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GAP Enterprises, Ltd.

International Business

Today

*Understanding the issues needed to
compete in today's global economy*

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THE ISSUES

In order to compete in the global marketplace, one needs to understand the issues involved which are:

1. Economic
2. Political
3. Cultural, including social and moral
4. Technology including computers, transportation and the Internet
5. Legal and financial including property rights and protection
6. Organization structures and strategic alliances
7. Global Monetary System

ECONOMIC

There are many trade theories that have been bantered about over the years, and many are just that – theories. The primary focus of theories and technology is obviously getting embryonic products, services or technology from "mind to market." But most of the challenge is finding a market and getting a product to that market.

So while theories like the Ricardo Theory or Heckscher-Ohlin Theory or Product Life Cycle Theory may sound good, in reality they are academia's way of identifying what business folks have done for years. Today there are newer theories like the "Innovation Diffusion" strategy, which are discussed in books such as "Crossing the Chasm" (Moore) or "Innovator's Dilemma" (Christensen).

As a colleague Mark Neely¹, LLB AIMM, states "When you mesh the dry science with qualitative/quantitative research (basically taking the 'technology adoption life cycle' and merging it with deep market data and consumer attitudinal research), you can pretty well come up with a no-brainer business strategy that tells you which consumer segments are going to buy, when and why, and (if you do your research well) for how much."

"This allows you to develop a succession of marketing and product development strategies (each consumer segment requires different marketing/product strategies), as well as map out the

¹ Mark Neely, LLB AIMM, Author & Technology Commercialisation Consultant, mpn@infolution.com.au
Moderator - I-Entrepreneur Digest - www.adventive.com/lists/ientrepreneur/summary.html

longevity of your product (so you can work out when to introduce further innovations or incremental/iterative enhancements without cannibalizing your market share etc.)”

And as my friend, Jacques Chevron² one of the world's leading branding gurus and author of the Delphi Theory™, states "The concept of life cycle is self-defeating. Look at Proctor and Gamble's Tide. While product formulae may have a limited life, the concept behind the product Tide ("tough or tougher on dirt") can continue as long as the formula is continually adapted to incorporate new advances, new lifestyles, etc. Tide has more than half a dozen formulations in test market at any one time and quietly replaces the old product with the updated one."

Fellow author, Prentis Hall³, Director of the Industrial Marketing Practice Association, says that most people (with the help of the business press) misunderstand the original meaning of "life cycle." As originally developed by Bruce Henderson, the life cycle curve is derived from something called the experience curve, which explains the rate at which manufacturing efficiency improves with time. He was talking about categories of technology, and entire markets, not individual products, or even individual companies. The experience curve is still a valid concept when you are talking manufacturing costs.⁴

Why do we need theories? Let's look at the basics. International trade is very simple – you have products; I want products; I buy your products. Of course there are other issues – like I don't know I want your products, or I can't afford your products or competitors have a better price/selection. That's where marketing comes into play. Tell me about your products; tell manufacturing to make the products so I can afford them; make me want to buy your products.

I consulted for a major US-based financial services company who wanted to expand globally and they wanted their products to reach everybody in the world – all 5.9 billion people. Their products ranged from \$200 to \$10,000 annually. The first thing I did was some simple market research.

1. There are 183 countries (out of 228) with per capita income under USD \$10,000 which represents 85.3% of the world's population.
2. There are 166 countries with per capita income under USD \$5,000 which represents 81.5% of the world's population.
3. There are 99 countries with per capita income under USD \$1,000 which represents 62.5% of the world's population.

How can somebody in Indonesia, China and India, with 41.5% of the population, and with average per capita income of USD \$649, afford \$200 annual fees? In effect, this company lost at least 3.9 billion at the low end and 5 billion at the high end. Why didn't they do the simple research? In any event, it meant a re-positioning of products and their marketing plan. And a realization that there are some areas of the world that they will not be able to penetrate.

LOGISTICS AND DISTRIBUTION

How do I get products distributed to other countries? It may be easy to manufacture products locally, but how does a company get those products to another country and how does one distribute in that country? The laws that govern selling in a country also affect logistics. For example, in Germany one must state the landed cost to the consumer, which must include all duties, freight and taxes, which therefore implies technology that can handle global pricing.

² Jacques Chevron is one of the world's leading authorities on branding. He has an impressive list of clients in the Fortune 50 group as well as independent businesses. His Delphi may be found on his site, or send him a note at mailto:Jacques@JRCandA.com?Subject=ETD_Delphi

³ Prentis Hall, Publisher, Industrial Marketing Practice Association. An Organization Dedicated to Providing Practical Ideas and Career Growth for Industrial Marketers email: hallpw@practitioner.com <http://www.practitioner.com>

⁴ A good book to read on the topic is "The Logic of Market Strategy" by Bruce Henderson.

These regional economic integration pacts will benefit the consumer the most with increased competition, which implies reduced prices. Of course, this will be an issue with businesses who may look to expand in a country because of the potential higher profits. For example, a Volkswagen Golf cost 55 percent more in Great Britain than in Denmark and 29 percent more in Ireland than in Greece. With a single market, those price differences will disappear.

There is a question whether countries still need to protect their domestic businesses at all, especially from those companies who engage in “dumping”, i.e., selling products far below cost to kill an industry in a country. The US imposed a high import duty on electronic components from Japan, which actually hurt US manufacturers like IBM, Apple, Compaq and others who used the components. The US Commerce Department was hoping to get Japanese manufacturers to set up operations in the US, which would never happen, since these companies invested heavily in Japan. US component manufacturers did not, and that industry segment is failing.

CULTURAL

The religious, moral and social cultures of a country are often overlooked, especially by more advanced countries like France and the U.S. (the “ugly American” syndrome), which causes hatred among many people.

When doing business in Japan for example, one must first discuss social or family issues, and not bring up business unless your host does so first. When dealing with the Muslim community, you must understand that they live by the Koran, and must pray five times a day. I was in a meeting with five Muslims, and they had to break for prayer right in the middle of a presentation. From that point on, I first asked for the prayer schedule for the day, so I could work around it.

Islam is also the only religion that dictates how business will be conducted. Muslims cannot do business with any person or company who charges or receives interest. They believe you do not put your sweat into work if you earn money from money. Hence, they don't use banks. Now, if they don't have a choice they can do business with these interest-laden companies. It is like eating pork. It is forbidden, however, if they were on an island and all that was there were pigs, then they could eat pork. Same with banks.

Muslim banks will not charge interest. Rather they take an equity position in a business to which they lend money, and share in the profits.

Considering there are 1.4 billion Muslims in the world, ruled by 300 royal families, who in turn are supported by tribal sheikhs, who oversee up to 40,000 individuals, it would behoove one to understand them if you want to do business with them. Offend them, and they will be gracious throughout your meeting, but never call you back nor tell you what you did to offend them. While doing business with this community, I had to attend a six-day behavioral training program that was given to diplomats and potential business partners worldwide.

TECHNOLOGY

While most economists may say it is impossible to identify one issue that contributed more to globalization, in my opinion it is technology. According to Moore's Law, technology doubles its capacity and halves its cost every 18 months. Today the Palm Pilot has more capacity than did mainframes in the 1960s (yes there were computers then).

Since computer programming is intellectual property, it is ideal for poorer countries to capitalize on, and to become the technical gurus of the world. India has become a software powerhouse in the past decade. They have the third largest concentration of software engineers in the world, yet the per capita income of India is only \$453! And India has a very poor information technology (IT) infrastructure (1.8 personal computers installed with a population of 1 billion) and is one of

Controlling costs will improve the bottom line. Let's look at an example and say we have a retail chain who is doing \$100 million in sales. Industry standards show that markdowns usually represent 19% of sales, shrinkage represents 3 ½ %, they turn inventory 2 ½ times a year and inventory carrying costs are 10% of inventory. If a company can manage inventory and control customers better, they could reduce markdowns and improve inventory turns.. And if they can control theft, they reduce shrink. If they can improve markdowns by one percent, shrink by ½ percent and improve inventory turn to three times a year, they would improve their bottom line by \$3,166,667 each year, or an improvement of 3.17%! And that's easily attainable.

On the balance sheet side of the financials, many financial managers try to improve accounts receivable and delay accounts payable to improve their cash position. Let's assume our sample company above has \$12 million in accounts receivable and \$6 million in accounts payable. This would mean it takes 43.2 days to collect receivables, and they are paying vendors in 21.6 days. The industry standards are normally 30 days on both. If they improved A/R to 30 days they would realize \$3.7 million and if they delayed A/P payments to 30 days, they would realize \$2.3 million or a cash flow improvement of \$6 million!

So, with some simple cash management and cost controls we have realized \$9.1 million this year!

ORGANIZATION STRUCTURES AND STRATEGIC ALLIANCES.

It is easy to establish an organization structure if operating in one country – typically sales, operations manufacturing and financial functions report to the CEO. What happens when you expand globally? Should you have centralized senior management? Regional managers? Functional managers? Should we have strategic alliances, or own the processing?

There is no clear cut answer to this and it all depends on the company and its culture. One needs to be careful that there is not an overlap of functions when regionalizing. Yet centralizing all functions is not productive either. For example, distribution of products may be possible from one country where products are shipped by the container load to customers. But that won't work if you are selling to independent retailers – which represent 70% of the US and European market - who don't have the capacity to accept a container load.

With any of these strategies, control is the most critical factor to consider. When companies expand globally, they usually begin with an international division, which rarely works because of the conflict between domestic and foreign operations. In my experience with a number of international companies, what works best is to give each regional group, or country operation, autonomy and monitor their results. Have them create a forecast and budget, and let them run their own operations, monitoring their performance against budget. By dictating policy to the regional operation, you run the risk of conflicting with local customs. Who best knows a region than the regional manager?

One company with whom I consulted is a Swedish corporate giftware company with global operations. They give the regional managers complete autonomy on the product mix, staffing, distribution and financials. Regional managers are part of the global executive team that oversees the entire worldwide operation. Each manager has a vote on policy and can bring to the table any new products, ideas, processes or strategic partners. They perform or suffer the consequence.

Another one is a US division of a Chinese polyresin manufacturer. The CEO of the US operation reports to the Chairman of the parent company, and has no say in any part of the operation. The parent company dictates what they will sell, how much and at what price. While the parent has complete control, the US operation is not growing as they would like, mainly because of their lack of experience with the US market.

of WWI when several governments financed part of their massive military expenditures by printing money.).

At the start of the first millennium, you could obtain a suit of clothes – a robe, sandals and belt for one ounce of gold. Today, 2000 years later, you can still buy a suit of clothes for one ounce of gold! ⁷ A company could transact business using digital gold and the currency would be more stable than present currencies. Since they would use digital gold, the transfer of funds would be immediate, rather than the cumbersome wire transfer methods presently in use. There are approximately 750,000 people using digital gold now, and that number is expected to climb to 1 billion within the next three years.

There is no such thing as a global bank. They may be regionalized and they do cooperate, but there is no global bank. In fact, even if you have an account in a bank, it doesn't necessarily mean you can transact business in that bank in another region.

The end of 2002 we shall see a new theory for a revolutionary global monetary system, one that supersedes the existing banking system or anything close to it. It will use gold and technology to pay suppliers in the retail supply chain. It is my doctoral dissertation! Stay tuned.

SUMMARY

In all cases, a company's core competence is critical for success. If technology or intellectual property is proprietary, then that company should not even consider joint ventures or licensing. And, global expansion will never happen successfully if the company does not have a great management team who can carry out expansion. It is critical that managers do not become victims of the Peter Principle, where they reach their level of incompetence, and not know it. They must be intellectually honest, and admit they don't know something.

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ABOUT THE AUTHOR.

George Matyjewicz is the Chief Global Strategist for GAP Enterprises, Ltd. responsible for defining strategy for global expansion for the firm's clients. He is a multi-faceted Senior Executive with expertise in business development, management, marketing, sales, operations, finance/accounting, and information systems. His major strength is the ability to analyze a situation and develop a simple, cost-effective solution. Mr Matyjewicz will be completing his doctoral dissertation this year in Global Marketing. He is a columnist for Gifts & Dec magazine, moderates E-Tailer's Digest and is called on by the media worldwide for expert opinions. You may reach him at georgem@gapent.com

⁷ "Why Gold" http://globalpaysystems.net/media/white_papers/why_gold.htm and The Creature from Jekyll Island: A Second Look at the Federal Reserve by G. Edward Griffin Paperback - 608 pages 3 edition (May 1998) American Media ISBN:0912986212 <http://philologos.org/guide/books/griffin.edward.1.htm>