marketing+

UNIVERSITÄT SIEGEN

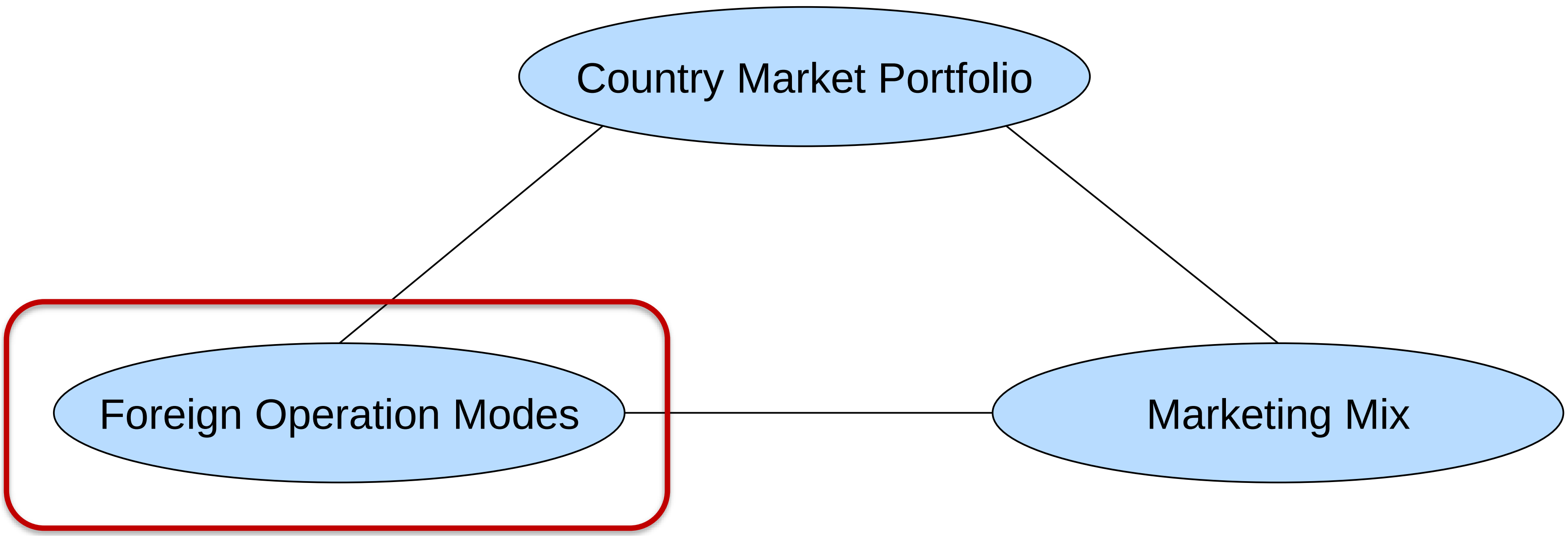
Lecture
International Marketing
Summer Term 2016

Dr. Gerhard Wagner

OPERATION MODES
IN INTERNATIONAL MARKETS (1)

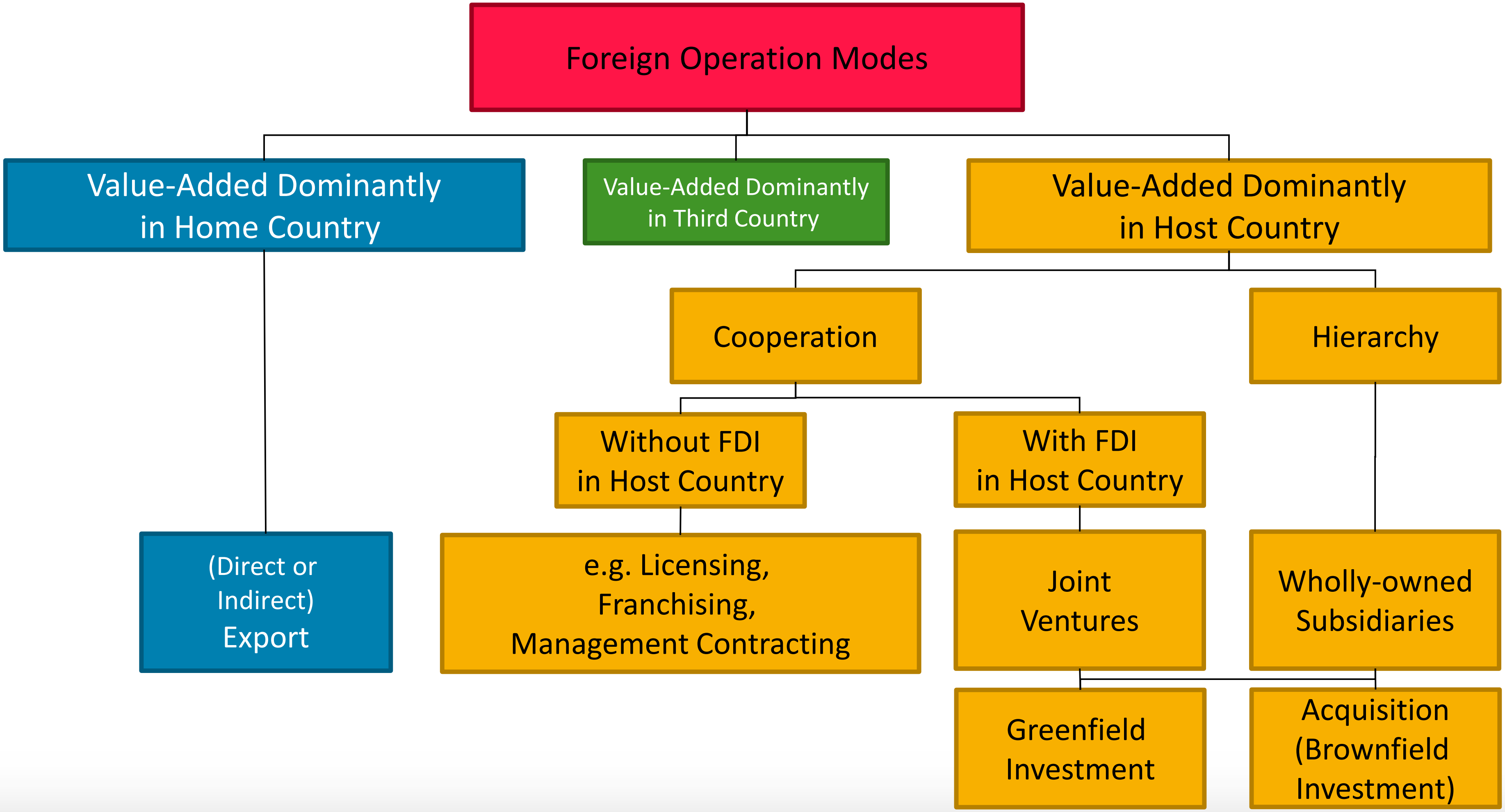
Categorical Decision Fields of International Marketing

REMINDER



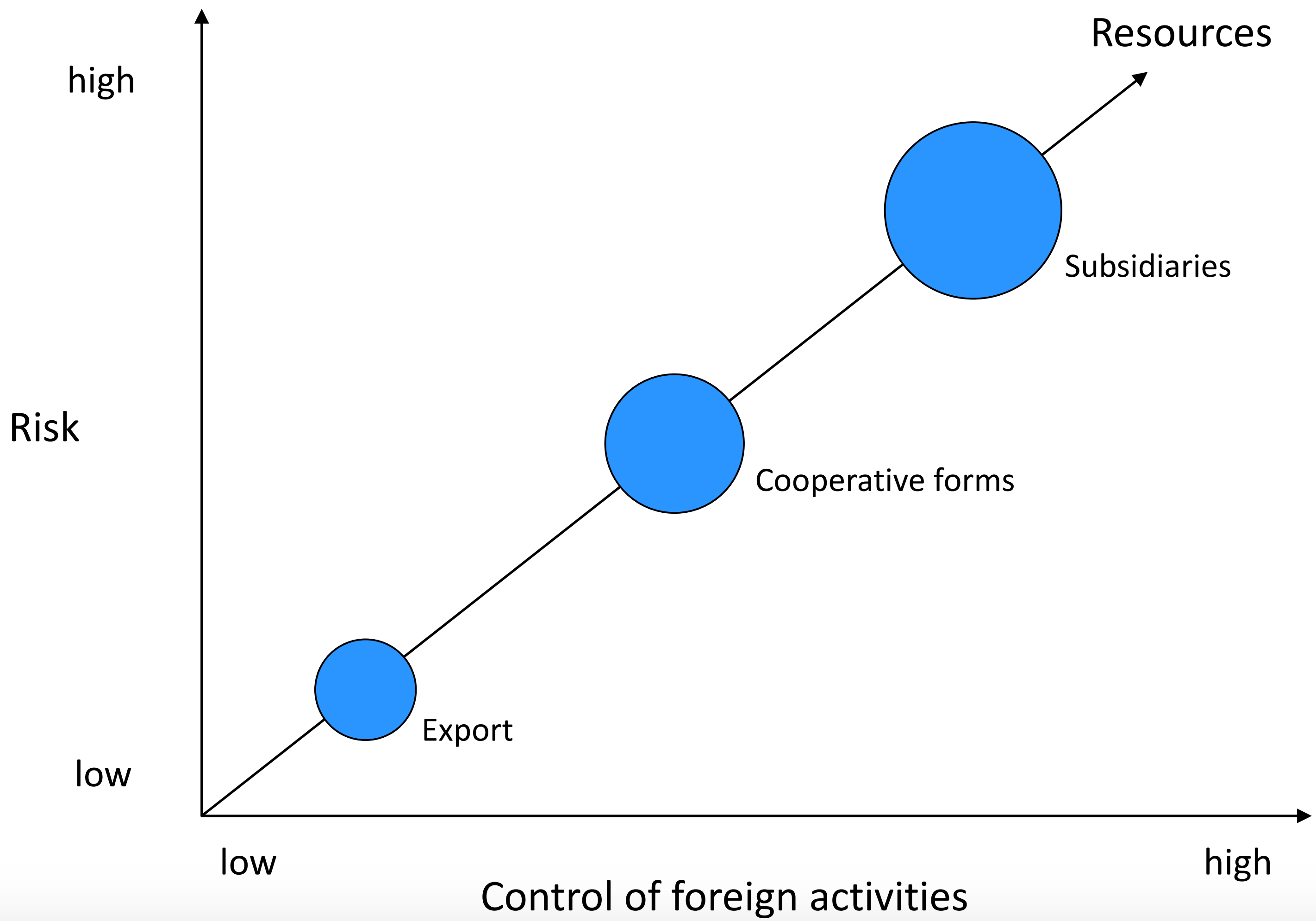
Source: Adapted from Zentes/Swoboda/Schramm-Klein 2013, p. 65.

Classification of Selected Foreign Operation Modes



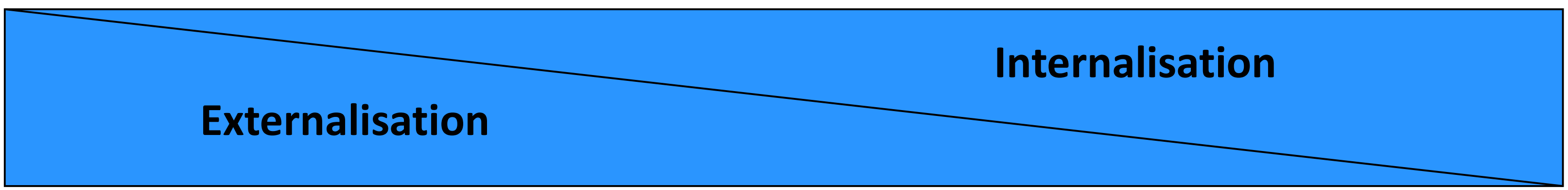
Source: adapted from Zentes 1993, p. 67 and Morschett/Schramm-Klein/Zentes 2015, p. 324.

Classification of Operation Modes



Source: adapted from Bradley 2005, p. 291 and Zentes/Swoboda/Schramm-Klein 2013, p. 227.

Transaction Format Band



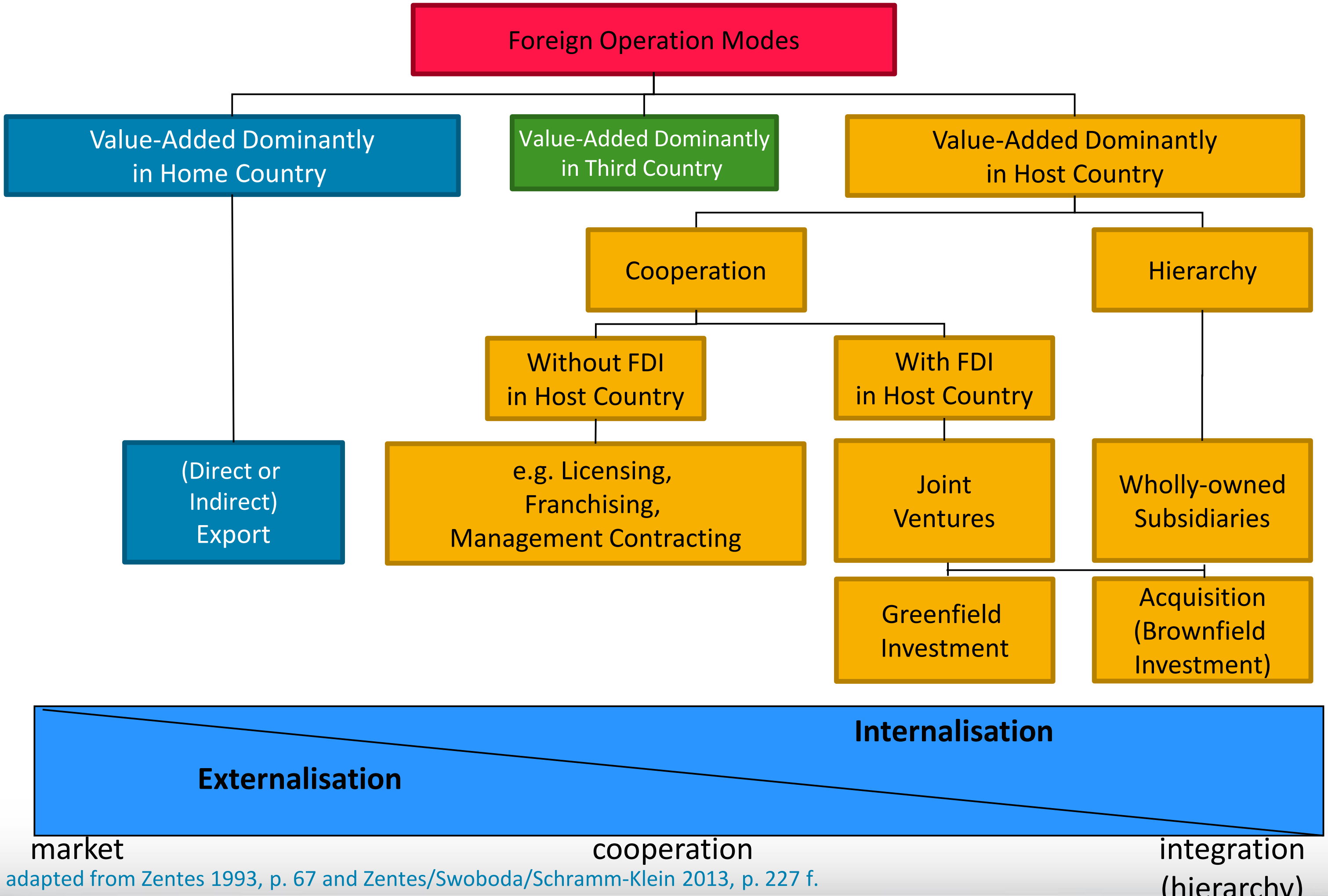
Market

Cooperation

Integration (Hierarchy)

Source: adapted from Zentes/Swoboda/Schramm-Klein 2013, p. 228.

Classification of Selected Foreign Operation Modes based on Competitive Strategy

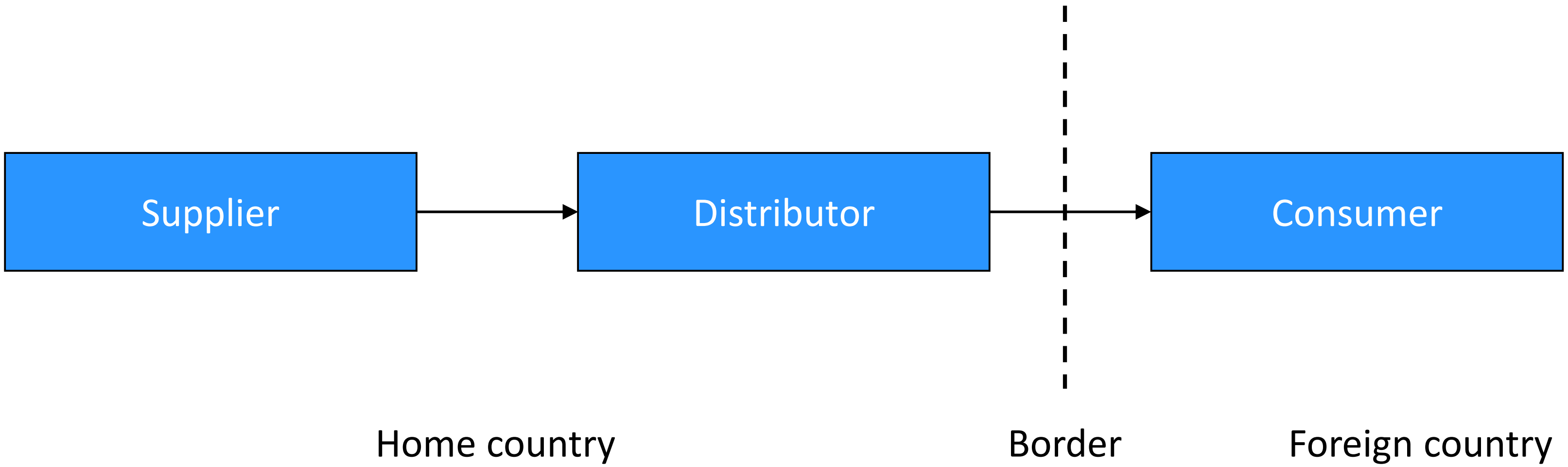


Source: adapted from Zentes 1993, p. 67 and Zentes/Swoboda/Schramm-Klein 2013, p. 227 f.

Sunquick's Foreign Operations Modes

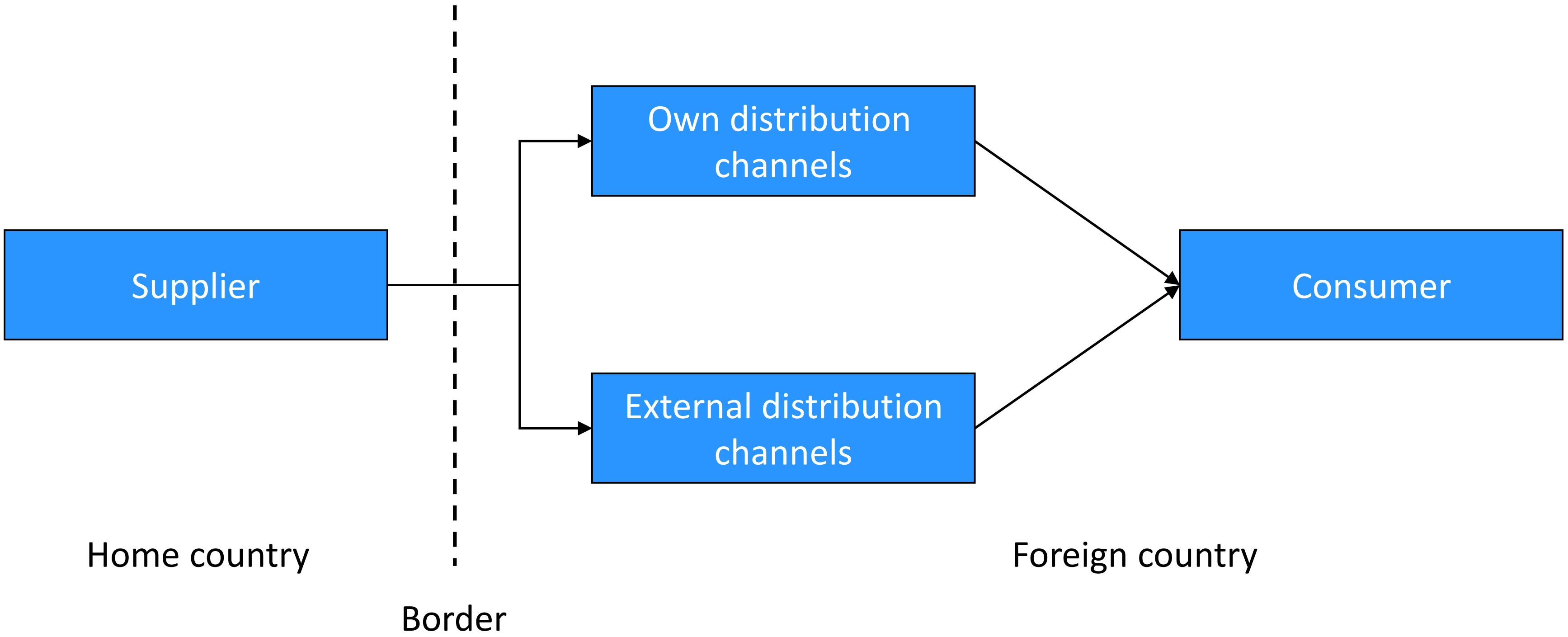
Source: www.co-ro.com/en/our%20company/markets

Structure of Indirect Export



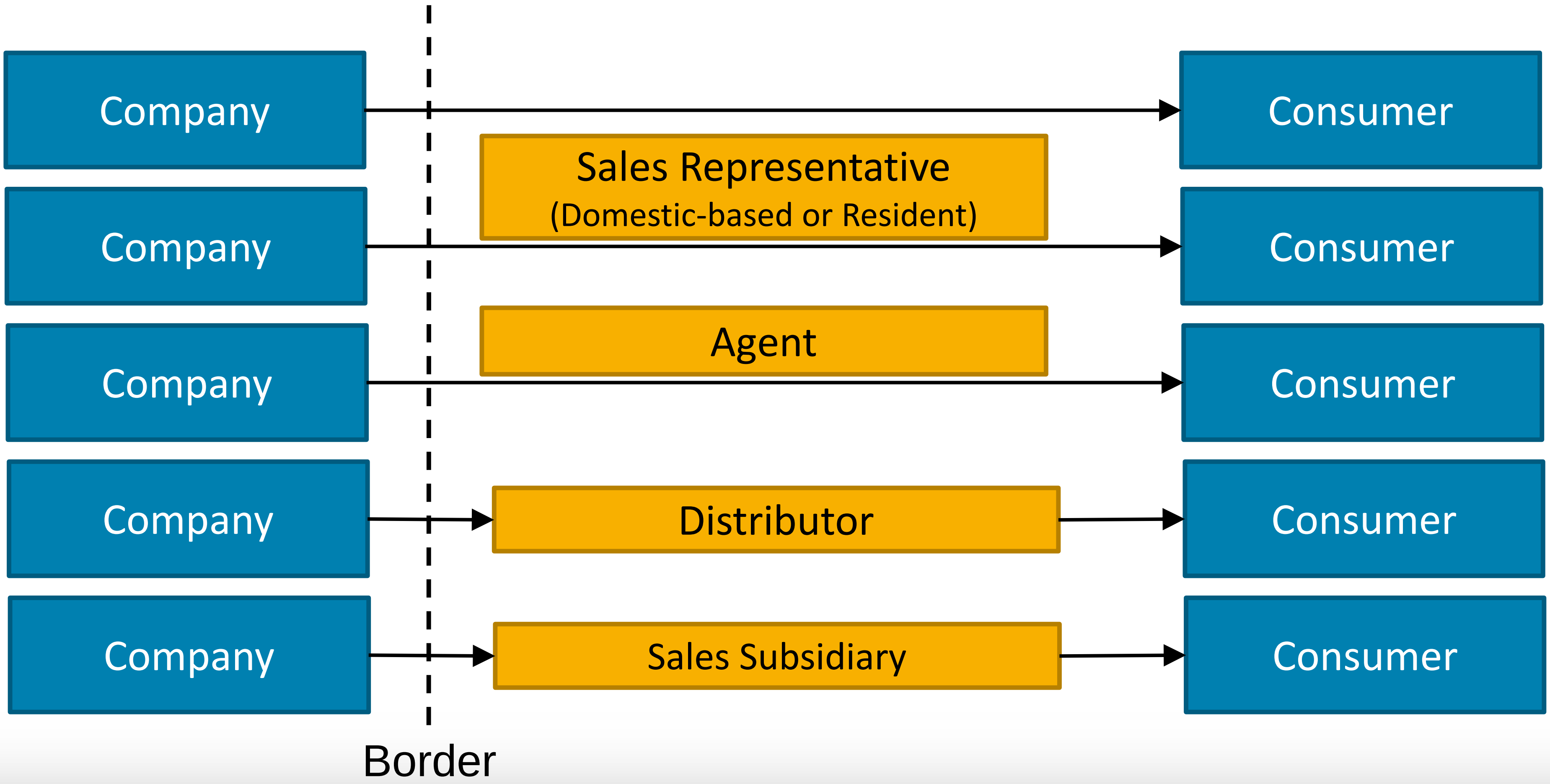
Source: adapted from Jahrmann 2007, p. 53 and Zentes/Swoboda/Schramm-Klein 2013, p. 231.

Structure of Direct Export



Source: adapted from Jahrmann 2007, p. 51 and Zentes/Swoboda/Schramm-Klein 2013, p. 233.

Different Distribution Channel Alternatives in the Case of (Direct) Exporting



Exporting – Advantages and Disadvantages

- Advantages
  - easy way to tap international market potential
  - avoids the substantial cost of establishing manufacturing operations in the host country
  - easy way to sell a surplus, thus helps to achieve experience curve advantages at home
  - low risk
  - remains flexibility
  - potentially country-of-origin advantages
- Disadvantages
  - There may be lower-cost locations for manufacturing abroad.
  - transport costs
  - tariff barriers
  - agents/distributors in a foreign country may not act in exporter's best interest

Source: Hill 2008.

Licensing

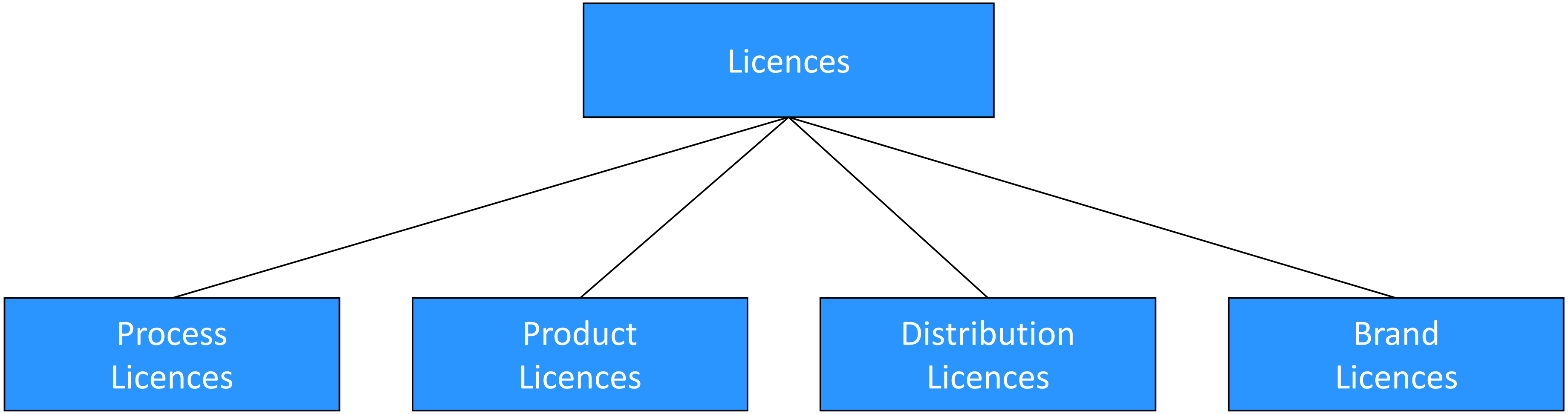
- A licensing agreement is an arrangement whereby a licensor grants the rights to intangible property to another entity (the licensee) for a specified time period, and in return, the licensor receives a payment from the licensee.
  - e.g. a licensor allows another company to manufacture a certain product that is based on a patent against some agreed royalty (or license fee).
- International licensing occurs when a firm provides (against payment), rights needed by another company to operate its business in a foreign market.
  - MAN B&W Diesel as a licensor to Hyundai Heavy Industries
- Licensing Out vs. Licensing In
  - active vs. passive licensing
  - licensor vs. licensee

Rights to be Licensed (the Potential License Package)

One or a combination of the following:

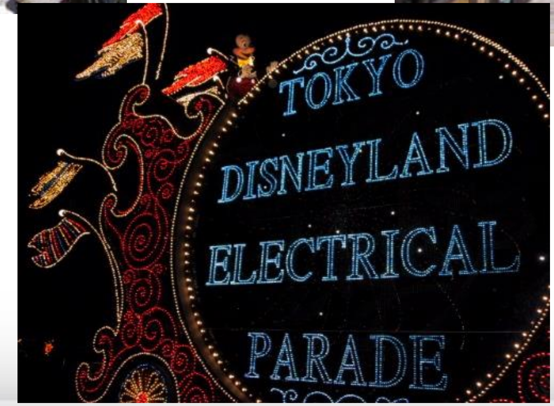
- Use of a trade mark/brand name
  - e.g. perfumes by Hugo Boss, Gucci, Lacoste, Escada
- Marketing advice and assistance
- Patent covering a product or (production) process
- Manufacturing know-how not subject to a patent
  - e.g. operations expertise referring to manufacturing layout, instruction materials, etc.
  - technical and commercial training programs
- Technical advice and assistance
- Licensing must (should) have exclusive and easily transferable property rights to product/process technology
  - it must also be possible to evaluate the value of the right!

Types of Licence Agreements



Source: Morschett/Schramm-Klein/Zentes 2015, p. 392.

Example: Tokyo-Disneyland



Source: Disney.

Licensing – Advantages/Motives (I)

- Easy way to **improve cash flow** from existing technology/know-how/brand
  - better **exploitation of past R&D** investment
  - maybe product is at end of product **life cycle** in advanced countries but stretching product life cycle is possible in less developed countries
- **Fast and cheap introduction** of licensed product (based on existing manufacturing facilities of licensee)
- **Production in the foreign** market
  - low transport costs
  - potentially lower labor cost
  - access to local inputs
  - circumvention of market barriers (such as host country restrictions, tariffs, non-tariff barriers)
  - local value added considered beneficial by host country officials

Source: Zentes/Swoboda/Schramm-Klein 2013, p. 242 ff.

Licensing – Advantages/Motives (II)

- Use of **market know-how**, **customer relationships** and **distribution channel**s of licensee

- Low own investment / **low commitment of own resources**
  - low capital risk, reduction of country risk to transfer risk for the payments of the licensee
  - good **opportunity for small companies** with limited financial, managerial or marketing resources to expand into a new market
  - good **opportunity** to **enter smaller foreign markets**, higher risk markets

- Improved delivery and service levels in local markets

Source: Zentes/Swoboda/Schramm-Klein 2013, p. 242 ff.

Licensing – Disadvantages (I)

- **Lack of control** over licensee operations in the foreign market
  - lack of commitment of foreign partner can **endanger the market success**
  - low possibility to influence the market policy of licensee
  - **quality control** problems concerning production and marketing of licensee (potentially negative image effects in host country and spill-over effects)
  - licensing might **not give a firm the tight control over manufacturing**, marketing, and strategy in a foreign country that may be required to maximize its profitability
  - licensing also includes **transaction cost** (identifying partner, monitoring, enforcing…)
    - risk of opportunism as greatest risk
  - **initial investment in adaptation of technology** to market/partner may be necessary

- Low own value added by own company

Source: Zentes/Swoboda/Schramm-Klein 2013, p. 242 ff.

Licensing – Disadvantages (II)

- Only **passive** interaction with the market
- Problems with integration of market **into international strategy**
  - change in market entry strategy not possible in the short term
- Disclosure of accumulated **competitive knowledge and experience**
  - creates possible **future competitors** (licensee may become a future competitor)
  - establishment of competitors by know-how-transfer (esp. on third markets)

- Low initial cost might be accompanied with less than optimal long-term income in foreign market

➢ Short-term vs. Long-term consequences need to be considered

Source: Zentes/Swoboda/Schramm-Klein 2013, p. 242 ff.

Franchising (I)

- Franchising is
  - a system of marketing goods and/or services and/or technology,
  - which is **based upon a close and ongoing collaboration** between **legally and financially separate** and independent undertakings, the Franchisor and its individual Franchisees,
  - whereby the Franchisor grants its individual Franchisee the right, and imposes the obligation, to **conduct a business in accordance with the Franchisor's concept**.

- The right entitles and compels the individual Franchisee, in exchange for a direct or indirect financial consideration, to use the **Franchisor's trade name**, and/or trade mark and /or service mark, **know-how, business and technical methods**, procedural system, and other industrial and /or intellectual property rights, **supported by continuing provision of commercial and technical assistance**, within the framework and for the term of a written franchise agreement, concluded between parties for this purpose.

Franchising (II)

- Business Format Franchising comprises of 5 essential elements
  - **A brand name** (registered as a brand name and/or a trademark, etc.) which serves as the umbrella sign for network, and a rallying sign for the consumer and public),
  - a **licence to the use the brand**, granted to the franchisee by the franchisor,
  - a **business system** - a business concept formatted into a duplicable value "package" founded on the franchisor's tested Know How and his continued assistance during the term of the agreement),
  - **payment by the franchisee of a financial consideration**, either in a direct form, such as an entrance fee and/or continuing fee ("royalty"), and/or an indirect form such as a mark-up on supplied goods.
  - the **investment** in, and ownership of, the assets of the franchised business by the franchisee.

- <u>Different:</u> Product and Trade Name Franchising
  - similar to licensing

Which company uses a Franchise System?

Source: adapted from Zentes/Swoboda/Schramm-Klein 2013, p. 251.

Leading Franchises in International Markets

Rank	Company	Industry	Stores	Sales in 2011 (in $ million)	Country Markets	Share of company owned stores (in %)
1	7-Eleven	**Grocery**	48,097	76,600	16	1
2	Subway	Gastronomy	37,199	16,600	95	0
3	McDonald's	Gastronomy	33,735	**27,006**	**119**	19.2
4	Kumon Institute of Education	Education	25,431	832	47	0
5	KFC	Gastronomy	17,401	n.a. [1]	115	25.1
6	Pizza Hut	Gastronomy	13,747	n.a. [1]	97	13.3
7	Burger King	Gastronomy	12,667	2,336	81	4.7
8	Dunkin' Donuts	Gastronomy	10,200	628	32	0
9	Domino's Pizza	Gastronomy	9,742	1,652	76	4
10	Century 21	Real estate	7,490	n.a.	73	0

1 KFC and Pizza Hut (next to others) belong to the Portfolio of Yum! Brands.

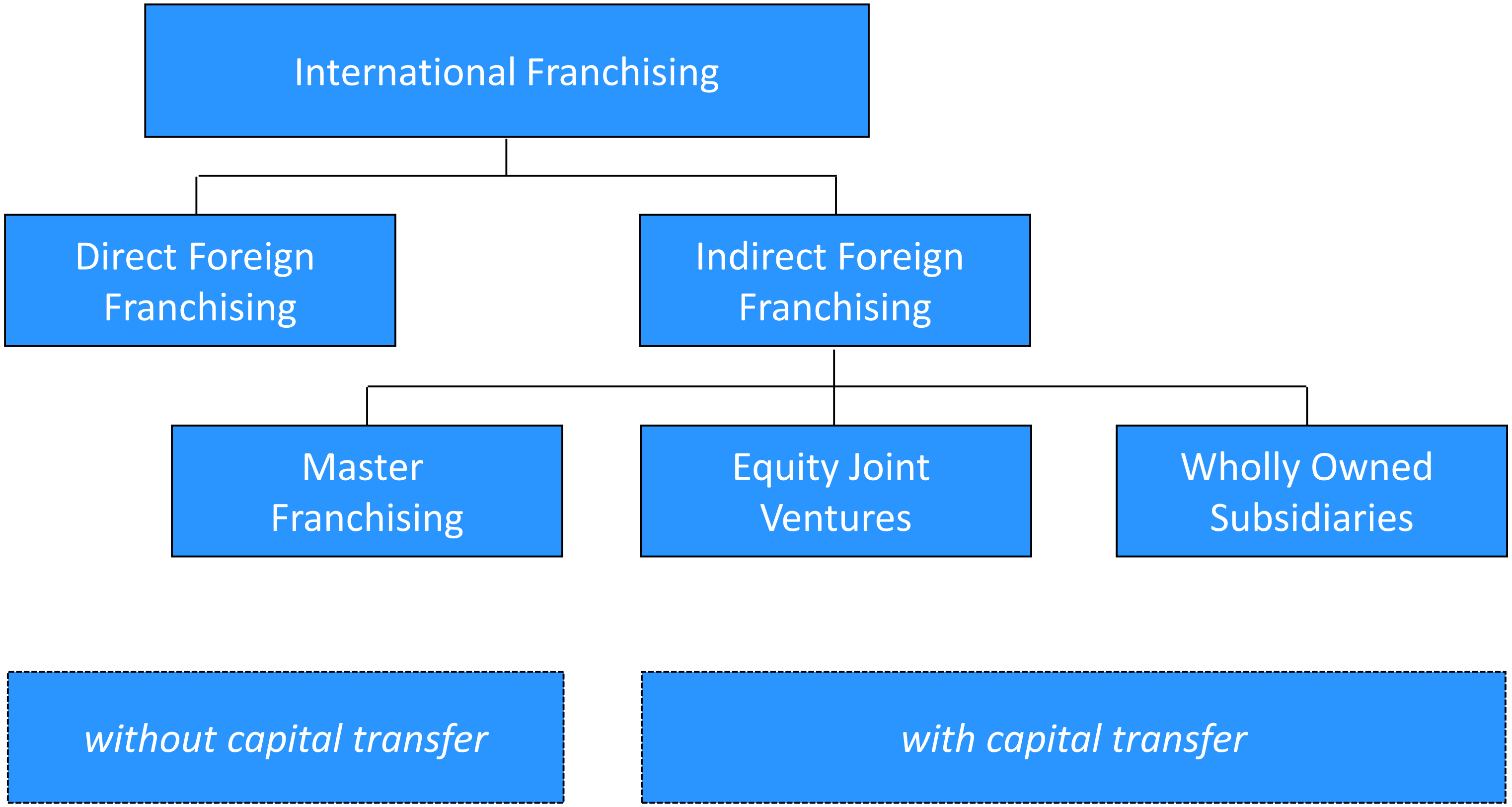
Source: adapted from Zentes/Swoboda/Schramm-Klein 2013, p. 251.

Business Format “Packages” for Franchises

- Trade marks/ trade names/ designs
- Patents and copyrights
- Business know-how/ trade secrets
- Geographic exclusivity
- Store design
- Market research
- Location selection

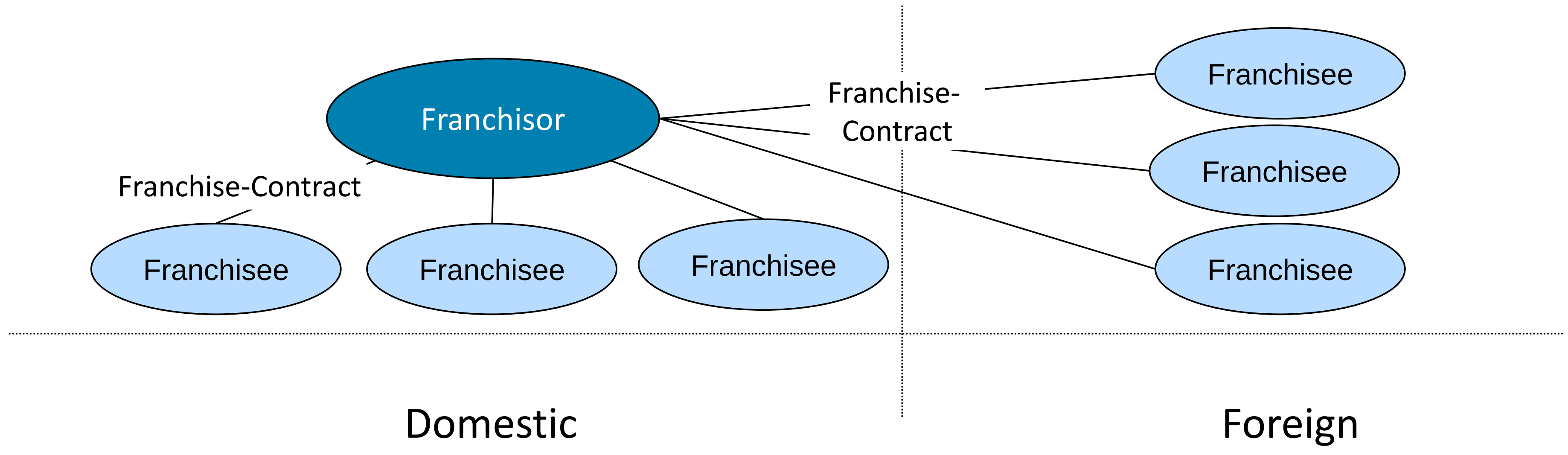
Source: adapted from Hollensen 2014, p. 376.

Types of International Franchise Systems



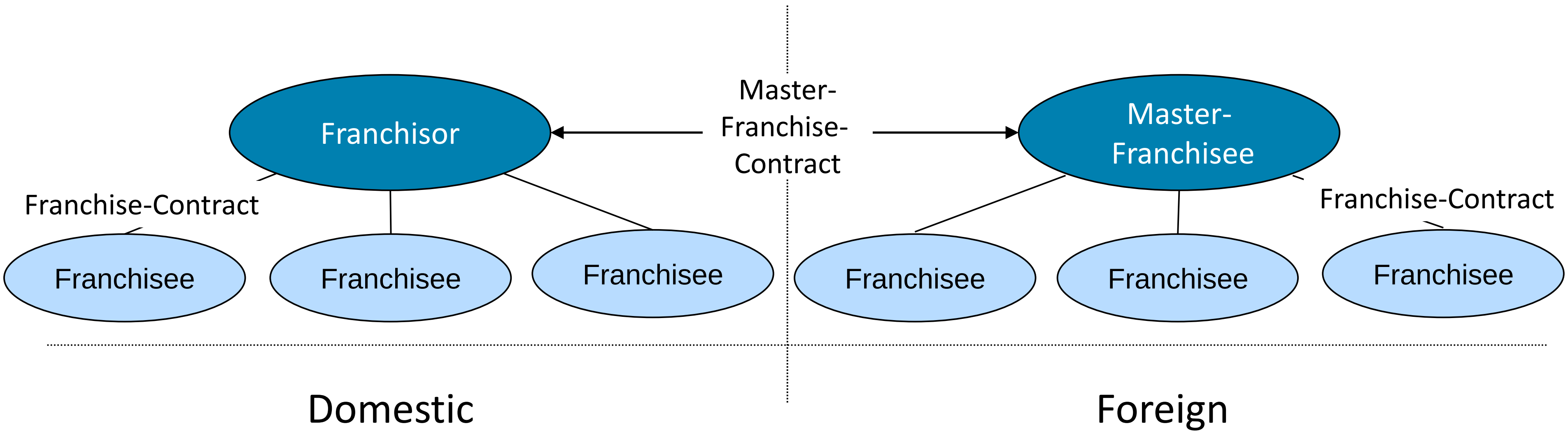
Source: Zentes/Swoboda/Schramm-Klein 2013, p. 249.

Direct Foreign Country Franchising



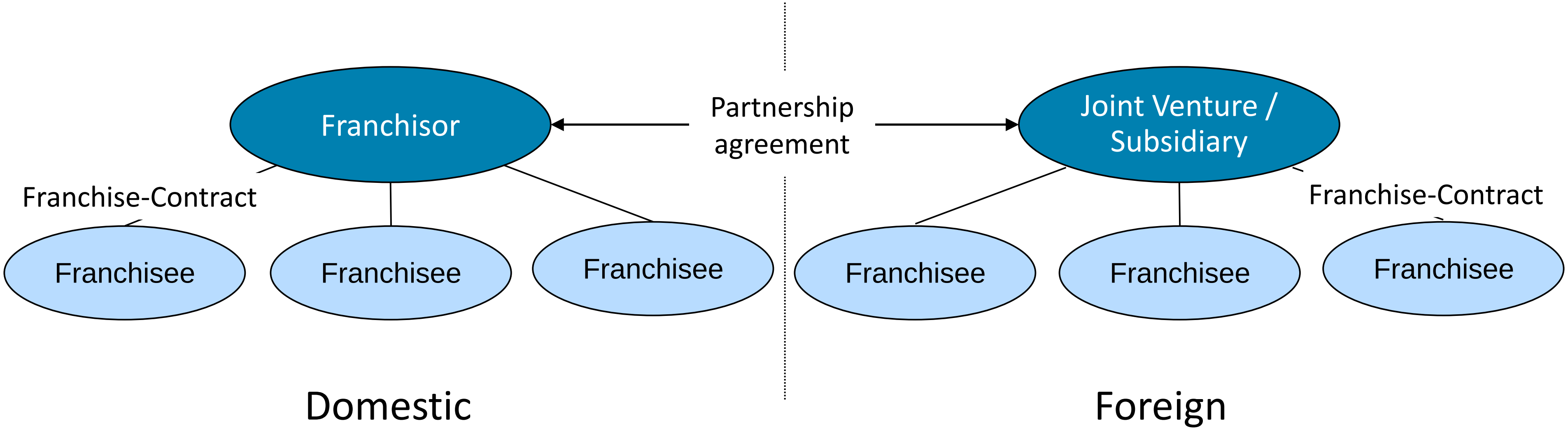
Source: adapted from Morschett/Schramm-Klein/Zentes 2015, p. 394.

Indirect Foreign Country Franchising: Example Master-Franchising



Source: adapted from Morschett/Schramm-Klein/Zentes 2015, p. 394.

Indirect Foreign Country Franchising: Example
Indirect Franchising via JV/Subsidiaries



Source: adapted from Morschett/Schramm-Klein/Zentes 2015, p. 394.

Franchising as Int'l Market Entry Strategy – Advantages

- The firm **avoids costs and risks** of opening up a foreign market
- **Rapid expansion** possible (see Fressnapf, McDonald's)
  - capital infusion by franchisee (direct or via bank)
- **Local network** of the franchisee
  - existing community goodwill
  - existing local market knowledge
- **Higher motivation / Involvement** of franchisee (as compared to employed "store manager") due to independent entrepreneurship
  - franchisees' profit **directly tied** to their efforts (low monitoring costs)
- **Mutual (bidirectional) know-how-transfer**
  - local knowledge combined with support from headquarters
  - simultaneous usage of advantages of large system with small units
- Value added dominantly in the host country

Source: Zentes/Swoboda/Schramm-Klein 2010, S. 237

Franchising as Int‘l Market Entry Strategy – Disadvantages

- Disadvantages for Franchisor
  - revenues **may not be adequate** (do not resemble true power of the product)
  - revenues **depend** on the franchisee(s)
  - **availability** of franchisees or a master franchisee sometimes **not given**
  - **absence of direct control** over franchisee’s operations
    - strong controlling **system is needed**
    - (European) Franchise Law grants substantial freedom to the franchisee (“in participating restaurants only”)
  - potentially problem in **performance standards**
  - potentially **cultural problems** with business partners (franchisees)
  - risk of **lowering quality of brand name** (franchisees’ effects on brand name)
  - only **passive interaction** with the market

- Disadvantages for Franchisees:
  - residual **risks of local operations**
  - only **limited expansion** possible
  - **not fully independent** in business decisions
  - **risk of failure of the franchisor**/the franchise-system (see Cha chà)

Source: Zentes/Swoboda/Schramm-Klein 2010, S. 237

Management Contracts

- A management contract is an arrangement whereby **one party hands over the actual operational control of a company to another company** which performs the necessary management functions in return for a fee.

- Examples: hotels, airports, casinos

- Advantages/motives
  - contract firm has no market risk, as it is rewarded **independent of the possible success** and only offers management; **investments are performance**
  - contract firm has no capital risk as it only offers management performance; **investments are executed by the managed firm**
  - possibility to use **excess management capacities**
  - frequently use for **"getting to know"** country markets

Source: Zentes/Swoboda/Schramm-Klein 2013, p. 253 ff.

Management Contracts – Basic Principle

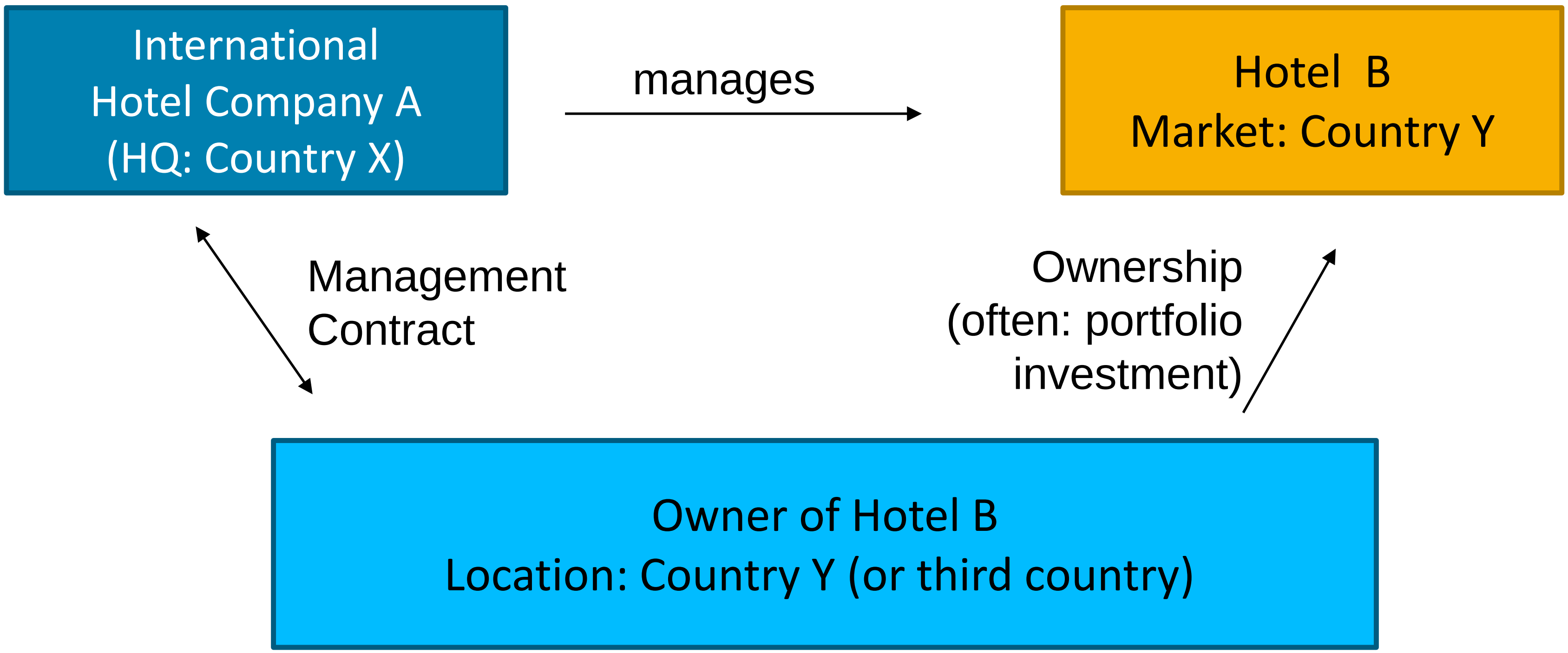
- Contracting firm **leads the company of the managed firm for a fee**, on account and risk of the managed firm under the name of the managed firm or under a different name.

- Contracting Firm
  - takes over management
  - offers the managerial know how
  - offers the operational goodwill
  - offers economic relationships
  - offers experience

- Managed Firm
  - pays the agreed fee
  - takes the risk
  - offers factual, financial and personnel production factors

Source: Zentes/Swoboda/Schramm-Klein 2013, p. 242 ff.

Structure of the management contract system – Example : Hotel



Source: adapted from Zentes/Swoboda/Schramm-Klein 2013, p. 255.

Management-Contracts – Example Accor

Present **in 90 countries, with 4,229 hotels and more than 500,000 rooms**, Accor’s brands offer hotel stays tailored to the specific needs of each business and leisure customer.

Source: Accor 2011.