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READING

Competing Globally

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1 INTRODUCTION

Business happens in a landscape—a complex backdrop shaped by national borders, government policies, natural resources, and cultural norms. That landscape is becoming increasingly global. Changes in technology and political economy are eroding and reshaping the barriers between countries, allowing firms with a home-market competitive advantage to create and capture value in new national markets. In today's global landscape, managers divide and coordinate activities across multiple locations, each with their own traits and cast of competitors. New business models rise and old ones collapse as cheaper sourcing options develop. Trends spread to consumers in distant and diverse cultures. New suppliers and complementors become accessible. Even organizations that forgo international expansion are at some point likely to face global competitors in their home market, if they have not already.

This Core Reading distills, synthesizes, and builds on insights from five academic domains that inform the topic of global competition: economics, international business, global strategy, business strategy, and corporate strategy. Together, these insights illustrate how competing globally differs from doing business in a single country and suggest frameworks that provide options for global value creation and value capture.

Global value creation is an extension of the concept of competitive advantage—that is, it depends on growing the wedge, relative to competitors, between the price customers are willing to pay for a product and the cost an organization incurs to produce it.

It is difficult to apply the resources and expertise gained through a home-market competitive advantage on a global stage. For reasons we will explore in Section 2.1, adjusting a successful business model to work in a new environment can be complicated, expensive, or even impossible.

To overcome these hurdles, an organization that competes globally needs a ***global strategy***—an approach to value creation that capitalizes on similarities and differences across geographic markets. Global strategies can be as diverse as the firms that craft them, but they generally boil down to three options: deployment, development, and/or deepening. Section 2.2 explains the advantages and constraints of these options and guides managers on selecting among them.

Of course, putting a global strategy into action is a complex and ongoing challenge. Factors that shape the competitive landscape in domestic markets—technological innovation, consumer demand, supplier relationships, government regulation, and competitors' moves, among others—are magnified exponentially when firms compete across multiple countries.

Sections 2.3, 2.4, and 2.5 therefore explore what happens *after* a firm selects a global strategy. Global managers will find guidance in two plain but powerful questions. The first—"What to do where?"—guides managers to evaluate the benefits *and the costs* of separating activities in the value chain across geographic markets. Outsourcing and/or offshoring an activity can enhance an organization's competitive advantage by tapping new markets for cheaper inputs or unique resources. But dispersing a value chain may also weaken the relationship between organizational units, undermining communication and innovation over time. Section 2.3 provides and explains a new framework for selecting activities to separate.

Asking the question "What to do where?" also reminds managers to choose new locations strategically. Location decisions are an opportunity for global organizations to enhance their competitive advantage, first by maximizing global value creation and capture, and second by minimizing the threats posed by competitors. Section 2.4 provides a framework for creating and capturing value when choosing new locations.

The second key question for managers enacting or refining a global strategy is "When to do what?" Carefully timing an expansion to new geographic areas allows an organization to maximize its access to new markets, new resources, and new suppliers, and to neutralize or box out competitors. In other words, good timing lets an organization create and capture more value with each global location decision. Section 2.4 helps managers unlock this potential using a new framework for entry timing.

Ultimately, global managers who think strategically while choosing where and when to expand their organization will have the building blocks of a ***global location strategy***: a cohesive set of location choices, enacted over time, that allows an organization to maximize the value creation and value capture of each location decision.

Section 2.5 closes our exploration of global value creation and capture by pointing out that even the best global strategy needs to be updated regularly. Business happens in real time with real competitors. Only by staying attentive to the shifting sands of innovation and competition can global organizations expect to thrive.

One final note before we begin our exploration of global value creation and capture: The ideas and frameworks in this chapter were designed to translate macro-level theory into micro-level practices—to bring the mountaintop to the managers, as it were. Interested readers will also benefit from exploring the insights of foundational thinkers such as Christopher Bartlett, Sumantra Ghoshal, and Pankaj Ghemawat, among others. A more detailed summary of their ideas can be found in the Supplemental Reading section.

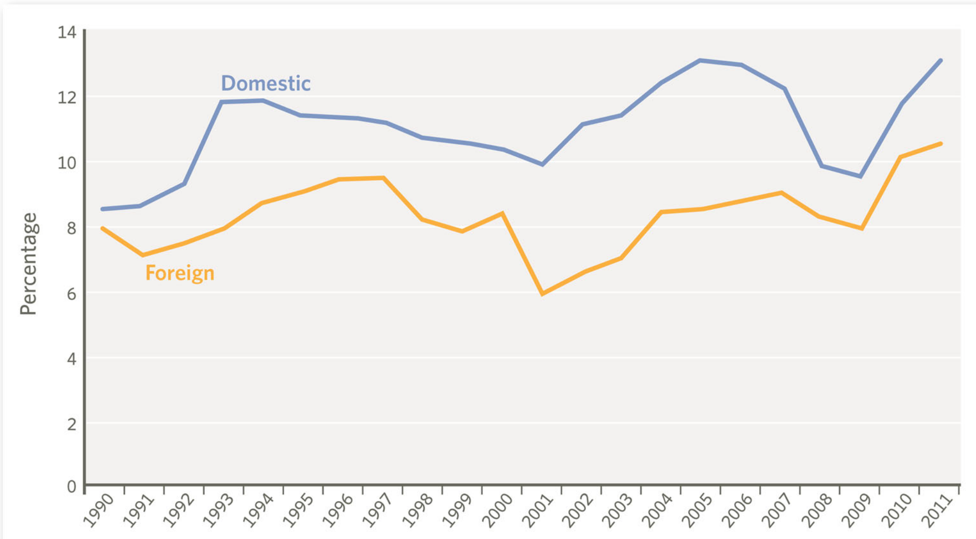
2 ESSENTIAL READING

2.1 Why Do Organizations Struggle in New National Markets?

Why expand abroad? The simplest answer is that international markets offer opportunities for organizations to remain competitive: the chance to tap new resources or lower costs, to learn from competitors, to reach consumers who would otherwise remain out of reach. A successful international expansion allows an organization to preserve or expand the competitive advantage it forged in its home market and to enact that advantage in more places. In other words, organizations expand abroad *to create more value than they would by staying home*.

Realizing the promise of new markets is significantly harder than it may sound, however. Organizations that step outside their home country are more likely to founder. They are so likely to fail, in fact, that most globally diversified organizations trade at a discount in financial markets—a discount that is larger and harder to erase than is the one experienced by industrially diversified firms.[1] **Figure 1** plots operating margins for US firms competing globally.

FIGURE 1
Domestic and Foreign Operating Margins for Publicly Traded US Firms, 1990–2011



Source: Based on data from Compustat.

Organizations with a proven competitive advantage in their home market are not immune from struggles abroad. Consider Walmart. Banking on its long record as America's most successful discount retailer, it responded to slowing domestic growth with a blitz of expansions abroad. By 2010, the company had more stores in Canada, Brazil, China, and other countries than it had in the United States. But results in those countries varied wildly.[2]

There are many reasons why organizations fall short in their efforts to create or capture value in new national markets, but among the most important are what we will call "the liability of being a foreigner" and "the paradox of being consistent."

The ***liability of being a foreigner*** refers to the vulnerability of organizations that venture outside familiar territory. Organizations expanding abroad face costs that they do not face in their home market.[3] Some of these costs originate in the country the organization expands to: for example, regulations that favor domestic competitors, caps on foreign ownership, and/or fees for new patents and trademarks. Other costs are created by spreading operations over diverse geographies, cultures, and economies. For instance, an organization may need to add technology, or hours to the workday, to ensure that employees in different time zones can coordinate tasks. An organization that lacks experience with a new country's norms for negotiating supplier contracts might find itself paying more. Or a new location might lack qualified suppliers entirely, forcing the organization to make expensive investments.

The ***paradox of being consistent***, on the other hand, arises from what an expanding organization knows well: how to create and capture value in its home market. Often, the organizations with the greatest advantage at home are also those most likely to fail when expanding abroad.[4]

Why? Because a home-market competitive advantage is the end product of a business model—a set of mutually reinforcing choices across value-chain activities (that achieve internal consistency), each carefully designed to take full advantage of an organization's home-market environment (thus achieving external consistency). The more attuned that strategy is—the more successful it is in the home market—the harder it often is to replicate in other markets. See the sidebar “Capabilities Begin at Home” for more detail.

Capabilities Begin at Home

An organization’s initial capabilities—and the competitive advantage those capabilities enable—cannot be fully separated from the business model in which they were developed. A business model, in turn, is born and evolves in a geographic environment with particular traits. These traits—government regulations, natural resources, weather conditions, infrastructures, concentrations of competitors and suppliers, and consumer demographics and preferences, among others—may vary by country, by region, or even by city.

An organization that is assessing whether to enter new geographic markets therefore needs a solid understanding of whether its business model is replicable outside its birth environment. More specifically, it needs to know which environmental traits its business model cannot function without, which parts of the model can be adjusted to fit new environments, and the implication of any adjustments on the organization’s source(s) of competitive advantage.

For example, Bharti Airtel became the largest mobile phone provider in India using a business model that outsourced the management of its wireless network. When it tried to replicate a similar model with its expansion into Africa, it failed to find a partner to run the network.

Similarly, the National Football League (NFL) failed in its early attempts to expand from the United States into Europe. Attracting a mass audience in Europe proved impossible, at least initially, in part because Europe lacked a crucial link in the value chain: a network of high schools and universities to identify and develop local talent. The NFL was forced to integrate upstream in the value chain to develop local players—a task it had never performed and for which it was poorly prepared.

Sources: Krishna G. Palepu and Tanya Bijlani, “Bharti Airtel in Africa,” HBS No. 112-096 (Boston: Harvard Business School Publishing, 2012); Juan Alcacer and Mary Furey, “The Globalization of the NFL,” HBS No. 711-455 (Boston: Harvard Business School Publishing, 2011).

When combined, the liability of being a foreigner and the paradox of being consistent can prevent the most successful domestic organization from fully duplicating its success abroad. Even where an organization overcomes the consistency paradox—identifying and entering foreign markets where its business model can be replicated—it may not perform as well because it is an outsider.

In addition to those two obstacles, organizations expanding abroad might be unable to capture (or appropriate) the value their expansion creates. Although the quickening pace of globalization since the 1980s has created broad similarities across markets, the institutions that govern ***value capture***—patents, trademarks, and copyright laws, for example—remain predominantly local.

In practice, this means that organizations with a successful business in one country may find that their idea, their product, or even their business model has been claimed by a local entrepreneur in another country. For example, the American fast-food giant Burger King operates in Australia as Hunger Jack: When the firm entered Australia in the early 1970s, the

Burger King trademark was owned by a local firm whose owner refused to sell the rights.[5] More recently, Apple paid $60 million to a Chinese company, Proview Technology, to settle a legal dispute over use of the iPad trademark in China.[6]

Even when the laws governing patent and trademark rights are similar across countries, the cost of applying for those rights in every country, before anyone else, can be economically crippling. One study found that, in 2008, the fees to obtain a single patent in 15 countries were approximately $120,000—and that figure didn't include the fees for lawyers in each country.[7]

Sometimes a source of value cannot be protected by law. Consider, for example, the dozens of major beer festivals around the world that copy elements of the original Oktoberfest in Munich, Germany. Although most of these festivals attract thousands of visitors, none of that value flows back to the concept's originators in Munich.[8]

2.2 Strategies to Create and Capture Value Abroad

To create and capture value from global expansion, an organization needs a solid global strategy—a strategy that leverages or builds on the organization's home-market competitive advantage in new countries or geographic regions. A successful global strategy *capitalizes on similarities and/or differences across geographic markets*. The potential permutations are as varied as the organizations and the countries involved. However, when we reduce this vast array of global strategies to their most basic elements, we see that most organizations create value abroad in one or more of three ways.

- They *deploy* a home-market competitive advantage in new geographic markets, aggregating demand.
- They *develop* a new and complementary source of competitive advantage by arbitraging technical and market knowledge.
- They *deepen* an existing advantage by aggregating production and/or arbitraging resources to reduce cost, or by adapting products to maximize demand in new markets.

Taken together, these three options—deployment, development, and deepening—constitute what we will call the DDD framework.

Deployment Strategies

When possible, the most obvious approach for creating value globally is to replicate a successful business model across countries.[9] Replication requires deploying the same source of competitive advantage developed in the home market across a myriad of national markets, generally without significant localization.

A ***deployment strategy*** aggregates demand across multiple country markets. The size of the wedge between production cost and customers' willingness to pay stays the same, but the volume of sales increases. In that sense, a deployment strategy for global expansion is similar to a domestic business-unit growth strategy.

Examples of deployment strategies can be found in nearly every industry, but they are perhaps most common in high-end and luxury consumer goods. Apple, for instance, sells the same lineup of premium computers, phones, and handheld devices, at nearly the same prices, from a global roster of more than 400 Apple Stores, each sporting the brand's trademarked minimalist interior.[10] Similarly, the French multinational luxury-goods company LVMH ensures that Moet & Chandon's signature champagne, Dom Perignon, tastes and looks the same from Paris to Phuket.[11]

To achieve similar willingness to pay across markets, an organization needs to target a homogeneous segment of customers across countries. This can be a segment that is well known already or one that the organization identifies and targets as a market for the first time.[12] The key is focusing on *similarities*, rather than differences, across country markets.

Even an organization with a global strategy that targets a core, homogeneous customer segment in multiple countries might adapt its products and operations to a small degree in each market to maximize local demand. What distinguishes a deployment strategy is that, underneath those adaptations, the core products and services the organization offers, and the ways it delivers them, are fundamentally the same. IKEA is a classic case.[13] The firm offers furniture assembly services to American customers, who are not enthusiastic about the company's do-it-yourself approach—but the same Kivik sofas or Billy bookcases are offered in 46 countries on four continents.

To keep costs similar across markets, organizations following deployment strategies generally choose between concentrating production in one or a few locations and exporting to different national markets, or replicating production across markets. Concentration lets organizations tap the comparative advantages of a given country (low wages, natural resources) and achieve economies of scale. But it may also inflate transportation costs or increase the risk of interruptions in supply (in the event of political upheaval or a hurricane, for instance).

Replicating production across countries may instead be necessary to meet the demands of local legislation ("buy local" laws or tariffs on imported goods, for example), to avoid eroding margins with higher transportation costs, or to ensure rapid delivery to customers. A replication approach to sourcing requires that an organization's production process does not depend on resources, infrastructure, or other characteristics unique to a particular location.

At an organizational level, deployment strategies require a corporate culture and an organizational form and processes that guarantee standardization of products and services. By emphasizing replication and standardization over adaptation and customization, organizations that follow a deployment strategy become more homogeneous and are well positioned to franchise their operations abroad.

Development Strategies

While deployment strategies are built on *similarities* across locations, development strategies depend on *differences*. Specific locations enjoy unique endowments. Some are geographic, such as natural ports or deposits of high-quality diamonds. Others are institutional, like the presence of a research center that generates unique knowledge to boost innovation. An organization that diversifies geographically to obtain new capabilities—for example, unique knowledge that helps it improve its products or services—is following a ***development strategy***.

An organization using a development strategy creates and captures value by identifying where a potential new capability resides, locating to acquire that capability, and integrating it for use across the organization's global markets. In some cases, the result may be new or enhanced products that increase customer willingness to pay. In others, it will be improved production and procurement procedures that reduce cost.

Japan's enthusiastic and sophisticated consumers enticed a number of leading global organizations to invest in development strategies in the late 1990s and 2000s. In the wireless communications industry, for example, rules against speaking on phones in trains and other crowded places created a powerful demand for texting and other mobile data services that barely existed in other world markets at the time. Meanwhile, the world's largest wireless service provider, Vodafone, was on the lookout for new products and services that used 3G, which it believed would reinvigorate its business globally. In 2001, Vodafone decided to buy a trailing player in the Japanese market, Japanese Telecom, and learn about the country's distinctive technologies firsthand.[14]

Similarly, consumer-goods giant P&G took note that Japanese women spent more time and more money on skin care than women anywhere else in the world did. By analyzing its product lineup at Max Factor Japan, the company identified the global potential of SK-II, a premium skin cream that had attracted a devoted following in Japan, Taiwan, and Hong Kong, but remained little known outside the region.[15]

Another way to think of a development strategy is as a process of *arbitraging knowledge across countries*. Arbitrage lets firms profit by buying low in one market and selling high in another. Classic forms of arbitrage depend on cheap labor or distinctive raw materials. Knowledge is generally complex and embedded in organizations, however, making it difficult to buy and sell directly. An inability to transact is also a barrier to imitation by rivals. These factors make knowledge arbitrage a better source of lasting competitive advantage.

Of course, it is important that the diversity among locations is not so great that an organization struggles to absorb local knowledge (because it is too different from what the organization already knows) or to apply that knowledge in other national markets (because it is too local). Thus, for a development strategy to be successful, a new location should be different enough to provide the organization with a unique capability but not so different that the capability cannot be applied somewhere else.

Successful development strategies require organizations to align their reporting structures and management incentives carefully to ensure that local innovations are identified and developed and that their potential for global success is communicated clearly to headquarters. Development strategies that overlook those prerequisites are unlikely to succeed. Consider again the experiences of Vodafone and P&G in Japan. As part of a global firm, Vodafone Japan struggled to stay competitive in its home market because investment directives from headquarters prioritized voice services over mobile data. In addition, hot products in Japan were useless in countries that lacked Japan's advanced 3G wireless infrastructure—basically everywhere *but* Japan.[16]

P&G's experience in Japan was very different. Its successful global rollout of SK-II, for example, was part of a larger strategy that in the space of a few years had given the world Swiffer, an electrostatic mop; Dryel, a dry-cleaning system for the home; and Lipfinity, a line of long-lasting lipsticks. Behind these successes was a radical restructuring in the early 2000s that moved profit responsibility from P&G's regional headquarters to its global business units and gave P&G managers hefty bonuses for identifying local products with global appeal.

The takeaway is that managers crafting a development strategy need to be clear about the capability they want to acquire. Some will require a physical presence, and others will not. Given that knowledge can be tacit and embedded in organizations, for instance, development strategies built on capturing knowledge will probably require an organization to locate operations where that knowledge is found. That said, even tacit capabilities can be acquired from a distance in some cases—through licensing or partnering with local organizations, for example. In those cases, organizations would be wise to avoid the cost and coordination burdens of an expansion.

Deepening Strategies

The third and final global strategy shares elements with each of the first two, but it uses those elements differently. Like a deployment strategy, a ***deepening strategy*** can leverage similarities across country markets. Like a development strategy, it can leverage differences across markets. In either case, the goal of a deepening strategy is to grow (or "deepen") an organization's existing competitive advantage—that is, to reduce costs or increase customer willingness to pay—without changing the organization's primary business model.[17]

Among deepening strategies that turn on reducing costs, the most common is arbitraging labor costs by offshoring activities to low-cost locations. These strategies rarely offer a sustainable competitive advantage, however, because other organizations are likely to follow, driving up the cost of labor over time.

A more enduring way to reduce costs is to aggregate production, R&D, or advertising across markets to create economies of scope and scale. Reducing cost through economies of scope and scale is an organization-specific process, so it is difficult for competitors to imitate.

The second and more desirable category of deepening strategy is based on increasing customer willingness to pay. This can be accomplished with three different mechanisms: adapting to local demand, leveraging a multinational presence, and flexing market power.

When tastes differ across countries but the need for a product is constant, an organization may increase willingness to pay by *adapting* the product to local tastes. This is often the case in food industries.[18] For instance in 2013, Chinese patrons of KFC, the first and largest western-style fast-food brand in China, were just as likely to order a rice dish as they were to order the chain's signature fried chicken.[19] Chinese Pizza Huts have also thrived by upscaling the chain's design and topping their pizzas with shrimp, squid, and other local favorites.

Adapting to local tastes can be expensive—so much so that some organizations will benefit from an intermediate approach. For example, an organization might offer regional products or build products on a platform that can be adapted to local tastes while minimizing costs.[20] Both strategies are particularly common in the automotive industry. Consider Volkswagen, which used its A0 platform for models customized in various European markets: the Audi 50, the Volkswagen Polo, the SEAT Ibiza, and the Skoda Fabia. Similarly, when Ford wanted to extract more value from its popular city car, the Ka, it developed versions with radically different styling and engines for drivers in Europe and Brazil.

In cases where products and services command higher prices precisely because they are available across national markets, an organization can increase willingness to pay using *multinationality*. Logoplaste, a small producer of plastic containers, fueled its international growth by becoming the preferred supplier to P&G, Unilever, and other large multinationals that preferred to deal with one supplier across markets.[21] Citibank created an early and enduring stronghold in Latin America when it traveled with corporate clients moving to the region. And McKinsey and other managerial consulting firms are able to charge higher fees when they serve multinational clients in multiple geographic markets.

Finally, an organization that can identify and own the part of the value chain where market power resides can increase willingness to pay using *market power*. In some industries, this will mean owning one key element of the value chain in a single location, as De Beers achieved in the diamond industry.[22] In other industries, such as cement and telecommunications, it will mean owning assets in each national market, thereby sustaining a high willingness to pay locally.

Note that strategies built on market power will create an enduring competitive advantage only when they obey the rules and regulations of the countries where an organization operates. Deepening strategies that exercise market power illegally—through market collusion, for instance—threaten an organization's long-term survival and should never be part of the toolkit of organizations moving abroad.

Selecting a Global Strategy

Each global strategy opens particular avenues for value creation. It also imposes particular constraints—limits on the *products* the organization sells, the *activities* it disperses geographically, the *locations* and *ownership structures* it selects for foreign operations, and the organizational *processes* it follows.[23] Managers selecting among the three global strategies can identify their most viable options by using the chart in **Table 1**. This chart breaks down the complex process of strategy selection into seven critical dimensions:

- The method of value creation (or *goal*) the organization wants to pursue.
- The *product* an organization offers and whether it needs to be similar or different across markets.
- The *value chain* used to produce that product (or products) and the extent to which it can be concentrated in a single location or spread across geographic markets.
- The similarities or differences across *locations* that will be necessary for value creation and capture.
- The *capabilities* the organization possesses or hopes to develop.
- The *organizational* processes necessary to enact an expansion successfully.
- The forms of *ownership* an organization might use in a new market.

The seven dimensions in Table 1 reflect the fundamental trade-off between localizing products to increase revenues and centralizing coordination and production to reduce costs—a trade-off whose presence and power are among the most important insights of international business scholars.[24] Strategists make a similar point: Steps that increase customers' willingness to pay usually increase costs, while steps that push down costs often undermine willingness to pay.[25]

Managers who examine the source (or sources) of their organization's competitive advantage carefully will be able to identify overlaps with key traits of a given global strategy. They will also be able to identify areas of conflict that might make a particular strategy a poor fit.

Of course, while each strategy is powerful in its own right, large organizations confronting global competition regularly use more than one global strategy at a time. For example, Vodafone struggled to build value with a development strategy in Japan, but it found success using a deployment strategy in Europe and a deepening strategy through adaptation in Qatar. IKEA generally follows a deployment strategy, but it has also learned from one market and applied that knowledge in other locations—a development strategy.

Selecting the best match between an organization and a global strategy (or strategies) is an ongoing process, one that changes with the opening and closing of geographic markets and with the waxing and waning of organizational resources, customer demand, technological innovation, and—above all—competition.

TABLE 1 Basic Global Strategies: Deployment, Development, and Deepening

Issue	Deployment	Development	Deepening
Goal(s)	Increase scale and maintain willingness to pay and costs.	Obtain new capabilities that increase willingness to pay or decrease cost.	Use existing capabilities to increase willingness to pay or decrease cost.
Product	Identify or create a common market for the same product.	Use similar products with potential for a common market segment in the future.	Use the same product.
Value Chain	Use standard sourcing from a few locations or from each national market (when production does not depend on specific location traits).	Depends on the activity associated with learning. A country-specific source of competitive advantage requires the firm to operate in that location.	Concentrate activities that control the value chain.
Location	Create value based on similarities across countries.	Create value based on differences across countries. Differences should be large enough to create value but small enough that new capabilities can be applied elsewhere.	In a business-to-business strategy, follow the client or optimize the location per firm traits. In a business-to-consumer strategy, allocate where location is best.
Capabilities	Replicate.	Identify, absorb, and diffuse.	Coordinate.
Organization	Standardize processes, products, and culture.	Be able to (1) identify a country-specific source of competitive advantage, (2) internalize it, and (3) diffuse it across countries.	Strong communication; create flexibility to move assets as location characteristics change.
Ownership	Franchising is possible.	Pursue one or more options, from full ownership to licensing.	Own only where necessary; outsource nonstrategic functions. Own in the bottleneck to create value.

Source: Adapted from Harvard Business School, "Why Do Firms Go Abroad? Strategies to Create Value Globally," HBS No. 713-057, by Juan Alcacer. Copyright © 2014 by the President and Fellows of Harvard College; all rights reserved.

2.3 Using Scope Decisions to Create and Capture Value Abroad

Once an organization has selected a global strategy for its expansion, managers have the complex task of enacting that strategy. In other words, they must answer the questions "What to do where?" and "When to do what?" This section begins our investigation of the first question.

Globalization gives organizations opportunities to create value by changing their geographic and vertical scope. In addition to ***outsourcing*** (performing activities outside the boundaries of the organization), organizations in a global world can more readily employ ***offshoring*** (performing activities within the organization but in locations abroad) and ***offshore outsourcing*** (performing activities outside the organization and abroad). Each approach varies in its potential to create and—more important—to capture value.

With outsourcing, organizations create and capture value by combining the competitive advantages of different organizations. This requires skillful coordination of activities and processes *across organizations*. It also exposes organizations to the risk of transferring valuable capabilities to other organizations that may at some point become competitors.

Offshoring creates value by combining organizational capabilities with the comparative advantages of different countries. This requires an ability to coordinate activities *within the organization and across locations*. It also carries a risk that organizational capabilities will be appropriated by competitors in the new country (through regulatory reporting requirements and employee migration, for example).

Offshore outsourcing offers the benefits and costs of both offshoring and outsourcing. Thus, the potential for value creation is magnified with offshore outsourcing, but so are the risks. On the one hand, offshore outsourcing frees up domestic producers to concentrate on innovation and other high-value activities (while suppliers deal with lower-value activities). On the other hand, it may trigger a migration of capabilities to foreign suppliers, allowing them to become rivals, and a loss of innovative capacity among domestic producers. See the sidebar "Hedging Risk with Mode of Entry" for more detail.

Hedging Risk with Mode of Entry

Organizations put off by the extremes of offshoring and offshore outsourcing can expand abroad using hybrid ownership forms such as joint ventures, alliances, and franchising. Among other benefits, these hybrid forms allow organizations to limit the liability of being foreign in a new country or to access new markets by obtaining a license or complying with a government cap on foreign ownership.[26]

When vetting partners for a new global alliance or joint venture, organizations need to look beyond the benefits of cooperation to consider the costs of competition.

Alliances are typically motivated in part by a desire to access a partner organization's capabilities. Cooperating allows organizations to develop new capabilities jointly, but it may also facilitate opportunistic behavior (taking propriety knowledge, for example, or demanding contract concessions after an investment is made).

Organizations considering an alliance or joint venture can maximize cooperation and minimize competition by evaluating a proposed partnership along four dimensions: partner choice, scope, structure, and measurements of success.

Partner choice. An ideal partner has complementary capabilities and a cooperative culture. Some overlap of capabilities is necessary for a fruitful alliance, but too much may encourage opportunistic behavior (and multiply losses for the "losing" organization). A cooperative culture allows an alliance to achieve its potential.

Scope. The goals and length of a partnership should be defined in advance, as should the type and amount of each partner's contribution and the mechanisms for collaboration. Being clear from the outset allows partnering organizations to achieve their common goals, limit unintended knowledge transfers, and rationalize their contributions.

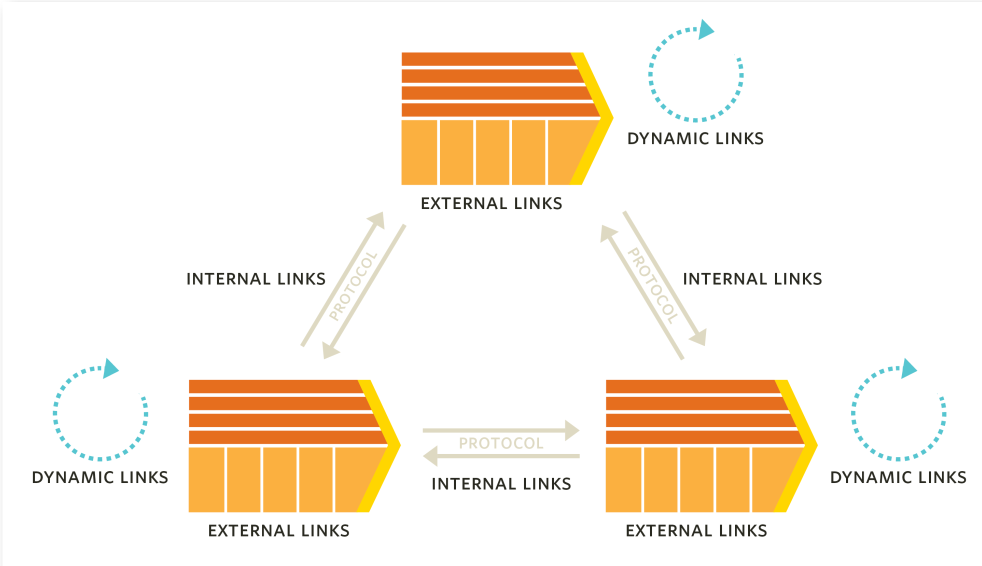
Structure. In addition to setting ownership stakes, hybrid forms contract to regulate the exchange of information and human capital, assign property rights for knowledge that the alliance creates, set requirements for future investment, and allocate decision-making rights. Partnering organizations can protect their relative competitive positions by limiting partners' access to capabilities outside the scope of the alliance.

Measurements of success. Common measures of a partnership's success, such as financial indicators, can mask the benefits and costs accruing to each partner separately. For an alliance to persist, each partner needs to pass the better-off test: Is the organization better off participating in the partnership than not participating in it?

While the careful allocation of activities across locations is a valuable mechanism for creating and capturing value globally, organizations considering offshoring and offshore outsourcing need to be mindful that the geographical dispersion of value-chain activities can break valuable links among them. Broken links increase costs to the organization by hampering internal communication and coordination, weakening access to location-specific resources, or even short-circuiting organizational learning and innovation.

The framework in **Figure 2** shows the value chain of a hypothetical organization, in this case divided into three tasks or activities (in yellow and orange). Each task or activity is connected to other tasks and activities by three types of links: internal links, external links, and dynamic links. An organization that splits its value chain across locations must take care not to break these links. Broken links undermine a firm's performance and ultimately its competitive advantage.[27]

FIGURE 2
Framework to Analyze the Impacts of Allocating Activities Across Locations



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Internal links govern the flow of information within the organization: everything from formal communications between activities (an R&D team asking manufacturing to vet a potential innovation, for example) to informal exchanges between employees in the elevator.[28] Some activities are highly interdependent; others are not. When separating activities geographically breaks important lines of communication, it can undermine the performance of each activity and of the organization overall. As organizations grow and activities become more specialized, organizations can develop protocols of interaction between activities—standardized weekly updates from R&D to manufacturing, for instance—that facilitate communication in spite of geographical dispersion.

External links govern the flow of information between the organization and its environment. Location decisions for a task are fundamentally about tapping one external environment rather than another. These decisions alter the way an organization relates to the external world, the resources it can accumulate, the way it compares to its rivals, and its perception and forecasting of future trends. Environments that are highly specific may limit whether an activity can be performed somewhere else. For example, a pharmaceuticals R&D lab must be in Cambridge, Massachusetts, if it requires continual, direct interaction with academics at the Massachusetts Institute of Technology (MIT). Locating in an environment that is very different from an organization's existing location (or locations) may also force it to perform activities it hasn't performed before.

Dynamic links regulate the accumulation of an organization's knowledge over time. Activities in a value chain can be conceptualized as a stock of organizational capabilities to perform specific tasks that result from an ongoing and evolving learning process. When an activity is split across locations or is no longer performed within the organization, the feedback loop that develops the organization's stock of capabilities may weaken and ultimately lead the organization to underperform. Severing this loop may also have performance consequences that spill over to other activities. For example, a firm that outsources production may see its production skills wither, which will in turn weaken its R&D and undermine innovation.

The value of links between organization activities is most readily apparent when organizations embrace offshore outsourcing. While public policy specialists have been vocal in their opposition to sending jobs overseas, organizations looking to shave costs have generally treated opportunities for offshore outsourcing as a boon, particularly in countries with lower wages.

As these relationships mature, it is becoming apparent that the short-term gains of low wages are sometimes undercut by long-term losses in revenue, a risk often referred to as ***hollowing out***. Why? Because outsourcing to organizations overseas is more likely to break links that nurture an organization's capabilities for innovation and customer service. For instance, after the Spanish banking giant Banco Santander moved its English-language call centers from the United Kingdom to India in 2003, customers dissatisfied with the level of service began dropping their accounts. In 2011, Santander reversed course and returned the centers to the United Kingdom.[29]

The cost of breaking links can be as high as creating a new competitor. That's what happened to the wireless firm Motorola after it hired Taiwanese handset manufacturer BenQ to design and build Motorola phones. Motorola cancelled the contract in 2005, after BenQ began marketing its own brand of handset in China—but by that time the damage was done.[30]

2.4 Using Location Choices to Create and Capture Value

When an organization determines it can expand abroad without undermining performance, it next needs to choose where, precisely, it will go. Students of firm strategy will already be familiar with the importance of crafting a fit between a firm and its environment, and they will understand that the entry and exit of competitors may alter the value of a particular product or geographic market. In a global context, however, these common dynamics—that is, answers to the question "What to do where?"—are complicated exponentially.

As organizations expand across global markets, they take on an increasing number of environments and competitors, each with its own advantages and competitive dynamics. Complicating matters further, global organizations often face the same competitor in multiple locations, each with its own strategic risks.

Organizations can maximize value creation and value capture during a global expansion by crafting a careful global location strategy—a strategy that accounts for the unique traits of the organization and its potential locations over time, leverages government incentive packages (where available), and anticipates the moves and countermoves of competitors.

Chosen well, new locations give organizations an opportunity to tap unique location characteristics, build capabilities, and enhance their competitive advantages. But **c**hosen poorly, new locations can dilute an organization's scarce resources, carry hidden costs that undercut profits globally, and allow competitors to thrive.

The vast academic research in strategy, economics, and international business on location choices can be distilled into the framework illustrated in **Figure 3**. The framework consists of four dimensions—location characteristics, government incentives, firm fit, and competitive effect—that together shape how much value an organization can create and capture in new locations.[31]

FIGURE 3 The Dimensions of Location Strategy

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Location Characteristics

Research on location decisions has produced an extensive list of location characteristics that can be grouped into three categories: natural endowments, institutional environments, and the presence or absence of clusters of same-industry organizations.[32] Natural endowments were originally thought of as the availability of basic production factors—from metals and oil to capital and labor—but the concept can be extended to include characteristics such as market size, physical infrastructure, and quality of the labor force. The institutional environment encompasses location characteristics such as political risk, enforcement of property rights, labor laws, and attitudes toward corruption, to name a few. Clusters provide organizations with access to specialized knowledge, suppliers, and workers, as well as to specific customers. Regardless of the type of location characteristic, differences among location characteristics give organizations multiple options for where to sell their products or locate specific activities in their value chains.

The first step in choosing the right location is recognizing what location characteristics matter for a specific organization. The list of must-haves will vary by industry, by organization, and even by activity within an organization. For example, semiconductors rely on intellectual property (IP) protection to capture value, so a sound IP regime is critical for semiconductor firms (think of Intel in China). Within an industry, the importance of IP varies by firm: fabless firms, for example, require less IP protection because they design and license technology, but outsource the production of what they sell.

The second step is to cover multiple geographic levels of analysis. It is commonly presumed that location decisions are all about choosing *countries*. In an organization's list of must-haves, some characteristics will be primarily country-specific, such as a strong IP regime and legal system, while others will be primarily site-specific, such as access to airports, ports, and a skilled local workforce. Site characteristics will be especially salient in countries like China or India, where vast intracountry variations exist.

The importance of country characteristics versus site characteristics depends on the activity an organization plans to perform at that location. For manufacturing, for instance, certain country characteristics are necessary but not sufficient because key factors like industrial parks, shipment channels, and labor are fundamentally local. For sales, on the other hand, local site conditions are less important than country characteristics because marketing decisions depend on country-level demand, channels, and advertising.

Government Incentives

By offering incentives to lure organizations or taking steps to block their entry, governments significantly influence the underlying value a location offers to a foreign entrant. In this sense, a package of government incentives creates a lens through which locating organizations view a location; the lens can either magnify or minimize the location's intrinsic value. This package may include advantageous regulations, tax breaks, lower utility rates, subsidies for training and other investments, improvements to local infrastructure, and accelerated depreciation, among other options. The package offered to a particular organization depends on the size of the organization's investment, the government's appetite for negotiation, and how highly the government values the organization's presence. In the case of Intel, for example, the Vietnamese government wanted to bring in a well-known high-tech company that would attract other foreign investors. In exchange, Intel negotiated generous conditions for taxes and utility prices that reduced the company's operating costs.[33]

In addition to the benefits of a given package, organizations negotiating for incentives should be mindful of the potential for hidden costs. These will vary by type of incentive and typically emerge after the deal has been struck, the investment has been sunk, and the organization starts operations. See the sidebar "Making a Deal" for more detail.

Of course, some governments also take action to *prevent* organizations from entering their countries. They may do so when a foreign entrant is perceived as a threat to a local organization that uses its strong ties with government authorities to limit foreign activity (via legislation, extra requirements for foreign organizations to operate in the country, denial of permits to operate, etc.). For example, after local carriers complained about competition from Dubai's airline, Emirates, Canada refused to expand the number of airports Emirates could use and limited the airline's volume on its existing Canadian routes. Elsewhere, national interests have been invoked to block foreign entrants from specific countries. For instance, the US government prevented Chinese information and communications technology firm Huawei from acquiring or selling to American firms three times because of Huawei's involvement with the Chinese government.[34]

Making a Deal

The number and size of incentive packages has increased dramatically with the spread of global competition. A 2012 analysis by the *New York Times* estimated that local governments in the United States alone grant economic incentives worth $80.4 billion each year to attract new foreign and local firms.[35]

For governments, the rationale for offering incentives is that attracting new entrants boosts the local economy by creating jobs, generating work for local suppliers, and attracting still more firms. Over time, the thinking goes, these activities will increase the tax base enough to offset the cost of an incentive package, and there is some evidence that attracting firms creates a net economic benefit in a location.[36]

Nevertheless, communities may perceive an incentives package as a zero-sum game: With fewer sources of public revenue, the benefits a firm receives may come at the expense of government services to its host community. Subsidies for infrastructure that benefit more than just the investing firm—widening a transportation artery, for example—may be less likely to trigger a negative public reaction.

Note that when the cost of a benefits package is perceived by the local community as being too generous, the risk of backlash can be substantially higher for foreign firms because the community may project nationalistic issues into the debate.

Firm Fit

International business studies show that organizations tend to expand first into countries that are similar to their home country, as when Spanish organizations move into Spanish-speaking countries of Latin America. This is likely in part because an affinity between the home and host country decreases the *liability of being a foreigner* and minimizes the downside of *the paradox of being consistent.*

Yet organizations with a home and host country in common—Chinese firms expanding into Tanzania, for example—may experience vastly different degrees of strategic fit. Why? Because every organization has particular traits that shape its relationship with the new setting, including the following:

- unique capabilities
- locations the organization selected previously
- location prerequisites embedded in the organization's business model

Organization characteristics and capabilities can enhance or decrease the value of a specific location. Before an organization moves abroad to any location, it must invest in resources—for example, integrated technology (IT) and human capital—that decrease coordination costs across markets. These investments are often organization-specific and can become sources of competitive advantage. For instance, clothing company Zara invested heavily in IT so it could track real-time demand in the cities where it located stores. Organizations also differ in their ability to coordinate and control across locations and to endure competitive pressures. Consider Southwest Airlines in the United States and Emirates Airline in international routes; the two airlines flourished despite their late entry into highly contested markets.

A new location must also be evaluated in terms of the locations where the organization already operates. An organization engaged in a regional expansion may temporarily forgo attractive locations elsewhere. For example, while Starbucks may believe China is a promising market, it may not consider expanding to Shanghai until it completes and solidifies its expansion in Europe.

All business models have an inherent geographic dimension that guides their location choices. For example, an organization whose competitive advantage is associated with economies of scale in production would have fewer, larger production facilities (e.g., Boeing and Airbus in aircraft manufacturing). If transportation costs are important, these few production sites would be dispersed and follow the loci of demand. The value proposition embedded in a business model can also influence the location decision. Consider Logoplaste's model of opening plants *inside* its clients' sites, which effectively defers location decisions to the clients.

Competitive Effect

The final element that shapes location choices is competition at two levels: competition for inputs and competition among products.

Alfred Marshall famously argued that same-industry firms located in the same geographic area—a geographic cluster of firms—would have easier access to key inputs, including specialized suppliers, trained workers, and knowledge from competitors. These benefits increase productivity, encouraging firms to cluster together with their peers.

But locating in a cluster can have costs as well as benefits. A firm's trained workers might move to a competing firm. Its suppliers might become a source for competitors. Its innovations and know-how might leak to its neighbors. Sometimes, these costs outweigh the benefits of joining the cluster; in that case, locating apart may be a better option.

Ultimately the trade-off between the benefits and costs of joining a cluster—the net effect of competition on a location's value—varies by organization. For example, firms that lead in their industry may have less need for the benefits that clustering creates because workers and suppliers are more likely to follow them. Leader firms that join clusters also give less-advanced competitors an opportunity to piggyback on their advantages (technical innovation, trained labor, specialized suppliers, etc.). Over time, this amounts to a cost that can erode the leader's competitive advantage.

Competitive forces in a location may also induce organizations to locate apart because organizations with different capabilities need to be mindful of losing critical knowledge to rivals. This danger is especially pronounced in markets that are not perfectly competitive. In oligopolistic markets, in particular, the choice among product markets shapes organizations' competitive advantage over time. For example, a firm that delays entry into a particular product market may leave an opening for a competitor to grab or strengthen a competitive advantage in that market.

Competition does not always drive organizations to locate apart; in some cases, competing in multiple geographic markets can soften or enhance an organization's competitive position by creating the possibility for cross-market retaliation. For example, a pattern of clustering in the cement industry since the 1980s cannot be easily attributed to natural endowments, institutional environments, or benefits from clustering. Instead, they are most likely associated with the desire for multimarket contact to soften competition.[37]

Overall, competitive effects dictate that managers need to look beyond attractive traits and instead treat locations as *the context where competition happens* when they craft a location strategy.

2.5 Timing Expansion to Maximize Value Capture

Carefully timing entry to new markets is another way organizations can influence their competitive advantage and maximize the value of geographic expansion. In this section, we pose the second key question managers face in global expansion—"When to do what?"—and answer it by revisiting the four elements of the location framework. **Figure 4** recasts the location framework in four "clocks"—the location clock, the incentives clock, the firm clock, and the competitive clock—each of which influences the optimal time of entry.[38]

FIGURE 4 Determinants of Time of Entry

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Location Clock

Locations need some level of maturation before they are viable options for expanding organizations. For example, an enormous array of markets opened in Eastern Europe and the former Soviet Union when communism collapsed. Nevertheless, most organizations decided to watch from the sidelines until the political and economic situation became clearer. A similar pattern played out when China and Vietnam opened to foreign direct investment in the late 1980s and will perhaps happen again now that Myanmar is becoming friendlier to foreign firms.

Changing country conditions affect entry timing even in mature markets. Foreign organizations delayed entering the European Union after the financial crisis in 2008. Similarly, the Arab Spring protests in 2011 dampened enthusiasm for expansion into the Middle East and North Africa.[39] Even in the United States, foreign investment typically slows in advance of tightly contested political events.[40]

The right time to enter a location may also be affected by what occurs in other locations. For example, the reason a firm reduces its rate of investment in one country might not be related to changes in that country, but instead to the emergence of options elsewhere that were previously unavailable.

The presence of other foreign organizations can also influence when it's optimal to enter a given market. Because first entrants in a country face the highest levels of market uncertainty and have no opportunity to learn from the experiences of previous entrants, they are more likely to make critical mistakes. For instance, when the Russian government opened its oil industry to foreign firms, eager first movers made commitments on the basis of government data that later proved faulty. The first movers also faced a period of fluctuating regulation as successive Russian governments built and changed the oil industry's institutional environment. Firms that arrived later responded by conducting their own yield assessments and demanding guarantees backed by the World Bank and other intergovernmental organizations (IGOs) to soften the impact of future regulatory changes.[41] As more foreign organizations settle in a country, their joint efforts to curb changes in regulation become more powerful.

Entering late is not always better, however: It may allow early entrants to develop valuable country-specific characteristics, including securing key suppliers and customers; building brand recognition; and, in some cases, influencing the standards and rules that govern an industry. So when is the best time to enter? There is no one-size-fits-all answer, but research and anecdotal evidence suggest that entrants perform best during the period when the density of existing foreign organizations is neither too low nor too high.

Incentives Clock

As governments change, so might their willingness to offer incentives to attract investors. A new government may also try to revise or even throw out agreements made with organizations in the past.

The window of opportunity to get the best deals may be limited when an antibusiness government follows a pro-business government. Governments may also become less generous after many organizations invest in a location or after earlier investment agreements create fewer benefits than promised. A backlash from the public can be so forceful that an organization not only loses its promised benefits but also ceases operations and exits the market. This was the case when Rio Tinto invested in a Papua New Guinea copper mine with a contract that paid the national government handsomely but gave almost nothing to residents near the mine site.[42]

Even with well-functioning governments, organizations' bargaining power decreases with time, so managers are advised to obtain as many incentives as possible up front. The longer the horizon of the incentive, the more likely it is that problems will arise and that benefits will not materialize.

Firm Clock

Even when markets are ripe for entry, organizations must possess the financial, managerial, and organizational resources to expand. The required quantity of resources depends on an organization's experience in the global arena. An organization expanding abroad for the first time is likely to require more slack resources because it may underestimate the efforts needed to operate abroad successfully. Organizations with more experience can leverage the knowledge and routines they developed and tested during previous global expansions.

An organization's basic business model influences its pace of global expansion. Organizations that follow deployment strategies are often positioned to expand quickly because their business model is standardized and can be readily replicated across locations. (McDonald's is famous for blanketing a region with multiple openings in a few months.) Where a business model requires transferring a strong corporate culture, however, deployment will be slower. For instance, IKEA's international expansion was slow for the retailing industry in part because the company's founder, Ingvar Kamprad, believed it was important to methodically transplant the so-called IKEA way in new stores.[43]

Organizations following a development strategy are also likely to expand more slowly because they need to identify, absorb, and distribute the capability they targeted with the move (a process that can be more or less lengthy depending on the nature of the capability).

The value of a particular location may also change as an organization expands, learns, and changes. Developing new capabilities for customizing products and services to specific markets, for instance, or for deploying financial and human resources globally may expand an organization's menu of options for new locations. IKEA, for instance, didn't venture outside Europe until it had honed its business system through successive entries in Scandinavia, Germany, the United Kingdom, France, and Mediterranean Europe.[44]

Competitive Clock

Because entering a new market requires resources, organizations cannot enter every potential market at once. Therefore, when an organization chooses one new geographic market, it postpones entry elsewhere, giving competitors time to improve their own competitive advantage in those markets. Managers who compare the benefits of entering against the opportunity costs of postponing can identify the best time to enter new markets and select between a location strategy that avoids competitors and one that locates with them.

How important is the competitive clock in timing decisions? The answer may vary by industry. In retailing, banking, energy, telecom, and other industries built around ***horizontal foreign direct investment***, where a firm invests in foreign markets to expand its current lines of business, the number of potential markets is fixed and being the first to enter may carry benefits. In these cases, making entry choices strategically is critical. An extreme example is the wireless industry. Because wireless licenses are granted by governments and are limited in number, wireless operators who pass up a licensing opportunity (or lose it to a competitor with a higher bid) may be locked out of that market permanently. Organizations intending to expand globally over time must therefore behave strategically with each location they choose.

2.6 Sustaining a Global Strategy

Just as time shapes when it is right to make a particular move, time shapes the potential value of a global strategy overall. As we've discussed so far, organizations following a global strategy can maximize the value they create and capture by:

- dispersing activities geographically without severing critical links among those activities
- adding new locations strategically
- timing geographic expansions to neutralize rivals

These are the building blocks of a successful global location strategy—a cohesive set of location choices over time and geographies that allows organizations to create and capture more value from a global strategy.

Like all matters of business strategy, a sustainable global location strategy cannot be static. Locations evolve as innovation centers rise and fall, demand shifts, competitors develop new capabilities, and governments come and go. For instance, innovation in wireless telecommunication was based in Scandinavia and Japan for many years, but it shifted to Silicon Valley after Apple introduced the iPhone. In terms of demand, firms that galloped into Brazil in the early 2000s have had to contend with falling demand there. And with governments, energy firms that flocked to Venezuela's newly opened oil industry in the 1990s had their assets nationalized in the 2000s, after the election of President Hugo Chavez in 1999.

Organizations evolve, too. In global settings, in particular, they must decide repeatedly whether to adapt their products to a new market or expand using standardization. Adapting to specific markets to increase customers' willingness to pay often has the corollary effect of hampering coordination across the organization, making it harder to achieve the cost savings available from standardization.

Consider the experience of Japanese automakers. Growth stalled when they followed a strategy of standardized products and heavy coordination across world markets. When they tried to increase sales by catering to local tastes, however, they found that doing so worked against the production efficiency at the center of their initial strategy.

Correcting those sources of organizational strain can be difficult. At Philips, for example, the autonomy that country managers had in developing products for each market created vast inefficiencies over time. When headquarters tried to rationalize product portfolios in order to exploit synergies across countries and decrease costs, it faced vehement opposition from country managers.[45]

The experience at Philips reminds us that globalization, and the strategies organizations use to exploit it, are still evolving. The promise of developing a worldwide competitive advantage—a ***global advantage***—is undeniably tantalizing. Nevertheless, to date, even the world's most capable global firms have not found the necessary but elusive balance point between being global and being local. Given the stakes, there is little doubt they will continue trying.

3 SUPPLEMENTAL READING

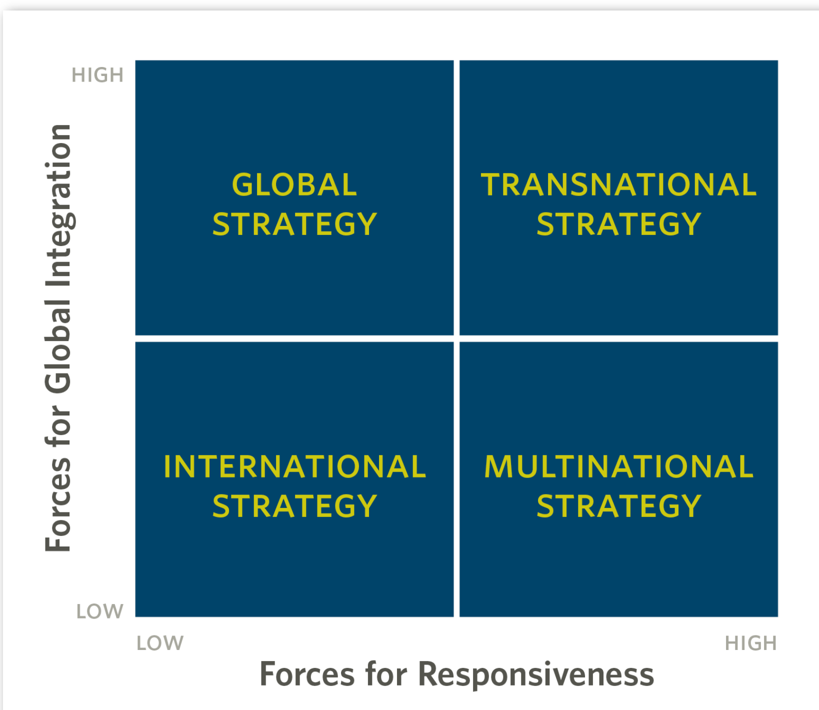
3.1 Antecedent Perspectives on Global Competition and Strategy

The taxonomy and frameworks in this reading are based largely on two academic literatures that explore global business. The first, from international business, has focused primarily on the influence of countries and the impacts of geographic dispersion across national borders. The second, from strategy, looks at the influence of firm capabilities and competitive advantage, customers' willingness to pay, cost, and economies of scale and scope. This section introduces key contributions from international business and briefly discusses their implications for how and where organizations compete globally.

Transnational Management

One stream of international business literature classifies organizations that compete globally by the degree to which their strategies emphasize (1) the integration of global operations and (2) responsiveness to country preferences.[46] **Figure 5** suggests how some of this literature classifies these strategies.[47]

FIGURE 5
Integration Responsiveness Framework for Organizations That Compete Globally



Source: Adapted from "Building and Managing the Transnational: The New Organizational Challenge," by Christopher A. Bartlett in *Competition in Global Industries*, Michael E. Porter, ed. Harvard Business Review Press, Boston, MA: 1986, p. 377. Copyright © 1986 by the Harvard Business Publishing Corporation; all rights reserved.

In this framework, differences in the need for integration and responsiveness lead to distinct strategies for global value creation.[48] An organization that has an ***international strategy*** attempts to create value mainly by adapting ideas and products that come from the firm's headquarters. Its national units thus have relatively little autonomy. In this strategy, the value perceived in being globally integrated or responsive to national differences is low.

An organization following a ***multinational strategy*** aims to differentiate products and services across country markets. Managers in multinational subsidiaries are highly independent, charged with both identifying local needs and finding ways to meet them. But their independence renders the multinational less efficient overall because its national units will be duplicating efforts.

An organization with a global strategy in this typology uses a global product for which there is substantial standardization across national markets. Concentrating production and centralizing R&D increases efficiency but limits opportunities to learn from developments in an organization's various markets. Concentrating activities in one or a few locations also exposes global organizations to sourcing risks caused by natural disasters or shifts in exchange rates and government policies.

An organization following a ***transnational strategy*** takes the cost and efficiency advantages of global organizations, and the localization of multinationals, and applies them in the markets where they will reap the greatest advantage. This gold-standard approach turns on a careful (and difficult to achieve) configuration of an organization's assets and capabilities to capture low costs *and* higher revenues, and global efficiency *and* local innovation. An organization that achieves and sustains this delicate balance gains what Bartlett and Ghoshal call a worldwide competitive advantage.[49]

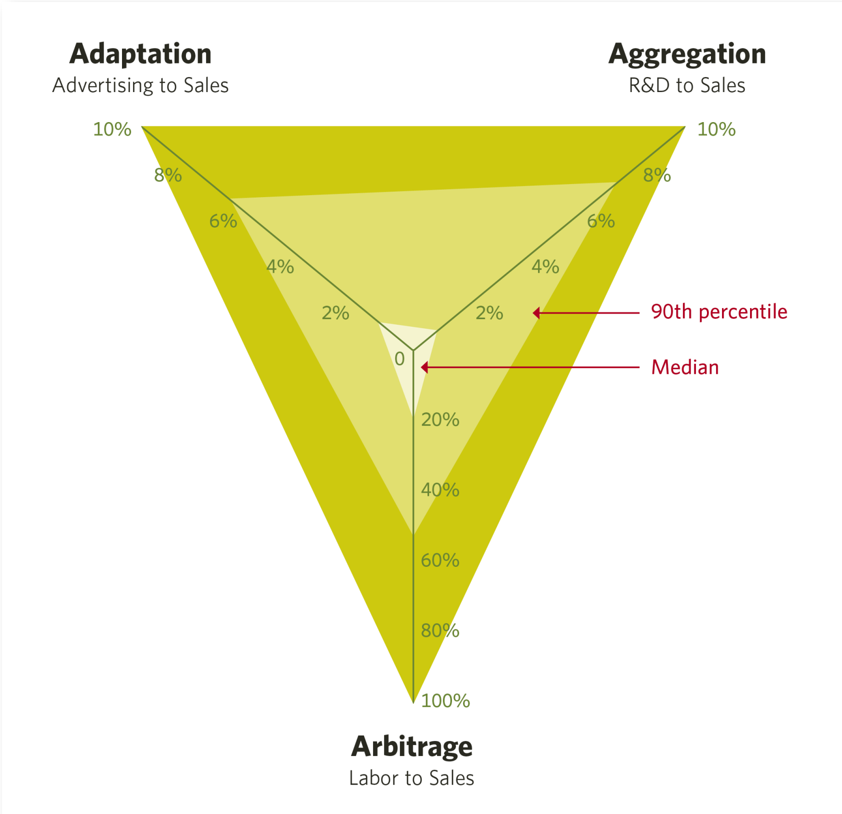
This typology has become a standard feature in international business courses, where it continues to offer important insights at the organizational level. Because it was largely built around observations of mature global organizations, however, it offers less guidance to managers charged with the nuts-and-bolts decisions of a global expansion.

AAA Triangle Framework

Pankaj Ghemawat observed that value-creation strategies focused on similarities across markets risk overlooking the historic and enduring importance of market *differences*.[50] One of the world's oldest forms of value creation is, after all, buying or developing a product in a location where it is abundant and transporting it (by foot, camel, or ship) to a location where it is not.

Ghemawat captured his insights in the AAA Triangle framework (**Figure 6**), wherein strategies for global value creation are defined by *aggregation, adaptation,* and *arbitrage*.[51] The AAA Triangle serves as a kind of strategy map for managers. The percentage of sales spent on advertising indicates how important adaptation is likely to be for the company, the percentage spent on R&D is a proxy for the importance of aggregation, and the percentage spent on labor helps gauge the importance of arbitrage. Managers should pay attention to any scores above the median because those areas most likely merit strategic focus. Scores above the 90th percentile may be perilous to ignore.

FIGURE 6 AAA Triangle Framework



Note: Median and top decile scores are based on US manufacturing data from Compustat's Global Vantage database and the US Census Bureau. The ratios of advertising and R&D to sales rarely exceed 10%, so those are given a maximum value of 10% in the figure.

Source: Reprinted from "Managing Differences: The Central Challenge of Global Strategy," by Pankaj Ghemawat, *Harvard Business Review*, March 2007. Copyright 2007 by the Harvard Business Publishing Corporation; all rights reserved.

Adaptation is the strategy of choice for organizations whose goal is to raise revenues and market share by optimizing their products and services for local markets; *aggregation* is the response of organizations trying to build economies of scale with regional or global operations; and *arbitrage* is for organizations looking to exploit market differences by, for instance, locating elements of their supply chain in different places.

In Ghemawat's conception, the strategic focus of an organization competing globally will shift from one A to another depending on its strategic priority: for example, marketing (adaptation), R&D (aggregation), or low-cost inputs (arbitrage). Only in rare cases will an organization (or a division of an organization) be able to pursue all three As at once. Instead, a more realistic approach is to select one or two As while remaining attentive to opportunities and threats that would necessitate a shift.

David Collis later highlighted the potential for a fourth A—*agglomeration*—which in his framework denotes the simultaneous pursuit of arbitrage, aggregation, and adaptation.[52] Collis suggested that, in addition to acting on market differences, managers should identify whether there is a common customer segment across countries. Where there is none, organizations may be able to create one by designing a product or product platform with worldwide appeal. The final step in Collis's framework is performing a cost analysis to evaluate whether (and which) changes can be made to adapt global products to local taste (which is similar to Bartlett and Ghoshal's transnational strategy).

CAGE Distance Framework

Ghemawat also distilled a vast literature on measures of distance into a simple but powerful framework called CAGE, in which distance along four dimensions—cultural, administrative, geographic, and economic—amplifies or decreases the attractiveness of a potential location or product market for a given firm (see **Table 2**).[53] For products, the framework addresses the point that even when a viable market appears to exist, organizations need to evaluate whether their offerings are close enough (i.e., similar enough) to inspire demand there. For activities, it speaks to why it is necessary to understand the underlying factors that determine whether an organization can achieve its goal in a given location.

TABLE 2 CAGE Distance Framework

	Cultural Distance	Administrative Distance	Geographic Distance	Economic Distance
Attributes Creating Distance	Different languages Different ethnicities; lack of connective ethnic or social networks Different religions Different social norms	Absence of colonial ties Absence of shared monetary or political association Political hostility Government policies Institutional weakness	Physical remoteness Lack of a common border Lack of sea or river access Size of country Weak transportation or communication links Differences in climate	Differences in consumer income Differences in cost and quality of: • natural resources • financial resources • human resources • infrastructure • intermediate inputs • information or knowledge
Industries or Products Affected by Distance	Products with high linguistic content (TV) Products affecting cultural or national identity of consumers (food) Product features that vary in terms of: • size (cars) • standards (electrical appliances) • packaging Products that carry country-specific quality associations (wines)	Industries in which government involvement is high, such as: • producers of staple goods (electricity) • producers of other entitlements (drugs) • large employers (farming) • large suppliers to government (mass transportation) • national champions (aerospace) • those that are vital to national security (telecommunications) • exploiters of natural resources (oil, mining) • industries that are subject to high sunk costs (infrastructure)	Products with a low value compared to weight or bulk ratio (cement) Products that are fragile or perishable (glass, fruit) Industries in which communications and connectivity are important (financial services) Industries in which local supervision and operational requirements are high (many services)	Industries in which the nature of demand varies with income level (cars) Industries in which economies of standardization or scale are important (mobile phones) Industries in which labor and other factor cost differences are salient (garments) Industries in which distribution or business systems are different (insurance) Companies that need to be responsive and agile (home appliances)

Source: Adapted from "Distance Still Matters: The Hard Reality of Global Expansion," by Pankaj Ghematwat, *Harvard Business Review*, September 2001. Copyright 2001 by the Harvard Business Publishing Corporation; all rights reserved.

The importance of each dimension for a given global expansion depends on two factors: the organization's industry and the organization's degree of internationalization. For example, cultural distance would be more important for a media firm because its products heavily reflect language and traditions. In contrast, administrative distance would be more important for a bank because its work depends on government regulation and laws.

By delineating areas of distance that persist in the modern global economy and their implications for firms, the CAGE Distance framework offers a powerful response to the one-world perspective popularized most recently by Thomas Friedman. Friedman's 2005 best seller, *The World Is Flat*, argued that the Internet and other advances in communications technology had fundamentally altered the business landscape by allowing unprecedented levels of collaboration (and competition) between individuals in diverse parts of the globe.[54] The CAGE Distance framework demonstrates that, notwithstanding the many new avenues for value creation created by increasing market similarities, organizations competing globally cannot ignore market differences.

Products for Global Value Creation

The DDD (deployment, developing, deepening) framework discussed in Section 2.2 teaches that the degree of product standardization (or, conversely, localization) an organization can pursue in a global expansion is controlled in part by the basic global strategy the organization follows. Each strategy requires some degree of common customer preferences across markets, but the amount shifts along a continuum.

The continuum itself is a synthesis of ideas from international business (including those from Bartlett, Ghoshal, and Ghemawat) and also from marketing, where scholars have a wide range of views about what products are most likely to generate value or new advantages in an increasingly globalized world.

On the global product side is Theodore Levitt, who in 1983 proclaimed that, as globalization progressed, customers would sacrifice local preferences for lower prices, and therefore their needs would become increasingly homogeneous.[55] Following this logic, Levitt prescribed that organizations competing globally should rationalize their product portfolios to offer products that were highly standardized and thus could be sold, without major changes, everywhere.

On the local product side, Susan Douglas and Yoram Wind argued that, in a globalized world with better technologies, organizations are even more capable of responding to customer needs.[56] In their prescription, local products are not only feasible but desirable.

Integrating these ideas in the DDD framework gives us *deployment strategies*, which replicate the same business model across countries, and *deepening strategies using multinationality*, which serve the same customer segment across markets. These strategies represent one end of a continuum and target similar segments with very similar products.

On the other end of the continuum are *deepening strategies using adaptation*, which create value by tailoring products and services to local tastes, thereby gaining market share and/or increasing customers' willingness to pay. At its most extreme, a deepening strategy can result in a wide array of country-specific products and services that have little in common.

Between these two extremes are *development strategies,* which tap unique resources in one market and apply them in others. Development strategies require products that are similar but not identical across markets.

4 KEY TERMS

deepening strategy A global strategy that widens an organization's existing competitive advantage. Competing across geographic markets allows an organization to enhance existing products or create new ones (increasing willingness to pay), or improve its production or procurement (decreasing costs).

deployment strategy A global strategy that creates value by aggregating demand across markets, thus increasing volume. The relationship between cost and willingness to pay stays the same but is enacted across multiple countries.

development strategy A global strategy that creates value by (1) expanding into countries to obtain new sources of competitive advantage and (2) using those capabilities to create value in the organization's other global markets.

global advantage The competitive advantage available to organizations that enact more than one global strategy (deployment, development, and deepening) simultaneously, applying each to the products and countries where it is most suited and developing organizational capabilities to reconcile the conflicts between them.

global location strategy A cohesive set of location choices, over time and geographies, that allows firms to create and capture value while competing globally.

global strategy A value-creation strategy that capitalizes on similarities and differences across geographic markets.

global value creation The act of increasing the wedge, relative to competitors, between the price customers are willing to pay for a product and the cost of producing it.

hollowing out The threat that domestic firms relying on offshore outsourcing may unintentionally transfer capabilities to their foreign suppliers, causing a long-term and irreversible decline in innovation.

horizontal foreign direct investment An investment that a firm makes in a foreign market in order to expand its operations for its current lines of business.

international strategy A strategy in which national units that have little autonomy focus primarily on adapting ideas and products that come from a firm's headquarters, where the value perceived in being globally integrated or responsive to national differences is low.

liability of being a foreigner The extra costs borne by organizations that expand beyond their home country.

multinational strategy A strategy in which a firm attempts to differentiate products and services across country markets.

offshore outsourcing Assigning a segment of the value chain to an organization that resides outside the home country of the originating firm. This approach creates value by lowering costs and/or freeing up domestic producers to concentrate on innovation and other high-value activities, but it may dampen innovation and allow capabilities to migrate to foreign suppliers.

offshoring Locating a segment of the value chain outside the organization's home country. This approach creates value by combining firm capabilities with the comparative advantages of different countries.

outsourcing Assigning a segment of the value chain to another organization. This approach creates value by combining the competitive advantages of different firms.

paradox of being consistent The contradiction that is created when firms with the greatest competitive advantages in their domestic markets have a business model that is optimized for those markets, but when expanding abroad, these firms find their advantages harder to replicate.

transnational strategy A strategy in which a firm attempts to realize the cost and efficiency advantages of global organizations while remaining responsive to national preferences.

value capture The appropriation of the value created by a product, service, or process.

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1 For details, see David J. Denis, Diane K. Denis, and Keven Yost, "Global Diversification, Industrial Diversification, and Firm Value," *The Journal of Finance* 57 (October 2002): 1951–1979. Similarly, Randall Morck and Bernard Yeung found that announcements of new firm subsidiaries abroad reduce market value, on average, unless a firm possesses intangible assets that cannot be transferred through market transactions; see "Why Investors Value Multinationality," *The Journal of Business* 64 (April 1991): 165–187.

2 For a complete description of Walmart's expansion efforts in 12 countries, see Juan Alcacer, Abhishek Agrawal, and Harshit Vaish, "Walmart Around the World," HBS No. 714-431 (Boston: Harvard Business School Publishing, 2013).

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4 The concept "paradox of being consistent" was originally developed for Competing Globally, an elective course Juan Alcacer developed for second-year MBA students at Harvard Business School. A more detailed description is available in Juan Alcacer, "Why Do Firms Go Abroad? Strategies to Create Value Globally," HBS No. 713-057 (Boston: Harvard Business School Publishing, 2014).

5 See Arturs Kalnins and Laure Mougeot Stroock, "Burger King Goes 'Down Under,' " Cornell University School of Hotel Administration case, March 2014.

6 Keith Bradsher, "Apple Settles iPad Trademark Dispute with Chinese Company," *New York Times*, July 12, 2012, http://www.nytimes.com/2012/07/03/technology/apple-settles-ipad-trademark-dispute-with-chinese-company.html, accessed July 2014.

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9 The following discussion of deployment, development, and deepening strategies is adapted from Harvard Business School, "Why Do Firms Go Abroad? Strategies to Create Value Globally," HBS No. 713-057, by Juan Alcacer. Copyright © 2014 by the President and Fellows of Harvard College; all rights reserved.

10 The strategy earned Apple higher sales per square foot than any other US-based retailer in 2014 (http://retail.emarketer.com/apple-murphy-usa-tiffany-co-top-new-emarketer-store-productivity-rankings/). Apple Stores have been so successful, in fact, that entrepreneurs peddling authorized and unauthorized Apple products in China built near-replicas in at least 22 locations (see http://www.bbc.com/news/technology-14503724).

11 To court wine lovers who find Dom too widely available to justify its prestige pricing, Moët announced in 2014 that it would release carefully aged batches held back from exceptional vintages. Dom Perignon Second Plenitude, or P2, will also taste the same in all markets but is expected to command twice the price of "regular" Dom of the same vintage (see http://www.forbes.com/sites/larryolmsted/2014/05/12/p2-a-new-even-more-luxurious-dom-perignon-champagne/).

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13 For more on how IKEA competes globally, see Christopher A. Bartlett and Ashish Nanda, "Ingvar Kamprad and IKEA," HBS No. 390-132 (Boston: Harvard Business School Publishing, 1990).

14 See Juan Alcacer, Mary Furey, and Mayuka Yamazaki, "Vodafone in Japan (A)," HBS No. 711-464 (Boston: Harvard Business School Publishing, 2010); "Vodafone in Japan (B)," HBS No. 711-469 (Boston: Harvard Business School Publishing, 2010); "Vodafone in Japan (C)," HBS No. 711-470 (Boston: Harvard Business School Publishing, 2011).

15 See Christopher A. Bartlett, "P&G Japan: The SK-II Globalization Project," HBS No. 303-003 (Boston: Harvard Business School Publishing, 2003).

16 See Juan Alcacer, Mary Furey, and Mayuka Yamazaki, "Vodafone in Japan (B)," HBS No. 711-469 (Boston: Harvard Business School Publishing, 2010).

17 Deepening strategies are based on the traditional strategy literature, which focuses on how to increase competitive advantage. In the international business literature, the concept of deepening strategies is closely related to the concept of arbitrage developed by Pankaj Ghemawat. The main difference is that, where arbitrage opportunities are associated with increasing competitive advantage by reducing costs, deepening strategies include strategies that increase advantage by enhancing revenue. This is an important clarification for managers because global strategies based solely on arbitrage across countries may not be a sustainable source of competitive advantage and because other firms may have access to the same sources of advantage, and those sources might rely on country characteristics that change rapidly.

18 See, for example, Pankaj Ghemawat and Tarun Khanna, "Tricon Restaurants International: Globalization Re-examined," HBS No. 700-030 (Boston: Harvard Business School Publishing, 1999).

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20 For more on the power of regional strategies, see Pankaj Ghemawat, "Regional Strategies for Global Leadership," *Harvard Business Review* 83 (December 2005): 98–108.

21 A complete description of Logoplaste's "follow-your-customer" approach to global expansion is available in Juan Alcacer and John Leitao, "Logoplaste: Global Growing Challenges," HBS No. 711-411 (Boston: Harvard Business School Publishing, 2010).

22 See Pankaj Ghemawat and Toby Lenk, "De Beers Consolidated Mines Ltd. (A)," HBS No. 391-076 (Boston: Harvard Business School Publishing, 1990.)

23 A more detailed description of the opportunities and constraints inherent in the three global strategies is available in Juan Alcacer, "Why Do Firms Go Abroad? Strategies to Create Value Globally," HBS No. 713-057 (Boston: Harvard Business School Publishing, 2014).

24 International business scholars Christopher Bartlett, Sumantra Ghoshal, C. K. Prahalad, and Yves L. Doz were the first to frame organization strategies abroad as a trade-off between global integration (standardization) and local responsiveness (localization). See Bartlett and Ghoshal, *Managing Across Borders: The Transnational Solution (*Boston: Harvard Business School Press, 1998) for a complete review; see Supplemental Reading 3.1 of this reading for a summary.

25 In strategy terms, being more responsive to a market means customizing the product to satisfy local customers, with the unintended consequence of increasing costs because of (1) investment to change the product or service and its delivery, and/or (2) losing economies of scale. Integration/standardization, on the other hand, increases efficiency but brings the risk of unsatisfied customers who, facing a product that doesn't fulfill their needs, may be willing to pay less or, in extreme situations, go without.

26 For more about how global competition influences ownership choices, see Juan Alcacer, "How to Execute Global Strategies?" HBS No. 713-060 (Boston: Harvard Business School Publishing, 2014).

27 The activity allocation framework was originally developed for Competing Globally, an elective course Juan Alcacer developed for second-year MBA students at Harvard Business School. A more detailed description is available in Juan Alcacer, "What Is Global? Allocating Products and Activities across Locations," HBS Module Note No. 713-058 (Boston: Harvard Business School Publishing, 2014).

28 The following discussion is adapted from Harvard Business School, "What Is Global? Allocating Products and Activities across Locations," HBS No. 713-058, by Juan Alcacer. Copyright © 2014 by the President and Fellows of Harvard College; all rights reserved.

29 See Josie Ensor, "Santander Brings India Call Centres Back to UK," *The Telegraph,* July 8, 2011, http: http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/8624959/Santander-brings-India-call-centres-back-to-UK.html, accessed July 2014.

30 For more on offshore outsourcing in the wireless industry, see Pete Engardio and Bruce Einhorn, "Outsourcing Innovation," *Bloomberg Businessweek Magazine*, March 20, 2005, http://www.businessweek.com/stories/2005-03-20/outsourcing-innovation, accessed July 2014. On the perils of transferring capabilities to suppliers, see Arruñada, B., and X. H. Vázquez, "When Your Contract Manufacturer Becomes Your Competitor," *Harvard Business Review* 84 (September 2006): 135–145.

31 The location framework was originally developed for Competing Globally, an elective course Juan Alcacer developed for second-year MBA students at Harvard Business School. For more detail, see Juan Alcacer, "Where and When to Locate? Crafting Location Strategies to Strengthen Competitive Advantage," HBS No. 713-059 (Boston: Harvard Business School Publishing, 2014).

32 The following discussion is adapted from Harvard Business School, "Competing Globally," HBS No. 713-422, by Juan Alcacer. Copyright © 2014 by the President and Fellows of Harvard College; all rights reserved.

33 See Juan Alcacer and Kerry Herman, "Intel: Strategic Decisions in Locating a New Assembly and Test Plant (A)," HBS No. 713-406 (Boston: Harvard Business School Publishing, 2012), and Juan Alcacer and Kerry Herman, "Intel: Strategic Decisions in Locating a New Assembly and Test Plant (B)," HBS No. 713-419 (Boston: Harvard Business School Publishing, 2012).

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35 Louise Story, "As Companies Seek Tax Deals, Governments Pay High Price," *The New York Times,* December 1, 2012, http://www.nytimes.com/2012/12/02/us/how-local-taxpayers-bankroll-corporations.html, accessed July 2014.

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37 A complete description of strategic interaction in the cement industry is available in Pankaj Ghemawat and Catherine Thomas, "Strategic Interaction across Countries and Multinational Agglomeration: An Application to the Cement Industry," *Management Science* 54 (December 2008): 1980–1996.

38 The timing framework was originally developed for Competing Globally, an elective course Juan Alcacer developed for second-year MBA students at Harvard Business School. A more detailed description is available in Juan Alcacer, "Where and When to Locate? Crafting Location Strategies to Strengthen Competitive Advantage," HBS No. 713-059 (Boston: Harvard Business School Publishing, 2014).

39 See "Middle East and Africa FDI Growth Affected by Arab Spring," *The FDI Report 2012* (March 2012), Financial Times Ltd., http://www.fdiintelligence.com/index.php/Info/What-s-New/Press-releases/Middle-East-and-Africa-FDI-growth-affected-by-Arab-Spring, accessed July 2014.

40 See the 2013 A. T. Kearney Foreign Direct Investment Index report, "Back to Business: Optimism amid Uncertainty," at http://www.atkearney.com/documents/10192/1464437/Back+to+Business+-+Optimism+Amid+Uncertainty+-+FDICI+2013.pdf/96039e18-5d34-49ca-9cec-5c1f27dc099d, accessed July 2014.

41 A complete description can be found in William W. Janosz, Julia Kou, and Debora L. Spar, "White Nights and Polar Lights: Investing in the Russian Oil Industry," HBS No. 795-022 (Boston: Harvard Business School Publishing, 1996).

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43 See Christopher A. Bartlett and Ashish Nanda, "Ingvar Kamprad and IKEA," HBS No. 390-132 (Boston: Harvard Business School Publishing, 1990).

44 Christopher A. Bartlett and Ashish Nanda, "Ingvar Kamprad and IKEA," HBS No. 390-132 (Boston: Harvard Business School Publishing, 1990).

45 See Christopher A. Bartlett, "Philips versus Matsushita: The Competitive Battle Continues," HBS No. 910-410 (Boston: Harvard Business School Publishing, 2009).

46 For an analysis of the trade-off between integration and responsiveness, see C. K. Prahalad and Yves L. Doz, *The Multinational Mission: Balancing Local Demands and Global Vision* (New York: The Free Press, 1987).

47 See Christopher A. Bartlett, "Building and Managing the Transnational: The New Organizational Challenge," in *Competition in Global Industries*, Michael E. Porter, ed. (Boston: Harvard Business School Publishing, 1986), which focuses on types of organizations, not specifically on strategies. It identifies three types of organizations: global, multinational, and transnational. Figure 5 incorporates other research on integration and responsiveness. It highlights some strategic implications of these four organizational types, and includes an "international" quadrant in which the forces for integration and responsiveness are low. See, for instance, Sumantra Ghoshal and Nitin Nohria, "Horses for Courses: Organizational Forms for Multinational Corporations," *Sloan Management Review* 34 (Winter 1993): 23–35.

48 For a more complete overview, see Christopher A. Bartlett, Sumantra Ghoshal, and Paul Beamish, *Transnational Management: Text, Cases, and Readings in Cross-Border Management,* 5th ed. (New York: McGraw-Hill Irwin, 2008), pp. 197–210.

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7 INDEX