necessary to bring it to market. Example: Kickstarter 13.5

Demand Risk: Sharply changing demand or the collapse of markets poses a significant risk for many firms. The web can be used to diversify a business by taking new products to new markets. 13.3

Digital Products: Downloadable digital goods, templates, courses, or media that must be purchased for consumption or licensed for use. For example, maybe you take a digital course online through LinkedIn Learning. 13.5

Dropshipping: The sale of a product, which is manufactured and shipped to the consumer by a third party. 13.5

E-commerce Business Model: This is the method that a business uses to generate revenue online. E-commerce can take on a variety of forms involving different transactional relationships between businesses and consumers. 13.5

E-commerce Platform: This is a way to build and create an online experience that allows a company to make sales and fulfill orders. 13.6

E-payment: Is any payment done electronically. This form of payment includes debit cards, credit cards, gift cards, e-transfers, email payments, mobile wallets, and cryptocurrency. 13.6

Electronic Business or E-business: In a broad sense, is the use of computer networks to improve organizational performance. Increasing profitability, gaining market share, improving customer service, and delivering products faster are some of the organizational performance gains possible by doing business electronically. E-business is more than ordering goods online, it involves all aspects of an organization's electronic interactions with its stakeholders. 13.1

Electronic Transfer or E-Transfer: This is the ability to send money from your bank account held at a Canadian financial institution through the Interac Corporation. With e-transfers, the sender logs on to their bank account and chooses a recipient to send money to. 13.6

Governance: The banking sector, both in individual countries (Bank of Canada and U. S. Federal Reserve System) and the world at large (the International Monetary Fund-IMF), controls financial transactions. 13.4

Financial Systems Collapse: Blockchain will result in the governance of financial transactions shifting away from these government-controlled institutions. 13.7

Hosted: Some e-commerce website builders offer a hosted platform. Building on a hosted e-commerce platform provides freedom to focus on the business and not the technology management of the site. 13.6

Hosting: Stores information on a server, which allows Internet users to visit a company's site and view all of the content. Every website is hosted somewhere, meaning it has dedicated server space from a provider. Some e-commerce platforms have hosting built-in, while others require self-hosting or open-source hosting. 13.6

Improved Technology: Has given mobile devices advanced capabilities and faster internet access enabling m-commerce to be available on even the most affordable devices. 13.4

Inefficiency Risk: Failure to match competitors' unit costs–inefficiency risk. The internet can help reduce operating costs, such as information distribution. 13.3

Innovation Risk: Not being adaptable, can lead to stagnation, and ultimately failure to remain competitive. Businesses need to be open to new ideas, and these ideas can come from customers. The internet allows communication with customers for this purpose. 13.3

Instant Gratification Online: This includes their online shopping needs. An increase in m-commerce for fast food, fresh produce and basic household items has been driven by this need for customers to get what they need when and where they want it. 13.4

Number of Global Mobile Users: This is steadily increasing: every year, resulting in an increased demand for mobile websites and applications. 13.4

Physical Products: Any tangible good that requires inventory to be replenished and orders to be physically shipped to customers as sales are made 13.5

Pure-Play Business: Such as Amazon and Well.ca, has an online presence only and uses the capabilities of the internet to create a new business. 13.4

Rapid Adoption of E-commerce: Means that evolving customers are looking for more options across more devices. 13.4

Retail: The sale of a product by a business directly to a customer without any intermediary. 13.5

Search Engine Marketing (SEM): SEM is a form of internet marketing that involves the promotion of websites by increasing their visibility in search engine result pages primarily through paid advertising. 13.6

Search Engine Optimization (SEO): Search Engine Optimization (SEO) refers to the techniques that help a website rank high in organic search results (such as on Google and other search engines). 13.6

Self-Hosted: Require companies to use their own server space or pay to rent space from a hosting provider. This makes ongoing website management complex, as you're responsible for updates, maintenance, and bug fixes. This requires a lot of internal resources that you could otherwise allocate elsewhere. Self-hosted platforms are typically open-source, and you use a third party to host your website data. 13.6

Services: A skill or set of skills provided in exchange for compensation. The service provider's time can be purchased for a fee. 13.5

Smart Contracts: The smart contract will re-shape how businesses interact. It is possible for blockchain to automatically send payment to a vendor the instant the product is delivered to the customer. Such "self-executing" contracts are already taking place in banking and venture capital funding (Iansiti & Lakhani, 2017). 13.7

Social Commerce: Where online social networks are utilized to promote the sale of goods and services. Social commerce provides a means for interactive shopping, including reviews, ratings, and social shopping websites where you can chat with merchant personnel or with friends while you are shopping. 13.9

Social Networks: Provide a platform for people to connect with each other and share information. Facebook, Instagram, Twitter, LinkedIn and TikTok are all examples of online social networks that allow for the exchange of information 13.9

Speed of Adoption: Initially there is a great deal of enthusiasm by a small group. However, adoption on a larger scale can take a great number of years even decades for a worldwide acceptance of a new method of doing business. 13.7

Subscription: The automatic recurring purchase of a product or service on a regular basis until the subscriber chooses to cancel. Examples: newspaper subscriptions, music streaming sites (Spotify) 13.5

Transaction Brokers: Companies who facilitate a transaction and take a portion of the revenue. Example Airbnb, Eventbrite 13.5

Wholesale: The sale of products in bulk, often to a retailer that then sells them directly to consumers. 13.5

CHAPTER 14: EMERGING TECHNOLOGY

Chapter Outline

14.0 CHAPTER INTRODUCTION

Learning Outcomes

After reading this section, students should be able to:

1. Describe the difference between the Internet and World Wide Web.
2. Discuss the history of artificial intelligence.
3. Define artificial intelligence and distinguish between the types.
4. Explain autonomous and extended reality technologies.
5. List some of the emerging technology trends and their impact on business.

Information systems have evolved at a rapid pace ever since their introduction in the 1950s. Today devices that you can hold in one hand are more powerful than the computers used to land a man on the moon in 1969. The last 10 years has seen the proliferation of intelligent devices, devices that can process information and make suggestions or provide responses. How does Netflix seem to know what types of programs or movies we like? How does Amazon post product displays to our account that sparks our interest? How does YouTube seem to provide video feeds that align with what we have previously watched and protect younger viewers from harmful content? This is achieved through artificial intelligence using algorithms and machine learning.

Artificial Intelligence (AI) is changing the way companies do business through improved data analytics, productivity, and efficiencies. AI uses software algorithms to simulate human intelligence processes such as reasoning and speaking within computers and other IoT devices. AI simulates human intelligence processes through robotics, intelligent agents, expert systems, algorithms, and natural-language processing. This chapter will provide an introduction to artificial intelligence and provide some examples of how businesses are leveraging this technology.

14.1 THE INTERNET

The **internet** is a network of networks—millions of them, actually. If the network at your university, your employer, or your home has internet access, it connects to an **internet service provider** (ISP). Many, but not all, ISPs are big telecommunications companies like Rogers Communications, Bell Canada, or Telus Inc . These providers connect to one another, exchanging traffic, and ensure your messages get to other computers that are online and willing to communicate with you.

The internet has no centre and no one owns it. That's a good thing. The internet was designed to be redundant and fault-tolerant—meaning that if one network, connecting wire, or server stops working, everything else should keep on running. Rising from military research and work at educational institutions dating as far back as the 1960s, the internet really took off in the 1990s, when graphical web browsing was invented. Much of the internet's operating infrastructure was transitioned to be supported by private firms rather than government grants. We will now explore this history in more detail.

History of the Internet

In the Beginning: ARPANET

The story of the internet, and networking in general, can be traced back to the late 1950s. The United States was in the depths of the Cold War with the USSR as each nation closely watched the other to determine which would gain a military or intelligence advantage. In 1957, the Soviets surprised the U.S. with the launch of Sputnik, propelling us into the space age. In response to Sputnik, the U.S. Government created the Advanced Research Projects Agency (ARPA), whose initial role was to ensure that the U.S. was not surprised again. It was from ARPA, now called DARPA (Defense Advanced Research Projects Agency), that the internet first sprang.

ARPA was the centre of computing research in the 1960s, but there was just one problem. Many of the computers could not communicate with each other. In 1968 ARPA sent out a request for proposals for a communication technology that would allow different computers located around the country to be integrated together into one network. Twelve companies responded to the request, and a company named Bolt, Beranek, and Newman (BBN) won the contract. They immediately began work and were able to complete the job just one year later.

ARPA Net 1969

Professor Len Kleinrock of UCLA along with a group of graduate students were the first to successfully send a transmission over the ARPANET. The event occurred on October 29, 1969 when they attempted to send the word "login" from their computer at UCLA to the Stanford Research Institute. The first four nodes were at UCLA, University of California, Stanford, and the University of Utah.

Fig 14.1 Adapted from "ARPA Net Nodes 1969" by D.Bourgeois CC BY-NC 4.0

The Internet

Over the next decade, the ARPANET grew and gained popularity. During this time, other networks also came into existence. Different organizations were connected to different networks. This led to a problem. The networks could not communicate with each other. Each network used its own proprietary language, or protocol to send information back and forth. A **protocol** is the set of rules that govern how communications take place on a network. This problem was solved by the invention of the **Transmission Control Protocol/ Internet Protocol (TCP/IP).** TCP/IP was designed to allow networks running on different protocols to have an intermediary protocol that would allow them to communicate. So as long as your network supported TCP/IP, you could communicate with all of the other networks running TCP/IP. TCP/IP quickly became the standard protocol and allowed networks to communicate with each other.

The 1980s witnessed a significant growth in internet usage. Internet access came primarily from government, academic, and research organizations. Much to the surprise of the engineers and developers, the early popularity of the internet was driven by the use of electronic mail. People connecting with people was the killer app for the internet.

The World Wide Web

Initially, internet use meant having to type commands, even including IP addresses, in order to access a web server. That all changed in 1990 when Tim Berners-Lee introduced his **World Wide Web** project which provided an easy way to navigate the internet through the use of hypertext. The World Wide Web gained even more steam in 1993 with the release of the Mosaic browser which allowed graphics and text to be combined as a way to present information and navigate the internet. Many times the terms "Internet" and "World Wide Web," or even just "the web," are used interchangeably. But really, they are not the same thing.

The Internet and the Web – What's the Difference?

The internet is an interconnected network of networks. Services such as email, voice and video, file transfer, and the World Wide Web (the web for short) all run across the internet. The web is simply one part of the internet. It is made up of web servers that have HTML pages that are being viewed on devices with web browsers. To see an interactive map of the world's major submarine cable systems go to TeleGeography's Submarine Cable Map. A snapshot of the interactive map can be seen below.

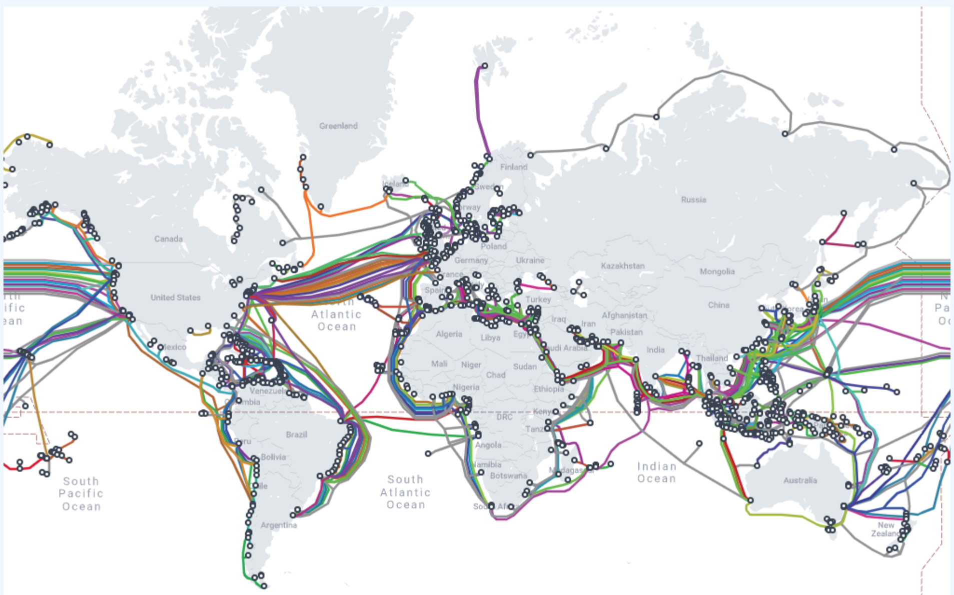


Fig 14.2
"Submarine Cable Map" by TeleGeography, CC BY-NC-SA 3.0

The Dot-Com Bubble

In the 1980s and early 1990s, the internet was being managed by the National Science Foundation (NSF). The NSF had restricted commercial ventures on the internet, which meant that no one could buy or sell anything online. In 1991, the NSF transferred its role to three other organizations, thus getting the US government out of direct control over the internet and essentially opening up commerce online.

This new commercialization of the internet led to what is now known as the dot-com bubble. A frenzy of investment in new dot-com companies took place in the late 1990s with new tech companies issuing Initial Public Offerings (IPO) and heating up the stock market. This investment bubble was driven by the fact that investors knew that online commerce would change everything. Unfortunately, many of these new companies had poor business models and anemic financial statements showing little or no profit. In 2000 and 2001, the bubble burst and many of these new companies went out of business. Some companies survived, including Amazon (started in 1994) and eBay (1995). After the dot-com bubble burst, a new reality became clear. In order to succeed online, e-business companies would need to develop business models appropriate for the online environment.

The Generations of the Web

In the first few years of the web, creating and hosting a website required a specific set of knowledge. A person had to know how to set up a web server, get a domain name, create web pages in HTML, and troubleshoot various technical issues. Since then the web has evolved. This evolution has been referred to as different phases.

- **Web 2.0** is also referred to as the social web and occurred between 2000-2010. During this time there was a shift from read only to read and write, which allowed individuals to be content creators. Social networking with apps such as Facebook, Twitter, YouTube, and personal blogs have allowed people to express their own view points and share content.
- **Web 3.0** is also referred to as the semantic web and is the time after 2010 when the web evolved again to allow individuals to read, write and execute. This means that the web is more intelligent and is able to interact with users. For example, algorithms that can personalize search results.
- **Web 4.0** is the future of the web, which is referred to as the intelligent web and will involve the Internet of Things and connected devices.

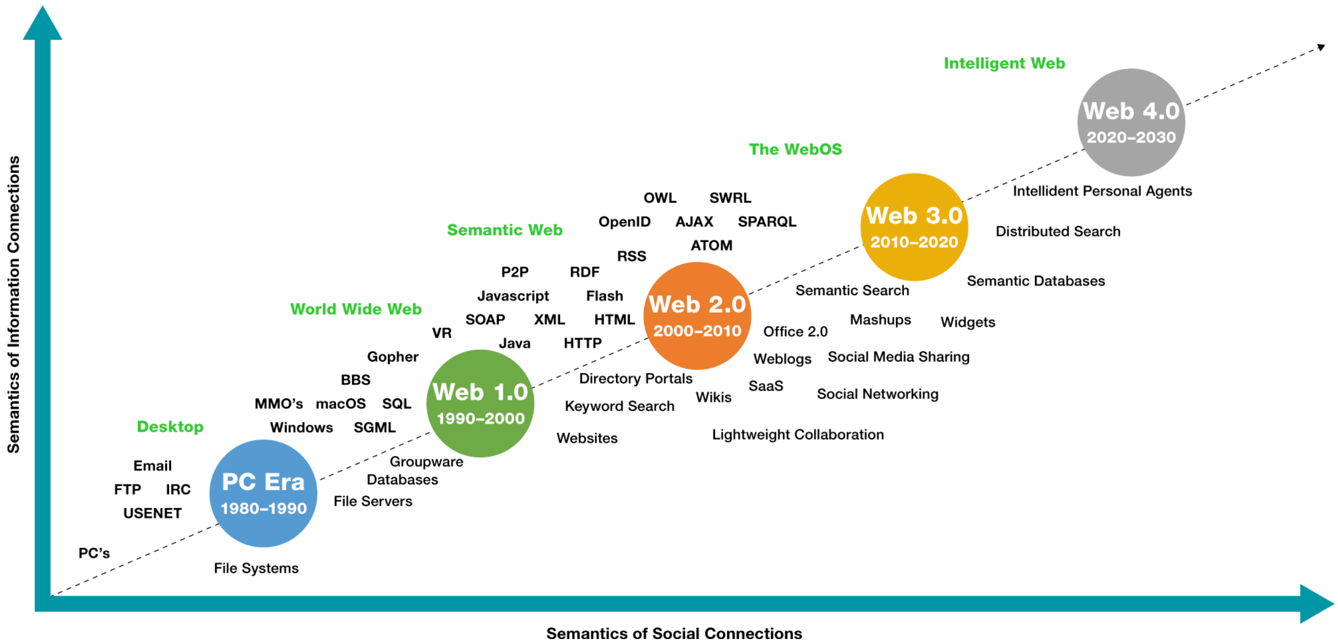


Fig 14.3 Phases of the Web (Click to enlarge)

There's Another Internet?

Internet2 is a research network created by a consortium of research, academic, industry, and government firms. These organizations have collectively set up a high-performance network running at speeds of up to one hundred gigabits per second to support and experiment with demanding applications. Examples include high-quality video conferencing; high-reliability, high-bandwidth imaging for the medical field; and applications that share huge data sets among researchers.

14.2 CAN MACHINES THINK?

Artificial intelligence, the ability of a computer or machine to think and learn, and mimic human behaviour became the focus of many in the 1950s. Alan Turing, a young British polymath, explored the mathematical possibility of artificial intelligence. Turing suggested that humans use available information as well as reason in order to solve problems and make decisions, so why can't machines do the same thing? This was the logical framework of his 1950 paper, Computing Machinery and Intelligence in which he discussed how to build intelligent machines and how to test their intelligence.

The Turing Test: Can Machines Think?

The Turing Test (referred to as the imitation game by Turing) was a test to determine whether or not a judge could be convinced that a computer is human. In the test, a human judge engages in a natural language conversation with a human and a machine asking questions of both. All participants are separated from one another, and the human and machine provide written responses to the questions. If the judge cannot reliably tell the machine from the human (imitating human behaviour), the machine is said to have passed the test, and therefore have the ability to think. There have been criticisms of the test, and Turing responded to some. He stated that he did not intend for the test to measure the presence of "consciousness" or "understanding", as he did not believe this was relevant to the issues that he was addressing. The test is still referred to today.

However the test could not be executed as at the time computers lacked a key prerequisite for intelligence: they couldn't store commands, only execute them. In other words, computers could be told what to do but couldn't remember what they did. As well, computing was extremely expensive. In the early 1950s, the cost of leasing a computer ran up to $200,000 a month.

Five years later, the proof of concept was initialized through Allen Newell, Cliff Shaw, and Herbert Simon's, *Logic Theorist*. The Logic Theorist was a program designed to mimic the problem solving skills of a human and was funded by Research and Development (RAND) Corporation. It's considered by many to be the first artificial intelligence program and was presented at the *Dartmouth Summer Research Project on Artificial Intelligence* (DSRPAI) in 1956. In this historic conference, John McCarthy, imagining a great collaborative effort, brought together top researchers from various fields for an open ended discussion on artificial intelligence, the term which he coined at the very event. Sadly, the conference fell short of McCarthy's expectations; people came and went as they pleased, and there was failure to agree on standard methods for the field. Despite this, everyone whole-heartedly aligned with the sentiment that AI was achievable. The significance of this event cannot be undermined as it catalyzed the next twenty years of AI research.

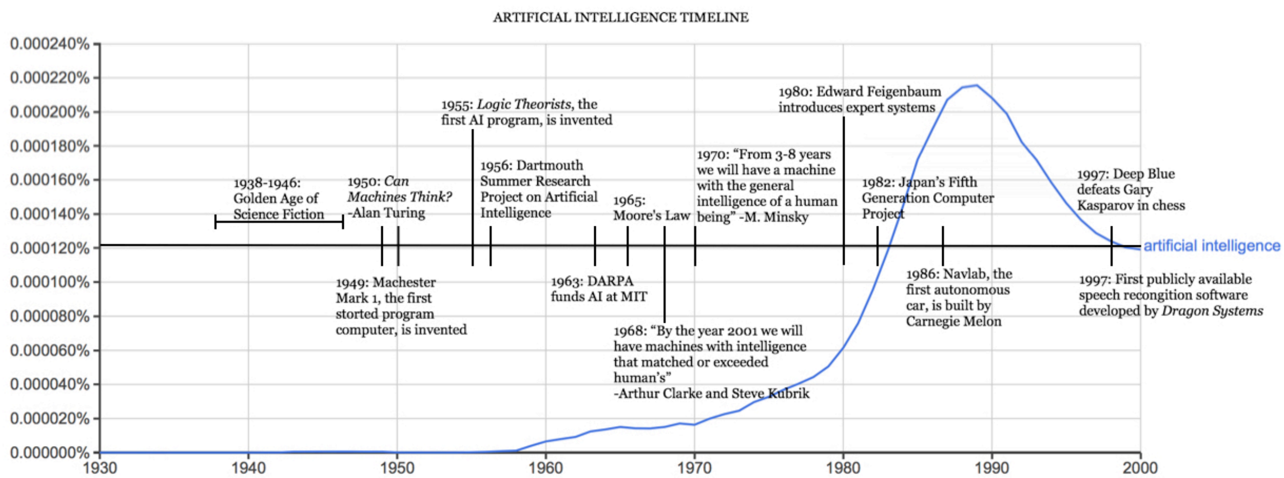


Fig 14.4 "Artificial Intelligence Timeline" by Rockwell Anyoha & SITN Boston, CC BY-NC-SA 4.0

From 1957 to 1974, AI flourished. Computers could store more information and became faster, cheaper, and more accessible. Machine learning algorithms also improved and people got better at knowing which algorithm to apply to their problem. Early demonstrations such as Newell and Simon's *General Problem Solver* and Joseph Weizenbaum's *ELIZA* showed promise toward the goals of problem solving and the interpretation of spoken language respectively. These successes, as well as the advocacy of leading researchers (namely the attendees of the DSRPAI) convinced government agencies such as the Defense Advanced Research Projects Agency (DARPA) to fund AI research at several institutions. The government was particularly interested in a machine that could transcribe and translate spoken language as well as high throughput data processing. While the basic proof of principle was there, there was still a long way to go before the end goals of natural language processing, abstract thinking, and self-recognition could be achieved.

14.3 AI EVOLUTION

AI was reignited in the 1980's by two sources: an expansion of the algorithmic toolkit, and a boost of funds. John Hopfield and David Rumelhart popularized "deep learning" techniques which allowed computers to learn using experience. On the other hand Edward Feigenbaum introduced expert systems which mimicked the decision making process of a human expert. The program would ask an expert in a field how to respond in a given situation, and once this was learned for virtually every situation, non-experts could receive advice from that program.

Expert systems were widely used in industries. The Japanese government heavily funded expert systems and other AI related endeavours as part of their *Fifth Generation Computer Project* (FGCP). From 1982-1990, they invested $400 million dollars with the goals of revolutionizing computer processing, implementing logic programming, and improving artificial intelligence. Unfortunately, most of the ambitious goals were not met. However, it could be argued that the indirect effects of the FGCP inspired a talented young generation of engineers and scientists. Regardless, funding of the FGCP ceased, and AI fell out of the limelight.

During the 1990s and 2000s, many of the landmark goals of artificial intelligence had been achieved. In 1997, reigning world chess champion and grand master Gary Kasparov was defeated by IBM's *Deep Blue*, a chess playing computer program. This highly publicized match was the first time a reigning world chess champion lost to a computer and served as a huge step towards an artificially intelligent decision making program. In the same year, speech recognition software, developed by Dragon Systems, was implemented on *Windows*. This was another great step forward but in the direction of the spoken language interpretation endeavour. It seemed that there wasn't a problem machines couldn't handle. Even human emotion was fair game as evidenced by Kismet, a robot developed by Cynthia Breazeal that could recognize and display emotions. in 2017, Google's *Alpha Go* was able to defeat Chinese Go champion Ke Jie.

The Future: A Cautionary Approach?

The application of artificial intelligence in the age of Big Data has been successful in several industries such as technology, banking, marketing, and entertainment. We've seen that even if algorithms don't improve much, big data and massive computing simply allow artificial intelligence to learn through brute force. The advancement in this technology also raises questions with respect to governance and regulations to its development. Concerns over ethical and privacy issues along with military development and deployment are among some issues to consider.

14.4 AI CATEGORIES

Now that we have explored the evolution of artificial intelligence and it is predictions for the future we will delve deeper into the types of AI and its applications. Artificial intelligence can be categorized in a number of ways based on ability and functionality.

Based on Ability

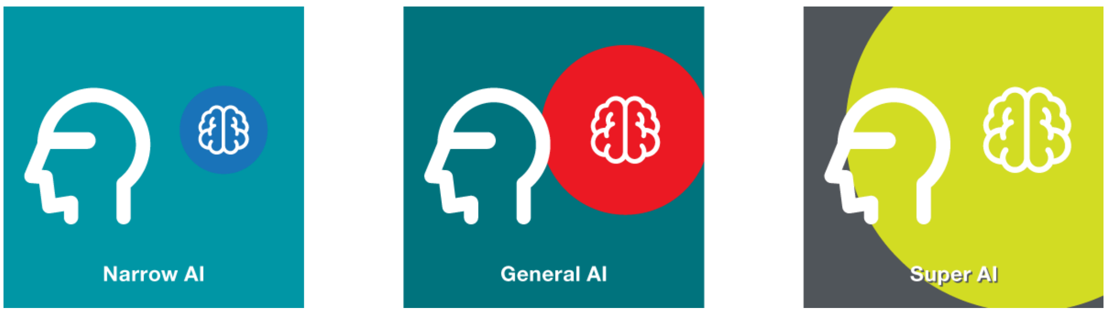


Fig 14.5 Categories of Artificial Intelligence Based on Ability

Narrow AI	Also referred to as artificial narrow intelligence (ANI) or weak AI is a computer's ability to perform a single task well. This is the type of AI we see today. Natural language processing used in smart assistants like Siri and Google are examples of narrow AI.
General AI	Also referred to as artificial general intelligence (AGI) or strong AI is where artificial intelligence is the same as human intelligence. It means that machines have the ability to apply what they have learned across different tasks, take in new information, and apply reason.
Super AI	Also referred to as artificial super intelligence (ASI) is when the computer will be exceed human capabilities.

Based on Functionality

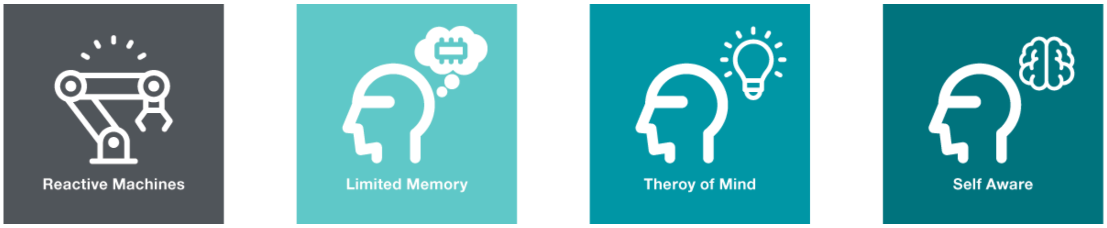


Fig 14.6 Categories of Artificial Intelligence Based on functionality

Reactive Machines	AI that conducts tasks for specific objectives. It is the first step of any AI system where no learning takes place. An example of this type of AI is Deep Blue the IBM program that beat chess champion Garry Kasparov.
Limited Memory	Is the ability of AI to use past experience and information to make predictions.
Theory of Mind	AI with the awareness that others have their own beliefs, objectives, and intentions. This type of AI is not yet developed and will be able to distinguish and understand emotion.
Self-Aware	AI with the sense of self and consciousness. This type of AI is not yet developed.

Applications of AI

There are a number of applications. See the list below.

Automation	The use of machines, control systems and information technologies to optimize productivity in the production of goods and delivery of services (automation, n.d.).
Robots	The use of machines to perform tasks traditionally done by humans.
Intelligent Agents	The use of software to perform specific tasks.
Expert Systems	Aim to emulate the human ability to make decisions in specific contexts.
Machine Learning	Uses data and algorithms to imitate the way humans learn.
Deep Learning	Uses a process that replicates the human brain in data processing and also creates patterns for decision making.
Natural Language Processing	Allows computers to understand and communicate in human language.

Many of these applications of AI will be explored in further detail in the following sections.

14.5 AUTONOMOUS TECHNOLOGY

One of the most widely used applications of AI is autonomous technologies. By combining software, sensors, and location technologies, devices that can operate themselves to perform specific functions are being developed. Some examples include: medical nanotechnology robots (nanobots), self-driving cars, or unmanned aerial vehicles (UAVs).

A **nanobot** is a robot whose components are on the scale of about a nanometer, which is one-billionth of a meter. While still an emerging field, it is showing promise for applications in the medical field. For example, a set of nanobots could be introduced into the human body to combat cancer or a specific disease.

In March of 2012, Google introduced the world to their **driverless car** by releasing a video on YouTube showing a blind man driving the car around the San Francisco area. The car combines several technologies, including a laser radar system, worth about $150,000. While the car is not available commercially yet, three US states (Nevada, Florida, and California) have already passed legislation making driverless cars legal.

A **UAV**, often referred to as a "drone," is a small airplane or helicopter that can fly without a pilot. Instead of a pilot, they are either run autonomously by computers in the vehicle or operated by a person using a remote control. While most drones today are used for military or civil applications, there is a growing market for personal drones.

Robots

Photo by Phasmatisnox, CC BY 3.0

Robots are automated machines that can execute specific tasks with very little or no human intervention and are able to accomplish tasks with both speed and precision (TechTarget, 2021). The development and deployment of robots is most common in manufacturing in the replacement of humans in repetitive tasks. Robots are also used in medicine, education, restaurants and hotels, and entertainment. Some of the most popular robots are ASIMO by Honda and Boston Dynamics robots like ATLAS. Robots can increase productivity and accuracy, but are costly. For more advantages and disadvantages, see the table below.

Advantages	Disadvantages
• Reduction of risk. Tasks that are dangerous to humans can be done by robots (i.e. defusing bombs, travelling to space) • Error reduction and increased level of precision • No downtime. Robots can work everyday all day • Good at performing repetitive tasks that may otherwise injure humans • Faster decisions can be made by robots programed with artificial intelligence than humans as they are able to process complex data at a much higher speed	• Reduction in specific employment opportunities in jobs being replaced by robots • High capital investment required by organizations to utilize and maintain • Lack of creativity and emotion in the performance of tasks or decision-making processes • Reduction in human interaction • Require constant power to run and maintain

With artificial intelligence, robots will be able to independently estimate the events around them and to make decisions on actions which they're required to make for their given objective. Robots can already both record human movement skills and replicate them as machine learning improves drive efficiency and mobility (Bryndin, 2019).

Intelligent Agents

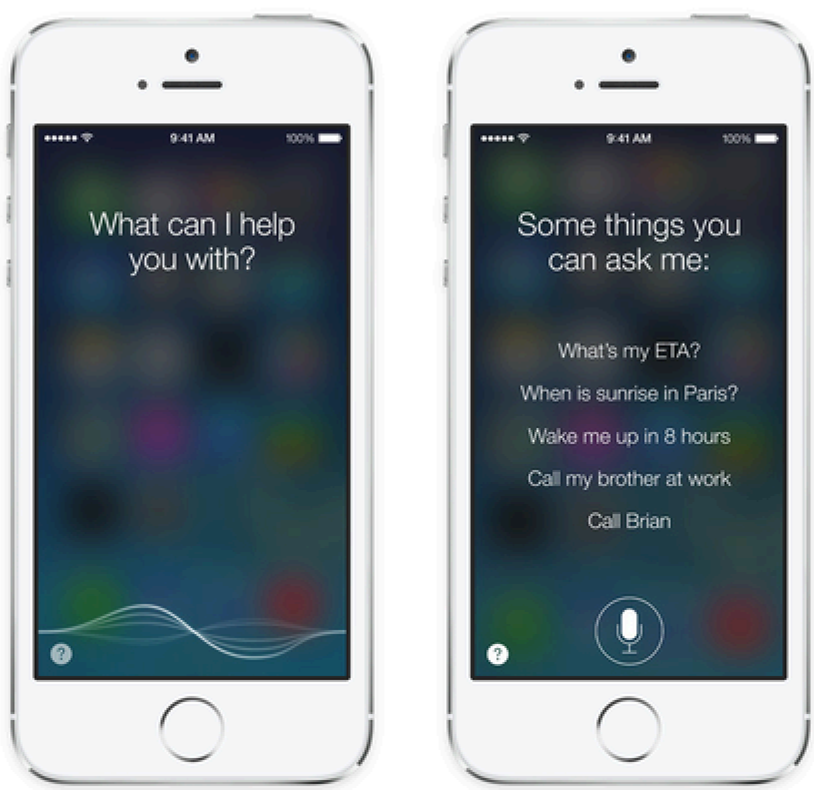


Fig 14.7 "IOS 7 Siri" by Kavakavins111, CC BY-SA 4.0

Intelligent agents process the inputs it receives, and makes decisions/takes action based on that information. Sensors allow intelligence agents to perceive their surroundings, while actuators allow them to act on that perception. A software agent, a human agent, and a robotic agent are all examples of agents, each with its own set of sensors and actuators to sense its environment and then perform actions through its actuators.

AI agents that can learn from their previous experiences or have learning capabilities are known as learning agents. Beginning by acting on basic knowledge, learning agents subsequently learn to act and adapt on their own automatically. Conversational intelligence tools are tools that have the ability to auto-record meetings, transcribe, and apply AI to speech. They can be helpful for individuals working in sales, and could possibly replace some functions performed by customer relationship management systems.

Siri, Alexa and Google Assistant are examples of intelligent agents that can be accessed from smartphones. These tools can allow users to open applications, send messages, make calls, play voicemails and check the weather.

Natural Language Processing (NLP)

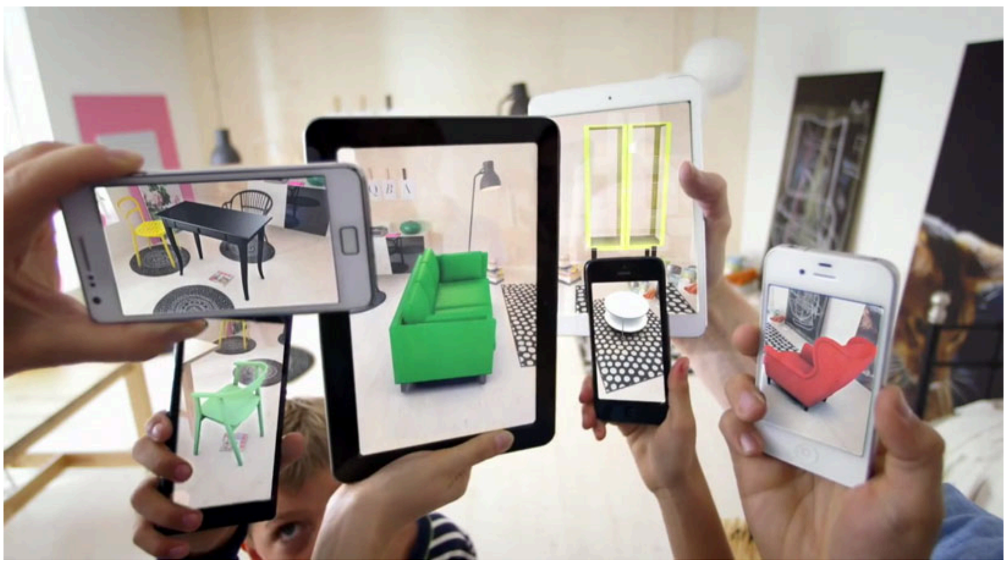
Natural Language Processing (NLP) allows computers to extract meaning from human language. Natural Language Processing's goal by design is to read, decipher, and comprehend human language. In Natural Language Processing, humans converse with the machine which records the conversation and converts the audio to text. After that, the system analyses the data and converts it to audio. The machine then plays the audio file back in response to the human.

Algorithms use natural language processing to detect natural language rules, resulting in the conversion of unstructured language input into a format that computers can recognize. Natural Language Processing (NLP) is used in many translation applications such as Google Translate, various interactive voice response (IVR) applications found in call centres, and software tools that check for grammatical accuracy of texts, like Microsoft Word and Grammarly. Additionally, it is also used in personal assistant tools like Siri, Cortana and Alexa.

14.6 EXTENDED REALITY

Another category of emerging technology is **extended reality** or XR. XR is an umbrella term that covers all forms and combinations of real and virtual environments. This includes: augmented reality (AR), virtual reality (VR) and a combination of the two or mixed reality (MR) (Likens, 2019).

Augmented Reality



"Augmented-reality" by OyundariZorigtbaatar, CC BY-SA 4.0

Augmented reality (AR) enhances one's view of the real world with layers of digital information added to it. With AR there is no created scenario; instead, an actual event is being altered in real time (Moawad et al., 2020). Some examples of this are Snapchat lenses and the game Pokémon Go. AR is being used in e-commerce to help purchasers visualize and interact with the products before purchasing them.

IKEA Augmented Reality Game

Escape the Clutter is a an AR escape room game for Snapchat developed by IKEA. In the game, a cluttered 3D room will appear on screen. The object of the game is to remove the clutter by adding in IKEA organization solutions. The organization products act as the 'keys' to the escape room. As users add the products they can learn more about them and their benefits (Ikea, 2022).

Virtual Reality

Photo by Minh Pham, Unsplash License

Virtual reality (VR) is a computer interaction in which a real or imagined environment is simulated. This allows users to both interact with and alter that reality within the environment. The popularity and development of virtual and augmented reality has grown due to advances in VR technology and devices based on smartphones like Google Cardboard. Some people view virtual reality as a gimmick to enhance video game playing at home, but the technology is being used in innovative ways.

One way in which businesses are leveraging VR technology is for training and education. This technology is especially valuable in high risk industries like the military, space exploration, and medicine where one wrong move can have disastrous consequences. As well, it can be helpful to simulate interview scenarios, or difficult conversations allowing users to role play and practice in varied scenarios. VR can also simulate in-person meetings for those working remotely through the use of avatars. Avatars are computer representation of people.

14.7 TRENDS

In recent decades, the business sector has experienced a digital revolution. This technological and digital transformation has caused a readjustment to all functional areas. In addition to AI; a number of other emerging technologies are forecast to have an impact on how businesses operate and communicate. The following are some trends that are driving these new and innovative technologies.

Wearable

The last section explored VR technologies, which include devices that can be worn to simulate virtual environments. Technology that can be worn or 'wearables' have been around for a long time, with technologies such as hearing aids and, later, bluetooth earpieces. Product lines have expanded to include the Smartwatch, body cameras, sports watch, and various fitness monitors. According to the Gartner Group, strong growth is predicted in the wearable market. Total wearable devices are projected to increase by about 45% from 2018 to 2021 (van der Meulen & Forli, 2017).

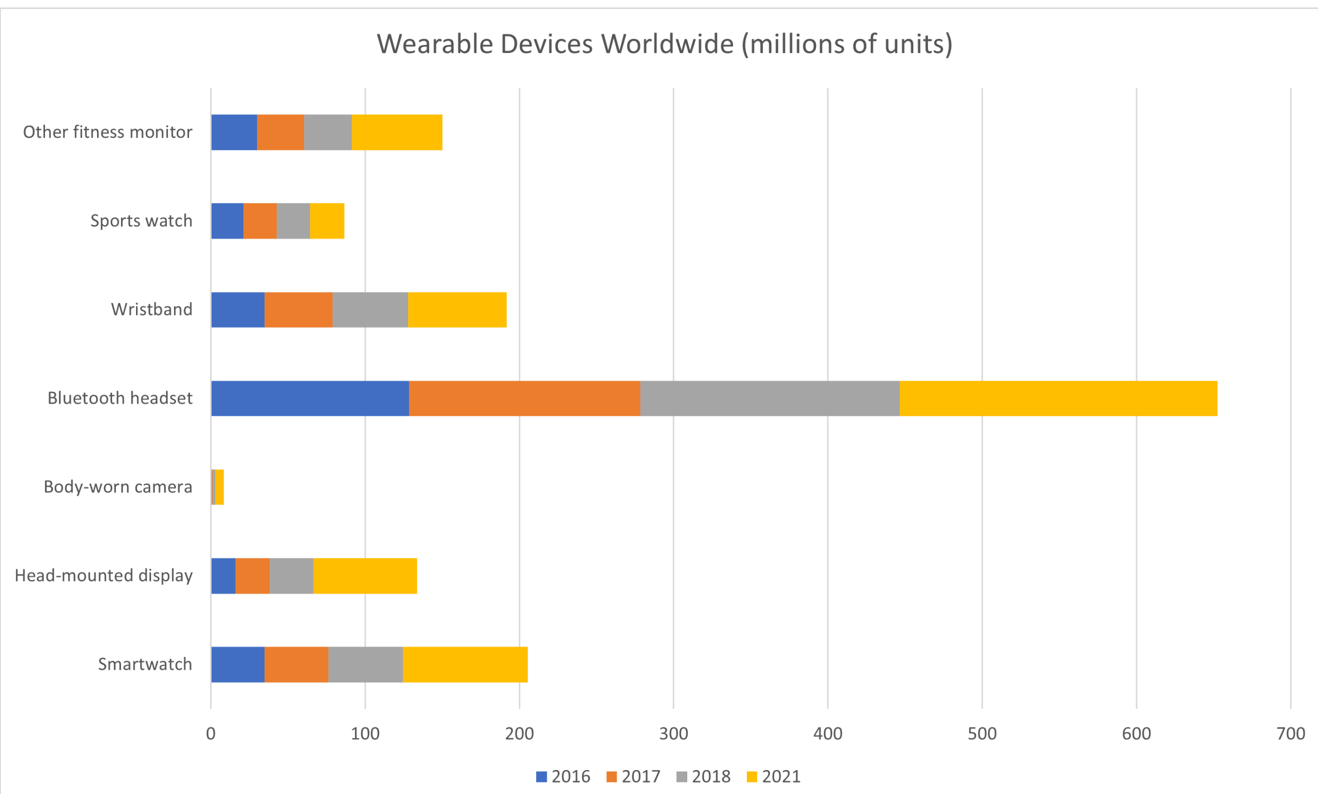


Fig 14.8 Chart created based on data from van der Meulen, R., & Forli, A. A. (2017, August 24).

Printable

A 3-D printer allows you to print virtually any 3-D object based on a model of that object designed on a computer. 3-D printers work by creating layer upon layer of the model using malleable materials, such as different types of glass, metals, or even wax. 3-D printing is quite useful for prototyping the designs of products to determine their feasibility and marketability. **Rapid Prototyping** similar to 3D printing will very quickly become widely sought. This can provide a platform where ideas and concepts that are discussed today can have the prototypes available the very next day. This reduction in time will provide incredible growth and a competitive advantage.

3-D printing has also been used to create working prosthetic legs and an ear that can hear beyond the range of normal hearing. The US military now uses 3-D printed parts on aircraft such as the F-18 9 (The Economist, 2013). Here are more amazing productions from 3D printers.

Buildings	Researchers at MIT in 2017 unveiled a 3D printing robot that can construct a building. It has a large arm and small arm. The large arm moves around the perimeter of the building while the small arm sprays a variety of materials including concrete and insulation. Total time to construct a dome-shaped building is just 14 hours.
Musical Instruments.	Flutes, fiddles, and acoustic guitars are being produced with 3D printing using both metal and plastic.
Medical Models	Medical models are being used to help doctors train in the areas of orthopedics, transplant surgery, and oncology.
Clothing	How would you like clothes that fit perfectly? Special software is used to measure a person, then 3D printing produces the clothing to the exact measurements. The result is well-fitting clothes that consume less raw materials. Initially the challenge was to find materials that would not break. You can read more about 3D printing of clothes and shoes (Bosavage, 2017).

Connected

As discussed in Information Systems for Business and Beyond: Chapter 3, the Internet of Things (IoT) refers to devices that have been embedded into a variety of objects including appliances, lamps, vehicles, lightbulbs, toys, thermostats, jet engines, etc. and then connecting them via Wi-Fi, BlueTooth, or LTE to the internet. Think of IoT as devices that you wouldn't normally consider being connected to the internet, and the connection is independent of human intervention. This interconnectedness or uploading of data is virtually automatic. So a PC is not an IoT, but a fitness band could be. Interconnected devices are becoming ubiquitous, meaning they are everywhere. Today there are IoTs for monitoring traffic, air quality, soil moisture, bridge conditions, consumer electronics, autonomous vehicles, and the list seemingly never stops.

Principally three factors have come together to give us IoT: inexpensive processors, wireless connectivity, and a new standard for addresses on the internet known as IPv6. Processors have become both smaller and cheaper in recent years, leading to their being embedded in more devices. Consider technological advancements in your vehicles. Your car can now collect data about how fast you drive, where you go, radio stations you listen to, and your driving performance such as acceleration and braking. Insurance companies are offering discounts for the right to monitor your driving behaviour. On the positive side, imagine the benefit of being informed instantly of anticipated traffic delays each time you adjust your route to work in the morning. Benefits from IoTs are virtually everywhere. Here is a quick list.

Optimization of Processes	IoTs in manufacturing monitor a variety of conditions that impact production including temperature, humidity, barometric pressure – all factors which require adjustment in application of manufacturing formulas.
Component Monitoring.	IoTs are added to components in the manufacturing process, then monitored to see how each component is performing.
Home Security Systems.	IoTs make the challenge of monitoring activity inside and outside your home are now easier.
Smart Thermostats.	Remote control of home thermostats through the use of IoTs allows the homeowner to be more efficient in consumption of utilities.
Residential Lighting	IoTs provide remote control of lighting.

While there are many benefits to these constantly connected devices privacy and security of personal data and information should also be considered.

Collaborative

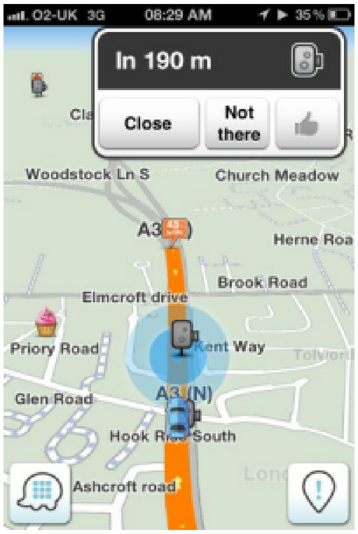


Fig 14.9 Waze Screen Shot (click to enlarge) by D. Bourgeois, CC BY-NC 4.0

As more people use smartphones and wearables, it will be simpler than ever to share data with each other for mutual benefit. Some of this sharing can be done passively, such as reporting your location in order to update traffic statistics. Other data can be reported actively, such as adding your rating of a restaurant to a review site. The smartphone app Waze is a community-based tool that keeps track of the route you are travelling and how fast you are making your way to your destination. In return for providing your data, you can benefit from the data being sent from all of the other users of the app. Waze directs you around traffic and accidents based upon real-time reports from other users.

Yelp! allows consumers to post ratings and reviews of local businesses into a database, and then it provides that data back to consumers via its website or mobile phone app. By compiling ratings of restaurants, shopping centres, and services, and then allowing consumers to search through its directory, Yelp! has become a huge source of business for many companies. Unlike data collected passively however, Yelp! relies on its users to take the time to provide honest ratings and reviews.

Super

Quantum computing, a technology that applies quantum mechanics to build novel supercomputers, high performance computers used to solve large scale computational tasks. Quantum computers can operate at speeds that are exponentially faster than common computers and can make calculations based on the probability of an object's state before it is measured. Google demonstrated that their quantum computers can solve a problem that no classical computer could ever solve. For the third year in a row, IBM managed to double its quantum computing power. Additionally, several web service providers, including Amazon, announced plans for cloud-based quantum computing services. Quantum computers can make drug development, power storage, manufacturing, and agriculture better, faster, and more sustainable. They may also unravel cybersecurity infrastructure around the world making them a potential threat to national security. The field of quantum computing is still in its infancy, and the question of scale remains unsolved.

14.8 CHAPTER REFERENCES

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14.9 KEY TERMS

Key Terms

Artificial Intelligence: The ability of a computer or machine to think and learn, and mimic human behaviour became the focus of many in the 1950s. 14.2

Augmented Reality (AR): Enhances one's view of the real world with layers of digital information added to it. With AR there is no created scenario; instead, an actual event is being altered in real-time (Moawad et al., 2020). 14.6

Automation: The use of machines, control systems and information technologies to optimize productivity in the production of goods and delivery of services (automation, n.d.). 14.4

Deep Learning: Uses a process that replicates the human brain in data processing and also creates patterns for decision making. 14.4

Expert Systems: Aim to emulate the human ability to make decisions in specific contexts. 14.4

Extended Reality or XR: XR is an umbrella term that covers all forms and combinations of real and virtual environments. This includes augmented reality (AR), virtual reality (VR) and a combination of the two or mixed reality (MR) (Likens, 2019). 14.6

Fifth Generation Computer Project (FGCP): From 1982-1990, they invested $400 million dollars with the goals of revolutionizing computer processing, implementing logic programming, and improving artificial intelligence. Unfortunately, most of the ambitious goals were not met. 14.3

General AI: Also referred to as artificial general intelligence (AGI) or strong AI is where artificial intelligence is the same as human intelligence. It means that machines have the ability to apply what they have learned across different tasks, take in new information, and apply reason. 14.4

Intelligent Agents: The use of software to perform specific tasks. 14.4

Internet: Is a network of networks—millions of them, actually. If the network at your university, your employer, or your home has internet access, it connects to an internet service provider (ISP). 14.1

Internet Service Provider (ISP): Many, but not all, ISPs are big telecommunications companies like Rogers Communications, Bell Canada, or Telus Inc . These providers connect to one another, exchanging traffic, and ensure your messages get to other computers that are online and willing to communicate with you. 14.1

Kismet: A robot developed by Cynthia Breazeal that could recognize and display emotions. in 2017, Google's Alpha Go was able to defeat Chinese Go champion Ke Jie. 14.3

Limited Memory: This is the ability of AI to use past experience and information to make predictions. 14.4

Machine Learning: Uses data and algorithms to imitate the way humans learn. 14.4

Nanobot: Is a robot whose components are on the scale of about a nanometer, which is one billionth of a meter. While still an emerging field, it is showing promise for applications in the medical field. 14.5

Natural Language Processing: This allows computers to understand and communicate in human language. 14.4

Narrow AI: Also referred to as artificial narrow intelligence (ANI) or weak AI is a computer's ability to perform a single task well. This is the type of AI we see today. Natural language processing used in smart assistants like Siri and Google are examples of narrow AI. 14.4

Protocol: is the set of rules that govern how communications take place on a network. This problem was solved by the invention of the 14.1

Rapid Prototyping: Similar to 3D printing will very quickly become widely sought. This can provide a platform where ideas and concepts that are discussed today can have the prototypes available the very next day. 14.7

Reactive Machines: AI that conducts tasks for specific objectives. It is the first step of any AI system where no learning takes place. An example of this type of AI is Deep Blue the IBM program that beat chess champion Garry Kasparov. 14.4

Robots: The use of machines to perform tasks traditionally done by humans. 14.4

Self-Aware: AI with the sense of self and consciousness. This type of AI is not yet developed. 14.4

Super AI: Also referred to as artificial super intelligence (ASI) is when the computer will be exceed human capabilities. 14.4

Theory of Mind: AI with the awareness that others have their own beliefs, objectives, and intentions. This type of AI is not yet developed and will be able to distinguish and understand emotion. 14.4

Transmission Control Protocol/Internet Protocol (TCP/IP): TCP/IP was designed to allow networks running on different protocols to have an intermediary protocol that would allow them to communicate. So as long as your network supported TCP/IP, you could communicate with all of the other networks running TCP/IP. TCP/IP quickly became the standard protocol and allowed networks to communicate with each other. 14.1

UAV: Often referred to as a “drone,” is a small airplane or helicopter that can fly without a pilot. Instead of a pilot, they are either run autonomously by computers in the vehicle or operated by a person using a remote control. While most drones today are used for military or civil applications, there is a growing market for personal drones. 14.5

Virtual Reality (VR): Is a computer interaction in which a real or imagined environment is simulated. This allows users to both interact with and alter that reality within the environment. 14.6

Web 2.0: Is also referred to as the social web and occurred between 2000-2010. During this time there was a shift from read only to read and write, which allowed individuals to be content creators. 14.1

Web 3.0: Is also referred to as the semantic web and is the time after 2010 when the web evolved again to allow individuals to read, write and execute. This means that the web is more intelligent and is able to interact with users. For example, algorithms that can personalize search results. 14.1

Web 4.0: Is the future of the web, which is referred to as the intelligent web and will involve the Internet of Things and connected devices. 14.1

World Wide Web Project: Which provided an easy way to navigate the internet through the use of hypertext. The World Wide Web gained even more steam in 1993 with the release of the Mosaic browser which allowed graphics and text to be combined as a way to present information and navigate the internet. 14.1

VERSIONING HISTORY

This page provides a record of edits and changes made to this book since its initial publication. Whenever edits or updates are made in the text, we provide a record and description of those changes here. If the change is minor, the version number increases by 0.1. If the edits involve a number of changes, the version number increases to the next full number.

The files posted alongside this book always reflect the most recent version.

Version	Date	Change	Affected Web Page
1.0	August 15, 2022	First Publication	N/A
1.1	August 30, 2023	1. Added student case studies. 2. Added sixth dimension of Hofstede's theory. 3. Expansion on CAGE analysis. 4. Added infographic on American companies that failed in China. 5. Updated table 6.1; added figure	1. 1.1 Defining Global Marketing; 1.3 The Motivation for Global Marketing; 2.1 The Economic Environment; 3.0 Introduction; 3.1 What is Culture; 4.2 Global Market Opportunity Assessment – CAGE Analysis; 6.1 International Entry Modes; 6.4 Franchising; 10.1 Integrated Marketing Communication; 11.4 Lululemon Marketing Strategy and Plan; 13.5 E-Commerce Models 2. 3.2 Describing Culture: Hofstede 3. 4.2 Global Market Opportunity Assessment – CAGE Analysis 4. 14.7 Trends 5. 6.1 International Entry Modes

ANCILLARY RESOURCES

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