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INTERNATIONAL MARKETING (MGMT 2122)

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Module introduction

Today, more and more businesses are exporting, importing and/or manufacturing their goods with other countries. The companies that are not involved in international business also feel the effects of their customers and competitors that are doing business overseas. There are many companies that sell a large portion of their goods overseas and depend on those profits to survive. When companies decide to go overseas with their products there are many environmental forces that the marketer will have to confront and adapt to. For example, the foreign uncontrollable elements include: political/legal forces, economic, competitive social and cultural forces, the level of technology, physical and geographical. The marketer may find it easier to deal with the marketing controllable, i.e., marketing mix or 4 P's and domestic uncontrollable as compared to the foreign uncontrollable.

The current development of the world economy is increasingly influenced by integration and globalization tendencies. The competitive environment in foreign markets enables an entry and participation in international trade activities for many companies. The decisions of the company related to the market selection and entry or operation on the foreign market are based on the principles of international marketing which can be defined as implementation of marketing activities exceeding national borders of countries. It presents the philosophy of company management focused on foreign markets and aimed at optimal placement of goods and services on these markets (Horská 2007). The implications of international marketing activities take place all around us every day, have a major effect on our lives and offer a wide variety of new opportunities and challenges (Czinkota and Ronkainen, 2012)

This module will explain what international marketing is, its task and how to deal with the marketing controllable and domestic and foreign uncontrollable.

In the era of globalization, international marketing is given much emphasis and plays crucial role in the development of a nation. It includes basic concepts of international marketing and its environment; relationship between international marketing and international trade; theory of comparative advantage; world trade situation and international marketing, analysis of marketing across national trade blocks' applications of marketing principles to international marketing, analysis of marketing across national boundaries, different levels of international marketing involvement; various ways of international market entry strategies, marketing-mix element decision international marketing process of practical international marketing; Opportunities and challenges of international marketing for Developing Countries like Ethiopia.

Module objective

What you should learn from this module

- ✓ What is meant by international marketing.
- ✓ To understand the scope of the international marketing task
- ✓ To comprehend the importance of the self-reference criterion (SRC) in international marketing.
- ✓ To be able to identify and manage the factors influencing internationalization of companies.
- ✓ To see how international marketing concepts, influence international marketers.
- ✓ To appreciate the increasing importance of global awareness.

CHAPTER ONE

NATURE OF INTERNATIONAL MARKETING

Chapter objectives

After studying this chapter, you should be able to:

- Differentiate between domestic marketing and international marketing
- Identifying the reasons why firms involve in international marketing
- Identify the stages of international marketing involvement
- Explaining the different orientation of firms towards international marketing?
- Differentiate the different international trade theories

Introduction

This chapter addresses the who, what, why, and how of international marketing by giving an overview of the nature of international business. The discussion begins with an examination of how marketing in general is defined and how that definition works for international marketing. The chapter examines the reason why firms involved in international marketing, stages of international marketing involvement, company's strategic orientations towards to international marketing, theories and barriers of international trade.

Activity 1.1
Do you think business organizations free from international trade?
______________________________ ______________________________ ______________________________

Today the corporate world cannot survive with restricting themselves within the domestic boundaries. As the consumers across countries become more universal in nature, the need to look at the whole world as a market is growing. The aim of this unit is to introduce the students to International Marketing, which explains how International Markets operate in

an International Environment. An elementary approach is used in the module, which emphasizes the reasons for undertaking International Market analysis and their interpretation. An international perspective is maintained throughout the text. The objective of the problems is to enhance the student's understanding of analytical techniques- more emphasis on policy and managerial implications of International Marketing. The module focuses on International skills required to be an effective manager. It will develop the student's ability to identify and appreciate effective ways of getting the objective fulfilled. It also develops practical applications ability and knowledge and how these can be used in the decision-making process.

All organizations in this world, large and small, have been so deeply involved in and affected by international business. A global economic boom, unprecedented in modern economic history, has been under way as the drive for efficiency, productivity, and open, unregulated marketers sweeps the world. Powerful economic, technological, industrial, political, and demographic forces are converging to build the foundation of a new global economic order on which the structure of a one world economic and market system will be built.

Whether or not an Ethiopian company wants to participate directly in international business, it cannot escape the effects of the ever-increasing number of foreign firms exporting, importing and manufacturing abroad. Nor can it ignore the number of foreign based firms operating in Ethiopia markets, the growth of regional trade areas, the rapid growth of world markets, and the increasing number of competitors for global markets.

An organization whose products are marketed in two or more countries is engaged in international marketing. The fundamentals of marketing apply to international marketing in the same way they apply to domestic marketing.

1.1. Definition of International Marketing

Understanding international marketing is easier if you have good Knowledge of the concept of marketing. As per the definition of American Marketing Association, "marketing is the process of planning and executing the conception, pricing, promotion and distribution of ideas, goods, and services to create exchanges that satisfy individual and organizational objectives". This definition can extend to define international marketing. Thus "international marketing is the multinational process of planning and

executing the conception, pricing, promotion and distribution of ideas, goods, and services to create exchanges that satisfy individual and organizational objectives." International marketing is the performance of business activities that direct the flow of companies' goods and services to consumers and users in more than one nation for a profit.

International Marketing is the marketing carried on cross national boundaries. It is a marketing techniques involved between countries. To understand in a better way let's read definitions of International Marketing given by different authors.

- "International Marketing has been defined by Franklin R, Root as "those activities performed by a business enterprise to promote, direct, support and control the penetrations and development of a foreign national market from a production base located either outside or inside that market."
- Walsh defines international marketing as; "the marketing of goods and services across national frontiers, and the marketing operations of an organization that sells or produces within a given country when; that organization is a part of an enterprise which also operates in other countries and, there is some degree of influence on or control of the organizations marketing activities from outside the country in which it sells or produces."
- "International Marketing is the performance of business activities designed to plan, price, promote, and direct the flow of a company's goods and services to consumers or users in more than one nation for a profit" Philip R. Cateora and John h. Graham (2002)

1.2. Reason for entering International Market /Internationalization

Few companies operate in an isolated and fewer can effectively avoid international involvement. Local firms manufacturing for local consumers are dependent on equipment, parts, and/or raw materials originating abroad. They sell to clients and final consumers who have expose to international products. The advances in information technology have facilitated the process of marketing across countries. This trend of globalization of the scope of business has made it essential for the corporate managers to understand international marketing operations. Companies most often cannot avoid

involvement in international marketing; increasingly companies cannot afford to avoid involvement in international marketing. Avoiding international marketing could mean losing market share to competitors and missing numerous opportunities created by changes in the international environment. Companies drive to internationalization by many reasons. They categorized in business environment and firm specific drives.

1.2.1. **Business Environment Drivers**- are elements in the business environment

- **Saturated home market:** If the home market for an organization's products or service is saturated or competition is so intense that it can no longer gain any significant market share improvement, it might consider extending its market activity to overseas markets.
- **Competition**: There are two cases in this instance: 1st competition may be less intense in overseas markets than in the domestic market; 2nd an organization is faced by particularly virulent international competition in its domestic market place. In this case it is difficult to compete from a domestic base against international competitors. So you have to move internationally to compete on a more equal footing with the opponent organization.
- **Regional Economic and Political Integration:** In addition to cultural similarities language and religion, economic and political integration play an important part in facilitating international trade. Regional agreements such as the North American Free Trade Agreement (NAFTA) and the politically and economically integrated European Union are best examples. It lowers or eliminates barriers between member countries and promoting trade within the perimeter of each common market.
- **Technology**: Technology has created opportunities for firms involved in international business.
- **Improvement in transportation and telecommunication infrastructure**
- **Economic Growth:** Economic growth constitutes a very important driver of internationalization. Economic growth increase buying power and create markets of high potential for international brands. Economic growth has also opened markets that have been previously closed that have limited international competition.
- **Transition to a market Economy:** The transition of countries to a market economy has lead to rapid economies development and has created important new markets for

international brands. Another important outcome of the transition to a marked economy has been the deregulation and privatization of former government monopolies. Opportunities exist for product manufactures to purchase or partner with local companies operating at loss, producing low quality goods and to turn them around in to successful enterprises selling global brands to local consumers.

- **Converging consumer needs:** Exposure to global brands in one's home country and while traveling abroad, to media advertising these brands has created demand for many global products. Consumers worldwide are loyal to international brands. Uniform consumer segments are emerging worldwide. During their international travels, consumers purchase brands and services available in their own home country, which they are familiar with. Most often, these offerings are successful international products and services. Alternatively, consumers who have traveled abroad bring with them product experiences and demand brands that may not be available in the home country market. This will generate pull demand, where by consumers request the product from the retailers who subsequently convey the information up the distribution chain to wholesalers, who would then order the product.

1.2.2. Firms Specific Drivers

- **Product life cycle differences:** A main drive behind international expansion is a firms attempt to prolong the product life cycle. Products that are in late maturity or even in the decline stage can change their position on the global product life-cycle stage by going in to markets where the product is in high demand. To illustrate this point, the cigarette industry is in either the late maturity stage or in the decline stage in many industrialized countries. By entering emerging markets where cigarettes are in the growth stage and consumers have increasing purchase power, such as China, central and Eastern Europe, the cigarette industry is in fact prolonging its products life cycle.
- **High new product development costs:** Companies often spend long period of time and significant amount of money to develop new products. So to fully recover the product developments cost and make a profit companies, going international is not a choice it is a pre-condition for survival.

- **Standardization:** During the maturity stage of the PLC, the core product is likely to achieve a standard in a particular industry. Competitors respond to consumer needs by offering products whose components are interchangeable and which converge towards the brand experiencing the greatest consumer franchise (demand).
- **Economies of scale:** During the maturity stage, firms also increasingly compete on price. Typically, they attempt to lower the product manufacturing cost by achieving economics of scale in production.
- **Cheap Labor:** Firms at maturity also move manufacturing operations and facilities abroad, to developing countries, in attempt to take advantage of significantly lower labor costs.
- **Experience transfers:** International firms benefit from lessons they learn in the different parts of the world.
- **Comparative advantage in product, skill or technology:** The organization may discover, when analyzing overseas market opportunities, that it has a comparative advantage against local competition in the foreign market. This advantage might be in product, skill or technology.
- **Excess Capacity:** Where an organization is operating successfully in its domestic market place but it is operating at below optimal capacity levels, there is excess capacity available for production. In these instances, it may be wise to consider international operations where the product or service can be coasted at marginal cost, thereby giving a potential price advantage for overseas marketing operations.

Activity

List the reason of why business organizations enter into international marketing?

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1.3. Stages of International Involvement

Once a company has decided to go international, it has to decide the degree of marketing involvement and commitment it is prepared to make. These decisions should reflect considerable analysis of market potential and company capabilities—a process not always followed. Many companies begin tentatively in international marketing, growing as they gain experience and gradually changing strategy and tactics as they become more committed. Others enter international marketing after

much research and with fully developed long-range plans, prepared to make investments to acquire a market position. Anyways, below we shall try to describe the six international marketing stages a company may encounter in marketing across national boundaries.

1. **No Direct Foreign Marketing:** A company in this stage does not actively cultivate customers outside national boundaries; however, this company's products may reach foreign markets. Sales may be made to trading companies as well as foreign customers who come directly to the firm, or products may reach foreign markets via domestic wholesalers. or distributors who sell abroad without explicit encouragement or even knowledge of the producer. Often an unsolicited order from a foreign buyer is what piques the interest of a company to seek additional international sales.
2. **Infrequent Foreign Marketing:** Temporary surpluses caused by variations in production levels or demand may result in infrequent marketing overseas. The surpluses are characterized by their temporary nature; therefore, sales to foreign markets are made as goods are available, with little or no intention of maintaining continuous market representation. As domestic demand increases and absorbs surpluses foreign sales activity is withdrawn. In this stage, there is little or no change in company organization or product lines. However, few companies today fit this model because customers around the world increasingly seek long- term commercial relationships.
3. **Regular Foreign Marketing:** At this level the firm has permanent productive capacity devoted to the production of good to be marketed in foreign markets. A firm may employ foreign or domestic overseas middlemen or it may have its own sales force or sales subsidiaries in important foreign markets. The primary focus of operations and production is to service domestic market needs. However, as overseas demand grows, production is allocated for foreign markets, and products may be adapted to meet the needs of individual foreign markets. Profit expectations from foreign markets move from being seen as a bonus to regular domestic profits to a position in which the company becomes dependent on foreign sales and profits to meet its goals.
4. **International Marketing:** Companies in this stage are fully committed and involved in international marketing activities. Such companies seek markets all over the world and sell products that are a result of planned production for markets in various countries. This generally entails not only the marketing but also the production of goods outside the home market. At this point a company becomes an international firm. The experience of Fedders, a manufacturer of room air conditioners, typifies that of a company that begins its international business at this stage. Even though it is the largest manufacturer of air conditioners in the United States, the firm faced constraints in its domestic market. Its sales were growing steadily, but air conditioner sales (the company's only product) are seasonal and thus there are times when

domestic sales do not even cover fixed costs. Furthermore, the US market is mature, with most customers buying only replacement units. Any growth would have to come from a rival's market share, and the rivals, Whirlpool and Matsushita, are formidable. Fedders decided that the only way to grow was to venture abroad. Fedders decided that Asia, with its steamy climate and expanding middle class, offered the best opportunity. China, India, and Indonesia were seen as the best prospects. China was selected because sales of room air conditioners had grown from 500,000 units to over 4 million in five years, which still accounted for only 12 percent of the homes in cities like Beijing, Shanghai, and Guangzhou. The company saw China as a market with terrific growth potential. After careful study, Fedders entered a joint venture with a small Chinese air conditioner company that was looking for a partner; a new company, Fedders Xinle, was formed.

5. **Multinational Marketing:** Now, in this stage, the number of countries in which the company is doing business gets bigger than that in earlier stage. And so, instead of producing different goods for different countries, company tries to identify different regions for which it can deliver same product. So, same product for countries lying in one region but different from product offered in countries of another region. e.g. a company may decide to offer same product to India, Srilanka and Pakistan if it thinks the taste of people of these countries is same but at the same time offering different product for American countries.

6. **Global Marketing:** At the global marketing level, the most profound change is the orientation of the company toward markets and associated planning activities. At this stage, companies treat the world, including their home market, as one market. Market segmentation decisions are no longer focused on national borders. Instead, market segments are defined by income levels, usage patterns, or other factors that often span countries and regions. Often this transition from international marketing to global marketing is catalyzed by a company's crossing the threshold of more than half its sales revenues coming from abroad. The best people in the company begin to seek international assignments and the entire operation—organizational structure, sources of finance, production, marketing, and so forth—begins to take on a global perspective.

1.4. Strategic Orientation

The stages of international marketing involvement described above do not necessarily concede with managers' thinking and strategic orientation. Often companies are led in to international and even global market by increasing consumers or customer demands, and strategic thinking. Management's orientation toward the internationalization of the firm's operations affects each of the functional areas of the firm, and as such, has a direct impact

on the marketing functions within the firm. Management's philosophy on international involvement affects decisions such as the firm's response to global threats and opportunities and related resource allocation. Companies' philosophies on international involvement can be described, based on the EPRG framework, as ethnocentric, polycentric, regiocentric and geocentric.

- **Ethnocentric Orientation**: is a strong orientation toward the home country. Firms with an ethnocentric orientation are guided by a domestic market extension concept. Firms with ethnocentric orientation consider that domestic strategies, techniques, and personnel are superior to foreign ones, and therefore provide the most effective framework for the company's overseas involvement; consequently, international operations and customers are considered secondary to domestic operations and customers. Ethnocentric firms are likely to be highly centralized, and consider that the purpose of their international operation is to identify markets that could absorb surplus domestic production; alternatively, international operations could represent a cash cow that generates revenue and necessitates only minimal attention and investment.

- **Polycentric Orientation:** It is the opposite of ethnocentricity, is a strong orientation to the host country. The attitude places emphasize on difference between markets that are caused by variations within such as income, culture, laws and politics. The assumption is that each market is a unique and consequently difficult for outsiders to understand. Thus such companies assume each market is unique and needs to be addressed in individually. Consequently, the company is fully decentralized and engages in minimal coordination with head quarters. Thus managers from the host country should be employed and allowed to have great deal of discretion in market decision. In the process of developing individual strategies for each market the company does not coordinate activities across the different countries and cannot benefit from economies of scale that such coordination will allow. Further more numerous functions are duplicated, and ultimate final product costs are higher to the end consumer.

- **Regiocentric Orientation:** Companies adapting a regiocentric orientation view world regions as distinct markets that share economic, political and/or cultural traits such that they would be viable candidates for a region wide marketing approach. A regiocentric orientation is now possible due to the success of regional economic and political integration that allows for implementing a uniform marketing strategy in the entire region.

- **Geocentric Orientation:** Firms in which top management adapts a geocentric orientation perceive the entire word-without national and regional distinctions-as a potential market with identifiable, homogenous segments, regardless of geographic location or nationality. Coordinated management policies are designed to reflect the full integration among worldwide operation. The objective of a geocentric company is most often to achieve a position as a low-cost manufacturer and markets of its product line, such a firm achieves a strategic competitive advantage by developing manufacturing process that add more value per unit cost to the final product than its rivals.

1.5. International marketing VS Domestic marketing

The answer lies not with different concepts of marketing but with the environment within which marketing plans must be implemented. The uniqueness of foreign marketing comes from the range of unfamiliar problems and the variety of strategies necessary to cope with different levels of uncertainty encountered in foreign markets.

Domestic marketing involves one set of uncontrollable derived from the domestic market. International marketing is much more complex because a marketer faces two or more sets of uncontrollable variables originating from various countries. The marketer must cope with different cultural, legal, political, and monetary systems.

Competition, legal restraints, government controls, weather, changeable consumers, and any number of other uncontrollable elements can, and frequently do, affect the profitable outcome of good, sound marketing plans. Generally speaking, the marketer cannot control or influence these uncontrollable elements but instead must adjust or adapt to them in a manner consistent with a successful outcome. What makes marketing interesting is the challenge of molding the controllable elements of marketing decisions

(product, price, promotion, distribution, and research) within the framework of the uncontrollable elements of the marketplace (competition, politics, laws, consumer behavior, level of technology, and so forth) in such a way that marketing objectives are achieved. Even though marketing principles and concepts are universally applicable, the environment within which the marketer must implement marketing plans can change dramatically from country to country or region to region. The difficulties created by different environments are the international marketer's primary concern.

1.6. Exporting Vs International Marketing

Exporting is often considered as the first step in the process of internationalization of a business. In general, the firms engaged in export operations have to concentrate on managing the 4 p's of marketing mix i.e. product, price, place and promotion. Exporting is primarily a transactional approach to marketing wherein goods are exchanged for value on deal to deal basis. International marketing on the other hand extends from identifying the customer needs to achieving customer satisfaction. Internationals marketing requires greater commitment of the executives' time and resources than exporting.

Exporting is usually a short-term solution to an immediate problem of under-capacity of production or over-capacity of the stocks. However, international marketing is a long-term approach to sustained business from a market. It helps to bridge the information gap between a company and the final consumer of its product. While, exporting may involve agents or intermediaries, the market and marketers are more close in marketing. The differences in exporting and international marketing can be shown in the form of the following table 1.1

Table 1.1 difference in export and international marketing

Export	International marketing
✓ To realize short run goals ✓ No systematic selection of market ✓ No systematic choice for mode of entry ✓ Minor product adaption necessary ✓ Mandatory legal obligation ✓ No effort to control channels objective	✓ To realize long run goals ✓ Systematic selection of market ✓ Systematic choice of most appropriate mode of entry ✓ Development of products for both home and foreign markets ✓ Major product adaption to suit to satisfy foreign

and goals ✓ Prices based on domestic full with some ad hoc adjustments to specific sales situations ✓ Promotion mix mainly confined to foreign tours or left to middlemen	buyers ✓ Effort to control channels to support of market ✓ Prices fixed in terms of demand conditions, competition and cost ✓ Promotion mix includes advertising sales promotion and foreign tours

1.7. Challenges in international marketing

1. **Political and legal differences**: The political and legal environment of foreign markets is different from that of the domestic. The complexity generally increases based on the operations in a number of countries.
2. **Cultural differences**: the cultural difference is one of the most difficult problems in international marketing. Many domestic markets are also free from cultural diversity.
3. **Economic differences**: Economic environment vary from country to country based on national income, spending pattern, rate of savings, debt position, business cycles etc.
4. **Differences in the currency unit**: Currency variation from nation to nation cause problems of currency convertibility, besides the problems of exchange rate fluctuations. The monetary system and regulations may also vary.
5. **Differences in the language**: An international marketer often encounters problems arising out of the differences in the language. Even when the same language is used in different countries, the same words or terms may have different meanings.
6. **Differences in the marketing infrastructure**: The availability and nature of the marketing facilities available in different countries may vary widely. For example an advertising medium very effective in one market may not be available or may be underdeveloped in another market.
7. **Trade restrictions**: Trade restriction, particularly import controls, is a very important problem which an international marketer faces. Every country has its

own customs duties and also rules and regulations relating to demand and supply of foreign exchange.

8. **High costs of distance**: When the markets are far away by distance, the transportation cost becomes high and the time required for effective delivery tends to become longer.
9. **Differences in trade practices**: Trade practices and customs may differ between markets. The export procedures and policies also vary from country to country. This directly reflects international business operations.
10. **Risks and uncertainties:** Long distance, dangers of sea transport, changing exchange rates etc create a number of risks and uncertainties leading to heavy losses or damages.

1.8. Theories of International Trade and Balance of Payment

1.8.1. International Trade Theories

Although our primary concern is international marketing rather than international trade, a brief survey of international trade will prove useful. Trading between groups has been going on since the beginning of recorded history. Much early trade was economically motivated and conducted through barter or commercial transactions. However, a large part of the exchange of goods historically occurred through military conquest: “To the victor belong the spoils.” The predominant pattern of international trade is the voluntary exchange of goods and services.

In domestic marketing, much emphasis is placed on the analysis of buyer behavior and motivation. For the international marketer, knowledge of the basic causes and nature of international trade is important. It is easier for a firm to work with the underlying economic forces than against them. To work with them, however, the firm must understand them.

Essentially, international trade theory seeks the answers to a few basic questions: Why do nations trade? What goods do they trade? Nations trade for economic, political, and cultural reasons, but the principal economic basis for international trade is difference in price; that is, a nation can buy some goods more cheaply from other nations than it can make them itself. In a sense, the nation faces the same "make or buy" decision, as does

the firm. Just as most firms do not go for complete vertical integration but buy many materials and supplies from outside firms, so most nations decide against complete self-sufficiency (or autarky) in favor of buying cheaper goods from other countries.

In the 1600 and 1700 centuries, mercantilism stressed that countries should simultaneously encourage exports and discourages imports. Although mercantilism is an old theory it echoes in modern politics and trade policies of many countries. The neoclassical economist Adam Smith, who developed the theory of absolute advantage, was the first to explain why unrestricted free trade is beneficial to a country. Smith argued that 'the invisible hand' of the market mechanism, rather than government policy, should determine what a country imports and what it exports. Two theories have been developed from Adam Smith's absolute advantage theory. The first is the English neoclassical economist David Ricardo's comparative advantage. Two Swedish economists, Eli Hecksher and Bertil Ohlin, develop the second theory.

The Heckscher-Ohlin theory is preferred on theoretical grounds, but in real-world international trade pattern it turned out not to be easily transferred, referred to as the Leontief paradox. Another theory trying to explain the failure of the Hecksher-Ohlin theory of international trade was the product life cycle theory developed by Raymond Vernon.

1. Mercantilism

According to Wild, 2000, the trade theory that states that nations should accumulate financial wealth, usually in the form of gold, by encouraging exports and discouraging imports is called mercantilism. According to this theory other measures of countries' well being, such as living standards or human development, are irrelevant. Mainly Great Britain, France, the Netherlands, Portugal and Spain used mercantilism during the 1500s to the late 1700s.

Mercantilist countries practiced the so-called zero-sum game, which meant that world wealth was limited and that countries only could increase their share at expense of their neighbors. The economic development was prevented when the mercantilist countries paid the colonies little for export and charged them high price for import. The main

problem with mercantilism is that all countries engaged in export but was restricted from import, prevention from development of international trade.

2. Absolute Advantage

Adam Smith may have been the first scholar to investigate formally the rationale behind foreign trade. In his book Wealth of Nations, Smith used the principle of absolute advantage as the justification for international trade. According to this principle, a country should export a commodity that can be produced at a lower cost than can other nations. Conversely, it should import a commodity that can only be produced at a higher cost than can other nations. Contrary to mercantilism Smith argued that a country should concentrate on production of goods in which it holds an absolute advantage. No country would then need to produce all the goods it consumed. The theory of absolute advantage destroys the mercantilist idea that international trade is a zero-sum game. According to the absolute advantage theory, international trade is a positive-sum game, because there are gains for both countries to an exchange. Unlike mercantilism this theory measures the nation's wealth by the living standards of its people and not by gold and silver.

There is a potential problem with absolute advantage. If there is one country that does not have an absolute advantage in the production of any product, will there still be benefit to trade, and will trade even occur? The answer may be found in the extension of absolute advantage, the theory of comparative advantage.

3. Comparative Advantage

The most basic concept in the whole of international trade theory is the principle of comparative advantage, first introduced by David Ricardo in 1817 and later improved by John Stuart Mill, Cairnes and Bastable. It remains a major influence on much international trade policy and is therefore important in understanding the modern global economy. The principle of comparative advantage states that a country should specialize in producing and exporting those products in which it has a comparative, or relative cost, advantage compared with other countries and should import those goods in which it has a comparative disadvantage. Out of such specialization, it is argued, will accrue greater benefit for all.

In this theory there are several assumptions that limit the real-world application. The assumption that countries are driven only by the maximization of production and consumption and not by issues out of concern for workers or consumers is a mistake.

David Ricardo advanced the concept of relative or comparative costs as the basis of international trade. The principle of comparative costs is based on the differences in production costs of similar commodities in different countries. Production costs differ in countries because of geographical division of labor and specialization in production. In this way, each country specializes in the production of that commodity in which its comparative cost of production is the least. Therefore, when a country enters in to trade with some other country, it will export those commodities in which its comparative production costs are less, and will import those commodities in which its comparative production costs are high. This is the basis of international trade, according to Richardo. It follows that each country will specialize in the production of those commodities in which it has greater comparative advantage.

In sum, his theory of comparative advantage states that even if a country is able to produce all its goods at lower cost than another country can, trade still benefits both countries, based on comparative, not absolute costs. In other words, countries should concentrate efforts on producing goods that have a comparative advantage over other countries, and then export those goods in exchange for goods that command advantage in their native countries.

To illustrate this point, let us assume the following information about the United State and Italy.

Labor costs per unit (in Hours)

Country	Hand calculator	Bottle of wine
United States	6	8
Italy	30	15

Although these figures show that the production cost of both hand calculators and wine is lower in the United States than in Italy, according to the theory of comparative advantage, the United States is better off specializing in hand calculators and exchanging them for Italian wine. This way, it can obtain from Italy a bottle of wine for only six

hours of labor instead of eight hours that would be required at home. Italy would also gain from the exchange by concentrating on producing wine and exchanging it for hand calculators at the cost of 15 instead of 30 hours of labor. The key to this concept is in the word “comparative” -which implies that each and every country has both definite ‘advantage’ in producing some goods and definite ‘disadvantage’ in producing other goods.

4. **Heckscher-Ohlin Theory/Factor Endowment Theory**

The principles of absolute and relative advantage provide a primary basis for trade to occur, but the usefulness of these principles is limited by their assumptions. One basic assumption is that the advantage, whether absolute or relative, is determined solely by labor in terms of time and cost. Labor then determines comparative production costs and subsequent product prices for the same commodity.

In the early 1900s an international trade theory called factor proportions theory emerged by two Swedish economists, Eli Heckscher and Bertil Ohlin. This theory is also called the Heckscher-Ohlin theory. The Heckscher-Ohlin theory stresses that countries should produce and export goods that require resources (factors) that are abundant and import goods that require resources in short supply. This theory differs from the theories of comparative advantage and absolute advantage since these theory focuses on the productivity of the production process for a particular good. On the contrary, the Heckscher-Ohlin theory states that a country should specialize production and export using the factors that are most abundant, and thus the cheapest. Not produce, as earlier theories stated, the goods it produces most efficiently.

The Heckscher-Ohlin theory is preferred to the Ricardo theory by many economists, because it makes fewer simplifying assumptions. In 1953, Wassily Leontief published a study, where he tested the validity of the Heckscher-Ohlin theory. The study showed that the U.S was more abundant in capital compared to other countries; therefore the U.S would export capital- intensive goods and import labor-intensive goods. Leontief found out that the U.S's export was less capital intensive than import.

5. **Product Life Cycle Theory**

Raymond Vernon developed the international product life cycle theory in the 1960s. The international product life cycle theory stresses that a company will begin to export its

product and later take on foreign direct investment as the product moves through its life cycle. Eventually a country's export becomes its import. Although the model is developed around the U.S, it can be generalized and applied to any of the developed and innovative markets of the world.

The product life cycle theory was developed during the 1960s and focused on the U.S since most innovations came from that market. This was an applicable theory at that time since the U.S dominated the world trade. Today, the U.S is no longer the only innovator of products in the world. Today companies design new products and modify them much quicker than before. Companies are forced to introduce the products in many different markets at the same time to gain cost benefits before its sales declines. The theory does not explain trade patterns of today.

Generally, mercantilism proposed that a country should try to export more than it imports, in order to receive gold. The main criticism of mercantilism is that countries are restricted from import, a prevention of international trade. Adam Smith developed the theory of absolute advantage that stressed that a country should produce goods or services if it uses a lesser amount of resources than other countries. David Ricardo stated in his theory of comparative advantage that a country should specialize in producing and exporting products in which it has a comparative advantage and it should import goods in which it has a comparative disadvantage. Hecksher-Ohlin's theory of factor endowments stressed that a country should produce and export goods that require resources (factors) that are abundant in the home country. Leontief tested the Hecksher-Ohlin theory in the U.S. and found that it was not applicable in the U.S. Raymond Vernon's product life cycle theory stresses that a company will begin to export its product and later take on foreign direct investment as the product moves through its life cycle. Eventually a country's export becomes its import.

According to this concept, many products go through a trade cycle wherein one nation is initially an exporter, then loses its export markets, and finally may become an importer of the product. Empirical studies have demonstrated the validity of the model for some kinds of manufactured goods. Outlined below are the four phases in the production and trade cycle, with the United States as an example. We'll assume a U.S. firm has come up with a high-tech product.

In Phase 1, product innovation is likely to be related to the needs of the home market. The firm usually serves its home market first. The new product is produce in the home market because, as the firm moves' down the production learning curve, it needs to communicate with both suppliers and customers. As it begins to fill home-market needs, the firm begins to export the new product, seizing on its first-mover advantages. (We assume the U.S. firm is exporting to Europe.)

In Phase 2, importing countries gain familiarity with the new product. Gradually, producers in wealthy countries begin producing the product for their own markets. (Most product innovations begin in one rich country and then move to other: rich countries.) Foreign production will reduce the exports of the innovating firm. (We assume that the U.S. firm's exports to Europe are replaced by production within, Europe.)

In Phase 3, foreign firms gain production experience and move down the cost curve. If they have lower costs than the innovating firm, which is frequently the case, they export to third-country markets, replacing the innovator's exports there. (We assume that European firms are now exporting to Latin America, taking away the U.S. firm's export markets there.)

In Phase 4, the foreign producers now have sufficient production experience and economies of scale to allow them to export back to the innovator's home country. (We will assume the European producers have now taken away the home market of the original U.S. innovator.)

In Phase 1 the product is "new." In Phase 2 it is "maturing." In Phases 3 and 4 it is "standardized." The product may become so standardized by Phase 4 that it almost becomes commodity. Textiles in general are an example of a product in Phase 4. Products in Phase 4 may be produced in less developed countries for export to the developed countries. This modification of the theory of comparative advantage provides further insight into patterns of international trade and production and helps the international company plan logistics, such as when it will need to produce—or source – abroad.

Activity

List the types of international trade

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1.8.2. Balance of Payments

When countries trade, financial transactions among businesses or consumers of different nations occur. Products and services are exported and imported, monetary gifts are exchanged, investments are made, cash payments are made and cash receipts received, and vacation and foreign travel occur. In short, over a period of time, there is a constant flow of money into and out of a country. The system of accounts that records a nation's international financial transactions is called its balance of payments.

A nation's balance-of-payments statement records all financial transactions between its residents and those of the rest of the world during a given period of time—usually one year. Because the balance-of-payments record is maintained on a double-entry bookkeeping system, it must always be in balance. As on an individual company's financial statement, the assets and liabilities or the credits and debits must offset each other. And like a company's statement, the fact that they balance does not mean a nation is in particularly good or poor financial condition. A balance of payments is a record of condition, not a determinant of condition. Each of the nation's financial transactions with other countries is reflected in its balance of payments.

A nation's balance-of-payments statement presents an overall view of its international economic position and is an important economic measure used by treasuries, central banks, and other government agencies whose responsibility is to maintain external and internal economic stability. A balance of payments represents the difference between receipts from foreign countries on one side and payments to them on the other. On the plus side of the U.S. balance of payments are merchandise export sales; money spent by foreign tourists; payments to the United States for insurance, transportation, and similar services; payments of dividends and interest on investments abroad; return on capital invested abroad; new foreign investments in the United States; and foreign government payments to the United States.

On the minus side are the costs of goods imported, spending by American tourists overseas, new overseas investments, and the cost of foreign military and economic aid. A deficit results when international payments are greater than receipts. It can be reduced or eliminated by increasing a country's international receipts (i.e., gain more exports to

other countries or more tourists from other countries) and/or reducing expenditures in other countries.

A balance-of-payments statement includes three accounts: the **current account**, a record of all merchandise exports, imports, and services plus unilateral transfers of funds; the **capital account**, a record of direct investment, portfolio investment, and short-term capital movements to and from countries; and the **official reserves account**, a record of exports and imports of gold, increases or decreases in foreign exchange, and increases or decreases in liabilities to foreign central banks. Of the three, the current account is of primary interest to international business.

The current account is important because it includes all international merchandise trade and service accounts, that is, accounts for the value of all merchandise and services imported and exported and all receipts and payments from investments and overseas employment.

1.8.3. Barriers of international trade

To encourage development of domestic industry and protect existing industry, governments may establish such barriers to trade as tariffs, quotas, boycotts, monetary barriers, non tariff barriers, and market barriers. Barriers are imposed against import and against foreign business. While the inspiration for such barriers may be economic or political, they are encouraged by local industry. Whether or not the barriers are economically logical the fact is they exist.

Trade barriers can be broadly classified into **tariff** and **non tariff** barriers.

A. Tariff barriers

A tariff is a duty or a tax which is imposed on a commodity when it crosses national borders. A tariff, simply defined, is a tax imposed by a government on goods entering at its border. Tariffs may be used as a revenue-generating tax or to discourage the importation of goods, or for both reasons. In general tariffs increase: inflationary pressures, special interests' privileges, government control and political considerations in economic matters the number of tariffs (they beget other tariffs via reciprocity). And weaken: balance-of-payments positions, supply-and-demand patterns, international

relations (they can start trade wars) Tariff also restrict: manufactures' supply sources, choices available to consumers and competition

In addition, tariffs are arbitrary, discriminatory, and require constant administration and supervision. They often are used as reprisals against protectionist moves of trading partners.

Tariffs can be classified as **protective tariffs** and **revenue tariffs.** The purpose of protective tariff is to protect home industry, agriculture and labor against foreign competitors by trying to keep foreign goods out of the country. Example, Brazil has 50% import tax on imported "flyaway' planes.

Protective tariffs can be further classified according to length of time.

A **tariff surcharge** is a temporary action. To adjust the Japanese imports, President Reagan concentrated national interest to provide import relief. The tariff surcharge on motor vehicles jumped from 4.4% to 45% for one year and declined in subsequent years.

A **countervailing duty** is a permanent surcharge. Countervailing duties are imposed on certain imports when products are subsidized by foreign governments. These duties are thus assessed to offset a special advantage or discount allowed by an exporter's government.

The purpose of a **revenue tariff** is to generate tax revenues for the government. Compared to a protective tariff, a revenue tariff is relatively low. Example: when Japanese and other foreign care are imported to U.S, there is a 3% duty. The U.S tax is a revenue tax: whereas the Japanese tax is more of a protective tariff.

There are three kinds of tax rates applied in tariffs.

1. Specific duties are a fixed or specified amount of money per unit of weight, or other measure of quantity. It is a fixed sum of money charged upon each unit of the commodity imported.

2. Ad-valorem duties are duties 'according to value'. An ad-valorem duty is charged as a fixed percentage of the value of the imported article.

3. Combined rates or duties: Is a combination of the specific and ad-valorem duties on a single product. They are duties based on both the specific rate and the ad-valorem rate that are applied to an imported product.

B. Non tariff barriers

Tariffs are at least straight forward and obvious. Non tariff barriers are more elusive and non transparent. Non tariff barriers can be grouped in to five major categories:

- **Government participation in trade:** The degree of government involvement in trade varies from passive to active. The types of participation include administrative guidance, state trading and subsidies.

- **Customs and entry procedures:** Customs and entry procedures can be employed as non tariff barriers. These restrictions involve classification, valuation, documentation, license, inspection and health and safety regulations.

- **Product requirements:** For goods to center a country, product requirements set by that country must be met. Requirements may apply to product standards and product specifications as well as to packaging, labeling and marking.

- **Quotas:** Quotas – A quota is a specific unit or dollar limit applied to a particular type of goods. Quotas put an absolute restriction on the quantity of a specific item that can be imported. They are specific provisions limiting the amount of foreign products imported in order to protect local firms and to conserve foreign currency. Quotas can be used for export control as well. There are three kinds of quotas: absolute, tariff and voluntary quotas.

- **Financial Control:** Financial regulations can also function to restrict international trade. These restrictive monetary policies are designed to control capital flow so that currencies can be defended or imports controlled.

Chapter summary

This chapter has provided an overview of the process and of the basic issues of international marketing. Similar to domestic marketing, international marketing is concerned with the process of creating and executing an effective marketing mix in order to satisfy the objectives of all parties seeking an exchange. International marketing is

relevant regardless of whether or not the activities are for profit. It is also of little consequence whether countries have the same level of economic development or political ideology, since marketing is a universal activity that has application in a variety of circumstances. The benefits of international marketing are considerable. Trade moderate's inflation and improves both employment and the standard of living, while providing a better understanding of the marketing process at home and abroad. For many companies, survival or the ability to diversify depends on the growth, sales, and profits from abroad. The more commitment a company makes to overseas markets in terms of personnel, sales, and resources, the more likely it is that it will become a multinational corporation. This is especially true when the management is geocentric rather than ethnocentric or polycentric. Since many view multinational companies (MNC) with envy and suspicion, the role of MNCs in society, their benefits as well as their abuses will continue to be debated.

The marketing principles may be fixed, but a company's marketing mix in the international context is not. Certain marketing practices may or may not be appropriate elsewhere, and the degree of appropriateness cannot be determined without careful investigation of the market in question. Key obstacles facing international marketers are not limited to environmental issues. Just as important are difficulties associated with the marketer's own self-reference criteria and ethnocentrism. Both limit the international marketer's abilities to understand and adapt to differences prevalent in foreign markets. A global awareness and sensitivity are the best solutions to these problems, and they should be nurtured in international marketing organizations.

Review questions

1. Distinguish between domestic marketing and international marketing?
2. Distinguish among: (a) ethnocentricity, (b) polycentricity, and (c) geocentricity.
3. What are the benefits of international marketing?
4. List the barriers of international marketing?

Chapter Two
International Marketing Environment

Objective of the chapter

After studying this chapter, you should be able to-

- ✓ Understand the environmental factors faced by global companies
- ✓ Know about the recent economic changes
- ✓ Discuss the role of culture in business.
- ✓ Understand the technological innovations in recent times

2. Introduction

In today's multi-polar world, the conditions under which the business functions are much more complex and uncertain than they were before. Whether by choice or by compulsion,

the business firms have to go international. Strategy formulation entails establishing a proper firm environment that highlights the critical importance of analyzing the international business environment. The essence of any successful business strategy is its environmental orientation. Since, there are some fundamental differences between the business operations in the domestic and the international markets, for a successful strategy, there is a need to understand the complexities of the international markets. It is more than unlikely that a firm can extend its domestic strategies into the foreign markets. Mere understanding of the customer requirements is not enough. A company has to go beyond its internal strategies, understanding customer requirements. What makes a business strategy successful in one market and a failure in another is because of the difference in the firms' capabilities to understand and respond to the international business environment.

Activity: do you believe that culture affect international marketing?

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2.1. Cultural Environment

A worldwide business success requires a respect for local customs. International marketers need to recognize and appreciate varying cultures. Culture plays a significant role in influencing consumer perception, which in turn influences preference and purchase. A good marketing plan can easily go twisted when it clashes with tradition. A marketing mix can be effective only as long as it is relevant to a given culture. One should expect that a product may have to be modified, that a new distribution may have to be found, or that a new promotional strategy may have to be considered. What is more surprising than the blunders which can occur are the underlying causes for these mistakes. The most fundamental problem appears to be the indifferent attitude of many firms toward international markets. The firms often enter foreign markets with a complete disregard for the customs and traditions there – something they would never do at home. In order to develop an appreciation for the role of culture in society as well as the marketing implications of culture, this part will explore the following: (1) what culture is, (2) what its characteristics are, and (3) how culture affects consumer behavior.

A definition of Culture

Anthropology, the study of humans, is a discipline that focuses on the understanding of human behavior. Cultural anthropology examines all human behaviors that have been learned, including social, linguistic, and family behaviors. Culture includes the entire heritage of a society transmitted by word, literature or any other form. It includes all traditions, habits, religion, art, and language.

Culture is a set of traditional beliefs and values that are transmitted and shared in a given society. Culture is also the total way of life and thinking patterns that are passed from generation to generation.

Cultural Influences on Marketing

The function of marketing is to earn profits from the satisfaction of human wants and needs. In order to understand and influence the consumer's wants and needs, marketers must understand the culture, especially in an international environment. Culture is embedded in elements of the society such as religion, language, history, and education. These elements send direct and indirect messages to consumers regarding the selection of goods and services. The culture we live in answers such questions as, Is tea or coffee the preferred drink? Is black or white worn at a funeral? What type of food is eaten for breakfast?

One of the most difficult tasks for global marketers is assessing the cultural influences that affect their operations. In the actual marketplace there are always several factors working simultaneously, and it is extremely difficult to isolate any one factor. Frequently, cultural differences have been held accountable for any noticeable differences between countries. However, when environmental factors differ, what is thought to be cultural may in fact be attributable to other factors. Consumption patterns, lifestyles, and the priority of needs are all dictated by culture. Culture prescribes the manner in which people satisfy their desires. Not only does culture influence what is to be consumed, but it also affects what should not be purchased.

Elements of Culture

Language

Language is a key component of culture because most of a society's culture finds its way into the spoken language. Thus, in many ways, language embodies the culture of the society. Knowing the language of a society can become the key to understanding its

culture. But language is not merely a collection words or terms. Language expresses the thinking pattern of a culture and to some extent even forms the thinking. Today, companies tend to choose product names carefully and test them in advance to ensure that the meaning in all major languages is neutral and positive. They also want to make sure the name can be easily pronounced. Language differences may have caused many blunders, but careful translations have now reduced the number of international marketing mistakes. However, the language barrier still remains, and companies that do more to overcome this barrier frequently achieve better results.

It is also possible to develop cultural empathy through learning a foreign language which is believed to help in developing cultural skill However, even when executives understand each other's language, there can still be plenty of room for misunderstanding. When an American executives says yes in a negotiation, this usually means, "yes, I accept the terms. "However, yes in Asian countries may mean four different things. First, it may mean that the other side recognizes that you are talking to them but not necessarily that they understand what is said. Second, it could mean that what was said was understood and was clear but not that it was agreed to. Third, it may mean that the other party has understood the proposal and will consult with others about it. And finally, yes may mean total agreement. It takes skill to understand just what yes means in any type of negotiation.

Non-Verbal Language

However, achieving some fluency in foreign is not the only cultural barrier to cross. At least as important is the use of nonverbal communication, or body language. Sometimes referred to as the "silent language," this includes such elements as touching, the distance between speakers, facial expressions, and speech inflection, as well as arm and hand gestures

Religion

Many business people ignore the influence religion may have on the marketing environment. There still are, however, religious customs that remain a major factor in international marketing today. Religion impacts people's habits, their outlook on life, the products they buy, the way they buy them, even the newspapers they read. Acceptance of

certain types of food, clothing, and behavior are frequently affected by religion, and such influence can extend to the acceptance or rejection of promotional messages as well. Religion is one of the most sensitive elements of a culture. When the marketer has little or no understanding of a religion, it is easy to offend customers unintentionally.

Education

Though the educational system of a country largely reflects its own culture and heritage, education can have a major impact on how receptive consumers are to foreign marketing techniques. Education shapes people's outlooks, desires, and motivation. To the extent that educational systems differ by country, we can expect differences among consumers. However, education not only affects potential consumers, it also shapes potential employees for foreign companies and for the business community overall. This will influence business practices and competitive behavior.

The Family

The role of the family varies greatly between cultures, as do the roles that the various family members play. Across cultures, we find differences in family sizes, in the employment of women, and in many other factors of great interest to marketers. Particularly since the family is a primary reference group and has always been considered an important determinant of purchasing behavior, these differences are of interest. In some countries, such as China, the family is valued more than individuals or even country resulting in a situation where individuals have no right in a family or expense is shared. In such cultures product advertising appeals must focus on family benefits, not individual benefits.

Family structure is also one cultural factor affecting international marketing decisions. The term nuclear family is normally used to refer to the immediate family group father, mother, and children living together. In cultures such as United States and some Western Europe countries, their family refers to only the nuclear family. However, for many cultures, the extended family including grandparents, in laws, aunts, uncles, and so on is of considerable importance.

Work and Leisure

The attitudes a society holds toward work have been documented to have a substantial impact on a society's or culture's economic performance. David McClelland has maintained that it is not a country's external resources that determine its economic rise but its level of entrepreneurial spirit in exploiting existing resources. What was found to be crucial was the orientation, or attitudes, toward achievement and work. Cultures with a high level of achievement motivation were found to show a faster rise in economic development than those with low achievement motivation.

Well-known German sociologist Max Weber investigated the relationship between attitudes toward work and those toward religion. McClelland later expanded Weber's theory to cover all religions and found that economies with a more protestant orientation exceeded economies with a Catholic orientation in per capita income. McClelland ascribed this difference to the Protestant belief that man did not necessarily receive salvation from God through work but that success in work could be viewed as an indication of God's grace. Consequently, accumulating wealth was not viewed as a shameful activity that needed to be hidden. Traditional Catholic doctrine viewed moneymaking in more negative terms. Thus, religion appears to be a primary influence on attitudes toward work.

Reference Groups

Reference groups are people such as family, friends, celebrities, common man and experts that consumers turn to for advice on product purchases. Past experience clearly indicates that the concept of reference group influence applies to many cultures. Differences can be found in the types of relevant reference groups and in the nature of their influence on individual consumers.

Famous sports celebrities, movie starts, etc., traditionally have been used to exploit the reference group concept. The idea is to tap the prestige of accomplished athletes and movie stars to promote certain products. The challenge is in finding a sport personality or a movie star that people around the world will recognize equally is difficult.

Analysis of the Elements

In general, cultural elements must be evaluated in light of how it could affect a proposed marketing program; some may have only indirect impact, while others may be totally involved. If a company is simply marketing an existing product in an already developed market, studying the total culture is certainly less crucial than for the marketer involved in total marketing from product development through promotion, to the final setting. The effect of all elements of marketing should be seen together since each element is interrelated with the other to produce a specific kind or culture.

The Challenges of Cultural Changes

Culture is dynamic in nature; it is not static, but a living process. But that change is constant seems paradoxical, because another important attribute of culture is that it is conservative and resists change. The dynamic character of culture is significant in assessing new markets even though changes face resistance. There are a variety of ways society changes. Some have change thrust upon them by war (for example, the changes in Japan after World War II) or by natural disaster. More commonly, change is a result of a society seeking ways to solve the problems created by its existence. One view is that culture is the accumulation of a series of the best solutions to problems faced in common by members of a given society.

Accident has provided solutions to some problems; invention has solved many other problems. Usually, however, societies have found answers by looking to other cultures from which they can borrow ideas. Cultural borrowing is common to all cultures. However, even though many behaviors are borrowed from other cultures, they are combined in a unique manner that becomes typical for a particular society. To the foreign marketer, this similar-but different feature of cultures has important meaning in gaining cultural empathy.

Several nationalities can speak the same language or have similar race and heritage, but it does not follow that similarities exist in other respects- that a product acceptable to one culture will be readily acceptable to the other. However, differences run much deeper than language differences. Thus, marketers must assess each country thoroughly in terms of the proposed products or services and never rely on an often used saying that if it sells in one country, it will surely sell in another.

Most cultures tend to be ethnocentric; that is, they have intense identification with the known and the familiar of their culture and tend to devalue the foreign and unknown of other cultures. Ethnocentrism complicates the process of cultural assimilation by producing fallings of superiority about one's own culture and, in varying degrees, generates attitudes that other cultures are inferior, barbaric, or at least peculiar.

There are many reasons cultures resist new ideas, techniques, or products. Even when an innovation is needed from the viewpoint of an objective observer, a culture may resist that innovation if the people lack an awareness of the need for it, local environmental conditions prevent functional use, the innovation is complex in nature affecting the culture's ability to understand it or effectively use it, if it conflicts, customs, traditions, or beliefs. An understanding of the process of acceptance of innovations is of crucial importance to the marketer. The marketer cannot wait centuries or even decades for acceptance but must gain acceptance within the limits of financial resources and project profitability periods.

Marketers have two options when introducing an innovation to a culture: they can wait, or they can cause change. The former requires hopeful waiting for eventual cultural changes that prove their innovations of value to the culture; the latter involves introducing an idea or product and deliberately setting about to overcome resistance and to cause change that accelerates the rate of acceptance.

2.2. Political-Legal Environment

Whether political interests precede or follow economic interests is debatable, but certainly the two are closely interrelated. A country or company may play politics in order to pursue its economic interests, but economic means may also be used to achieve political objectives. As in the case of the steel industry, President Trump imposed the tariffs in 2018, up to 25 percent, on foreign-made steel so as to give the domestic industry time to regroup to become more competitive. The economic interests of multinational companies can differ widely from the economic interests of the countries in which these firms do business. A lack of convergent interests often exists between a company’s home country and its various host countries. In the absence of mutual interests, political pressures can lead to political decisions, resulting in laws and proclamations that affect business. This part examines the interrelationships among political, legal, and business

decisions. The discussion will focus on how the political climate affects the investment climate.

Marketing decisions are thus affected by political considerations. When investing in a foreign country, companies must be sensitive to that country's political concerns. Because of the dynamic nature of politics in general, companies should prepare a contingency plan to cope with changes that occur in the political environment.

Political and legal factors often play a critical role in international marketing activities. Even the best business plans can go wrong as a result of unexpected political or legal influences. A single international political and legal environment does not exist. The business executive must be aware of political and legal factors on a variety of planes. For example, while it is useful to understand the complexities of the host country legal system, such knowledge does not protect against a home-country- imposed export embargo.

We will examine the political -legal environment from the manager's point of view. In making decisions about his or her firm's international marketing activities, the manager will need to concentrate on three areas: the political and legal circumstances of the home country; those of the host country; and the bilateral and multilateral agreements, treaties and laws governing the relations between host and home countries.

1. Home Country Political and Legal Environment

No manager can afford to ignore the policies and regulations of the country from which he/she conducts international marketing transactions. Wherever a firm is located, it will be affected by government policies and the legal system.

Many of these laws and regulations may not be designed specifically to address international marketing issues, yet they can have a major impact on a firm's opportunities abroad. Minimum wage legislation, for example, affects the international competitiveness of a firm using production processes that are highly labor intensive. The cost of domestic safety regulations may significantly affect the pricing policies of firms in their international marketing efforts.

Other legal and regulatory measures, however, are clearly aimed at international marketing activities. Some may be designed to help firms in their international efforts.

Apart from specific areas that result in government involvement, the political environment in most countries tends to provide general support for the international marketing efforts of the country's firms. For example, a government may work to reduce trade barriers or to increase trade opportunities through bilateral and multilateral negotiations. Such actions will affect individual firms to the extent that they affect the international climate for free trade.

Often, however, governments also have specific rules and regulations restricting international marketing. Such regulations are frequently political in nature and are based on the fact that governments believe commerce to be only one objective among others, such as foreign policy and national security. Four main areas of governmental activities are of major concern to the international marketer here. These are: embargoes or trade sanctions, export controls, import controls, and the regulation of international business behavior.

Embargoes and Sanctions

The terms trade sanctions and embargoes as used here refer to governmental actions that distort the free flow of trade in goods, services, or ideas for decidedly adversarial and political, rather than economic, purposes. To understand them better, it is useful to examine the backing and legal justifications under which they are imposed.

Trade sanctions have been used quite frequently and successfully in times of war or to address specific grievances. The basic idea was that economic sanctions could force countries to behave peacefully in the international community.

The problem with sanctions is that frequently a unilateral imposition has not produced the desired result. Sanctions may make the obtaining of goods more difficult or expensive for the sanctioned country, yet achievement of the purported objective almost never occurs. Moreover, unilateral embargoes expose businesses from that country to competitive disadvantage and thus are often fought by business interest. In order to work, sanctions need to be imposed multilaterally, a goal that is clear, yet difficult to implement. Quite often individual countries have different relationships with the country subject to the sanctions, and for one reason or another they cannot or do not wish to terminate trade relations.

In addition, sanctions imposed by governments always raise the issue of compensation for the domestic firms that are affected

Export Controls

Many nations have export control systems designed to deny the acquisition of strategically important. Goods to adversaries or at least to delay their acquisition. Some counties require that an exporter get export license for certain products from the appropriate government offices before the export can take place.

The international marketing repercussions of export controls have become increasingly important. To design a control system that is effective and, in consideration of important national concerns, restricts some international business activities is one thing. It is quite another when controls lose their effectiveness and when, because of a control system, firms are placed at a competitive disadvantage with firms in other countries whose control system is less severe or nonexistent.

Import Controls

Many nations exert substantial restraints on international marketers through import controls. This is particularly true of countries that suffer from major balance-of-trade deficits or major infrastructural problems. These countries, either all imports or the imports of particular products are controlled through mechanisms such as tariffs, voluntary restraint agreements, or quota systems. On occasion, countries cut off imports of certain products entirely in order to stimulate the development of a domestic industry.

For the international marketer, such restrictions may mean that the most efficient sources of supply are not available, because government regulations restrict importation from those sources. The result is either second best products or higher costs for restricted supplies. This in turn means that the customer is served less well and often has to pay significantly higher prices.

Policymakers are faced with several problems when trying to administer import controls. First, most of the time, such controls exact a huge price from domestic consumers. Even though the wide distribution of the burden among many consumers may result in a less obvious burden, the social cost of these controls may be damaging to the economy and subject to severe attack by individuals. However; these attacks are counteracted by pressures from protected groups that benefit from import restrictions. For example, while

citizens of the European Union may be forced because of import controls to pay an elevated price for all agricultural products they consume, agricultural producers in the region benefit from higher levels of income. Achieving a proper trade-off is often difficult not impossible for the policymaker.

A second major problem resulting from import controls is the downstream change in import composition that results from these controls. For example, if the import of copper ore is restricted, either through voluntary restraints or through quotas, producing countries may opt to shift their production systems and produce copper wire instead, which they then export. As a result, initially narrowly defined protectionist measures may have to snowball in order to protect one downstream industry after another.

A final major problem that confronts the policymaker is that of efficiency. Import controls that are frequently designed to provide breathing room to a domestic industry either to grow or to recapture its competitive position often turn out not to work. Rather than improve the productivity of an industry, such controls provide it with a level of safety and a cushion of increased income, yet let overall technological advancement fall behind. Alternatively, supply may respond to artificial stimulation and grow totally out of proportion.

2. Host Country Political and Legal Environment

The host country environment, both political and legal, affects the international marketing operations of firms in a variety of ways. The good manager will understand the country in which the firm operates so that he s/he is able to work within the existing parameters and can anticipate and plan for changes that may occur.

Political Action and Risk

Firms usually prefer to conduct business in a country with a stable and friendly government, but such governments are not always easy to find. Therefore, international managers need to analyze the host country's government, its policies, and its stability to determine the potential for political change that could adversely affect corporate operations.

A manager will want to think twice before conducting business in a country in which the likelihood of conflict and violent change is high. If conflict breaks out, the firm and its employees will possibly face violence in the form of guerrilla warfare, civil disturbances,

or terrorism. Such violence often has an anti-industry element, making companies and their employee's potential targets.

Less dramatic but still worrisome are changes in government policies that are caused, not by changes in the government itself, but as a result of pressure from nationalist or religious factions or widespread anti-foreigner feeling. The aware manager will work to anticipate these changes and plan ways to cope with them.

Generally, international firms need to look for answers to six broad key questions

- How stable is the host country's political system?
- How strong is the host government's commitment to specific rules of the game, such as ownership or contractual rights, given its ideology and power position?
- How long is the government likely to remain in power?
- If the present government is succeeded, how would the specific rule of the game change?
- What would be the expected changes in the specific rule of the game?
- In light of those effects, what decisions and actions should be taken now?

Possible actions of governments:

What sort of changes in policy result from the various events described? The range of possible actions is broad. All of them can affect international marketing operations, but not all are equal in weight. Except for extreme cases, companies do not usually have to fear violence against employees, although violence against company property is quite common. Common also are changes in policy that take a strong nationalist and anti-foreign investment stance. The most drastic steps resulting from such policy changes are usually confiscation and expropriation.

Expropriation was an appealing action to many countries because it demonstrated nationalism and transferred a certain amount of wealth and resources from foreign companies to the host country immediately. It did have costs to the host country, however, to the extent that it made other firms more hesitant to invest in the country. Expropriation does not relieve the host government of providing compensation to the former owners. However, these compensation negotiations are often prolonged and result in settlements that are frequently unsatisfactory to the owners. The use of expropriation as a policy tool has sharply decreased over time.

Confiscation is similar to expropriation in that it results in a transfer of ownership from the foreign firm to the host country. It differs, however, in that it does not involve compensation for the firm.

Some industries are more vulnerable than others to confiscation and expropriation because of their importance to the host country economy and their lack of ability to shift operations. For this reason, sectors such as mining, energy, public utilities, and banking have been targets of such government actions.

Confiscation and expropriation constitute major political risks for foreign investors. Other government actions, however, are nearly as damaging. Many countries are turning from confiscation and expropriation to subtler forms of control, such as domestication. The goal of domestication is the same, to gain control over foreign investment, but the method is different. Through domestication, the government demands partial transfer of ownership and management responsibility, and imposes regulations to ensure that a large share of the product is locally produced and a larger share of the profit is retained in the country.

Domestication can have profound effects on the international marketer for a number of reasons. First, if a firm is forced to hire nationals as managers, poor cooperation and communication can result. If the domestication is imposed within a very short time span, corporate operations overseas may have to be headed by poorly trained and inexperienced local managers. Further, domestic content requirements may force a firm to purchase supplies and parts locally, which can result in increased costs, inefficiency, and lower quality products, thus further damaging a firm's interest. Export requirements imposed on companies may also create confusion for the international distribution plan of a corporation and force it to change or even shut down operations in third countries. Finally, domestication usually will shield the industry within one country from foreign competition. As a result, inefficiencies will be allowed to grow due to a lack of market discipline. In the long run this will affect the international competitiveness of an operation abroad and may become a major problem when, years later, the removal of domestication is considered by the government.

Ways to lessen the risk:

Managers face political and economic risk whenever they conduct business overseas, but there may be ways to lessen the risk. In order to reduce the risk of government intervention, a firm need to demonstrate that it is concerned with the host country's society and that it considers itself an integral part of the host country rather than simply an exploitative foreign corporation. Ways to do this include intensive local hiring and training practices, good pay, more charity, and more socially useful investment. In addition, a company can form joint ventures with local partners in order to demonstrate a willingness to share its benefits with nationals. Although such actions will not guarantee freedom from risk, they will certainly lessen the exposure.

Local borrowing can be taken as another strategy to reduce political risk. Financing local operations from indigenous banks and maintaining a high level of local accounts payable maximize the negative effect on the local economy if adverse political actions were taken. Typically, host governments do not expropriate themselves, and they are reluctant to cause problems for their local financial institutions. It is also advisable to minimize fixed investment in the host country by taking actions like leasing facilities instead of buying them. It is also possible to purchase insurance to cover political risk.

Other actions that can be taken by corporations to protect against political risk consist of the close monitoring of political developments. Increasingly, private sector firms offer assistance in such monitoring activities, permitting the overseas corporation to discover potential trouble spots as early as possible and react quickly to prevent major losses.

Clearly, the international marketer must consider the likelihood of negative political factors in making decisions on conducting business overseas. On the other hand, host-country political and legal systems can have a positive impact on the conduct of international business. Many governments, for example, encourage foreign investments, especially if they believe that the investment will produce economy to foreign investment, will produce economic and political benefits domestically. Some governments have opened up their economy to foreign investors, placing only minimal constraints on them, in the hope that such policies will lead to rapid economic development. Others have provided for substantial subsidization of new investment activities in the hope that investments will generate additional employment. The international marketer, in his investment decision, can and should therefore also pay close

attention to the extent and forms of incentives available from foreign governments. Although international marketing decisions should be driven by market forces, the basic economies of these decisions may change depending on incentives offered.

3. The International Environment

In addition to the politics and laws of both the home and the host countries, the international marketer must consider the overall international political and legal environment. Relations between countries can have a profound impact on firms trying to do business internationally.

International Politics

The effect of politics on international marketing is determined by both the bilateral political relations between home and host countries and by multilateral agreements governing the relations among groups of countries.

The government-to-government relationship can have a profound effect, particularly if it becomes hostile. International political relations do not always have harmful effects on international marketers. If bilateral political relations between countries improve, business can benefit.

The good international marketer will be aware of political currents worldwide and will attempt to anticipate changes in the international political environment, good or bad, so that his or her firm can plan for them.

International Law

International law plays an important role in the conduct of international business. Although no enforceable body of international law exists, certain treaties and agreements respected by a number of countries profoundly influence international business operations. As an example, the World Trade Organization (WTO) defines internationally acceptable economic practices for its member nations. Although it does not directly affect individual firms, it does affect them indirectly by providing a more stable and predictable international market environment.

A number of efforts have been made to simplify business procedures. For example, firms wanting to patent their products in the past had to register them separately in each country in order to have protection. In response to the chaos and expense of such procedures, several multilateral simplification efforts have been undertaken. European

countries have been at the forefront of such efforts, having developed the European Patent Convention and the Community Patent Convention. Similar efforts have been undertaken with regard to trademarks so that firms can benefit from various multilateral agreements.

2.3. THE ECONOMIC ENVIRONMENT

The world economy has changed profoundly since World War II. Perhaps the most fundamental change is the emergence of global markets; responding to new opportunities, global competitors have steadily displaced local ones. Concurrently, the integration of the world economy has increased significantly.

The assessment of a foreign market environment should start with the evaluation of economic variables relating to the size and nature of the markets. Because of the large number of worthwhile alternatives, initial screening of markets should be done efficiently yet effectively enough, with a wide array of economic criteria, to establish a preliminary estimate of market potential.

The discussion that follows is designed to summarize a set of criteria that helps identify foreign markets and screen the most opportune ones for future entry or change of entry mode.

1. Market Characteristics

The main dimensions of a market can be captured by considering variables such as those relating to the population and its various characteristics, infrastructure, geographical features of the environment, and foreign involvement in the economy.

Population

The number of people in a particular market provides one of the most basic indicators of market size and in itself, indicative of the potential demand for certain staple items that have universal appeal and are generally affordable. Population figures themselves must be broken down into meaningful categories in order for the marketer to take better advantage of them. Because market entry decisions may lie in the future, it is worthwhile to analyze population projections in the areas of interest and focus on their possible implications.

Depending on the marketer's interest, population figures can be classified to show specific characteristics of their respective markets. Age distribution and life expectancy

correlate heavily with the level of development of the market. An important variable for the international marketer is the size of the household. A household describes all the persons, both related and unrelated, who occupy a housing unit.

Income

Markets require not only people but also purchasing power, which is a function of income, prices, savings, and credit availability.

A part from basic staple items, for which population figures provide an estimate, income is most indicative of the market potential for most consumer and industrial products and services. For the marketer to make use of information on gross national products of various nations, further knowledge is needed on distribution of income. Per capita GNP is often used as a primary indicator for evaluating purchasing power. In some markets, income distribution produces wide gaps between population groups. The more developed the economy, the more income distribution tends to converge toward the middle class.

In general, income figures are useful in the initial screening of markets. However, in product specific cases, income may not play a major role, and startling scenarios may emerge. Some products, such as motorcycles and television sets in China, are in demand regardless of their high price in relation to wages because of their high prestige value.

Consumption Patterns

Depending on the sophistication of a country's data collection systems, economic data on consumption patterns can be obtained and analyzed. The share of income spent on necessities will provide an indication of the market's development level as well as an approximation of how much money the consumer has left for other purchases.

Infrastructure

The availability and quality of an infrastructure is critically important in evaluating marketing operations abroad. Each international marketer will rely heavily on services provided by the local market for transportation, communication, and energy as well as on organizations participating in the facilitating functions of marketing: marketing communications, distributing, information, and financing. Indicators such as steel consumption, cement production, and electricity production relate to the overall industrialization of the market and a be used effectively by suppliers of industrial products and services. As an example, energy consumption per capita may serve as an

indicator of market potential for electrical markets, provided evenness of distribution exists over the market. Yet the marketer must make sure that the energy is affordable and compatible (in terms of current and voltage) with the products to be marketed.

Foreign Involvement in the Economy

For the international marketer interested in entering a foreign market, it is important to know the extent to which such entry is accepted by a country. An economy's overall acceptance of foreign involvement can be estimated by analyzing the degree of foreign direct investment by country and by industry in a given market as well as by the rules governing such investment.

2. Regional Economic Integration

Economic integration has been one of the main economic developments affecting world markets since World War II. Countries have wanted to engage in economic cooperation to use their respective resources more effectively and to provide larger markets for member-country producers. Some integration efforts have had quite ambitious goals, such as political integration; some have failed as the result of perceptions of unequal benefits from the arrangement or parting of ways politically. Exhibit 3-2, a summary of the major forms of economic cooperation in regional markets, shows the varying degrees of formality with which integration can take place. These economic integration efforts are dividing the world into trading blocs. Each type of economic integration is discussed below.

Exhibit 3-2: Forms of Economic Integration in Regional Markets

Free Trade Association	Free trade among members
Customs Union	Common external trade Policy
Common Market	Factor Mobility
Economic Union	Harmonization of Economic Policies

Levels of Economic Integration

i. Free Trade Area

The free trade area is the least restrictive and loosest form of economic integration among nations. In a free trade area, all barriers to trade among member countries are removed.

Goods and services are freely traded among member countries. Each member country maintains its own trade barriers vis-à-vis nonmembers.

ii. Customs Union

The customs union is one step further along the spectrum of economic integration. As in the free trade area, members of the customs union dismantle barriers to trade in goods and services among members. In addition, however, the customs union establishes a common trade policy with respect to nonmembers. Typically, this takes the form of a common external tariff, where imports from nonmembers are subject to the same tariff when sold to any member country.

iii. Common Market

The common market amounts to a customs union covering the exchange of goods and services, the prohibition of duties in exports and imports between members, and the adoption of a common external tariff in respect to nonmembers. In addition, factors of production (labor, capital, and technology) are mobile among members. Restrictions on immigration and cross-border investment are abolished.

iv. Economic Union

The creation of a true economic union requires integration of economic policies in addition to the free movement of goods, services, and factors of production across borders. Under an economic union, members will harmonize monetary policies, taxation, and government spending. In addition, a common currency is be used by members. This could be accomplished, de facto, by a system of fixed exchange rates. Clearly, the formation of an economic union requires members to surrender a large measure of their national sovereignty to supranational authorities in community wide institutions such as the European Parliament. The final step would be a political union calling for political unification.

Economic Integration and the International Marketer

Regional economic integration creates opportunities and potential problems for the international marketer. It may have an impact on a company's entry mode by favoring direct investment because one of the basic rationales of integration is to generate favorable conditions for local production and intraregional trade. By design, larger

markets are created with potentially more opportunity. Because of harmonization efforts, regulations may be standardized, thus positively affecting the international marketer.

The international marketer must, however, make integration assessments to envision the outcome of the change. Change in the competitive landscape can be dramatic if scale opportunities can be exploited in relatively homogeneous demand conditions. The international marketer will have to take into consideration varying degrees of change readiness within the markets themselves; that is, governments and other stakeholders, such as labor unions, may oppose the liberalization of competition in all market segments. For example, while plans have called for liberalization of air travel and automobile marketing in Europe, European Union (EU) members have found loopholes to protect their own companies.

The international marketer will then have to develop a strategic response to the new environment to maintain a sustainable long-term competitive advantage.

Economic integration will create its own powers and procedures similar to those of the EU and its directives. The international marketer is not powerless to influence both of them; as a matter of fact, a passive approach may result in competitors gaining an advantage or it may put the company at a disadvantage.

2.4. Technological Environment

Technology is changing day by day at a greater pace that it causes a major threat for domestic as well as international marketing. Due to globalization effect, there has been unlimited innovational opportunities worldwide. Moreover, international marketers are pumping out more resources for research and development activities of their products. Ultimately technology change is a force for creative destruction. Technological advances have had substantial effect on the variety of goods and services.

Chapter Summary

Culture prescribes acceptable beliefs, traditions, customs, and values that are then socially shared. Culture is subjective, enduring yet dynamic, and cumulative. It affects people’s behavior in diverse ways through logic, communication, and consumption. Although some cultural traits are universal, many others are unique and vary from

country to country. And in spite of national norms, cultural differences as a rule even exist within each country.

The international marketer's political environment is complex and difficult due to the interaction among domestic, foreign, and international politics. If a product is imported or produced overseas, political groups and labor organizations accuse the marketer of taking jobs from people in the home country. On the other hand, foreign governments are not always receptive to overseas capital and investment because of suspicions about the marketer's motives and commitment. When both the host country and the home country have different political and national interests, their conflicting policies can complicate the problem further.

Review questions

1. What are the characteristics of culture?
2. Explain the impact of culture on consumption?
3. What measures can be undertaken to minimize political risk?

Chapter Three

International Market Entry Modes

Chapter objectives

After studying this chapter, you will be able to:

- Identifying international marketing entry modes
- Define each international market entry mode
- Differentiate the advantage and disadvantage of each international marketing entry decision
- Identify the criteria for selecting a market entry mode

3.Introduction

Even a large multinational corporation, with all its power, still has to adapt its operating methods and formulate multiple entry strategies. The dynamic nature of many overseas markets makes it impossible for a single method to work effectively in all markets. This chapter is devoted to a coverage of the various market entry strategies. Some of these techniques – such as exporting, licensing, and management contracts – are indirect in the sense that they require no investment overseas. Other techniques, however, require

varying degrees of foreign direct investment. These foreign direct investment methods range from joint venture to complete overseas manufacturing facilities, with such strategies as assembly operations, turnkey operations, and acquisitions falling somewhere in between. These strategies do not operate in sequence, and any one of them can be appropriate at any time. Further, the use of one strategy in one market does not rule out the use of the other strategies elsewhere. The methods vary in terms of risk accepted and, to a certain extent, the degree of commitment to the foreign market. Another purpose of this chapter is to discuss the advantages and disadvantages associated with each method. Factors that have an impact on the appropriateness of entry methods are covered in order to provide guidelines for the selection of market entry strategies.

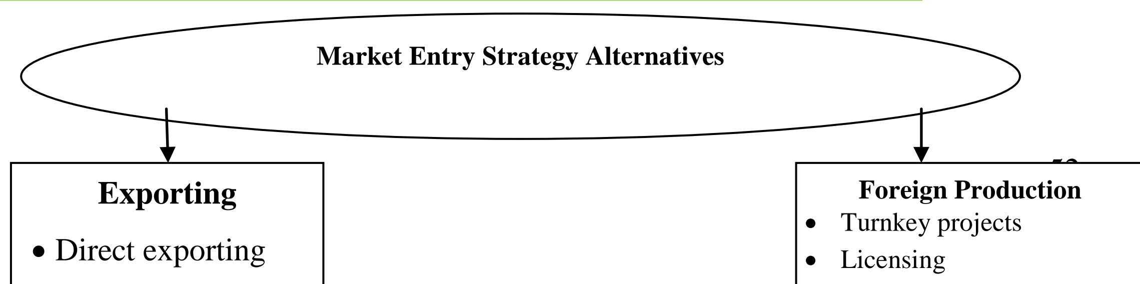
Activity

How products from china available in Ethiopian market?

3.1 MARKET ENTRY DECISION

When a firm is considering entering a foreign market, the question arises as to the best means of achieving it. There are basically eight ways to enter a foreign market: exporting, turnkey projects, licensing, franchising, management contracts, joint venturing with a host-country firm, and setting up a wholly owned subsidiary in the host country. Each entry mode has advantages and disadvantages. Managers need to consider these carefully when deciding which entry mode to use.

Figure 3.1 Market Entry Strategies



1.8.4. Exporting

Exporting is a strategy in which a company, without any marketing or production organization overseas, exports a product from its home base. Often, the exported product is fundamentally the same as the one marketed in the home market. Most manufacturing firms begin their global expansion as exporters and only later switch to another mode for serving a foreign market. Here we focus on the advantages and disadvantages of exporting as an entry mode.

Advantages:

The main advantage of an exporting strategy is the ease in implementing the strategy. Risks are minimal because the company simply exports its excess production capacity when it receives orders from abroad. As a result, its international marketing effort is casual at best. This is very likely the most common overseas entry approach for small firms. Many companies employ this entry strategy when they first become involved with international business and may continue to use it on a more or less permanent basis. Since most countries do not offer a large enough opportunity to justify local production,

exporting allows a company to centrally manufacture its products and, therefore obtain economies of scale. It avoids the costs of establishing manufacturing operations in the host country, which are often substantial. Exporting also may help a firm achieve and exporting it to other national markets, the firm may be able to realize substantial scale of economies from its global sales volume.

Disadvantages:

The problem with using an exporting strategy is that it is not always an optimal strategy. A desire to keep international activities simple, together with a lack of product modification, make a company's marketing strategy inflexible and unresponsive. The exporting strategy functions poorly when the company's home country currency is strong.

- Exporting from the firm's home base may not be appropriate if there are lower-cost locations for manufacturing the product abroad.
- High transport costs can make exporting uneconomical, particularly for bulk products.
- Tariff barriers can make it uneconomical. Similarly, the threat of tariff barriers by the host-country government can make it very risky.
- When a firm delegates its marketing in each country where it does business to a local agent, the foreign agent may not do as good a job as the firm would if it managed its marketing itself. This problem is common for firms that are just beginning to export.

Activity

List Ethiopian products exported to world market?

____
____
____

1.8.5. Turnkey projects

A turnkey operation is an agreement by the seller to supply a buyer with a facility fully equipped and ready to be operated by the buyer's personnel, who will be trained by the seller. The term is sometimes used in fast-food franchising when a franchisor agrees to select a store site, build the store, equip it, train the franchisee and employees, and sometimes arrange for the financing. In international marketing, the term is usually associated with giant projects that are sold to governments or government-run companies.

Large-scale plants requiring technology and large-scale construction processes unavailable in local markets commonly use this strategy. Such large-scale projects include building steel mills; cement, fertilizer, and chemical plants; and those related to such advanced technologies as telecommunication.

Firms that specialize in the design, construction, and start-up of turnkey plants are common in some industries. In a turnkey project, the contractor agrees to handle every detail of the project for a foreign client including the training of operation personnel. At completion of the contract, the foreign client handled the "key" to a plan that is ready for full operation –hence the term turnkey. This is actually a means of exporting process technology to other countries. I a sense it is just a very specialized kind of exporting. Turnkey projects are most common in the chemical, pharmaceutical, petroleum refining, and metal refining industries, all of which use complex, expensive production-process technologies.

Advantages:

- They are a way of earning great economic returns from the asset. (The know-how required to assemble and run a technologically complex process, such as refining petroleum or steel, is a valuable asset.)
- It is particularly useful in cases where foreign direct investment (FDI) is limited by host-government regulations.
- It is useful to invest in a country were the political and economic environment is unstable such that a longer-term investment might expose the firm to unacceptable political and/or economic risks (e.g., the risk of nationalization or of economic collapse)

Disadvantage

- The firm that enters into a turnkey deal will have no long-term interest in the foreign country. This can be a disadvantage if that country subsequently proves to be a major market for the output of the process that has been exported.
- The firm that enters into a turnkey project with a foreign enterprise may inadvertently create a competitor.

- If the firm's technology is a source of competitive advantage, then selling this technology through a turnkey project is also selling competitive advantage to potential and/or actual competition.

1.8.6. Licensing

When a company finds exporting ineffective but is hesitant to have direct investment abroad, licensing can be a reasonable compromise.

Licensing is an agreement that permits a foreign company to use industrial property (i.e., patents, trademarks, and copyrights), technical know-how and skills (e.g. Feasibility studies, manuals, technical advice), architectural and engineering designs, or any combination of these in a foreign market. Essentially, a licensor allows a foreign company to manufacture a product for sale in the licensee's country and sometimes in other specified markets. A licensing agreement is an arrangement whereby a licensor grants the rights to intangible property to another entity (the licensee) for a specified period of time, and in return, the licensor receives a royalty fee from the licensee. Intangible property includes patents, inventions, formulas, processes, designs, copyrights and trademarks.

Advantages:

- The firm does not have to bear the development costs and risks associated with opening a foreign market. To reduce the need for a large amount of investment for fixed assets.
- Licensing is a very attractive option for firms lacking the capital to develop operations overseas.
- Licensing can be attractive when a firm is unwilling to commit substantial financial resources to an unfamiliar or politically volatile foreign market.
- Licensing is also often used when a firm wishes to participate in a foreign market but is prohibited from doing so by barriers to investment.
- To operate oversea where, a company may not have the knowledge or the time to engage more actively in international marketing.

Disadvantages

- It limits the firm's ability to realize experience curve and location economies by manufacturing its products in a centralize location.

- Competing in a global market may require a firm to coordinate strategic moves across countries by using profits earned in one country to support competitive attacks in another. But licensing severely limits a firm's ability to do this. A licensee is unlikely to allow a multinational firm to use its profits (beyond those due in the form of royalty payments) to support a different licensee operating in another country.
- A firm can quickly lose control over its technology (technological know-how) by licensing it.
- Insuring a uniform quality requires additional resources from the licenser that may reduce the profitability of the licensing activity.

1.8.7. Franchising

In many respects, franchising is similar to licensing, although franchising tends to involve longer-term commitments than licensing. Franchising is basically a specialized form of licensing in which the franchisor not only sells intangible property to the franchisee (normally a trademark), but also insists the franchisee agree to abide by strict rules as to how it does business. The franchisor will also often assist the franchisee to run this business on an ongoing basis. As with licensing the franchisor typically receives a royalty payment that amounts to some percentage of the franchisee's revenues. Whereas licensing is pursued primarily by manufacturing firms, franchising is employed primarily by service firms.

McDonald's provides us with a good example of a firm that has grown by using a franchising strategy. McDonald's has set down strict rules as to how franchisees should operate a restaurant. These rules extended to control over the menu, cooking methods, staffing policies, and the design and location of a restaurant. McDonald's also organizes the supply chain for its franchisees and provided management training and financial assistance for franchisees.

Advantages:

- By using franchising strategy, a service firm can build a global presence quickly and at a relatively low cost and risk.
- The firm is relieved of many of the costs and risks of operating in a foreign market by itself. Instead, the franchisee typically assumes those costs and risks. This creates a

good incentive for the franchisee to build up a profitable operation as quickly as possible.

Disadvantage:

- Franchising inhibit the firm's ability to take profits out of one country to support competitive attacks in another.
- Quality control in franchising is mandatory. A more significant disadvantage of franchising comes from difficulty to quality control because of;
  - geographical distance of the firm from its foreign franchisees and
  - the sheer number of franchisees.

The foundation of franchising arrangements is that the firm's brand name conveys a message to consumers about the quality of the firm's product. So consumers need to experience the same product quality wherever they are. So the result of poor quality in one foreign market can extend beyond lost sales in particular foreign market to a decline in the firm's worldwide reputation.

1.8.8. Management contracts

An arrangement whereby a company operates a foreign firm for a client who retains the ownership is known as management contract. There are a number of variations but a broad distinction between foreign management and local ownership is a characteristic feature, and the management typically extends to all functions.

In the management contract the principal (the contractor) operates a complete management system. This method of conducting business has only gradually emerged. It can be said to carry the divorce between ownership and management that has been a feature of the business scene for many years, one stage further.

Management contracts may be used as a sound strategy for entering a market with a minimum investment and minimum political risks. In a basic management contract the local (host country) company holds all the equity, but in practice the contractor often takes a small amount. The holding of equity makes it easier to negotiate the other terms; the contractor company does not feel so encouraged to provide for an increasing royalty in the event of success as it knows that it will share anyway. On the other hand, the holding of equity may bias the advice the contractor gives, especially when it's not managing all the functions.

Advantage:

The reasons for developing management contracts as policies are similar to those; or licenses and franchises with a number of additions which include the following, Dissatisfaction with an existing licensing agreement where the licensee or franchisor does not show sufficient marketing, financial or other expertise to develop the business.

The expropriation or nationalization of a subsidiary where the parent company's commercial expertise is still required. When fees for management services may be easier to transfer, and subject to less tax than royalties or dividends. The case of under-employed-skills and resources are common factors in deciding to opt for management contracts. The contracts provide a useful contribution to a global strategy. They are particularly appropriate to the more difficult markets in the less developed countries. Management contracts can provide support to other business arrangements, tike technical agreements and joint ventures, and general support for existing markets where domestication or expropriation are likely. Minority equity holdings are also safeguarded in this way. For countries, this method brings the foreign expertise without the drawbacks of foreign ownership.

Disadvantages:

The disadvantages are similar to those for licenses and franchises.

- From the principal's point of view, direct export or investment might have been more lucrative.
- From the point of view of some countries, contracts are still regarded as the intervention of a foreign authority- and the issue of foreign management remains delicate, however badly it may be needed.

1.8.9. Joint Ventures

The joint venture is another alternative a firm may consider as a way of entering an overseas market. A joint venture is simply a partnership at corporate level, and it may be either domestic or international. For the discussion here, an international joint venture is one in which the partners are from more than one country.

A joint venture entails establishing a firm that is jointly owned by two or more otherwise independent firms. Establishing a joint venture with a foreign firm has long been a popular mode for entering a new market. The most typical joint venture is a 50/50

arrangement in which there are two parties, each of which holds a 50 percent ownership stake and contributes a team of managers to share operating control. Some firms however, have sought joint ventures in which they have a majority share and thus tighter control.

Advantages:

- A firm is able to benefit from a local partner's knowledge of the host country's competitive conditions, culture, language, political systems, and business systems.
- When the development costs and/or risks of opening a foreign market are high, a firm might gain by sharing these costs and/or risks with a local partner.
- Local partners minimize the influence of political/legal factors of the host country.
- Joint ventures are sometimes necessary to enter countries where the economy is largely under state control. In such countries, foreign investors are only allowed to take minority positions in conjunction with local firms.

Disadvantages:

- A firm that enters into a joint venture risks giving control of its technology to its partner.
- A joint venture does not give a firm the tight control over subsidiaries that it might need to realize experience curve or location economies.
- It does not give a firm the tight control over a foreign subsidiary that it might need for engaging coordinated global attacks against its rivals.
- Shared ownership arrangement can lead to, conflicts and battles for control between the investing firms if their goals and objectives change over time, or if they take different views as to what the strategy of the venture should be.

1.8.10. Strategic Alliances

It is a business relationship established by two or more companies to cooperate out of mutual need and to share risk in achieving a common objective. It is a situation when each partner brings a particular skill or resource (usually they are complementary) and by joining forces, each expects to profit from the other's experience. In alliance, two entire firms pool their resources directly in a collaboration that goes beyond the limits of a joint venture. Although a new entity may be formed, it is not a requirement. Typically,

alliances involve distribution access, technology transfers, or production technology, with each partner contributing a different element to the venture.

The alliance can be, technology-based alliance, product-based alliance, Distribution-based alliance. Strategic alliance implies that there is a common objective, alone partner's weakness is offset by the other's strength, reaching the objective alone would be too costly, take too much time, or be too risky; and, together their respective strength make possible what otherwise would be unattainable.

Reasons for going into strategic alliances include

- To gain access to new technologies and acquire the skills necessary to achieve their objectives more efficiently, at a lower cost, or with less risk than if they acted along.
- To enter" blocked" markets
- To reduce required investment
- To gain access to a brand name or customer group
- To achieve more global coverage, etc.

Problems/ Disadvantage

- Partners may disagree on further investment
- Different expectations of return
- Inability to change with changing market conditions
- Cultural communications barriers
- Difficulties in integrating the two companies' accounting and information systems

8. Wholly Owned Subsidiaries

In a wholly owned subsidiary, the firm owns 100 percent of the subsidiary. Establishing a wholly owned subsidiary in a foreign market can be done in two ways. The firm can either setup a new operation in that country or it can acquire an established firm or use that firm to promote its products in the country's market.

Advantages:

- When a firm's competitive advantage is based on technological competence, a wholly owned subsidiary will often be the preferred entry mode, since it reduces the risk of losing control over that competence.
- A wholly owned subsidiary gives a firm the kind of tight control over operations in different countries that are necessary for engaging in global strategic

coordination(i.e., using profits from one country to support competitive attacks in another).

- A wholly owned subsidiary may be required if a firm is trying to realize location and experience curve economies (as firms pursuing global and transnational strategies try to do).

Disadvantages:

- Establishing a wholly owned subsidiary is generally the most costly method of serving a foreign market.
- Firms doing this must bear the full costs and risks of setting up overseas operations.

3.2 Selecting an Entry Mode

As the preceding discussion demonstrated, there are advantages and disadvantages associated with all the entry modes. Due to these advantages and disadvantages, trade-offs are inevitable when selecting an entry mode. For example, when considering entry into an unfamiliar country with a track record for nationalizing foreign enterprises, a firm might favor a joint venture with a local enterprise. Its rationale might be that the local partner will help it establish operations in an unfamiliar environment and will speak out against nationalization should the possibility arise. However, if the firm's core competence is based on proprietary technology, entering a joint venture might risk losing control of that technology to the joint-venture partner in which case the strategy may seem very unattractive. Despite the existence of such trade-offs, it is possible to make some generalizations about the, optimal choice of entry mode.

1.9. Criteria for selecting a market entry mode

Selection of market entry mode has an important bearing on strategy, and can later prove to be a severe constraint on future intended international expansion unless due care and attention has been exercised in terms of any contractual arrangement. The criteria to be considered include:

1. **Speed of market entry desired:** If speed is required, building up a wholly owned subsidiary is too slow and so acquisition and licensing or exporting will be the likely ways to ensure quick effective distribution in the foreign market.

2. **Costs to include direct and indirect costs:** Subjectivity which is ever present may force a wrong decision. Commitment to establishing a market presence does not mean blindness to facts. Possible savings may be outweighed by indirect costs such as freight, strikes, or disruptions to output, lack of continuity with the power supply, or irregularity in the supply of raw materials. Against this the cost of doing nothing has to be considered; this may be higher than the attendant risks of moving into a relatively unknown market.
3. **Flexibility require –** The laws of a country exist to protect that country's nationals. There is as yet no such thing as international law. In disputes between two countries the domestic law of a neutral third country is often called on, so that domestic law then becomes used for a purpose for which it was never designed; international disputes.
4. **Risk factors - including** political risk and economic as well as competitive risk. In a dynamic market, time is of the essence. No product remains 'new' forever. Getting the product to market is important but so, too, is avoiding the creation of a competitor, a common criticism of licensing. Risk may be diminished by minimizing the investment stake in the company by accepting a local joint-venture partner.
5. **Investment payback period –** Sorter-term payback may be realized from licensing and franchising deals, whereas joint ventures or wholly owned subsidiaries will tie up capital for a number of years.
6. **Long-term profit objectives –** the growth expected in that market for the years ahead. Here, the question of distribution channel policy is very important. A wholly owned foreign subsidiary may build up its own technical service department alongside a small but growing sales team.

Chapter Summary

If a company wants to avoid foreign direct investment when marketing in foreign markets, it has a number of options. It can export its product from its home base, or it can grant a license permitting another company to manufacture and market its product in a foreign market. Another option is to sign a contract to sell its expertise by managing the business for a foreign owner.

If the firm is interested in making foreign direct investment, it can either start its business from the ground up or acquire another company. The acquisition, however, may receive a less than enthusiastic response from the foreign government. If the company decides to start a new business overseas, it must consider whether a sole venture or joint venture will best suit the objective. Sole ventures provide a company with better control and profit whereas joint ventures reduce risk and exploit the strengths of a local partner. Regardless of whether a sole venture or joint venture is used, the company must still decide whether local production is going to be complete or partial (i.e., assembly). Finally, foreign sales to governments often take the form of giant turnkey projects that require the company to provide a complete package, including financing, construction, and training.

Once a particular market is chosen, management needs to decide on the market entry strategy. In addition, the company should consider the feasibility of operating all or some of its international business in a free trade zone, since such a zone can complement many of the market penetration options. Each market entry strategy has its own unique strengths and weaknesses. In most circumstances the strategies are not mutually exclusive. A manufacturer may use multiple strategies in different markets as well as within the same market. No single market entry is ideal for all markets or all circumstances. The appropriateness of a strategic option depends on corporate objectives, market conditions, and political realities.

Review questions

1. Briefly explain these market entry strategies:
   - **A.** Exporting
   - **B.** Licensing
   - **C.** Joint venture
   - **D.** Manufacturing
   - **E.** Assembly operations
   - **F.**Management contract
   - **G.** Turnkey operations
   - **H.** Acquisition
2. Since exporting is a relatively risk-free market entry strategy, is there a need for a company to consider other market entry strategies?
3. Can a service be licensed for market entry purposes?

CHAPTER FOUR

4. PRODUCT POLICY DECISIONS

Chapter Objectives

After studying this Chapter you should be able to explain;

- the difference between product standardization and product adaptation
- the branding and packaging decision
- International product life cycle

4.1 INTRODUCTION

If you travel around the world, you will come across familiar products and brands. You can see Coca-Cola, Xerox, Levi's, Mercedes etc. just about everywhere. These are global products. All products, however, are not available worldwide. These are called local products. Some companies specialize in global products while others develop local products. Let us focus our attention on the decisions managers take to offer products to international markets.

4.2 PRODUCT STANDARDIZATION V/S ADAPTATION

Activity 1

Differentiate between product standardization and product adaptation

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When management does not match products with target markets effectively, a product blunder occurs. Two common reasons are:

- Marketing wrong products to wrong market
- Marketing right product but not adapting the products according to the needs of the target market.

These reasons call for two tasks to be performed by the managers when they formulate product strategies for overseas markets. The first task is to take care in deciding what product to market and the second is to decide whether the company should standardize its products or adapt according to the needs of the market.

Some international firms enjoy strong customer preferences for their products. When these conditions occur, customer adaptation needs are minimal, and companies can follow a global strategy, selling a standardized product on a worldwide basis. IBM, Xerox, Coca-Cola, and Mercedes-Benz are example. Other firms have to cater to market specific needs to be successful. These firms use product adaptation strategies. Levi's, for example, sells its blue jeans internationally but adjusts to different body types in different countries. McDonalds has also adapted its menu according to Indian customer's tastes and preferences by using cheese instead of ham and pork in its burgers.

A. Product Adaptation

Product Adaptation- modifying product to reflect characteristics of a market

Premise-- consumers are not the same

Advantages: improved fit between product and consumer, expanded penetration

Factors encouraging adaptation are:

- Differing usage conditions. These may be due to climate, skills, level of literacy, culture or physical conditions.
- General market factors - incomes, tastes etc.
- Government - taxation, import quotas, non tariff barriers, labelling, health requirements.
- Financial considerations. In order to maximize sales or profits the organization may have no choice but to adapt its products to local conditions.
- Pressure. Sometimes, as in the case of the EU, suppliers are forced to adapt to the rules and regulations imposed on them if they wish to enter into the market.

B. Product Standardization

Standardization- developing same product for multiple countries

- Premise-- consumes share some common values, beliefs, and consumption patterns
- **Advantages:** economies of scale and scope, price competitiveness, uniform image

Aims of standardization and Standards

Standard is a document which provides, inter alia, requirements, rules, and guidelines, for a process, product or service. These requirements are sometimes complemented by a description of the process, products or services. Following are the primary aims of standardization:

1. **Fitness for purpose**

Fitness for purpose is the ability of the process, product or service to fulfill a defined purpose under specific conditions. Any product, process or service is intended to meet the needs of the user. Sometimes the expectations of the users may be at variance with the actual purpose. In addition, it is difficult for the users to always spell out the desirable quality of the process, product or service. Standards help by identifying the optimum parameters for the performance of a process, product or service (e.g. product standards) and the method for evaluating product conformity (such as test method standards and quality control standards). Standards also lay down conditions for using the process, product or service, as otherwise any failure of the process, product or service due to

improper use may be attributed by the users to a deficiency or lack of quality of the process, product or service.

2. **Interchangeability**

The suitability for a process, product or service to be used in place of another to fulfill a relevant requirement is called interchangeability. Through a deliberate standardization process, it is possible to make processes, products or services interchangeable, even if they are created in different countries. For example, shaving blades of different brands may be designed to be used in the same razor, injection needles of different sizes and brands may be designed to fit the same hypodermic syringe.

3. **Variety reduction**

It is popularly believed that variety is the spice of life. While a large number of varieties for a particular process, product or service may be helpful to consumers and enable them to select the most appropriate; this large number of varieties requires large inventories, resulting in high costs to manufacturers. Variety reduction is one of the aims of standardization for the selection, inter alia, of the optimum number of sizes, ratings, grades, compositions and practices to meet prevailing needs. Balancing between too many and too few varieties is in the best interest of both manufacturers and consumers.

4. **Compatibility**

Parallel developments of processes, products or services, which are required to be used in combination, pose problems if they are not compatible. One of the aims of standardization is compatibility, namely, suitability of processes, products or services to be used together under specific conditions to fulfill the relevant requirements, without causing unnecessary interaction. For example in electronic data processing, information has to be coded for storage, transmission and retrieval in the form of electronic pulses. To make the code recognizable for any machine and all times, it has to be standardized. Such standardization helps to establish compatibility between various machines or subsystems and permits expansion features and information exchange amongst different systems.

5. **Guarding against factors that affect the health and safety of consumers**

Safety of the process, product or service is of great importance if, under certain conditions, the use of the process, product or service may pose a threat to human life or property. Therefore, identification of processes, products or services and their safety

parameters, not only under normal use but under possible misuse, is one of the important requirements of standardization. For example, items for human consumption should be free from poisonous substances: if food colors are used in candy or sweets, they should be free from poisonous substances like lead or arsenic. If an electrical appliance is manufactured, it should be well insulated to be free from electrical hazards: electric irons, for example, should be designed so as to guard their user against electrical shock from any part of the iron. Safety standards also broadly cover the requirements to ensure the safety of equipment (e.g. a dust proof enclosure for equipment) and that of people and the environment (e.g. flame proof enclosures for equipment used in mines).

6. Environmental protection

Environmental protection is an important aim of standardization: the focus here is on preserving nature from damage that may be caused during the manufacture of a product or during its use or disposal after use. For example, the domestic use of a washing machine should generate only a minimum of pollutants.

7. Better utilization of resources

Achievement of maximum overall economy through better utilization of resources such as capital, human effort and materials is an important aim of standardization. In manufacturing organizations, it is this aspect of standardization of materials, components and production methods that makes it possible to reduce waste and to carry out mass production in an economic way. For example, in construction and civil engineering, the use of the appropriate quantities of cement and steel to achieve a required strength are recommended in building standards and codes of practices.

8. Better communication and understanding

Whenever the transfer of goods and services is involved, standards spell out what means of communication are to be used between different parties. Since standards contain information that is recorded in a precise and documented form, they contribute towards better communication and understanding in a large variety of settings.

9. Transfer of technology

Standards act as a good vehicle for technology transfer. Since standards incorporate the results of advances in science, technology and experience, they reflect the state of the art

in technical development. As standardization is a dynamic process, standards are updated as new technologies are developed.

10. Removal of trade barriers

Restrictions on the export of processes, products or services by the introduction of some technical barriers to trade, such as arbitrary product requirements, are being viewed with great concern. Standards prevent such non-tariff barriers to trade by harmonizing requirements in a manner that promotes fair competition. Purchasers can be convinced about the quality level of a product that has been manufactured according to a recognized standard.

Benefits of standardization

By its very definition, standardization is aimed at achieving maximum overall economy. Standards provide benefits to different sectors of society. Some of the benefits of standardization are as follows:

1. **For manufacturers, standards:**
    - Rationalize the manufacturing process.
    - Eliminate or reduce wasteful material or labor.
    - Reduce inventories of both raw material and finished products.
    - Reduce the cost of manufacture.
2. **For customers, standards:**
    - Assure the quality of goods purchased and services received.
    - Provide better value for money.
    - Are convenient for settling disputes, if any, with suppliers.
3. **For traders, standards:**
    - Provide a workable basis for acceptance or rejection of goods or consequential disputes, if any.
    - Minimize delays, correspondence, etc., resulting from inaccurate or incomplete specification of materials or products.
4. **For technologists, standards:**

Provide starting points for research and development for further improvement of goods and services.

4.3 INTERNATIONAL PRODUCT LIFE CYCLE

Product life cycle is a well – known theory in marketing. But its international counterpart, International Product Life Cycle (IPLC), is relatively unknown. The theory developed and verified by economists to explain international trade in a context of comparative advantage, has been covered rather briefly in some international economics and international marketing texts and in a few marketing articles.

The IPLC theory describes the diffusion process of an innovation across national boundaries. The life cycle begins when a developed country, having a new product to satisfy consumer needs, wants to exploit its technological breakthrough by selling abroad. Other advanced nations soon start up their own production facilities, and before long Least Developed Countries (LDCs) do the same. Efficiency/comparative advantage shifts from developed countries to developing nations. Finally, advanced nations, no longer cost – effective, import products from their former customers. The moral of this process could be that an advanced nation becomes a victim of its own creation.

One reason that IPLC theory has not made a significant impact is that its marketing implications are somewhat obscure, even though it has the potential to be a valuable framework for marketing planning on a multinational basis. In this section, the IPLC is examined from the marketing perspective, and marketing implications for both innovators and imitators are discussed.

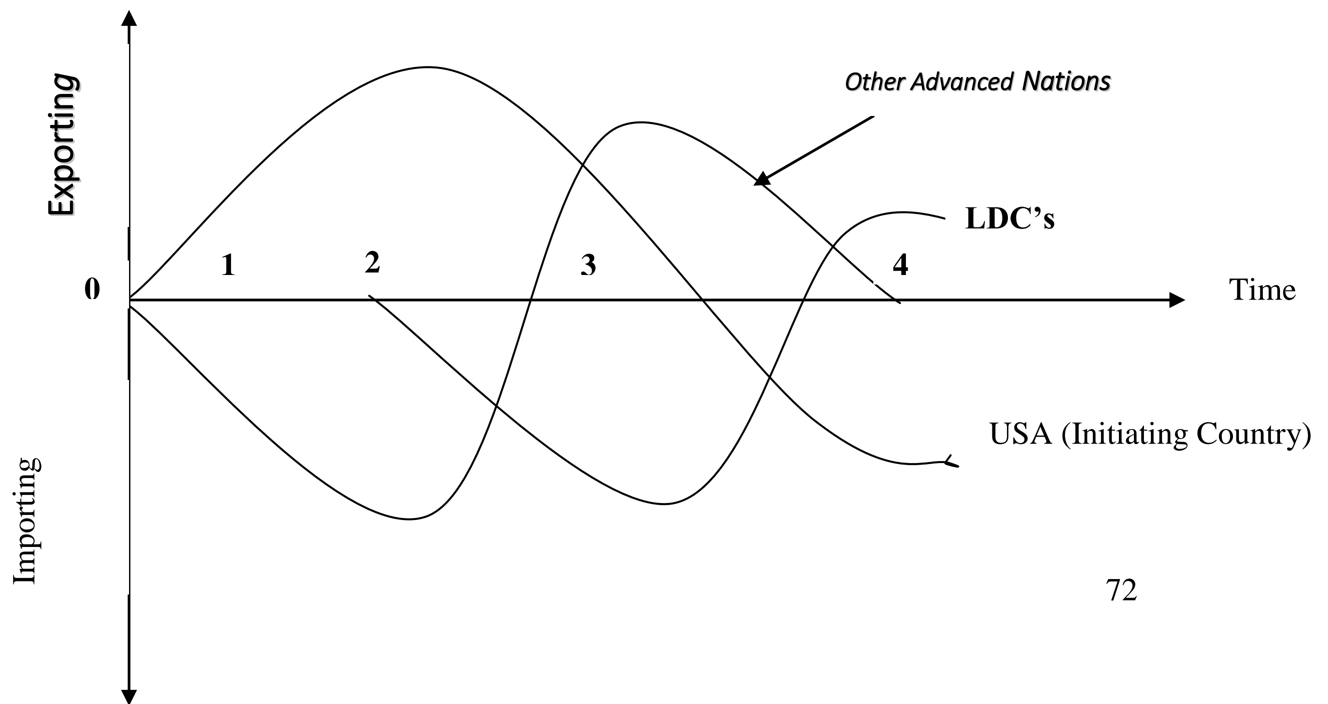
Stages and characteristics

There are five distinct stages (stage 0 through Stage 4) in the IPLC. Table 2-1 shows the major characteristics of the IPLC stages, with the United States as the developer of the innovation in question. Exhibit 2-2 shows three life – cycle curves for the same innovation: one for the initiating country (i.e., the United States in this instance), one for other advanced nations, and one for LDCs. For each curve, net export results when the curve is above the horizontal line; if under the horizontal line, net import results for that particular country. As the innovation moves through time, directions of all three curves change. Time is relative, because the time needed for a cycle to be completed varies from

one kind of product to another. In addition, the time interval also varies from one stage to the next.

Table 4-1 IPLC stages and characteristics (for the initiating country)

Stage		Import/Export	Target Market	Competitors	Production Costs
0	Local Innovation	None	USA	Few: Local Firms	Initially High
1	Overseas Innovation	Increasing Export	USA & Advanced Nations	Few: Local Firms	Decline Owing to Economies of Scale
2	Maturity	Stable Export	Advanced Nations & LDCs	Advanced Nations	Stable
3	Worldwide Imitation	Declining Export	LDCs	Advanced Nations	Increase Owing to Lower Economics of Scale
4	Reversal	Increasing Import	USA	Advanced Nations & LDCs	Increase Owing to Comparative Disadvantage



IPLC curves

1. Stage 0 – Local Innovation

Stage 0, depicted as time 0 on the left of the vertical importing/exporting axis, represents a regular and highly familiar product life cycle in operation within its original market. Innovations are most likely to occur in highly developed countries because consumers in such countries are affluent and have relatively unlimited wants. From the supply side, firms in advanced nations have both the technological know-how and abundant capital to develop new products. Developed countries, in addition to being the original case where innovation take place, in all likely hood will be the place where such new products are first introduced to the public. Introduction occurs there because marketers are familiar with local desires and marketing conditions, making them believe that the risks in introducing any product at home, rather than some where else, are smaller. Furthermore, it is common for a new product to have technical problems even after market introduction and acceptance, perhaps necessitating significant modifications. Products sold overseas may have to be adjusted to be suitable for their intended markets. All of these considerations together may be too complicated for innovative firms to deal with at the beginning. Thus, it is easier and more logical for a firm to concentrate its effort in its home market before looking to overseas markets.

Many of the products found in the world's market where originally created in the United States before being introduced and refined to other countries. In most instances, regardless of whether a product is intended for later export or not, an innovation is initially designed with an eye to capture the U.S. market, the largest consumer nation.

Stage 1- Overseas Innovation

As soon as the new product is well developed, its original market well cultivated, and local demands adequately supplied, the innovating firm will look to overseas markets in

order to expand its sales and profit. Thus, this stage is known as a “pioneering” or “International Introduction” stage. The technological gap is first noticed in other advanced nations because of their similar needs and high income levels. Not surprisingly, English – Speaking countries such as the United Kingdom, Canada, and Austria account for about half of the sales of US innovations when such products are first introduced overseas. Countries with similar cultures and economic conditions are often perceived by exporters as posing less risk and thus are approached first before proceeding to less familiar territories.

Competition in this stage usually comes from US firms, since firms in other countries may not have much knowledge about the innovation. Production cost tends to be decreasing at this stage because by this time the innovating firm will normally have improved the production process. Supported by overseas sales, aggregate production costs tend to decline further because of increase economies of scale. A low introductory price overseas is usually not necessary because of the technological breakthrough; a low price is not desirable because of the heavy and costly marketing effort needed in order to educate consumers in other countries about the new product. In any case, as the product penetrates the market during this stage, there will be more export from the United States and, correspondingly, an increase in imports by other developed countries.

Stage 2 – Maturity

Growing demand in advanced nations provides an impetus for firms their to commit themselves to starting local production, often with the help of their governments' protective measures to preserve infant industries. Thus, these firms can survive and thrive in spite of relative inefficiency. This process may explain the changing national concentrations of high – technology exports and the laws of the US share to Japan, France, and perhaps the United Kingdom.

Development of competition does not mean that the initiating countrie's export level will immediately suffer. The innovating firm's sales and export volumes are kept stable because LDCs are now beginning to generate a need the product. Introduction of the product in LDCs helps offset any reduction in export sales to advanced countries.

Stage 3 – World Wide Imitation

This stage means tough times for the innovating nation because of its continuous decline in export. There is no more new demand anywhere to cultivate. The decline will inevitably affect the US innovating firm's economies of scale and its production costs thus begin to rise again. Consequently, firms in other advanced nations use their lower prices (coupled with product - differentiation techniques) to gain more consumer acceptance abroad at the expense of the US firm. As the product becomes more and more widely disseminated, imitation picks up at a faster pace. Toward the end of this stage, US export dwindles almost to nothing, and any US production still remaining is basically for local consumption. The US automobile industry is a good example of this phenomenon. There are about 30 different companies selling cars in the United States, with several on the rise. Of these, only 4 are US firms, with the rest being from Western Europe, Japan, South Korea, Taiwan, Mexico, Brazil, and Malaysia.

Stage 4 – Reversal

Not only must all good things end, but also misfortune frequently accompanies the end of a favorable situation. The major functional characteristics of this stage are product standardization and comparative disadvantage. The innovative country's comparative advantage has disappeared, and what is left is comparative disadvantage. This disadvantage is brought about because the product is no longer capital – intensive or technology – intensive but instead has become labor – intensive - a strong advantage possessed by LDCs. Thus, LDCs – the last imitators – establish sufficient production facilities to satisfy their own domestic needs as well as to produce for the biggest market in the world, the United States. US firms are now undersold in their own country. Black – and – white television sets, for example, are no longer manufactured in the United States because many Asian firms can produce them much less expensively than any US firm. Consumers' price sensitivity exacerbates the problem for the initiating country.

The IPLC is probably more applicable for products related through an emerging technology. These newly emerging products are likely to provide functional utility rather than aesthetic values. Furthermore, these products likely satisfy basic needs that are universally common in most parts of the world.

Washers, for example, are much more likely to fit this theory than are dryers. Dish washing machines are not useful in countries where labor is plentiful and cheap, and the diffusion of this kind of innovation as described in IPLC is not likely occur.

4.4. BRANDING

In developing a marketing strategy for individual products, the seller has to confront the branding decision, branding is a major issue in product strategy. On the one hand, developing a branded product requires a great deal of long-term investment spending, especially from advertising, promotion, and packaging.

Perhaps the most distinctive skill of professional marketers is their ability to create, maintain, protect, and enhance brands, marketers say that "Branding is the art and cornerstone of marketing." The American marketing association defines a brand as follows: -

"A Brand is a name, term, sign, symbol, or design, or a combination of them, intended to identify the goods or services of one seller or group of sellers and to differentiate them from those of competitors".

A brand is essentially a seller's promise to consistently deliver a specific set of features, benefits, and services to the buyers.

A brand name is the part of brand consisting of words, letters, and/or numbers that can be vocalized. A trademark is defined as a brand that is given legal protection. Therefore, trademark is a legal term meaning the words, names, or symbols that the law designates as trademarks.

The best brands convey a warranty of quality. But a brand is even a more complex symbol. A brand can convey up to six levels of meaning.

i. **Attributes:-**A brand first brings to mind certain attributes. Thus, Mercedes suggests expensive, well built, well-engineered, durable, high prestige, high resale value, fast, and so on.

ii. **Benefits:-**A brand is more than a set of attributes, customers are not buying attributes; they are buying benefits. Attributes need to be translated into functional and/or emotional benefits. The attribute "durable" could translate into the functional benefit, "I won't have to buy a new car every few years". The attribute "Expensive" might translate into the emotional benefit, "The car helps

me feel important and admired". The attribute "well build" might translate into the functional and emotional benefit, "I am safe incase of an accident".

iii. **Values:-**The brand also says something about the product values. Thus, Mercedes stands for high performance, safety, prestige, and soon. The brand marketer must figure out the specific groups of car buyers who are seeking these values.

iv. **Culture:-** The brand may represent a certain culture. The Mercedes represents German culture. Organized, efficient, high quality.

v. **Personality:-**The brand can also project a certain personality. If the brand were a person, an animal, or an object, what would come to mind? Some time it might take on the personality of an actual well-known person or spokesperson.

vi. **User:-**The brand suggests the kind of consumers who buys or uses the product. The users will be those who respect the product's values, culture, and personality.

The challenge in branding is to develop a deep set of meanings for the brand. When the audience can visualize all six dimensions of a brand, the brand is deep otherwise it is shallow.

4.4.1 Brand Equity

Brand varies in the amount of power and value they have in the market place. At one extreme are brands that are not known by most buyers in the market place. Then there are brands for which buyers have a fairly high degree of brand awareness (measured either by brand recall or recognition). Beyond this are brands with a high degree of brand acceptability. In other words, brands that most customers would not resist buying. Then there are brands that enjoy a high degree of brand preference. These are brands that are selected over the others. Finally there is brands that command a high degree of loyalty.

High brand equity provides a number of competitive advantages: -

- The company will enjoy reduced marketing costs because of high level of consumer's brand awareness and loyalty.
- The company will have more trade leverage in bargaining with distribution and retailers since customers expect them to carry the brand.

- The company can charge a higher price than its competitors because the brand has higher perceived quality.
- The company can more easily launch brand extension since the brand name carries high credibility.
- The brand offers the company some defense against fierce price competition

A brand name needs to be carefully managed so that its brand equity doesn't depreciate. Thus requires maintaining or improving over time brand awareness, brand perceived quality and functionality, positive brand associates, and so on.

4.4.2 Brand Name Selection

A good name can add greatly to a products' success. However, finding the best brand name is a difficult task. It begins with a careful review of the product and its benefits, the target market and proposed marketing strategies.

Desirable qualities for a brand name includes:-

1. It should suggest something about the product's benefits & qualities
2. It should be easy to pronounce, recognize, and remember. The brand name should be distinctive
3. It should be capable of registration and legal protection

Once, chosen, the brand name must be protected. Many times try to build a brand name that will eventually become identified with the product category.

4.4.3 Branding Decisions

To understand the role of trademark in strategic planning, one must understand what a trademark is from a legal standpoint. In many countries, branding may be nothing more than the simple process of putting a manufacturer's name, signature or picture on a product or its package.

The basic purpose of branding is the same everywhere in the world. In general the functions of a brand are: -

- Create identification and brand awareness
- Guarantee a certain level of quality, quantity and satisfaction and
- Used as a promotional tool etc.

All of these purposes have the ultimate goal to induce repeat sales.

Activity:
Prepare a List of Examples of Branding Decisions.

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4.4.4 Branding Levels and Alternatives

There are four levels of branding decisions:

1. Branding Vs No Brand
2. Private brand Vs manufacture's brand
3. Single brand Vs multiple brands
4. Local brands Vs worldwide brand

1. Branding Vs No Brand

To brand or not to brand, that is the question. Branding is not a cost free preposition because of the added cost associated with marking, labeling, packaging and legal procedures. Branding is then probably undesirable because brand promotion is ineffective in a practical sense and adds unnecessary expenses to operations costs.

On the positive side, a brand fewer products allow flexibility in quality and quantity control, resulting in lower production costs along with lower marketing and legal costs. On the other hand, branding makes pricing possible because of better identification, awareness, promotion, differentiation, consumer confidence, brand loyalty, and repeats sales.

2. Private Brand Vs manufacturer's Brand

Branding to promote sales and move products necessities a further branding decision: whether the manufacturers should use its own brand or a distributor's brand on its product. Distributors in the world of international business include trading companies, importers, and retailers, among others; their brands are called private brands.

Clearly, the manufacturer has two basic alternatives: 1) its brand or 2) private brand. Its choice depends in part on its bargaining power. If the distributor is prominent and the manufacturer itself is unknown and anxious to penetrate a market, then the latter may have to use the formers brand on the product. But, if the manufacturer has superior strength, it can afford to put its own brand on the product and can insist that the distributor accept that brand as part of the product.

3. Single Brand Vs Multiple Brand

When a single brand is marketed by the manufacturer, the brand is assured of receiving full attention for maximum impact. But a company may choose to make several brands within a single market based on the assumption that the market is heterogeneous and thus be segmented.

Multiple brands are suitable when a company wants to trade either up or down because both moves have a tendency to hurt the firm's main business. If a company has the reputation of quality, trading down without creating a new brand will hurt the prestige of the existing brand. By the same rationale, if a company is known for its low priced, mass produced products, trading up without creating a new brand is hampered by the image of the existing products.

4. Local Brands Vs Worldwide Brand

When the manufacture decides to put its own brand name on the product, the problem does not end there if the manufacture is an international marketer. The possibility of having to modify trademark cannot be dismissed. The international marketer must then consider whether to use just one brand name worldwide or different brands for different markets or countries.

Brand strategy

A company has four choices when it comes to brand strategy, which are as follows:-

i) Line extension: Line extension occur when a company introduces additional items in the same product category under the same brand name, usually with features, such as new flavors, forms, colors, added ingredients, package sizes, and so on.

ii) Brand Extension: A company may decide to use an existing brand name to launch a product in a new category. Brand extension strategy offers a number of advantages. A well-regarded brand name gives the new product instant recognition and earlier

acceptance. It enables the company to enter new product categories more easily. i.e. Sony puts its name on most of its electronic products and instantly establish a connection of the new products high quality.

iii) Multi brands: A company will often introduce additional brands in the same product category. There are various motives for doing this. Sometimes the company is trying to establish different features and/or appeal to different buying motives. A multi branding strategy also enables the company to lock up more distributors shelf space and to protect its major brand by setting up flanker brands. For example, Seiko establishes different brand names for its higher priced (Seiko LaSalle) and lower-priced watch (pulsar) to protect its flanks.

iv) New brand: When a company launches products in a new category, it may find that none of its current brand names are appropriate.

v) Co-brands :A rising phenomenon is the appearance of co-branding (also called dual branding), is which two or more well-known brands are combined in an offer. Each brand sponsor expects that the other brand name will strengthen brand preference or purchase intention. In the case of co-packaged products, each brand hopes it might be reaching a new audience by associating with the other brand.

Advantages of Branding

- The brand name makes it easier for the seller to process orders and track down problems. Furthermore, he seller find it easier to trace the order if it is misshaped, or to determine why the beer was rancid if consumer complain.
- The seller's brand name and trademark provide legal protection of unique product features; which competitors would otherwise be likely to copy.
- Branding gives the seller the opportunity to attract a loyal and profitable set of customers. Brand loyalty gives sellers some protection from competition and greater control in planning their marketing program
- Branding helps the seller segment markets.
- Strong brands help build the corporate image, making it easier to launch new brands and gain acceptance by distributors and consumers.

There is evidence that distributors want manufacturers; brand names because brand makes the product easier to handle, hold production to certain quality standards, strengthen buyer's preferences, and make it easier to identify suppliers. Consumers want brand names to help them identify quality differences and shop more efficiently.

4.5 PACKAGING

Even after a product is developed and branded, strategies must still be developed for other product related aspects of the marketing mix. One such product feature, and a critical one for some products, is packaging, which consists of all activities of designing and producing the container or wrapper. Thus packaging is a business function and a package is an item.

Packaging can be defined as follows:

"Packaging includes the activities of designing and producing the container or wrapper for a product."The container or wrapper is called the package. The package might include up to three levels of material. Thus, old spice, after shave lotion is in bottle (primary package) that is in a cardboard box (secondary package) that is in a corrugated box (shipping package) containing six-dozen boxes of old spice.

In recent times, packaging has become a potent marketing tool. Well-designed packages can create convenience value for the consumer and promotional value for the producer.

Packaging and the resulting package are intended to serve several vital purposes.

i) Protect the product on its way to the consumer:-

A package protects products during shipment. Furthermore, it can prevent tampering with products, notably medications and food products, in the warehouse or the retail store.

ii) Provide protection after the product is purchased:-Compared with bulk (that is unpackaged) items, packaged goods generally are more convenient, cleaner, and less susceptible to losses form evaporation, spilling and spoilage.

iii) Be part of a company's trade marketing program:-

A product must be packaged to meet the needs of wholesaling and retailing middlemen. For instance, a packages size and shape must be suitable for displaying and stacking the product in the store.

iv) Be part of a company's consumer marketing program:-

Packaging helps identify a product and thus may prevent substitution of competitive product. At the point of purchase such as supermarket aisle - the package can serve as a 'silent sales person'

Ultimately, a package may become a product's differential advantage, or at least a significant part of it. In the case of convenience goods and operating suppliers buyers feel that are well-known brand is about as good as another. Thus a feature of the package - reusable jar, self-contained applicator etc, might differentiate these types of a product.

i) Product description:- The package is expected to show not only what the product is, but also what it does in terms of benefits it gives the promotional message. This could be done using words or pictures.

ii) Product image- The packaging material ought to match the image of the product inside. Highly prestigious products and inferior products should be packed differently.

iii) Product value- The pack is often designed to make its contents look more than they really are in terms of value a small value item looks huge in certain packages.

iv) Shelf display- It is also important products are packed in such a way that they occupy small space, they are protected from shocks damages, their shelf life increases, they are protected from pilferage

Packaging Functions and Criteria

Much like the brand name, packaging is another integral part of a product. Packaging serves two primary purposes: functional and promotional. First and foremost, a package must be functional in the sense that it is capable of protecting the product at minimum cost.

For most packaging applications, marketers should keep in mind that foreign consumers are more concerned with the functional aspect of a package than they are with convenience. In addition to functional and promotional functions, good packaging should also satisfy secondary criteria. A good design should have impact, visibility, legibility, simplicity, consistency, versatility and honesty. Packaging does not have to be dull. Novel shapes and designs can be used to stimulate interest and create excitement.

Mandatory package modification

A package change may be either mandatory or at the discretion of the marketer. A mandatory change is usually necessitated by government regulations.

The complexity of packaging regulations is very well demonstrated by the experience of R.J.Reynolds in marketing cigarettes, a relatively simple product. The pack sold in USA can be shipped to only three or four markets. The company has to employ more than 1400 product codes for all its brands in all countries. I.e. Ethiopia requires the imprint "Ethiopia" on the cigarette paper in addition to a special closure seal on every pack indicating retail price in Ethiopian currency.

Optional package modification

Optional modification of a package, although not absolutely necessary, may have to be undertaken for marketing impact or for facilitating marketing activities. In addition to condition of use, other cultural factors should be taken into consideration because such factors often determines and influence consumer preference.

Symbols and colors of packages may have t be changed to be consistent with cultural norms. If packages are offensive, they must be made more acceptable if the product is to be marketed successfully.

Packing

Packaging may be viewed as consisting of two distinct types

i. Industrial (exterior) and
ii. Consumer (interior)

The aim of packaging is to prepare and protect merchandise for shipment and storage. Packing is more critical for overseas shipment than for domestic shipment because of the longer transit time and a greater number of hazards.

Packing problems

There are four common packaging problems; same of them are in direct conflict with one another. They are

- Weight
- Breakage
- Moisture and temperature and
- Pilferage and theft

i. **Weight:** Over packing not only directly increases packing cost but also increases

weight and size of cargo. Any undue increases in weight or size only serves to raise freight changes. Moreover, import fees or customs duties may also rise when import duties are based on gross weight. Thus overprotection, of the cargo can cost more than it is worth.

ii. **Breakage:** Although over packing is undesirable, so is under packing because the latter allows a products to be susceptible to breakage or damage. The breakage problem is present in every step of ocean transport. In order to protect the breakage, cargo should be unitized or palletized whenever possible.

Palletizing is the assembly of one or more packages on a pallet base and the securing of the load to the pallet. Unitizing is the assembly of one or more items into a compact load secured together and provided with acids and cleats for ease handling. These two packing methods force cargo handlers to use mechanical handling equipment to move cargo.

iii) Moisture and temperature: Certain products can easily be damaged by moisture and temperature. Such products are subject to condensation even in the hold of a shipped equipped with air conditioning or dehumidifying equipment. Another problem is that the cargo may be unloaded in the rain. Many foreign parts do not have covered storage facilities, and the cargo may have to be left in the open subject to heat, rain, cold or adverse elements. One very effective means of eliminating moisture is shrink wrapping, which involves sealing merchandise in a plastic film. Waterproofing can also be provided by using waterproof inner lines or moisture absorbing agents and by coating finished metal parts with a preservative or rust inhibitor.

iv) Pilferage and theft: Cargo should be adequately protected against theft. One method to discouraging theft is to use shrink wrapping seals, or strapping. Gummed sealing tapes with patterns when used, will quickly reveal any sign of tampering. Also, only well constructed packing in good condition should be used. I.e. containerization.

Another area of concern is marking. The main purpose of marking is to identify the shipment so that the carrier can forward the shipment to the designated consignee. Container can take care of most of the four packing problems. Because of a container's

construction, a product does not have to have heavy packing. A container is a large box made of durable material such as steel, aluminum, plywood and glass reinforced plastics. The container by itself provides good protection for the product against breakage, moisture and temperature. Because breaking in to a container is difficult, this method of shipment discourages pilferage and theft as well.

4.6. LABELING

Labeling which is closely related to packaging is another product feature that requires managerial attention. A label is a part of a product that carries information about the product and the seller. A label may be part of the package, or it may be a tag attached to the product. Obviously there is a close relationship among labeling, packaging, and branding.

Types of labels:-Labels fall into three primary kinds:-

i) A brand label:-It is simply the brand name applied to the product or package.

ii) A descriptive label: It gives objectives information about the products' use construction, care, performance, and/or other pertinent features ingredients and nutritional contents.

iii) A grade label: It identifies the products judged quality with a letter, number, or word. Canned peaches are grade labeled A,B,C, corn and wheat are grade labeled 1 & 2.

Brand labeling is an acceptable form of labeling, but it does not supply sufficient information to a buyer. Descriptive labels provide more product information but not necessarily all that is needed or desired by a consumer in making a purchase decision.

Functions of Labeling

Labeling performs several functions. Some of which are illustrated below:-

- The label identifies the product or brand
- The label might also describe several things about the product, which made it, where it was made, when it was made, its contents, how it is to be used, and how to use it safely.
- The label might promote the product through attractive graphics

CHAPTER SUMMARY

Decisions about products involve such issues as what products and product lines to introduce in various countries, to what extent a product should be adapted to local customs and characteristics, whether new products should be introduced, where the R & D effort should be concentrated, whether the firm should diversify into unrelated areas, which products should be eliminated, how products should be packaged, what brand policy to pursue, what after-sale services to offer, and what warranties the company should provide on various products.

Product means a bundle of attributes put together to satisfy a customer need. The product objectives for each country or market should be defined separately and be based on (1) overall corporate objectives and (2) the concerns of the individual national governments.

Product design is a major strategic issue. A company can either offer a standard product worldwide or adapt it to local requirements. Adaptation can be promoted by physical requirements or cultural requirements. The decision to standardize or adapt is dictated by the nature of the product, market development, cost/benefit considerations, legal requirements, competition, support system, physical environment, and market conditions. Generally, companies try to market a standardized product internationally. Although this helps in cost savings, standardization can also lead to missed opportunities.

There are four alternatives for formulating an international brand strategy: using one name worldwide, using one name with adaptations for each market, using different names in different markets, and using the company name as a family name for all brands. International packaging is influenced by such considerations as customers, distribution channels, shippers, and host governments. The service/warranty component provides a company with an important opportunity to differentiate its product from the competition.

Review Questions

1. Compare and contrast product standardization and adaptation options with suitable examples.
2. What factors are important in the standardization versus adaptation product decision process?
3. List and describe the five stages of international product life cycle?
4. Describe the significance of packing and labeling in international marketing?

CHAPTER FIVE

5. INTERNATIONAL PROMOTION DECISION

Chapter Objectives

After studying this chapter you should be able

- To understand the utility of various promotion tools for international markets.
- To know the qualities of each promotional mix elements
- To know the challenges a marketer faces while promoting its products overseas.
- To understand the standardized and adapted approaches of promotion.

5.1 INTRODUCTION

Promotion of a company's products and services are very important not only for domestic market but also for international markets. International promotion decisions are, however, more complicated and critical. This lesson will provide you an opportunity to understand promotion in international context.

Promotion is an attempt to influence. More specifically, promotion is the element in an organization's marketing mix that serves to inform, persuade, and remind the market of a product and/or the organization selling it, in hopes of influencing the recipients' feelings, beliefs, or behavior.

Product promotion decisions become much more difficult and complicated when companies start operating at international level. The global marketer must choose a proper combination of the various promotional tools like advertising, personal selling, publicity, and sales promotion. The choice of promotional mix will naturally depend on the target audience, company objectives, the products or services marketed the available resources, and the availability of the tool in a particular market.

Promotion is a term taken from Latin promovere, which means moving from one end to another. In marketing, promotion means all those tools that help a marketer to make his product move from the factory to the customer and hence involves advertising, sales promotion, personal selling, and publicity etc. The marketing communications mix (also called the promotion mix) consists of five major tools that are as follows:

i. **Advertising:** Any paid form of non-personal presentation and promotion of ideas, goods, or services by an identified sponsor.

ii. **Sales Promotion:** Short-term incentives to encourage trial or purchase of a product or service.

iii. **Personal Selling:** Face-to-face interaction with one or more prospective purchasers for the purpose of making sales.

iv. **Public Relations and Publicity:** A variety of programs designed to promote and/or protect a company's image or its individual products.

v. **Direct Marketing:** Use of mail, telephone, and other non-personal contact tools to communicate with or solicit a response from specific customers and prospects.

Deciding on the Promotion Mix for International Markets

The basic framework and concepts of international promotion are essentially the same wherever employed. Six steps are involved:

1. Study the target market (s);
2. Determine the extent of worldwide standardization;
3. Determine the promotional mix (the blend of advertising, personal selling, sales promotion, and public relations);
4. Develop the most effective message (s);
5. Select effective media; and
6. Establish the necessary controls to assist in monitoring and achieving worldwide marketing objectives.

5.2 INTERNATIONAL PROMOTION DECISION

Promotion encompasses all efforts by an international firm to enhance the desirability of its products among potential buyers. The international marketer must choose a proper combination of the various promotional tools - advertising, personal selling, sales promotion, and public relations - to create images among the intended target audience. The choice will depend on the target audience, firm's objectives, the products or services marketed the resources available for the endeavor, and the availability of promotion tool in a particular market.

5.2.1 Global Advertising

Communication experts generally agree that the overall requirements of effective communication and persuasion are fixed and do not vary from country to country. The same thing is true of the components of the communication process: The marketer or sender's message must be encoded, conveyed via the appropriate channel(s), and decoded by the customer or receiver. Communication takes place only when meaning is transferred.

Four major difficulties can compromise an organization's attempt to communicate with customers in any location.

a) **The message may not get through to the intended recipient.** This problem may be the result of an advertiser's lack of knowledge about appropriate media for reaching certain types of audiences. For example, the effectiveness of television as: a medium

for reaching mass audiences will vary proportionately with the extent to which television viewing occurs with a country.

b) **The message may reach the target audience but may not be understood or may even be misunderstood.** This can be the result of an inadequate understanding of the target audience’s level of sophistication or improper encoding.

c) **The message may reach the target audience and may be understood but still may' not induce the recipient to take the action desired by the sender.** This could result from lack of cultural knowledge about a target audience.

d) **The effectiveness of the message can be impaired by noise.** Noise in this case is an external influence such as competitive advertising, other sales personnel, and confusion at the receiving end, which can detract from the ultimate effectiveness of the communication.

Generally, as a firm develops its advertising strategy at international level, it must at least consider three factors: the message it wants to convey, the media available for conveying the message and the extent to which the firm wants to globalize its advertising effort (whether to follow standardization or adaptation). At the same time, the international marketer must take into account relevant cultural, linguistic, and legal constraints found in various national markets.

Global Advertising Decisions

The Extension (Standardization) Vs Adaptation Debate: The key question for global marketers is whether the specific advertising message and media strategies must be changed from region to region or country-to-country because of environmental requirements. Proponents of the one world, one voice" approach to global advertising believes that the era of the global village is fast approaching and that tastes and preferences are converging worldwide. According to the standardization argument, because people everywhere want the same products for the same reasons, companies can achieve great economies of scale by unifying advertising around the globe. Advertisers who follow the localized approach are skeptical of the global village argument. Even Coca-Cola, the most global brand in the world, records radio spots in 40 languages with 140 different music backgrounds. Coca-Cola asserts at consumers still differ from country to country must be reached by advertising tailored to their respective countries.

Proponents of localization point out that most blunders occur because advertisers have failed to understand and adapt to foreign cultures.

Certain consumer products lend themselves to advertising extension. If a product appeals to the same need around the world, there is a possibility of extending the appeal to that need. The list of products "going global," once confined to a score of consumer and luxury goods, is growing. Global advertising is partly responsible for increased worldwide sales of disposable diapers, diamond watches, shampoos, and athletic shoes. Some longtime global advertisers are benefiting from fresh campaigns. Jeans marketer Levi Strauss & Company racked up record sales in 1991 on the strength of a campaign extended unchanged to Europeans, Latin Americans, Africans and Australians. The basic issue is whether there is in fact a global market for the product. If the market is global, appeals can be standardized and extended. Soft drinks, Scotch whiskey, Swiss watches, and designer clothing are examples of product categories whose markets are truly global.

As Kansu correctly notes, the controversy over advertising approaches will probably continue for years to come. Localized and standardized advertising both have their place and both will continue to be used. Kansu's conclusion: What is needed for successful international advertising is a global commitment to local vision. In the final analysis, the decision of whether to use a global or localized campaign depends on recognition by managers of the trade-offs involved. On the one hand, a global campaign will result in the substantial benefits of cost savings, increased control, and the potential creative leverage of a global appeal. On the other hand, localized campaigns have the advantage of appeals that focus on the most important attributes of a product in each nation or culture. The question of when to use each approach depends on the product involved and a company's objectives in a particular market.

A. **Selecting an advertising agency:** Another global advertising issue company's face is whether to create ads in house, use an outside agency, or combine both strategies. For example, Chanel, Benetton, and Diesel rely on in-house marketing and advertising staffs for creative; Coca-Cola has its own agency, Edge Creative, but also uses the services of outside agencies such as Leo Burnett. When one or more outside agencies are used, they can serve product accounts on a multi-

country or even global basis. It is possible to select a local agency in each national market or an agency with both domestic and overseas offices. Today, however, there is a growing tendency for Western clients to designate global agencies for product accounts in order to support the integration of the marketing and advertising functions; Japan based companies are less inclined to use this approach. Agencies are aware of this trend and are themselves pursuing international acquisitions and joint ventures to extend their geographic reach and their ability to serve clients on a global account basis. In selecting an advertising agency, the following issues should be considered:

- **Company organization:** Companies that are decentralized may want to leave the choice to the local subsidiary.
- **National responsiveness:** Is the global agency familiar with local culture and buying habits in a particular country, or should a local selection be made?
- **Area coverage:** Does the candidate agency cover all relevant markets?
- **Buyer perception:** What kind of brand age does the company want to project? If the product needs a strong local identification, it would be best to select a national agency.

B. **The Message:** The message of an advertisement refers to the facts or impressions the advertiser wants to convey to potential customers. For example, an automobile manufacturer may want to convey a message of value (low price) and / or reliability (quality). The choice of message is an important reflection on how the firm sees its own products and services and how it wants them to be seen by customers. For example, coca-cola believes that its products help consumers enjoy life, and its advertising messages consistently stress this theme worldwide. Consider the company's today's advertising logo of "enjoy the Coke side of life". Products that are used for different purposes in different areas will need to be marketed differently. The country of origin of a product often serves as an important part of the advertising message. For example, among fashion-conscious teenagers and young adults in Europe and Japan, USA, even in Africa goods are often viewed as being very trendy. Thus, Jeans producers, among others, highlight the origins of their products.

C. **Medium:** The medium is the communication channel used by the advertiser to convey a message. A firm’s international marketing manager must alter the media used to convey its message from market to market based on availability, legal restrictions, standards of living, literacy levels, the cultural homogeneity of the national market, and other factors. In bilingual or multilingual nations, international marketers must adjust their mix of media outlets in order to reach each of the country's cultural groups. A nation's level of economic development may also affect the media firm’s use. For example, in many less developed countries like Ethiopia, television ownership may be limited and literacy rates low. This eliminates television, newspapers, and magazines as useful media but favors radio advertising. Price may also come into play. For ex, television advertising is mostly very costly than Radio, newspaper ads. Legal restrictions may also prompt the use of certain media. Most national governments limit the number of television channels.

To sum up, to help deal with issues related to message and media, many international marketers use multinational advertising agencies, which have branch offices or affiliates in many national markets. International marketers sometimes use local advertising agencies too.

a) **Cultural Considerations:** Knowledge of cultural diversity, especially the symbolism associated with cultural traits, is essential when creating advertising. Local country managers will be able to share important information, such as when to use caution in advertising creativity. Use of colors and man-woman relationships can often be stumbling blocks. For example, white in Asia is associated with death. In Japan, intimate scenes between men and woman are considered to be in bad taste; they are outlawed in Saudi Arabia.

Activity 1

List the qualities of advertising as compared to other promotional mix elements

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Qualities of advertising

- **Public Presentation:** Advertising is a highly public mode of communication. Its public nature confers a kind of legitimacy on the product and also suggests a standardized offering. Because many persons receive the same message, buyers know that their motives for purchasing the product will be publicly understood.
- **Pervasiveness:** Advertising is a pervasive medium that permits the seller to repeat a message many times. It also allows the buyer to receive and compare the messages of various competitors. Large-scale advertising by a seller says something positive about the seller's size, power, and success.
- **Amplified Expressiveness:** Advertising provides opportunities for dramatizing the company and its products through the artful use of print, sound, and color. Sometimes, however, the tool's very success at expressiveness may dilute or distract from the message.
- **Impersonality:** Advertising cannot be as compelling as a company sales representative can. The audience does not feel obligated to pay attention or respond. Advertising is able to carry on only a monologue, not a dialogue, with the audience.

5.2.2 Public Relations and Publicity

Public relations consist of efforts aimed at enhancing a firm's reputation and image with the general public. The consequence of effective public relations is a general belief that the firm is a good corporate citizen, that it is reputable and that it can be trusted. Ineffective public relations can often lead to a public perception that the firm cannot be trusted or that it carries little for the community. A significant part of the public relations activity focuses on portraying corporations as good citizens of their host countries. Public relations activity involves anticipating and countering criticism. The criticism ranges from general ones against all multinational corporations to specific complaints.

Thus, a company's public relations (PR) effort should-foster goodwill and understanding among constituents both inside and outside the company. PR practitioners attempt to generate favorable publicity, which, by definition, is a non-paid form of communication. (In the PR world, publicity is sometimes referred to as earned media, whereas advertising and promotions are known unearned media.) PR personnel also play a key role in responding to unflattering media reports or controversies that arise because of company

activities in different parts of the globe. In such instances, PR's job is to make sure that the company responds promptly and gets its side of the story told. The basic tools of PR include news releases, newsletters, press conferences, tours of plants and ether company facilities, articles in trade or professional journals, company publications and brochures, TV and radio talk show appearances by company personnel, special events, and homepages on Internet. As noted earlier, a company exerts complete control over the content of its advertising and pays for message placement in the media. However, the media typically receive far more press releases and other PR materials than they can use. Generally speaking, a company has little control over when, or if, a news story runs. The company cannot directly control the "spin," slant, or tone of the story.

The appeal of public relations is based on its three distinctive qualities:

- **High credibility:** News stories and lectures seem more authentic and credible to readers than ads do.
- **Off guard:** Public relations can reach many prospects that might avoid salespeople and advertisements. The message gets to the buyers as news rather than as a sales-directed communication.
- **Dramatization:** Public relation has, like advertising, a potential for dramatizing a company or product.

The Growing Role of Public Relations in Global Marketing Communications

Public relations professionals with international responsibility must go beyond media relations and serve as more than a company mouthpiece; they are called on to simultaneously build consensus's and understanding, create trust and harmony, articulate and influence public opinion, anticipate conflicts, and resolve disputes. As companies become more involved in global marketing and the globalization of industries continues, it is important that company management recognize the value of international public relations. One recent study found that, internationally; PR expenditures are growing an average of 20 percent annually.

The number of international PR associations is growing as well. The new Austrian Public Relations Association is a case in point; many European PR trade associations are part of the Confederation Europeans des Relations Publiques and the International Public

Relations Association. Another factor fueling the growth of international PR is increased governmental relations between countries. Governments and organizations are dealing with broad-based issues of mutual concern such as the environment and world peace. Finally, the technology-driven communication revolution that has ushered in the information age makes public relations a profession with truly global reach. Faxes, satellites, high-speed modems, and the Internet allow PR professionals to be in contact with media virtually anywhere in the world.

In spite of these technological advances, PR professionals must still build good personal working relationships with journalists and other media representatives as well as leaders of other primary constituencies. Therefore, strong interpersonal skills are needed. One of the cost basic concepts of the practice of public relations is to know the audience. For the global PR practitioner, this means knowing the audiences in both the home country and the host country or countries. Specific skills needed include the ability to communicate in the language of the host country and familiarity with local customs. Obviously a PR professional who is unable to speak the language of the host country will be unable to communicate directly with a huge portion of an essential audience. Likewise the PR professional working outside the home country must be sensitive to nonverbal communication issues in order to maintain good working relationships with host-country nationals. Commenting on the complexity of the international PR professional's job, one expert notes that, in general, audiences are "increasingly more unfamiliar and more hostile, as well more organized and powerful . . . more demanding, more skeptical, and more' diverse." International PR practitioners can play an important role as "brides over the shrinking chasm of the global village.

5.2.3 Personal Selling

Personal selling is two-way, personal communication between a company representative and a potential customer as well as back to the company. The salesperson's job is to correctly understand the buyer's needs, match those needs to the company's product(s), and then persuade the customer to buy. Effective personal selling in a salesperson's home country requires building a relationship' with the customer; global marketing presents additional challenges because the buyer and seller may come from different national or

cultural backgrounds. It is difficult to overstate the importance of a face-to-face, personal selling effort for industrial products in global markets

The selling process is typically divided into several stages: prospecting, pre-approaching, approaching, presenting, problem solving, handling objections, closing the sale, and following up. The relative importance of each stage can vary by country or region. Experienced sales reps know that persistence is one tactic often required to win an order in the market; however, persistence often means tenacity, as in "don't take 'no' for an answer." Persistence is also required if a global industrial marketing effort is to succeed; in some markets, however, persistence often means endurance, a willingness to patiently invest months or years before' the effort results in an actual sale. For example, a company wishing to enter the Japanese market must be prepared for negotiations to take from 3 to 10 years.

Prospecting is the process of identifying potential purchasers and assessing their probability of purchase. If Ford wanted to sell vans in another country where they would be used as delivery vehicle, which businesses would need delivery vehicles? Which businesses have the financial resources to purchase such a van? Those businesses that match these two needs are better prospects than those who do not. Successful prospecting requires problem-solving techniques, which involve understanding and matching the customer's needs and the company's products in developing a sales presentation.

The purpose of the pre-approach stage is to gather information on a prospective customer's problem areas. If a potential customer has a grocery business, their needs in a van would be different from a customer who owns a carpentry business. The sales representative would need to select the best models of Ford vans collect the appropriate model specifications, and so on to prepare for an effective presentation.

The approach stage involves one or more meetings between seller and buyer. In global selling, it is absolutely essential for the salesperson to understand cultural norms and proper protocol. In some countries, the approach is drawn out as the buyer-gets to know or takes the measure of the salesperson on a personal level with no mention of the pending

deal. In such instances, the presentation comes only after rapport has been firmly established.

Presentation and Problem solving tailor a presentation that demonstrates how the company's product can solve these specific problems

During the presentation, the salesperson must deal with objections. Objections may be of business or personal nature. A common theme in sales training is the notion of active listening; naturally, in cross-cultural selling, verbal and nonverbal communication barriers present special challenges for the salesperson. When objections are successfully overcome, the salesperson moves on to the close and asks for the order. A successful sale does not end there however; the final step of the selling process involves following up with the customer to ensure his or her ongoing satisfaction with the purchase.

Activity 2

List the distinctive qualities of personal selling as compared to advertising

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Personal selling, when compared with advertising, has three distinctive qualities:

- **Personal Confrontation:** Personal selling involves an alive, immediate, and interactive relationship between two or more persons. Each party is able to observe each other’s needs and characteristics at close hand and make immediate adjustments.
- **Cultivation**: Personal selling permits all kinds of relationships to spring up, ranging from a matter-of-fact selling relationship to a deep personal friendship. Effective sales representatives will normally keep their customers’ interests at heart if they want long run relationship.
- **Response:** Personal selling makes the buyer feel under some obligation for having listened to the sales talk. The buyer has a greater need to attend and response; even if the response is a polite ‘thank you.’

These distinctive qualities come at a cost. A sales-force represents a greater long-term cost commitment than advertising. Advertising can be turned on and off, but the size of a sales-force is more difficult to alter. Similarly, for an international company,

standardization of personal selling efforts becomes much more complicated, especially if the product offering is standardized.

5.2.4 Sales Promotion

Sales promotion refers to any consumer or trade program of limited duration that adds tangible value to a product or brand. Sales promotion laws and usage vary around the world but may consist of any of the following: promotional pricing tactics, contests, sweepstakes and games, premium and specialties, dealer loaders, merchandising materials, tie-ins and cross-promotions, packaging, trade shows (also known as exhibitions), and sponsorship. The EU, however, is working to harmonize promotional tactics across its member countries. It is considering "mutual recognition" that would allow a company to carry out promotional activities in another country as long as that tactic is legal in the company's home country. The tangible value created by the promotion may come in various forms, such as a price reduction or a "buy one, get one free" offer. The purpose of a sales promotion may be to stimulate customers to sample a product or to increase consumer demand. Trade promotions are designed to increase product availability in distribution channels.

The increasing popularity of sales promotion as a marketing communication tool can be explained in terms of several strengths and advantages. Besides providing a tangible incentive to buyers, sales promotion also reduces the perceived risk buyers may associate with purchasing the product. From the point of view of the company, sales promotion provides accountability; the manager in charge of the promotion can immediately track the results of the promotion. Moreover, some consumer sales promotions, including sweepstakes and rebates, require buyers to fill out a form and mail it to the company. This allows a company to build up information in its database, which it can use when communicating with customers in the future.

Although sales promotion tools – coupons, contests, premiums, and the like – are highly diverse, they have three distinctive characters:

- Communications: They gain attention and usually provide information that may lead the consumer to the product.

- Incentive: They incorporate some concession, inducement, or contribution that gives value to the consumer.
- Invitation: They include a distinct invitation to engage in the transaction now.

5.2.5 Direct Marketing

The use of direct marketing is growing rapidly in many parts of the world due to increased use of computer databases, credit cards, and toll-free numbers, as well as changing life styles. Direct marketing is a system of marketing that integrates ordinarily separate marketing mix elements to sell directly to both consumers and other businesses; it is used by virtually every consumer and business to-business category from banks to airlines to nonprofit organizations. Because the customer responds directly to the company making the offer, international considerations that apply to communications, distribution, and sales have to be considered. Direct marketing uses a wide spectrum of media, including direct mail; telephone; broadcast, including television and radio; and print, including newspapers and magazines.

The usage of direct mail, the most popular type of direct marketing, varies around the world based on literacy rates, level of acceptance, infrastructure, and culture. In countries with low levels of literacy, a medium that requires reading is not effective. In other countries, the literacy rate may be high, but consumers are unfamiliar with direct mail and suspicious of products they cannot see.

The infrastructure of a country must be developed sufficiently to handle direct mail the postal system must deliver mail on a timely basis and be free of corruption. In addition to physical infrastructure, a system for developing databases and retrieving appropriate target names and the tracking results is necessary. In one former Soviet republic, merchants were resistant to having their name and address publicly listed in the telephone directory. They feared that the local "mafia" could readily use this information to extort protection money from these.

Culture also plays a significant role in the decision to use direct mail. In Thailand, the local astrologer plays an important role in many business decisions. If the day that a direct-mail campaign is scheduled to begin is not auspicious, the marketer may delay the mailing until a more fortuitous day appears.

Database marketing uses extensive lists of prospects and relevant demographic and psycho-graphic information to narrow target markets to serious prospects and then to customize an offer to the prospect's interests. This is essential not only for direct marketing but also for market research and personal selling. Lists can be created in house from the company's current customers, from responses to previous direct-marketing offers, or from telephone or membership directories. These lists may also be purchased from list brokers, companies that specialize in the acquisition and sale of lists of prospective customers.

Although direct marketing has several forms – direct mail, telemarketing, electronic marketing, and so on – it has a few distinctive characteristics:

- Non-public: The message is normally addressed to a specific person and does not reach others.
- Customized: The message can be customized to appeal to the addressed individual.
- Up-to-date: A message can be prepared very quickly for delivery to an individual.

5.2.6 Overseas Product Exhibitions

One type of sales promotion that can be highly effective is the exhibition of a product overseas. This type of promotion may be very important because regular advertising and sales letters and brochures may not be adequate. For certain products, quality can be judged only by physical examination, and product exhibition can facilitate this process.

One very effective way to exhibit products abroad is to use trade fairs. A strong feature of a trade fair is that prospects are in a buying mood. Another advantage is that buyers are seeking out sellers at a central location. Obviously, a trade show presents a much easier contact situation for a salesperson because there is no travel to many diverse locations to call on potential buyers.

An exhibitor should investigate whether it is worthwhile to use a carnet for products that will be shipped or taken to the exhibition. A carnet is an international customs document that facilitates the temporary duty-free importation of product samples in lieu of the usual customs documents required to bring merchandise into several major trading countries

That is, a carnet is a series of vouchers listing the goods and countries involved where the product will be exhibited.

5.2.7 Sponsorship Promotion

Sponsorship serves purposes other than sales promotion. Sponsorship can be used to increase awareness and esteem, to build the brand identification, to-enhance the brand's positioning and sales, and to circumvent advertising restrictions in some countries. Examples of global sponsorship are the Olympics, the World Cup in Soccer, The English premier League, The Spanish la Liga, The Italian serie A, The African Cup of Nation and the Tour de France etc.

5.3 SUMMARY

The promotion of goods and services is an important part of the marketing mix. The purpose of promotion is to inform, persuade, and remind the customer that certain goods and services are available. The four ingredients of promotion are advertising, personal selling, sales promotion, and publicity. An important decision for international advertisers to make is whether the advertising campaign should be standardized worldwide or localized. Arguments for standardized advertising are (1) a successful campaign in one country is likely to be effective in another nation as well and (2) standardized advertising is economical. The argument against standardization is that advertising campaigns effective in some countries are not always effective in others, because of differences in cultural traits, language, economic life, and the like.

Personal selling is an important ingredient of any marketing program. The three sources of sales by personnel are expatriates, natives, and third country nationals. In the realm of international business, most personal selling jobs are handled by the local management. The head office, however, can provide useful support to local management on such aspects as selection, training, supervision, compensation, and evaluation. In ways similar to domestic marketing, sales promotion and public relations are also relevant to international marketing. An appropriate sales promotion program for an overseas market should be geared to the local environment. Public relations provide a justification and an identity for the foreign enterprise in the economic sphere of the host country. It is desirable to hire the program. Publicity programs, which give the firm and its products

broad exposure to customers and prospects as well as third-party endorsement by the media, provide a cost-efficient use of a limited promotional budget.

Review Questions

1. Explain in brief the elements of promotion?
2. What is advertising? Explain in detail its objectives?
3. What is an advertising media? Explain in detail the factors determine media selection

CHAPTER SIX

PRICING AND TERMS OF PAYMENT

Chapter Objectives:

After studying this chapter, you should be able to:

- Understand the meaning of pricing
- Explain the environmental factors that influences on pricing decisions
- Understand alternative pricing strategies and global pricing policies
- Differentiate the different types of dumping
- Define the meaning countertrade

INTRODUCTION

This chapter deals with pricing from international context and terms of payment. The task of determining prices in global marketing is complicated by fluctuating exchange rates, which may bear only limited relationship to underlying costs. There are environmental factors that influences on pricing decisions such as currency fluctuations, inflation, government controls and subsidies, competitive behavior, and market demand. The chapter also discussed about the several payment methods. It ca be consignment, open account, cash in advance or bill of exchange. When a consignment is used, goods are shipped but ownership is retained by the seller. In a bill of exchange, the request is an unconditional order in writing from one person (drawer) requiring the person to whom it is addressed (drawee) to pay the payee or bearer on demand or at a fixed or determinable time. Finally, this section will provide the different types of dumping and countertrade.

6.1 Basic International Pricing Concepts

As the experience of many companies show, the global manager must develop pricing systems and pricing policies that address price floors, price ceilings, and optimum prices in each of the national markets in which his or her company operates.

The task of determining prices in global marketing is complicated by fluctuating exchange rates, which may bear only limited relationship to underlying costs. According to the concept of purchasing power parity, changes in domestic prices will be reflected in the exchange rate of the country's currency. Thus, in theory, fluctuating exchange rates should not present serious problems for the global marketer because a rise or decline in domestic price levels should be offset by an opposite rise or decline in the value of the home-country currency and vice versa. In the real world, however, exchange rates do not move in lockstep fashion with inflation. This means that global marketers are faced with difficult decisions about how to deal with windfalls resulting from favorable exchange rates, as well as losses due to unfavorable exchange rates.

A firm's pricing system and policies must also be consistent with other unique global constraints. Those responsible for global pricing decisions must take into account international transportation costs, middlemen in elongated international channels of distribution, and the demands of global accounts for equal price treatment regardless of location. In addition to the diversity of national markets in all three basic dimensions-cost, competition, and demand-the international executive is also confronted by conflicting governmental tax policies and claims as well as various types of price controls. These include dumping legislation, resale price maintenance legislation, price ceilings, and general reviews of price levels. For example, Procter & Gamble (P&G) encountered strict price controls in Venezuela in the late 1980. Despite increases in the cost of raw materials, P&G was granted only about 50 percent of the price increases it requested; even then, months passed before permission to raise prices was forthcoming. As a result, by 1988 detergent prices in Venezuela were less than what they were elsewhere.

6.2. Environmental Influences On Pricing Decisions

Global marketers must deal with a number of environmental considerations when making pricing decisions. Among these are currency fluctuations, inflation, government controls and subsidies, competitive behavior, and market demand.

1. **Currency Fluctuations**

Fluctuating currency values are a fact of life in international business. The marketer must decide what to do about this fact. Are price adjustments appropriate when currencies strengthen or weaken? There are two extreme positions; one is to fix the price of products in country target markets. If this is done, any appreciation or depreciation of the value of the currency in the country of production will lead to gains or losses for the seller. The other extreme position is to fix the price of products in home country currency. If this is done, any appreciation or depreciation of the home-country currency will result in price increases or decreases for customers with no immediate consequences for the seller.

For companies that are in a strong, competitive market position, price increases can be passed on to customers without significant decreases in sales volume. In more competitive market situations, companies in a strong-currency country will often absorb any price increase by maintaining international market prices at pre-revaluation levels. If a country's currency weakens relative to a trading partner's currency, a producer in a weak-currency country can cut export prices to hold market share or leave prices alone for healthier profit margins.

2. Exchange Rate Clauses

Many sales are contracts to supply goods or services over time. When these contracts are between parties in two countries, the problem of exchange rate fluctuations and exchange risk must be addressed.

An exchange rate clause allows the buyer and seller to agree to supply and purchase at fixed prices in each company's national currency. The basic design of an exchange rate clause is straightforward: Review exchange rates periodically (this is determined by the parties; any interval is possible, but most clauses specify a monthly or quarterly review), and compare the daily average during the review period and the initial base average. If the comparison produces exchange rate fluctuations that are outside the agreed range of

fluctuation, an adjustment is made to align prices with the new exchange rate if the fluctuation is within some range. If the fluctuation is greater than some limit (10 percent in our example), the parties agree to discuss and negotiate new prices.

3. Pricing in an Inflationary Environment

Inflation, or a persistent upward change in price levels, is a worldwide phenomenon. Inflation requires periodic price adjustments. These adjustments are necessitated by rising costs that must be covered by increased selling prices. An essential requirement when pricing in an inflationary environment is the maintenance of operating profit margins. Regardless of cost accounting practices, if a company maintains its margins, it has effectively protected itself from the effects of inflation.

4. Government Controls and Subsidies

If government action limits the freedom of management to adjust prices, the maintenance of margins is definitely compromised. Under certain conditions, government action is a real threat to the profitability of a subsidiary operation. In a country that is undergoing severe financial difficulties and is in the midst of a financial crisis (e.g., a foreign exchange shortage caused in part by runaway inflation), government officials are under pressure to take some type of action. This has been true in Brazil for many years. In some cases, governments will take expedient steps rather than getting at the underlying causes of inflation and foreign exchange shortages.

Government control can also take the form of prior cash deposit requirements imposed on importers. This is a requirement that a company has to tie up funds in the form of a non-interest-bearing deposit for a specified period of time if it wishes to import products.

5. Competitive Behavior

Pricing decisions are bounded not only by cost and the nature of demand but also by competitive action. If competitors do not adjust their prices in response to rising costs, management even if acutely aware of the effect of rising costs on operating margins-will be severely constrained in its ability to adjust prices accordingly. Conversely, if competitors are manufacturing or sourcing in a

lowermost country, it may be necessary to cut prices to stay competitive.

6. Price and Quality Relationships

The lack of a strong price-quality relationship appears to be an international phenomenon. This is not surprising when one recognizes that consumers make purchase decisions with limited information and rely more on product appearance and style and less on technical quality as measured by testing organizations.

6.3. Price Standardization

One area of pricing that has received some attention is the issue of pricing standardization. A study of the marketing mix by large US-based industrial firms in their Latin American businesses found that the degree of standardization varied across individual elements, with branding and product being least adapted. Perhaps because of government regulations, price and advertising elements were most adapted. In comparison with the same firms' European and Latin American strategies, price was similarly adapted in both regions. According to one study, most American multinational firms standardize their prices in most world markets because they are probably cost driven. Due to market variations, one has to wonder why these firms are inflexible and whether they have been successful overseas. Perhaps these firms have been able to be rigid due to the fact that they do not rely on foreign sales very much and that they do business primarily with industrialized countries. In contrast, those companies that are more committed to international business localize their prices and are more successful overseas.

Whether price should be uniform worldwide is a subject of much debate. One school of thought holds that, from the management's viewpoint, there is no reason for an export price to differ from the home price. In addition, economists believe that arbitrage will eliminate any price differential between markets. This is especially the case with the European Union due to the free movement of goods, the elimination of customs barriers, and the harmonization of VAT rates. In addition, the free movement of people will enable them to easily observe prices of the same products in neighboring countries. As a result, internationally recognized consumer goods with wide European distribution are likely to have a more uniform pricing system. A multinational corporation needs to coordinate prices across its multiple markets – without violating national laws. A study of South Korean, Taiwanese, Hong Kong, and Singaporean firms operating in Europe found that

they had closer relationships with their parent firms and that they had greater autonomy in strategy and pricing decisions.

6.4. Global Pricing Policies

6.4.1. Standard Price Policy

An international marketer following a geocentric approach to international marketing will adopt a standard price policy. Under standard price policy the firm charges the same price for its goods and services regardless of where they are sold. Firms that adopt this policy are generally of two types: first, firms whose products or services are highly visible and allow price comparisons to be readily made. Second, a firm that sells commodity goods in competitive markets.

6.4.2. Two- Tiered Pricing Policy:

An international firm that follows an ethnocentric approach will use two-tiered pricing policy. Under two-tiered pricing policy, the firm sets one price for all its domestic sales and a second price for all its international sales. A firm that adopts a two-tiered pricing policy commonly allocates to domestic sales all accounting charges associated with research & development, administrative overheads, capital depreciation, and so on. The international marketer can then establish a uniform foreign sales price without having to worry about covering these costs. Domestic marketers that are just beginning to go international often use two-tiered pricing policy. International marketers that adopt a two-tiered pricing policy are also vulnerable to charges of dumping.

6.4.3. Market Pricing Policy:

International marketers that follow a polycentric approach to international marketing use market-pricing policy. Market pricing policy is the most complex of the three pricing policies and the one most commonly used. An international marketer utilizing market pricing policy customizes its prices on a market - by - market basis to maximize its profits in each market. Two conditions must be met if an international marketer is to successfully practice market pricing:

- The firm must face different demand and / or cost conditions in which it sells its products.

- ❖ The firm must be able to prevent arbitrage. (there may be companies that buy at lower price from the producer company and sells at high price)

Assuming these conditions are met, the advantages of this market pricing are obvious. For example, the firm can set higher prices where markets will tolerate them and lower prices where necessary in order to remain competitive. International marketers most likely to use this approach are those that produce and market their products in many different countries.

A market pricing policy can, however expose a firm to dumping complaints as well as to two other risks: Damage to its brand name and Development of gray market for its products.

Activity

1. Discuss environmental influences on pricing decisions?

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2. Explain in detail the price standardization?

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Under each of these policies, accompany may follow different pricing strategies which are clarified below one by one.

i) **Market Skimming**:

The market skimming pricing strategy is a deliberate attempt to reach a market segment that is willing to pay a premium price for a product. In such instances, the product must create high value for buyers. This pricing strategy is often used in the introductory phase of the product life cycle, when both production capacity and competition are limited. By setting a deliberately high price, demand is limited to early adopters who are willing and able to pay the price. One goal of this pricing strategy is to maximize revenue on limited volume and to match demand to available supply. Another goal of market skimming pricing is to reinforce customers' perceptions of high product value. When this is done, the price is part of the total product positioning strategy.

ii) **Penetration Pricing**:

Penetration pricing uses price as a competitive weapon to gain market position. The majority of companies using this type of pricing in international marketing are located in the Pacific Rim. Scale-efficient plants and low-cost labor allow these companies to blitz the market. It should be noted that a first-time exporter is unlikely to use penetration pricing. The reason is simple: Penetration pricing often means that the product may be sold at a loss for a certain length of time. Companies that are new to exporting cannot absorb such losses. They are not likely to have the marketing system in place (including transportation, distribution, and sales organizations) that allows global companies to make effective use of a penetration strategy. However, a company whose product is not penetrable may wish to use penetration pricing to achieve market saturation before the product is copied by competitors.

iii) **Market Holding**:

The market holding strategy is frequently adopted by companies that want to maintain their share of the market. In single-country marketing, this strategy often involves reacting to price adjustments by competitors. For example, when one airline announces special bargain fares, most competing carriers must match the offer or risk losing passengers. In global marketing, currency fluctuations often trigger price adjustments. Market holding strategies dictate that source country currency appreciation will not be automatically passed on in the form of higher prices. If the competitive situation in market countries is price sensitive, manufacturers must absorb the cost of currency appreciation by accepting lower margins in order to maintain competitive prices in country markets.

iv) **Cost Plus:**

Companies new to exporting frequently use a strategy known as cost -plus pricing to gain a toehold in the global marketplace. There are two cost-plus pricing methods: The older is the historical accounting cost method, which defines cost as the sum of all direct and indirect manufacturing and overhead costs. An approach used in recent years is known as the estimated future cost method. Cost-plus pricing requires adding up all the costs

required to get the product to where it must go, plus shipping and ancillary charges, and a profit percentage. The obvious advantage of using this method is its low threshold: It is relatively easy to arrive at a selling price, assuming that accounting costs are readily available. The disadvantage of using historical accounting costs to arrive at a price is that this approach completely ignores demand and competitive conditions in target markets. Therefore, historical accounting cost-plus prices will frequently be either too high or too low in the light of market and competitive conditions. If historical accounting cost-plus prices are right, it is only by chance. However, novice exporters do not care-they are reactively responding to global market opportunities, not proactively seeking them. Experienced global marketers realize that nothing in the historical accounting cost-plus formula directly addresses the competitive and customer-value issues that must be considered in a rational pricing strategy.

6.5. Alternative Pricing Strategies

Transfer Pricing

Transfer pricing refers to the pricing of goods and service bought and sold by operating units or divisions of a single company. In other words, transfer pricing concerns intra-corporate exchanges-transactions between buyers and sellers that have the same corporate parent. As companies expand and create decentralized operations, profit centers become an increasingly important component in the overall corporate financial picture. Appropriate intra-corporate transfer pricing systems and policies are required to ensure profitability at each level. There are three major alternative approaches to transfer pricing. The approach used will vary with the nature of the firm, products, markets, and the historical circumstances of each case. The alternatives are:

i) **Cost-Based Transfer Pricing:**

Because companies define costs differently, some companies using the cost-based approach may arrive at transfer prices that reflect variable and fixed manufacturing costs only. Alternatively, transfer prices may be based-on full costs, including overhead costs from marketing, research and development (R&D), and other functional areas. The way

costs are defined may have an impact on tariffs and duties on sales to affiliates and subsidiaries by global companies. Cost-plus pricing is a variation of the cost-based approach. Companies that follow the cost-plus pricing method are taking the position that profit must be shown for any product or service at every stage of movement through the corporate system. While cost-plus pricing may result in a price that is completely unrelated to competitive or demand conditions in international markets, many exporters use this approach successfully.

***ii)* Market-Based Transfer Price:**

A market based transfer price is derived from the price required to be competitive in the international market. The constraint on this price is cost. However, as noted previously, there is a considerable degree of variation in how costs are defined. Because costs generally decline with volume, a decision must be made regarding whether to price on the basis of current or planned volume levels. To use market-based transfer prices to enter a new market that is too small to support local manufacturing, third-country sourcing may be required. This enables a company to establish its name or franchise in the market without committing to a major capital investment.

***iii)* Negotiated Transfer Prices:**

A third alternative is to allow the organization's affiliates to negotiate transfer prices among themselves. In some instances, the final transfer price may reflect costs and market prices, but this is not a requirement. The gold standard of negotiated transfer prices is known as an arm's-length price: the price that two independent, unrelated entities would negotiate.

6.6. Dumping

Dumping is an important global pricing strategy issue. Dumping can be defined as the sale of an imported product at a price lower than that nominally charged in a domestic market or country of origin in addition, many countries have their own policies and procedures for protecting national companies from dumping. There are several types of dumping: sporadic, predatory, persistent, and reverse.

A. **Sporadic dumping** occurs when a manufacturer with unsold inventories wants to get rid of distressed and excess merchandise. To preserve its competitive position at home, the manufacturer must avoid starting a price war that could harm its home market. One way to find a solution involves destroying excess supplies, as in the example of Asian farmers dumping small chickens in the sea or burning them. Another way to solve the problem is to cut losses by selling for any price that can be realized. The excess supply is dumped abroad in a market where tee product is normally not sold.

B. **Predatory dumping** is more permanent than sporadic dumping. This strategy involves selling at a loss to gain access to a market and perhaps to drive out competition. Once the competition is gone or the market established, the company uses its monopoly position to increase price. Some critics question the allegation that predatory dumping is harmful by pointing out that if price is subsequently raised by the firm that does the dumping, former competitors can rejoin the market when it becomes more profitable again.

C. **Persistent dumping** is the most permanent type of dumping, requiring a consistent selling at lower prices in one market than in others. This practice may be the result of a firm's recognition that markets are different in terms of overhead costs and demand characteristics. For example, a firm may assume that demand abroad is more elastic than it is at home. Based on this perception, the firm may decide to use incremental or marginal-cost pricing abroad while using full-cost pricing to cover fixed costs at home. This practice benefits foreign consumers, but it works to the disadvantage of local consumers.

The three kinds of dumping just discussed have one characteristic in common: each involves charging lower prices abroad than at home. It is possible, however, to have the opposite tactic-reverse dumping. In order to have such a case, the overseas demand must be less elastic, and the market will tolerate a higher price. Any dumping will thus be done in the manufacturer's home market by selling locally at a lower price.

6.6.1. Legal Aspect of Dumping

Whether dumping is illegal or not depends on whether the practice is tolerated in a particular country. Switzerland has no specific antidumping laws. Most countries,

however, have dumping laws that set a minimum price or a floor on prices that can be charged in the market

One item of evidence of dumping occurs when a product is sold at less than fair value. The Commerce Department, for example, made a final determination that imports of certain small-business telephone systems and subassemblies from Japan and Taiwan were being sold in America at less than fair value. Subsequently, the U.S. International Trade Commission made final determinations and found injury to industries in the United States from such imports. The Commission's injury finding led to antidumping duties being placed on imported products to offset their price advantage.

Another example of dumping evidence is a product sold at a price below its borne-market price or production cost. The United States relies on the official U.S. trigger price, which is designed to curb dumping by giving an early signal of an unacceptable import price. In the case of steel, the trigger price sets a minimum price on imported steel that is pegged to the cost of producing steel in Japan. According to the General Accounting Office, some 40 percent of all imports at one time
were priced below the trigger price

Activity

1. Discuss the different types of dumping
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2. Differentiate market skimming and penetration pricing.
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6.7. Methods of Financing and Means of Payment

There are several payment methods. It should be noted that how buyers handle payments can vary from one part of the world to another.

i. **Consignment**

When a consignment is used, goods are shipped but ownership is retained by the seller. This means that the product is furnished on a deferred-payment basis, and once the

product is sold the seller is reimbursed by the consignee. In effect, the seller is providing full financing for the consignee. The problem with consignment sales is that a high degree of risk prevails. First of all, it is costly to arrange for the return of merchandise that is unsold.

In addition, due to the distance involved, the seller has difficulty keeping track of the inventory and its condition. Certain safeguards are thus necessary.

Consignment, however, can be a satisfactory arrangement when the sale involves an affiliated firm or the seller's own sales representative or dealer.

ii. Open account

With an open account, goods are shipped without documents calling for payment, other than the invoice. The buyer can pick up goods without having to make payment first. The advantage with the open account is simplicity and assistance to the buyer, who does not have to pay credit charges to banks. In return the seller expects that the invoice will be paid at the agreed time. A major weakness of this method is that there is no safeguard against default, since a tangible payment instrument does not exist. The lack of payment instrument also makes it difficult to sell the account receivable. To compound the problem, the buyer often delays payment until the merchandise is received – a standard practice in many countries. Because of the inherent risks of an open account, precautions should be taken. The seller must determine the integrity of the buyer by relying on prior experience, or through a credit investigation.

iii. Cash in advance

The seller may want to demand cash in advance when:

1 The buyer is financially weak or an unknown credit risk.

2 The economic/political conditions in the buyer's country are unstable.

3 The seller is not interested in assuming credit risk, as in the case of consignment and open account sales.

Because of the immediate uses of money and the maximum protection, sellers naturally prefer cash in advance. The problem, of course, is that the buyer is not eager to tie up its money, especially if the buyer has some doubt about whether it will receive the goods as

ordered. By insisting on cash in advance, the seller shifts the risk completely to the buyer, but the seller may end up losing the sale by this insistence.

iv. Bill of exchange (draft)

A means of financing international transactions is through a bill of exchange or draft, which is a request for payment. The request is an unconditional order in writing from one person (drawer) requiring the person to whom it is addressed (drawee) to pay the payee or bearer on demand or at a fixed or determinable time. The drawer, usually the exporter, is the maker or originator of the draft requesting payment. The drawee, usually the buyer, is the party responsible for honoring or paying the draft. The payee may be the exporter, the exporter's bank, the bearer, or any specified person. In short, a draft is a request for payment. It is a negotiable instrument that contains an order to pay a payee. As noted by John Stuart Mill many years ago, the purpose is to save expense and minimize the risk of transporting precious metals from place to place as payment of imports. The bill of exchange simply allows banks to make adjustments by debiting or crediting accounts maintained in buyer or seller names with other banks. The transaction process occurs in this way. The drawee accepts the draft by signing an acceptance on the face of the instrument. If the buyer does not accept (sign) the bill, the buyer is not given the attached documents to obtain goods from the steamship company, since the shipment is made on the negotiable order bill of lading. In practice, banks are responsible for payment collection. The original order bill of lading is endorsed by the shipper and sent to the buyer's bank along with the bill of exchange, invoices, and other required documents (e.g., consular invoice, insurance certificate, inspection certificate). Once notified by the bank, the buyer pays the amount on the draft and is given the bill of lading, which allows the buyer to obtain the shipment. There are two principal types of bill of exchange: **-**

A. A sight draft

A sight draft, as the name implies, is drawn at sight, meaning that it is paid when it is first seen by the drawee. A sight draft is commonly used for either credit reasons or for the purpose of title retention.

B. A time (date) draft

A time (date) draft is drawn for the purpose of financing the sale or temporary storage of specified goods for a specified number of days after sight (e.g., thirty, sixty, ninety days, or longer). It specifies payment of a stated amount at maturity. As such, it offers less security than a sight draft since the sight draft demands payment prior to the release of shipping documents.

The time draft, on the other hand, allows the buyer to obtain shipping documents to draw up merchandise when accepting the draft, even though the buyer can actually defer payment. At first sight, it may seem that a time draft is not really different from an open account, since the goods may be obtained or picked up by the buyer before making payment. There is one crucial difference, however. In the case of the time draft, there is a negotiable instrument evidencing the obligation. Since this document may be sold to factors and discounted immediately, the seller can obtain cash before maturity.

v. Letter of credit (L/C)

An alternative to the sight draft is a sight letter of credit (L/C). As a legal instrument, it is a written undertaking by a bank through prior agreement with its client to honor a withdrawal by a third party for goods and services rendered. The document, issued by the bank at the buyer's request in favor of the seller, is the bank's promise to pay an agreed amount of money on its receipt of certain documents within the specified time period.

Usually, the required documents are the same as those used with the sight draft. In effect, the bank is being asked to substitute its credit for that of the buyer. The bank agrees to allow one party to the transaction (the seller, creditor, or exporter) to collect payment from that party's correspondent bank or branch abroad. Drafts presented for payment under the L/C are thus drawn on the bank. The importer can repay the bank by either making an appropriate deposit in cash or borrowing all or part of the money from the bank. The drawee (buyer) is usually responsible for the collection charges by banks at home and overseas. The issuing bank, as a rule, issues letters of credit for its current customers only, even if collateral is offered by someone else. In contrast, the advising bank is the bank which notifies the exporter that an L/C has been issued. The issuing

bank forwards the L/C to the advising bank (its foreign correspondent), which is usually selected for its proximity to the beneficiary. In the case of a confirming bank the same services are performed as the advising bank but also the confirming bank becomes liable for payment.

Activity

1. Discuss in detail about market pricing policy?

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2. Explain cost-based transfer pricing and market-based transfer price:

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6.8. Countertrade

Counter trade constitutes an estimated 5 to 30 percent of total world trade. Counter trade greatly proliferated in the 1980s. Counter trade, one of the oldest forms of trade, is a government mandate to pay for goods and services with something other than cash. It is a practice, which requires a seller as a condition of sale, to commit contractually to reciprocate and undertake certain business initiatives that compensate and benefit the buyer. In short, a goods-for-goods deal is counter trade. Unlike monetary trade, suppliers are required to take customers' products for their use or for resale. In most cases, there are multiple deals that are separate yet related, and a contract links these separable transactions. Counter trade may involve several products, and such products may move at different points in time while involving several countries. Monetary payments' may or may not be part of the deal.

There are three primary reasons for counter trade: (1) counter trade provides a trade financing alternative to those countries that have international debt and liquidity problems, (2) counter trade relationships may provide LDCs and MNCs with access to new markets, and (3) counter trade fits well conceptually with the resurgence of bilateral trade agreements between governments.

6.8.1. Types of Counter Trade

1. Barter- Barter, possibly the simplest of the many types of counter trade, is a onetime direct and simultaneous exchange of products of equal value (i.e., one product for another). By removing money as a medium of exchange barter makes it possible for cash-tight countries to buy and sell. Although price must be considered in any counter trade, price is only implicit at best in the case of barter. For example, Chinese coal was exchanged for the construction of a seaport by the Dutch, and Polish coal was exchanged for concerts given by a Swedish band in Poland.

2. Counter purchase (Parallel Barter)- Counter purchase occurs when there are two contracts or a set of parallel cash sales agreements, each paid in cash. Unlike barter which is a single transaction with an exchange price only implied. A counter purchase involves two separate transactions-each
with its own cash value. A supplier sells a facility or product at a set price and orders unrelated or non-resultant products to offset the cost to the initial buyer. Thus, the buyer pays with hard currency, whereas the supplier agrees to buy certain products within a specified period. Therefore, money does not need to change hands.

3. Compensation Trade (Buyback)-A compensation trade requires a company' to provide machinery, factories, or technology and to buy products made from this machinery over an agreed-on period. Unlike counter purchase, which involves two unrelated products, the two contracts in a
compensation trade is highly related. Under a separate agreement to the sale of plant or equipment, a supplier agrees to buy part of the plant's output for a number of years.

4. Switch Trading-Switch trading involves a triangular rather than bilateral trade agreement. When goods, all or part, from the buying country are not easily usable or salable; it may be necessary to bring in a third party to dispose of the merchandise. The third party pays hard currency for the unwanted merchandise at a considerable discount.

5. Offset- In an offset, a foreign supplier is required to manufacture/assemble the product locally and/or purchase local components as an exchange for the right to sell its products locally. In effect, the supplier has to manufacture at a location that may not be optimal

from an economic standpoint. Offsets are often found in purchases of aircraft and military equipment.

6. Clearing Agreement- A clearing agreement is clearing account barter with no currency transaction required. With a line of credit being established in the central banks of the two countries, the trade in this case is continuous, and the exchange of products between two governments is designed to achieve an agreed-on value or volume of trade tabulated or calculated in nonconvertible clearing account units.

6.8.2. Problems and Opportunities of Counter Trade

Although counter trade is a common and growing practice, it has been criticized on several fronts.

First, counter trade is considered by some as a form of protectionism that poses a new threat to world trade. Such countries as Sweden, Australia, Spain, Brazil, Indonesia, and much of Eastern Europe demand reciprocity in order to impose a discipline on their balance of payments. In other words, imports must be offset by exports.

Second, counter trade is alleged to be nothing but “covert dumping.” To compensate any supplying partners for the nuisance of taking another-product as payment, a counter trading country frequently trades its products away at a discount. If the counter trading country discounts directly by selling its goods itself in another market instead of through a foreign firm, dumping would clearly occur.

Third, counter trade is alleged to increase overhead costs and ultimately the price of a product. Counter trade involves time, personnel, and expenses in selling a customer’s product-often at a discount. If another middleman is used to dispose of the product a commission must also be paid. Because of these expenses, a selling company has to raise-the price of the original order to compensate for such expenses as well as for the risk of taking another product in return as payment. The fact that the goods are saleable—either for other goods or, in the end, for cash somewhere else means that additional and probably unnecessary costs must be incurred.

Firms that tend to benefit from counter trade are the following: (1) large firms that have extensive trade operations from large, complex products; (2) vertically integrated firms that can accommodate counter trade take backs; and (3) firms that trade with countries that have inappropriate exchange rates, rationed foreign exchange, import restrictions, and importers inexperienced in assessing technology or in export marketing. In contrast firms whose characteristics are the opposite of those just enumerated are likely to encounter significant barriers to counter trade operations and to receive few benefits.

Summary

A firm's pricing system and policies must also be consistent with other unique global constraints. Global marketers must deal with a number of environmental considerations when making pricing decisions. Among these are currency fluctuations, inflation, government controls and subsidies, competitive behavior, and market demand. An international firm that follows an ethnocentric approach will use two-tiered pricing policy. Under two-tiered pricing policy, the firm sets one price for all its domestic sales and a second price for all its international sales.

The market skimming pricing strategy is a deliberate attempt to reach a market segment that is willing to pay a premium price for a product. In such instances, the product must create high value for buyers. Transfer pricing refers to the pricing of goods and service bought and sold by operating units or divisions of a single company. In other words, transfer pricing concerns intra-corporate exchanges-transactions between buyers and sellers that have the same corporate parent. A market based transfer price is derived from the price required to be competitive in the international market. The constraint on this price is cost. However, as noted previously, there is a considerable degree of variation in how costs are defined.

Review Questions

1. List and briefly discuss the types of counter trade.
2. Discuss the methods of financing and means of payment.
3. Differentiate market-based transfer pricing and negotiated transfer pricing.

4. Explain in detail the legal aspect of dumping
5. Discuss in detail about means of payment

CHAPTER SEVEN

DISTRIBUTION STRATEGIES IN INTERNATIONAL CONTEXT

Chapter Objectives:

After studying this chapter, you should be able to:

- Define the physical distribution
- Understand the different distribution strategies
- Differentiate home- country middlemen and foreign-country middlemen
- Explain the factors
- affecting choice of channels
- Understand the documents that are used in clearing goods from customs authority

Introduction

This chapter deals with the patterns of distribution that confront international marketers in the world market place, alternative middleman choices both in their home country and foreign countries, and the factors affecting choice of channels of distribution. Distribution is a necessary as well as costly activity. According to one executive at Procter & Gamble, the average time required to move a typical product from "farm to shelf" is four to five months. Although it takes only about seventeen minutes to actually produce a product, the rest of the time is spent in logistical activities- storage, handling, transportation, packing and so on.

7.1 Marketing logistics (or physical distribution)

To some managers, marketing logistics means only trucks and warehouses. But modern logistics is much more than this. Marketing logistics or physical distribution involves planning, implementing, and controlling the physical flow of goods, services, and related information from points of origin to points of consumption to meet customer requirements at a profit. In short, it involves getting the right product to the right customer in the right place at the right time.

When a company is primarily an exporter from a single country to a single market, the typical approach to the physical movement of goods is the selection of a dependable mode of transportation that ensures safe arrival of the goods within a reasonable time for a reasonable carrier cost. As a company becomes global, such a solution to the movement of products could prove costly and highly inefficient for seller and buyer. As some global marketers say, the hardest part is not making the sale but getting the correct quantity of the product to customers in the required time frame at a cost that leaves enough margins for a profit.

At some point in the growth and expansion of an international firm, costs other than transportation are such that an optimal cost solution to the physical movement of goods cannot be achieved without thinking of the physical distribution process as an integrated system. When an international marketer begins producing and selling in more than one country and becomes a global marketer, it is time to consider the concept of logistics management, a total systems approach to the management of the distribution process that

includes all activities involved in physically moving raw material, in-process inventory, and finished goods inventory from the point of origin to the point of use or consumption.

A physical distribution system involves more than the physical movement of goods. It includes the location of plants and warehousing (storage), transportation mode, inventory quantities, and packing. The concept of physical distribution takes into account the interdependence of the costs of each activity; a decision involving one activity affects the cost and efficiency of one or all others. In fact, because of their interdependence, the sum of each of the different activity costs entails an infinite number of "total costs." (Total cost of the system is defined as the sum of the costs of all these activities).

The concept behind physical distribution is the achievement of the optimum (lowest) system cost, consistent with customer service objectives of the firm. If the activities in the physical distribution system are viewed separately, without consideration of their interdependence, the final cost of distribution may be higher than the lowest possible cost (optimum cost), and the quality of service may be adversely affected. Additional variables and costs that are interdependent and must be included in the total physical distribution decision heighten the distribution problems confronting the international marketer. As the international firm broadens the scope of its operations, the additional variables and costs become more crucial in their effect on the efficiency of the distribution system.

7.2 Distribution Strategies

In every country and in every market, urban or rural, rich or poor, all consumer and industrial products eventually go through a distribution process. The distribution process includes the physical handling and distribution of goods, the passage of ownership (title), and- most important from the standpoint of marketing strategy-the buying and selling negotiations between producers and middleman and between middleman and customers.

Each country market has a distribution structure through which goods pass from producer to user. Within this structure are a variety of middleman hose customary functions, activities, and services reflect existing competition, market characteristics, tradition, and economic development. In short, the behavior of channel members is the result of the interactions between the cultural environment and marketing process.

7.2.1. Distribution Patterns

International marketers need a general awareness of the patterns of distribution that confront them in world marketplaces. Nearly every international trading firm is forced by the structure of the market to use at least some middlemen in the distribution arrangement. However, the pattern to structure may differ from market to market. Thus, understanding the various kinds of distribution patterns may assist international marketers to make an appropriate choice.

- **Middlemen Services:** The service attitudes of people in trade vary sharply at both retail and wholesale levels from country to country. In Egypt, for example, the primary purpose of the simple trading system is to handle the physical distribution of available goods. On the other hand, when margins are low and there is a continuing battle for customer preference, both wholesalers and retailers try to offer extra services to make their goods attractive to consumers. When middlemen are disinterested in promoting or selling individual items of merchandise, the manufacturer must provide adequate inducement to the middlemen or undertake much of the promotion and selling effort.
- **Line Breadth**: Every nation has a distinct pattern relative to the breadth of line carried by wholesalers and retailers. The distribution system of some countries seems to be characterized by middleman who carry or can get everything; in others, every middleman seems to be a specialist dealing only in extremely narrow lines. Government regulations in some countries limit the breadth of line that can be carried by middleman and licensing requirements to handle certain merchandise are not uncommon.
- **Cost and Margins**: Cost levels and middleman margins vary widely from country to country, depending on the level of competition, services offered, efficiencies or inefficiencies of scale, and geographic and turnover factors related to market size, purchasing power, tradition, and other basic determinants. In India, competition in large cities is so intense that costs are low and margins thin; but in rural areas, the lack of capital has permitted the few traders with capital to gain monopolies with consequent high prices and wide margins.

- **Channel Length:** Some correlation may be found between the stage of economic development and the length of marketing channels. In every country channels are likely to be shorter for industrial goods and for high-priced consumer goods than for low-priced products. In general, there is an inverse relationship between channel length and the size of the purchase. Combination wholesaler-retailers or semi-wholesalers exist in many countries, adding one or two links to the length of the distribution chain.
- **Nonexistent Channels:** one of the things companies discover about international channel of distribution patterns that in many countries adequate marketer coverage through a simple channel of distribution is nearly impossible. In many instances, appropriate channels do not exist; in others, parts of channel system are available but other parts are not.
- **Blocked Channels**: International marketers may be blocked from using the channel of their choice. Blockage can result from competitors' already-established lines in the various channels and trade associations or cartels having closed certain channels. Associations of middleman sometimes restrict the number of distribution alternatives available to a producer.
- **Stocking:** The high cost of credit, danger of loss through inflation, lack of capital, and other concerns cause foreign middleman in many countries to limit inventories. This often results in out-of-stock conditions and sales lost to competitors. Physical distribution lags intensify their problem so that in many cases the manufacturer must provide local warehousing or extend long credit to encourage middlemen to carry large inventories.
- **Power and competition:** Distribution power tends to concentrate in countries where a few large wholesalers distribute to a mass of small middleman. Large wholesaler generally finances middlemen downstream. The strong allegiance they command from their customers enables them to effectively block existing channels and force an outsider to rely on less effective and costlier distribution.

7.3. **Alternative Middleman Choices**

A marketer's options range from assuming the entire distribution activity (by establishing its own subsidiaries and marketing directly to end user) to depending on intermediaries for distribution of the product. Channel selection must be given considerable thought since one initiated it is difficult to change, and if it proves inappropriate, future growth of market share may be affected.

The channel process includes all activities beginning with the manufacturer and ending with the final consumer. This means the seller must exert influence over two sets of channels, one in the home country and one in the foreign-market country. In the home country, the seller must have an organization (generally the international marketing division of a company) to deal with channel members needed to move goods between countries. In the foreign market, the seller must supervise the channels that supply the product to the end user. Ideally, the company wants to control or be involved in the process directly through the various channel members to the final user. To do less may result in unsatisfactory distribution and the failure of marketing objectives. In practice, however, such involvement throughout the channel process is not always practical or cost effective. Consequently, selection of channel members and effective controls are high priorities in establishing the distribution process.

Once the marketer has clarified company objectives and policies, the next step is the selection of specific intermediaries needed to develop a channel. External middleman is differentiated on whether or not they take title to the goods- agent middleman represent the principle rather than themselves, and merchant middleman take title to the goods and buy and sell on their own account. The distinction between agent and merchant middleman is important because a manufacturer's control of the distribution process is affected by who has title to the goods in the channel.

Agent middleman work on commission and arrange for sales in the foreign country but do not take title to the merchandise. By using agents, the manufacturer assumes trading risk but maintains the right to establish policy guidelines and prices and to require its agents to provide sales records and customer information.

Merchant middlemen actually take title to manufacturers' goods and assume the trading risks, so they tend to be less controllable than agent middleman. Merchant middlemen

provide a variety of import and export wholesaling functions involved in purchasing for their own account and selling in other countries. Because merchant middlemen primarily are concerned with sales and profit margins on their merchandise, they are frequently criticized for not representing the best interests of a manufacturer. Unless they have a franchise or a strong and profitable brand, merchant middlemen seek goods from any source and are likely to have low risk and elimination of all merchandise handling outside the home country.

Middlemen are not clear-cut, precise, easily defined entities. It is exceptional to find a firm that represents one of the pure types identified here. Thus, intimate knowledge of middlemen functions is especially important in international activity because misleading titles can fool a marketer unable to look beyond mere names.

Only by analyzing middlemen functions in detailed simplicity can the nature of the channel be determined. Two alternatives are presented: first, middlemen physically located in the manufacturer's home country; and second, middlemen located in foreign countries.

7.3.1. **Home- country Middlemen**

Home country middlemen, or domestic middlemen, located in the producing firm's country provide marketing services from a domestic base. By selecting domestic middlemen as intermediaries in the distribution processes, companies transfer foreign-market distribution to others. Domestic middlemen offer many advantages for companies with small international sales volume, those inexperienced with foreign markets, those not wanting to become immediately involved with the complexities of international marketing, and those wanting to sell abroad with minimum financial and management commitment. A major trade-off for using home-country middlemen is limited control over the entire process. Domestic middlemen are most likely to be used when the marketer is uncertain and/or desires to minimize financial and management investment. A brief discussion of the more frequently used domestic middleman follows.

A. **Trading Companies:** Trading companies have a long history as important intermediaries in the development of trade between nations. Trading companies accumulate, and distribute goods from countries. Large, established trading companies generally are located in developed countries; they sell manufactured goods

to developing countries and buy raw materials and unprocessed goods from developing countries.

B. **Complementary Marketers:** Companies with marketing facilities or contacts in different countries with excess marketing capacity or a desire for a broader product line sometimes like on additional lines for international distribution; although the generic name for such activities is complementary marketing, it is commonly called piggybacking. It accepts products that are noncompetitive but complementary and that add to the basic distribution strength of the company itself.

C. **Manufacturer's Export Agent**: The manufacturer's export agent (MEA) is an individual agent middleman or an agent middleman firm providing a selling service for manufacturers. The MEA does not serve as the producer's export department but has a short-term relationship, covers only one or two markets, and operates on a straight commission basis.

D. **Home Country Brokers**: The term broker is an applicable for a variety of middlemen performing low-cost agent services. The term is typically applied to import-export brokers who provide the intermediary function of bringing buyers and sellers together and who do not have a continuing relationship with their clients. Most brokers specialize in one or more commodities for which they maintain contact with major producers and purchasers throughout the world.

E. **Export Merchants**: Export merchants are essentially domestic merchants operating in foreign markets. As such, they operate much like the domestic wholesaler. Specifically, they purchase goods from a large number of manufacturers, ship them to foreign countries, and take full responsibility for their marketing. Sometimes they utilize their own organizations, but, more commonly, they sell through middlemen. They may carry competing lines, have full control over prices, and maintain little loyalty to suppliers, although they continue to handle products as long as they are profitable.

Activity

1. What are more frequently used domestic middleman? Discuss

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7.3.2. **Foreign-Country Middlemen**

An international marketer seeking greater control over the distribution process may elect to deal directly with middlemen in the foreign market. They gain the advantage of shorter channels and deal with middlemen in constant contact with the market. As with all middlemen, particularly those working at a distance, effectiveness is directly dependent on the selection of middlemen and on the degree of control the manufacturer can and/or will exert.

Using foreign-country middlemen moves the manufacturer closer to the market and involves the company more closely with problems of language, physical distribution, communications, and financing. Foreign middlemen may be agents or merchants; they may be associated with the parent company to varying degrees; or they may be temporarily hired for special purposes. Some of the more important foreign-country middlemen are manufacturer's representatives and foreign distributors.

1. **Manufacturer's Representatives**: Manufacturer's representatives are agent middlemen who take responsibility for a producer's goods in a city, regional market area, entire country, or several adjacent countries. When responsible for an entire country, the middleman is often called a sole agent. Foreign manufacturer's representatives have a variety of titles, including sales agent, resident sales agent, exclusive agent, commission agent, and indent agent. They take no credit, exchange, or market risk but deal strictly as field sales representatives. Manufacturers who wish the type of control and intensive market coverage their own sales force would afford, but who cannot field one, may find the manufacturer's representative a satisfactory choice.
2. **Distributors:** A foreign distributor is a merchant middleman. This intermediary often has exclusive sales rights in a specific country and works in close cooperation with the manufacturer. The distributor has a relatively high degree of dependence on the supplier companies, and arrangements are likely to be on a long-run, continuous basis. Working through distributors permits the manufacturer a reasonable degree of

control over prices, promotional effort inventories, servicing, and other distribution functions. If a line is profitable for distributors, they can be depended on to handle it a manner closely approximating the desires of the manufacturer.

3. **Foreign-Country Brokers:** Like the export broker discussed in an earlier section, foreign-country brokers are agents who deal largely in commodities and food products. The foreign brokers are typically part of small brokerage firms operating in one country or in a few contiguous countries. Their strength is in having good continuing relationship with customers and providing speedy market coverage at a low cost.
4. **Dealers:** Generally speaking anyone who has a continuing relationship with a supplier in buying and selling goods is considered a dealer. More specifically, dealers are middlemen selling industrial goods or durable consumer goods direct to customers; they are the last step in the channel of distribution. Dealers have continuing, close working relationships with their suppliers and exclusive selling rights for their producer's products within a given geographic area.

Some of the best examples of dealer operations are found in the farm equipment, earth-moving, and automotive industries.

7.4. **Factors Affecting Choice of Channels**

There is no single across the board solution for all manufacturers' channel decisions. Yet there are certain guidelines that can assist a manufacturer in making a good decision factors that must be taken into account include legal regulations, product image, product characteristics, intermediary's loyalty and conflict, and local customs.

1. Legal Regulations

A country may have specific laws that rule out the use of particular channels or middlemen for example, prohibits the use of doors to door selling. The overseas distribution channel often has to be longer than desired. Because of government regulations, a foreign company may find it necessary to go through a local agent/ distributor. In china, foreign firms cannot wholly own retail

outlets, and they can to engage in wholesaling activities. In addition, only fourteen foreign retail ventures have direct import authority, forcing those without direct import authority to add another layer of middlemen.

2. Product Image

The product image desired by a manufacturer can dictate the manner in which the product is distributed. A product with a low- rice image requires intensive distribution. On the other hand, it is not necessary nor even desirable for a prestigious product to have wide distribution. Although intensive distribution may increase sales in the short run, it is potentially harmful to the products image in the long run.

3. Product Characteristics

The type of product determines how that product should be distributed. For low- high-turnover convenience products, the requirement is for an intensive distribution network. The intensive distribution of ice cream is an example walls (formerly Foremast's) success in Thailand can be attributed in part to its intensive distribution and channel adaptation tailored its distribution activities to the local Thai scene by sending its products (Ice cream, milk, and other dairy products) into market in every conceivable manner. Such traditional channels as wholesalers and such new channels as company-owned retail outlets (modern soda fountains) and push-carts are also used.

4. Middlemen's Loyalty and Conflict

One ingredient for an effective channel is satisfied channel member. As the channel widens and as the number of channels increases, more direct competition among channel members in inevitable. Some members will perceive large competing member and self-service members as being unfair. Some members will blame the manufacturer for being motivated by greed when setting up a more intensive network. In effect for being motivated by greed when setting up a more intensive network. In effect intensive distribution reduces channel members.

5. Local Customs

Local business practices, whether outmoded or not, can interfere with efficiency and productivity and may force a manufacturer to employ a channel of distribution that is longer and wider than desired.

6. Control

If it has a choice, a manufacturer that wants to have better control over its product distribution may want to both shorten 'and-narrow 'its distribution channel- One study of Bntaill's' machine tool importers-f6imd that, in light of the EU integration and competitive pressures, there has been an
increase in the number of sales subsidiaries as compared with distributors or agents. Apparently, manufacturers want to get closer to final customers.

One study employed a model based on transaction cost analysis to explain ex-porters' vertical control selections. Exporters of specialized products should establish channel structures that require a greater commitment of resource. Such structures, however, require larger fixed costs. Conversely, in the case of a relatively competitive market with large numbers of buyers and sellers, an exporter may want to give up some control and switch to a looser structure by contracting in the market place for the provision of marketing functions.

Activity

1. Discuss the factors determining the channel decision?

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2. Discuss the types of intermediaries involved in direct channel?

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7.5. Shipping Documents

It is not an exaggeration to say that, "paper moves cargo". To move cargo, documentation is a necessity. Moving cargo to an overseas destination is a much more complex task than transportation of freight locally. Other than the usual package designed to protect and/or promote a product while on display, packing (shipping package) is necessary if the merchandise is to be properly protected during shipment. Before a seller can request payment, the seller must provide the buyer with a number of documents showing that the terms agreed upon have been compiled with. The buyer requires such documents to protect him and to satisfy its government requirements. The documents that is used in clearing goods from customs authority are as follows:

1. Commercial Invoice

To collect payment, an invoice is needed. There are two kinds of invoices.

i. **Pro-forma invoice:** is an invoice provided by a supplier prior to the shipment of merchandise. The purpose of this invoice is to inform the buyer of the kinds and quantities of goods to be sent their value and important specification (weight, size and so on). The buyer may also need the pro-forma invoice in order to be able to apply for an import license and/or a letter of credit.

ii. **Commercial invoice:** A commercial invoice is a document that provides an itemized list of goods shipped and other charges. As a complete record of the business transaction between two parties, it provides a complete description of merchandise quantity, price and shipping and payment terms.

2. Certificate of origin

A certificate of origin is a document prepared by the exporter and used to identify or declare that the merchandise originated in a certain country. It assures the buyer or importer of the country of manufacture. These documents are necessary for tariff and control purposes. Some countries may require statements of origin to establish possible preferential rates of import duties under the most favored nation arrangements. This certificate also prevents the inadvertent important of goods from prohibited or unfriendly countries.

3. Packing list

A packing list is a document that lists the type and number of pieces, the contents, weights, and measurement of each, as well as the marks and numbers. Its purpose is to facilitate customs clearance, keep track of inventory of goods, and assists in tracing lost goods. For insurance purpose, the packing list can be used in determining the contents of a lost piece. Furthermore, it is also useful in estimating shipping costs prior to export.

4. Airway bill / Bill of lading

An airway bill is basically a bill of lading issued by air carriers for air shipments. This transport instrument is not a negotiable document. As a result, a carrier will release goods to a designated consignee without the waybill. Bill of lading is a document issued

to record shipment transportation. Usually prepared by a shipper on the shippers' carrier's forms, this document serves three useful functions.

As a document of title: it is a certificate of ownership that allows a holder or consignee to claim the merchandise described.
As a receipt of goods: the carrier issues it to the shipper for goods entrusted to the carrier's possession of the freight.
As a contract of carriage: the bill of lading defines the contract terms between the shipper and his carrier. The conditions under which the goods are to be carried and the carrier's responsibility for the delivery are specified.

5. Insurance certificate

A certificate of insurance is a negotiable document issued to provide coverage for a specific shipment. It briefly describes the transaction and its coverage.

6. Special purpose documents

As in the case of an inspection certificate, an importer may request other special documents, such as a certificate of weight / measurements and certificate of analysis in order to protect the importer's interest. Other documents may include - inspection report, warranty, bank permit, etc.

Summary

Goods have to move from the point of production to consumption. The process traditionally is called physical distribution. Physical distribution consists of all activities concerned with moving the right amount of the right products to the right place at the right time. The activities comprising physical distribution are: inventory location and warehousing, material handling, inventory control, order processing and transportation.
A marketer's options range from assuming the entire distribution activity (by establishing its own subsidiaries and marketing directly to end user) to depending on intermediaries for distribution of the product. Channel selection must be given considerable thought since one initiated it is difficult to change, and if it proves inappropriate, future growth of

market share may be affected. The channel process includes all activities beginning with the manufacturer and ending with the final consumer.

To move goods across the customs boundary, documentation is necessary. Moving cargo to an overseas destination is much more complex task than transportation of freight locally. Some of the documents necessary to clear goods from customs are: certificate of origin, bill of lading, packing list, air way bill, insurance certificate, special purpose documents, etc.

Review Questions

1. Explain in detail the different distribution strategies
2. What are the documents that is used in clearing goods from customs authority? Discuss them.
3. Distinguish home- country middlemen and foreign-country middlemen.
4. Discuss the two kinds of commercial invoices.

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International Marketing Assignment Questions (30%)

1. Discuss the difference between domestic and international marketing
2. List the entry modes of international market
3. Discuss the stage of international marketing involvement
4. List and discuss the types of international marketing environments
5. What are the principal elements of culture that influence international marketing decisions and how do they need to be addressed by an international firm in establishing business in the host country?
6. What are the documents that are used in clearing goods from customs authority? Discuss them.
7. Briefly discuss the global pricing policies
8. Explain in detail international marketing payment methods.
9. Explain the concept of international product life cycle (IPLC) with appropriate examples.
10. Describe the criteria for selection of Distributors / dealers in a foreign market.

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