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COMPETE

Competence Platform on Energy Crop and Agroforestry Systems for Arid and Semi-arid Ecosystems - Africa

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PREFACE

This report comprises the results from the work accomplished under task 4.8 of the project COMPETE (Competence Platform on Energy Crop and Agroforestry Systems for Arid and Semi-arid Ecosystems - Africa), co-funded by the European Commission in the 6th Framework Programme – Specific Measures in Support of International Cooperation (Contract No. INCO-CT- 2006-032448).

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Editing and Reporting: COMPETE - North-South Cooperation on promising bioenergy schemes

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ABBREVIATION

C: the capital value
EBRD: European Bank for Reconstruction and Development
EU: European Union
FDI: Foreign Direct Investment
GDP: Gross Domestic Product
JV: Joint Venture
MTOE: Million of ton oil equivalent
ORI: Operation Risk Index
PLC: Product Life Cycle
R: the relevance number
ROA: return on assets
ROC: return on capital
ROE: return on equity
SIC: Standard Industrial Classification
TQM: Total Quality Management
US: United States
VPC: value of the product category

1 INTRODUCTION

Because Africa, with a population increasing, needs more and more energy, Bioenergy appears as a concrete positive answer to this issue. But, actually, Africa is also characterised by low energy efficiency, lack of Bioenergy technologies and of organisation for a good application of those technologies.

For this reason it has been considered very important, in the COMPETE project, to develop South-South Cooperation with countries where the implementation of alternative energy crops and agro forestry schemes has recently gained large interest with the objective of linking the project activities in Africa with on-going successful research and demonstration efforts in Latin America and Asia,. The development of North-South Cooperation is also important in order to allow the transfer of knowledge and technical know-how between developed and developing countries and promote joint ventures for common activities in the field of new energy crop and agroforestry systems.

In order to answer to those requests, a preliminary report describes the market conditions of European Bioenergy technology (i.e. carbonisation, stoves, gasification, microdistillery) for the exploitation of the biomass residues that are produced in arid and semi-arid area of Africa. “Deliverable 4.6: Report on innovative Bioenergy complexes on village level for the combined production of food, animal feed and energy and other commercially sound Bioenergy technologies; EUBIA December 2008”.

The present “Report on promotion of knowledge transfer and joint ventures - Definition of the rules for implementing an industrial cooperation in Bioenergy” proposes a broad overview of the way to promote knowledge transfer and joint venture and which are the rules defined for implementing an industrial cooperation in Bioenergy.

The report is composed of 5 main parts, the first one gives the rules for implementation of industrial cooperation in Bioenergy, presenting the general requirements, the factors to be analysed like, country specific situation, market, competitiveness and environmental factors that are presented and commented. The second part makes an overview of the customer analysis in order to know the characteristics of the buyers and how the product should be sold and distributed, in order to understand the market’s sustainability. The third part presents a very broad overview of the analysis to be done to the company with the one it is planned to establish certain kind of collaboration. The fourth part presents an overview of the different kind of technology providing in third country (Export, Franchising, foreign direct investment or Joint Venture). The last part will go in details in the description of the mechanism of joint Ventures: advantages and disadvantages, the different forms of joint ventures, the better way to identify successful joint venture and also makes an overview of how to implement the joint venture (negotiations, agreement, financial management, Contract)

2 DEFINITION OF THE RULES FOR IMPLEMENTATION OF INDUSTRIAL COOPERATION IN BIOENERGY

In order to implement an industrial cooperation in Bioenergy some primordial rules have to be followed. Those rules are presented and defined in this paragraph.

2.1 General Requirements

If a company wants to expand its activity field to the foreign market, these basic questions have to be asked:

- Which competitive advantages are available?
- How shall the geographic structure of the activity look like?
- Which type of market entry strategy should be chosen?
- How shall the foreign activity be organised?

First of all, a company wishful to penetrate in a new foreign market must start with a series of analysis that show the general situation of that particular market: for example, if a marked is already saturated or if it is dominated by a monopolistic firm, its convenient for the incoming firm to not enter in it.

2.2 Analysis of the country specific situation

The first analysis to conduct is an analysis of the situation specific for the country in which the enterprise wants to expand its activity. Analysing a Market's Attractiveness is important for several reasons. First, market attractiveness determines whether there are current competitors on the market, if existing competitors are likely to continue in the market or want to exit, and whether others are likely to enter. Second the state of an industry in terms of future profits and growth often determines the level of commitment. Third, analysis of key trends in technology, regulation, and so on suggests major threats and opportunities. Analysing a market is crucial for developing sound objectives and strategies.

There are three major categories of variables, which are considered for our market analysis. First we focus on basic descriptive statistics of the industry: its size and sales patterns. Next we discuss several aspects of the competitive and profit situation. Third, we discuss general environmental influences (technology, etc.). For each of these factors, the procedure has two important steps. First, past and current data are gathered and interpreted. That is, analysis goes beyond mere listing of facts. Then, projections are made. These projections are important, because they impact other analyses (e.g., if new competitors are expected) and provide many of the basic planning assumptions behind forecasts and profit projections.

Figure 1: Bases For Industry Analysis

Market Factors	*Environmental Factors*
Size	Technological
Growth	Economic
Stage in life cycle	Social
Profit	Political
Performance Ratios	Regulatory
Competitive Factors:	
Concentration	
Power of buyers	
Power of suppliers	
Rivalry	
Pressure from substitutes	
Capacity utilisation	
Entries and exits	

We now analyse in short each of the previous mentioned points.

2.3 Aggregate Market Factors

The Aggregate Market factors to be considered for the industry analysis are:

2.3.1 Size

Market size, measured in both units and dollars, is clearly an important criterion as it relates to the likelihood of a product producing revenues to support a given investment.

2.3.2 Growth

Not only is current growth important, but, because of the product life cycle, growth projections over the horizon of the plan are also critical. Fast-growing markets are almost universally desired because they support high margins and sustain profits into future years. However, they also attract competitors. The growth rate can be estimated with the help of a market forecast.

2.3.3 Life Cycle Stage

Two factors, market size and growth, are often portrayed simultaneously in the form of the product life cycle. This curve can be divided up into four segments: introduction, growth, maturity, and decline.

Figure 2: PLC Portfolio

size	growth: low	growth: high
high	Maturity	Growth
low	Decline	Intro-duction

2.3.4 Profit

While there is certainly variability in profits, margins, and cash flows in an industry, there are also inter industry differences. Differences in profitability can be due to a number of factors of production including labour versus capital intensity, raw materials, manufacturing technology, and competitive rivalry.

2.3.5 Performance Ratios

Like profits, financial ratios vary substantially across competitors in an industry and hence are considered separately in a competitive analysis. Most ratios are expressed as returns (e.g., return on assets (ROA), return on equity (ROE), return on capital (ROC) etc.). These ratios provide indications of both the rewards for successful performance and the requirements for participation (e.g., capital intensity).

2.4 Competitiveness factors

The competitive factors can be listed and defined as follow:

2.4.1 Concentration

A simple indicator of the competition in an industry is its concentration, the market share controlled by a few top firms. Various simple measures are used, such as:

- The share of the largest firm.
- The number of firms with at least *x* percent of the market.
- The combined shares of the largest three or four firms.
- The share of the largest firm divided by the share of the next three largest competitors.

Markets where two or more firms have nearly equal shares are likely to be most competitive; and, in general, the more competitive the industry, the greater the requirements for expenditures and the lower the profit.

2.4.2 Power of buyers

Buyers are any people or institutions who receive goods or service. High buyer bargaining power is negatively related to industry attractiveness. In such circumstances, buyers can force down prices and play competitors against each other for other benefits, such as service. Some conditions when buyer bargaining power is high include:

- When the buyer accounts for a large percentage of the industry's output. The more important a buyer is to an industry's well being in terms of sales and profit, the more power the buyer has.
- When the product is undifferentiated.
- When the buyers are earning low profits.
- When the buyer has full information.

In general, consumers are limited in their buying power on an individual basis. (Notable exceptions exist, of course, such as a government as a purchaser of military equipment). However, if consumers can be motivated as a group, they become a more important customer and thus exert more power than would otherwise be the case.

2.4.3 Power of suppliers

Suppliers are any institutions that supply the industry with factors of production, such as labour, energy, capital, components, and machinery. High supplier power is clearly not an attractive situation, as it allows suppliers to dictate price and other terms such as delivery dates to the buying industry. Some conditions when supplier bargaining power will be high are:

- When suppliers are highly concentrated, that is, a few firms dominate them.
- When there is no substitute for the product supplied.
- When the supplier has differentiated its products and/or build-in switching costs.

2.4.4 Rivalry

Industries characterised by intensive combat between the major participants may not be as attractive as those where the rivalry is more sedate. Often, a high degree of rivalry results in escalated marketing expenditures, price wars, employee raids, etc. Such actions can go beyond, what is considered to be "normal" market competition and can result in decreased welfare for both consumers and competitors.

Some of the major characteristics of industries exhibiting intensive rivalry are summarised below:

- **Many or balanced competitors**
- **Slow growth**
- **High fixed costs:** in such industries, there is extreme pressure to operate at full capacity to keep average unit costs down. For this reason capital-intensive industries such as paper or chemicals are highly competitive.
- **Lack of product differentiation:** Basic commodities, such as aluminium or chemicals, suffer from this problem.

In fact, any industry where the basic competitive weapon is price suffers from a lack of differentiation and its concomitant extensive rivalry.

- **Pressure from substitutes:** Industries making products or delivering services for which there are a large number of substitutes are less attractive than those delivering a relatively proprietary service. In general, in industries where the range of substitutes is low high rates of return can be earned.
- **Capacity utilisation:** A final characteristic to observe is the historical supply and demand situation in the industry. When an industry is operating at capacity, its costs stay low and its bargaining power with buyers is normally high. Thus, often a key indicator about the health of an industry is whether there is a consistent tendency toward operating at or under capacity. Chronic overcapacity is not a positive sign for long-term profitability. Related to capacity utilisation is the ease or difficulty of either adding new capacity or retiring unused capacity. This is typically assessed in terms of the financial resources and time required.
- **Ease of entries and exits:** a high threat of new entrants diminishes the attractiveness of an industry. New entrants bring additional capacity and resources that usually heighten the competitiveness of a market diminish margins. Key to the likelihood of new competitors entering a market is the

barrier to entry erected by the competition. Often these barriers are legal such as those based on legislated monopolies (e.g., utilities) or patents.

Besides these formal barriers to entry or exit, other influences on entry/exit decisions include:

- **Economies of scale**
- **Product differentiation:** well-established company reputations can make it difficult for new competitors to enter a market.
- **Capital requirements:** these requirements could be related to manufacturing facilities and marketing.
- **Switching costs:** these are costs to buyers of switching from one supplier to another. If switching costs are high, it is difficult to convert a competitor's existing customers.
- **Distribution**
- **The industry's willingness** to vigorously retaliate against newcomers

2.4.5 Competitive factors' summary

Basically an industry tends to be attractive when it is large, growing, profitable, and non-competitive, as the following figure indicates**.**

Figure 3: Attractiveness to Entrants

	Attractiveness	
	High	**Low**
Market Factors		
Size	Large	Small
Growth	High	Slow
Stage in life cycle	Early	Late
Profit	High	Low
Performance ratios	High	Low
Competitive Factors		
Concentration	Low	High
Power of buyers	Low	High
Power of suppliers	Low	High
Rivalry	Low	High
Pressure from substitutes	Low	High
Capacity utilisation	High	Low
Threat of entry	Low	High

2.5 Environmental factors

The environment includes those factors outside the control of both the firm and its industry. High susceptibility to changes in the environment is generally undesirable; but on the other hand, industries that are well positioned to take advantage of environmental changes may prosper.

Environmental factors to be examined can be put in five groups: technological, social, political, economic, and regulatory. These factors should be examined not only to assess industry attractiveness but also to determine if any forecasted changes in these areas dictate changes in strategy.

2.5.1 Technological

Technology refers to the procedures used for developing, making, and distributing a product or service to customers. In the narrowest sense, technology refers to the state of art for product design as well as the production process. A key issue is whether any technologies are emerging that can affect or replace current industry technology. Technical obsolescence is a major factor in many industries. Monitoring both continuous improvements and possible discrete changes is extremely important. Major changes continue to occur in the energy, materials, transportation, information, and genetic (bioengineering) areas. Less technologically strong industries are particularly vulnerable to competition from new industries and from foreign competitors that have invested in technology.

2.5.2 Economic

Almost all capital goods industries (machine tools, computers) are sensitive to Interest Rate fluctuations since their high costs are often financed at short-term rates. Inflation Rates are tied in with interest rate fluctuations and have a similar impact. Again, the impact of having foreign markets or producing in other countries can vary widely over time depending on Currency Exchange Rates.

2.5.3 Employment Conditions

Another factor to be considered is Employment Conditions, especially if relatively unskilled labour at low wage rates is needed. When employment rates are high, employees are hard to find, as higher-paying jobs are available. The conditions of demand and supply of labour for each industry must be considered as well. For example, the supply of engineers is cyclical. When supply is down, many firms in technical businesses suffer from a shortage of skilled labour. Industries that have broad customer bases (for example machine tools, copiers) are often sensitive to Fluctuations in GDP Growth. When the country is in a recession, so are these industries.

2.5.4 Social

Trends in demographics, lifestyles, attitudes, and personal values among the general population are of particular concern for consumer product manufacturers for. Changes in the birth rate, ageing, shifting ethnic and geographic compositions, and the increased availability of home technology are all significant factors. Understanding lifestyle trends is also important for industrial product industries. Since the demand for industrial products is often derived demand (i.e., generated ultimately by consumers), changes in consumer product sales in turn affect demand for the product. For example, when the number of TV-sets per household increases, so does the consumption of energy increase.

2.5.5 Regulatory

Government and other agencies affect industry attractiveness through regulations, for example: environmental, labour and safety laws, laws concerning foreign direct investment, testing and labelling requirements, local content regulations, and depreciation regulations. Over time some industries have become less attractive because laws have restricted their abilities to market or raise the overall cost of doing business.

2.5.6 Political

An important environmental consideration is the industry's sensitivity to political factors. Figure 4 conceptualises the sources of political risk, the groups through which political risk can be generated, and the political problem's effect on the operation of the business.

Figure 4: Conceptualising Political Risks

Sources of Political Risk	Groups through Which Political Risk Can Be Generated	Effects on International Business Operations
• Competing political philosophies (nationalism, socialism, communism) • Social unrest and disorder • Vested interest of local business groups • Recent and impending political independence • Armed conflicts and internal rebellions for political power • New international alliances	• Government in power and its operating agencies • Parliamentary opposition groups • Non-parliamentary opposition groups (guerrilla movements working within or outside country) • Non-organised common interest groups: students, workers, peasants, minorities, etc. • Foreign governments or intergovernmental agencies such as the EU • Foreign governments willing to enter into armed conflict or to support internal rebellion	• Confiscation: loss of assets without compensation • Expropriation with compensation: loss of freedom to operate • Operational restrictions: market shares, product characteristics, employment policies, locally shared ownership, and so on • Loss of transfer freedom: financial (for example: dividends, interest payments, goods, personnel, or ownership rights) • Breaches or unilateral revisions in contracts and agreements • Discrimination such as taxes or compulsory subcontracting • Damage to property or personnel from riots, insurrections, revolutions, and wars

2.5.7 Environmental factors summary

In this section, major factors in the environment related to an industry and its attractiveness were identified. Important influences on the long-term prospects for an industry lie outside its control. Environmental data can not only be used to assess an industry's future health, it also can and should be used to plan new products and/or processes and product and/or process improvements.

In the literature some instruments for the determination of advantageous environmental situations on foreign markets have been developed. The best known methods are:

- Checklists
- Scoring models
- Analysis of the utility value
- Factor analysis combined with cluster analysis

The more common model is the Operation Risk Index (ORI) – a scoring model. The ORI consists of the following factors:

- Political stability
- Attitude towards foreign investors and revenues
- Nationalisation
- Currency devaluation
- Balance of payment
- Bureaucracy
- Economic growth
- Currency convertibility
- Possibility to put through contracts
- Labour costs and productivity
- Availability of experts
- Communication and transport
- Local management and partners
- Availability of short-term credits and
- Long-term credits and capital resources.

The ORI mainly was developed to facilitate the decision process for western nations.

3 CUSTOMER ANALYSIS

The second type of analysis to develop is a customer analysis; in fact a marketing strategy development has at its core understanding customers. Customer analysis includes systematically, who the customers are, how they can be described, and how they can be grouped.

3.1 Characteristics of the customer

3.1.1 Who Buys And Uses The Product

For most industrial goods and many consumer goods, the "who" must be broken into who buys it, and who uses it (the ultimate consumer), identities which may be widely different.

3.1.2 Consumer goods

- ***Demographics***: age, sex, family size, and stage in the life cycle (number and age of children), geographic variables (region, city size, climate).
- ***Socio-economics:*** income, education, occupation, social class, housing types.
- ***Lifestyles and values:*** lifestyles basically represent an evolution from general personality variables to attitudes and behaviours more closely related to consumption of goods and services. Generally, they fall into three categories: activities (cooking, sports, and so on), interests, and opinions (concerning environmental protections etc.).

3.1.3 Industrial goods

Industrial goods can be segmented using the same types of variables as consumer goods. For industrial goods, the focus has been on firm characteristics such as size of company (e.g., number of employees), industry, and location, which are the logical equivalent of demographics and socio-economic variables such as sales. In many countries as basis for industrial segmentation a "Standard Industrial Classification" (SIC) coding system exists.

3.1.4 What they buy

What customers do falls into two basic groupings: what they purchase in the product category, and what they do with it. Concerning what they purchase within the product category, the two major variables are the amount (usage rate) of the category and which brands/products/services are purchased. Order size and frequency of use are also employed as segmenting variables.
For industrial and consumer goods, analysis of what competing products they currently use provides a useful basis for segmentation.
Another way of looking at the "what" question is to see what they are doing with the product.
One basic set of distinctions is:

- Customer/final users.
- Industrial customers, who incorporate our product in one or more products they make.
- Resellers, who simply mark up and resell our product.

The usage situation is crucial to understanding customers. This includes both where they use it and how they use it, which may or may not be related to why they originally bought it.

3.1.5 Where they buy it

Purchase location is also a very important basis for analysis. Where they actually make the purchase has a tendency to change over time. New products are generally first purchased through speciality outlets, but as the products become better known they tend to be purchased more often through mass merchandisers.

3.1.6 When they buy

When they buy encompasses time of year (seasonality), time of month, and even, potentially, time of day. "When" can also include when they buy in terms of sales or price breaks and rebates.

3.1.7 How they choose

The process by which customers buy can and should be described in several ways. First, the people involved, both formally and informally, should be identified. We can specify five different buying roles applicable to both consumer and industrial product purchasing decisions:

1. Initiator (identifies the need for the product)
2. Influencer (has informational or preference input to the decision)
3. Decider (makes the final decision through budget authorisation)
4. Purchaser (makes the actual purchase)
5. User

As indicated previously, the same person or different persons could potentially occupy each role. The different roles provide a basis for segmenting customers within a particular family or company.

A useful distinction in how customers buy is among (1) planned, (2) experienced, (3) impulse, and (4) emergency purchases. And a final way to describe how customers buy is in terms of information sources used - Consumer Reports, talk to sales people, get recommendations from friends, examine the product in stores, and/or observe the behaviour of experts.

3.1.8 Why they prefer a product: Customer Value

Assuming customers are at least thinking about a choice, and then it is useful to understand the basis of customer value. The concept of customer value is simple: "customer value is what a product is worth to the customer". It depends on the benefits offered (from the customer's point of view) and costs involved (price, hassle in purchasing, etc.) Knowing the value customers place on a product makes it much easier to make key decisions, such as setting price.

3.1.9 Manifestations on Customer Value

- ***Price.*** Price is the company's assessment of the product's value.
- ***Price sensitivity***. A product whose sales stay constant when prices increase generally is of greater value than the price.
- ***Complaints and compliments.*** The number of complaints and/or compliments received by a company indicates the product's value.
- ***Worth-of-mouth.*** Although hard to measure, worth-of-mouth comments provide a useful subjective assessment of a product's value.
- ***Margin/profit contribution.*** Generally higher margins indicate semi-monopoly positions and, therefore, higher relative value.
- ***Total sales in value.*** Total sales provide an aggregate measure of the value of a product as assessed by the market.
- ***Competitive activity***. Competitive activity such as new product introductions suggests the gap between customer value and company costs is sufficiently large to allow for profits even when more companies divide the difference.
- ***Repeat purchase rate.*** High loyalty indicates high brand value.

3.1.10 Assessing the value of the product category

There are many ways to estimate the value of a product category. The method presented here is basically an armchair/think-about-it approach that requires the following four steps.

- ***Determining the uses:*** Determine the present and potential uses to which a particular product category may be put. This is usually done by combination of logical analysis (e.g., asking people involved with the product or a creative individual what the product can do) plus customer date in the form of surveys of present users and focus groups.
- ***Estimating the importance of the uses:*** Survey methods are often used that ask the importance question, another useful measure of importance is the total sales potential of products that serve this use.
- ***Listing the competing product categories:*** Both present and potential, that service each of the uses. Competitive products can be determined from published sources, sales records, introspection, or surveys.

- ***Determining the relative effectiveness of the product category in each usage situation:*** Besides introspection and expert opinion, a survey can address this.

The value of the product category (VPC) is then estimated as the sum over all uses of importance of the use times the relative effectiveness of the product category:

$$VPC = \sum \text{(Importance)} \times \text{(Relative Effectiveness)}$$

3.1.11 Assessing the value of the brand/product/service:

Assessing the total value of a brand can be done indirectly. A high value brand has: high share, high repeat purchase rate, low elasticity with respect to price, and limited competitive brand shopping. A direct estimation of the total value of a brand can be conducted through a conjoint analysis.

3.2 Will the product will be bought again

3.2.1 Satisfaction

Actually providing quality in order to satisfy customers and retain them as future customers is simply a restatement of the basic principle of marketing, to create and maintain customers. Quality is ultimately measured in terms of customer satisfaction. The direct measurement of satisfaction has evolved to consider several aspects:

1. Expectations of performance/quality
2. Perceived performance/quality
3. The gap between expectations and performance

Indirect measures of satisfaction include worth-of-mouth comments, complaints, and perhaps most importantly repeat purchase. Measures of intended or actual repeat purchasing provide a useful way to simultaneously measure satisfaction and its impact.

3.2.2 Intentions

Intentions are imprecise predictors of future purchase, still they provide early signs of future sales.

3.3 Sensitivity to elements of the marketing mix

Why consumers buy also includes response to elements of the marketing mix. In addition to the product itself, sensitivity to and preference for prices (and means of payment), distribution and availability, advertising, promotion, and service are fundamental aspects of a market.

Methods for assessing sensitivity include:

1. ***Expert judgement,*** using the knowledge of managers, the sales force, etc.
2. ***Customer survey-based methods,*** including both direct questioning (e.g., “How important is...?”) and more subtle approaches such as conjoint analysis.
3. ***Experiments,*** including both controlled settings and in actual markets.
4. ***Analysis of past data,*** comparing results across markets, or where individual customer record data are available (e.g., scanner data) at the individual level. Such analysis often uses techniques such as regression analysis to predict

sales as a function of mix elements or logit analysis (basically a type of regression) to assess the impact of mix elements on market share or individual choice probabilities.

4 ANALYSIS OF COMPANY SITUATION

If a company is interested in establishing a certain kind of collaboration with a foreign enterprise (an acquisition or a joint venture), it must conducts an analysis of this enterprise. First of all, it has to be analysed if the company has at least one Competitive Advantage, which could be transferred to other markets. Competitive advantages can be:

- Advantages in production technology
- Advantages in process technology
- Advantages in management technology
- Advantages in raw material supply
- Advantages in acquisition of other resources like human or financial capital
- Advantages in the home market
- Advantages in the location
- Advantages in capacity utilisation

It is not necessary (and probably not possible) for one company to possess advantages in all those fields, but the question is: Has the company the competitive advantage, which is relevant for the foreign market? The internationalisation potential of a company can be determined with the help of a "Scoring Model". Starting point if using a scoring model is the question: How does the competitive situation of the company look like?

Figure 5: Scoring Model For The Evaluation Of Competitive Advantages

ADVANTAGES IN:	**-2**	**-1**	**0**	**1**	**2**
product technology					
process technology					
management technology					
raw material provision					
acquisition of other resources					
the home market					
the location					
capacity utilisation					

↑ Profile 1 ↑ Profile 2

This figure shows two extremes: Profile 1 shows a company, which has in all factors great competitive disadvantages, whilst profile 2 shows the situation of a company, which has in all areas great advantages.

If the competitive advantage of one company is not sufficient for going into a foreign market, a co-operation partner must be found which can supply the missing, but necessary, attributes.

5 MODES OF MARKET ENTRY

The specific situation in a country can restrict the choice between different types of foreign activity, which can be implemented. In general three types of market-entry can be distinguished:

- Exporting (direct and indirect)
- Licensing and franchising
- Foreign Direct Investment (in the form of wholly owned enterprises or different kind of joint ventures)

Selecting a suitable entry mode, or strategy, for doing business in foreign country is a decision European company must make before entering the market. Companies have a number of choices of entry mode depending on their prior international experience, financial and managerial resources, and long and short term goals. These choices include exporting products or technology from Europe, using licensing or franchising which is often called contractual joint venture, equity joint ventures, and wholly owned modes such as greenfield or acquisition.

No one entry strategy is suitable to all European companies because different companies may have different goals for doing business with foreign country, resource basis (both financial and managerial) available, international business experience and acceptable levels of risks. Any company, regardless of the nationality, has to look at its own goals, resources, strengths and weakness and how much risk it is willing to take in deciding which entry strategy to use for doing business. Companies with limited resources and international business experience should start with export strategy such as national-based salespersons and progress cautiously in the direction of equity joint ventures.

In the next paragraphs, we'll explain the different kind of strategies, looking at the strengths and weaknesses points of everyone, to finally demonstrate that Joint Ventures are the most suitable and recommended form of investment.

5.1 Export

Indirect Exporting refers to the use of home country agencies (trading companies, export management firms) to get the product to the foreign market. Direct Exporting by contrast, means the firm itself contacts the buyers abroad, be they independent agents and distributors or the firm's own subsidiaries.

Companies that use Indirect Exporting to solicit export contracts from foreign country like African ones usually have designated individuals that travel to and in the country for extended periods. These people work as representatives of their company to initiate business relationships and contracts with the people in the country.

The advantage of this strategy is that it is low risk: in fact, are often used by companies that seek a relatively less risky method of doing business in a foreign market seen to be unstable and difficult. Export strategies put at risk only a limited amount of product, samples or advertising dollars if a company decides to beat a hasty retreat. The company does not make a capital investment abroad and can pull out at any point without huge capital write-off. At worst, samples and advertising costs could be lost. In addition, the company also has full control over its products and technology because the technology and means of production remain in the country that exports and only the products are exported to Africa in our case.

There is a down-side to exporting. First, most exporters are unwilling to stay beyond signing the contract. People responsible to engage relationship with foreign marketers usually have tight schedules which often leave little or no room for socializing and building relationship. In addition, because the representatives travel back and forth, the company that exports may be perceived not to have a permanent presence in the country. By not being there in the market, the company may not feel the changing pulse of the market thus insulated from some business opportunities.

Second, the African partners may feel that the foreign company is not committed to the market, because the company can come and go at any point. Third, the foreign company's representatives are not available at all times, if they have any questions or concerns.

Because of these drawbacks, many companies wishful to export in the foreign market use local based distributors. Most distributors use one of two forms to market products. The distributor could market the products through product catalogues or other advertising that is distributed to the target market. The distributor could also use local sales people to sell the foreign products or technology to the local customers. Some distributors set up a national office. In this case, the distributor's sales people travel around the country. Other, perhaps larger and well established distributors have set up regional offices to serve the local market.

The main advantage of the export strategy seems to be its low cost because the main cost of using this strategy comes from marketing, selling and related overheads that support the efforts. This strategy allows the European company to test and possibly establish a foot-hold in the local market without being exposed to the large amount of uncertainty of doing business in Africa. The main criticisms of this strategy could come from African partners that could be less keen on doing business with foreign companies if they are only interested in selling them their goods and will not find any benefit to only import. Importation not only creates dependency on foreign companies but adds to sustainable benefits to the local countries. It is not viable over the long term - the African country may not have the hard currency to buy from foreign companies if it does not export and earn some hard currency". This seems to be the most important problems: products manufactured with European technologies and resources are too costly for African people, and could hardly be exported in Africa.

5.2 Licensing and Franchising

Licensing involves offering a foreign company the rights to use the firm’s proprietary technology and other know-how, usually in return for a fee plus a royalty on revenues. Among licensing modes, Franchising has become a well know alternative for foreign market entry with services. In franchising, the firm provides technological expertise to the reseller abroad and also helps with the management of the franchise and often with the capital investment that is needed for start-up. The other licensing options are all similar, differing mainly in the type of know-how transmitted. Turnkey contracts provide for the construction of whole plants and often the training of personnel capable of running the operations. Contract Manufacture is hiring a firm to produce a pre-specified product.

The placing of technology in form of licensing allows market entry. The firm can gain information about the foreign market and profit from the fees from technology or know-how transfer.

This entry mode is often used by smaller companies that do not have the financial or human resources to enter a foreign market. A company is able to finance its entry into a foreign market using the financial and human resources of the licensee.

5.3 Foreign Direct Investment

The aim of foreign direct investment is to have immediate influence on the management of the capital-receiving enterprise. The term of capital includes not only the transfer of money, but also the transfer of human resources, know-how, and technical equipment.

Direct investments are investments of a firm, which are conducted in a certain country, but they are controlled by citizens of another country. By way of contrast, the definition of the US Department of Commerce: Direct investment is every capital investment ≥ 10%.

Direct investments can occur in different forms:

- Construction of a wholly owned manufacturing subsidiary
- Acquisition of a foreign company as 100% subsidiary
- Acquisition of a minority/majority of a foreign company
- Co-operation with a national or foreign company in the form of a Joint Venture or strategic alliance.

5.3.1 Description of a 'Wholly Foreign Owned Enterprise'

Wholly owned entry modes include the development of subsidiaries using a Greenfield approach, or through acquisition of existing companies. These strategies transfer capital, staff and/or technology into African country so that a product may be developed, manufactured, marketed, sold and/or serviced from a wholly owned African location. Some companies may transfer all these functions while others may have a simple sales office.

Wholly foreign owned enterprises are permitted to register in cases where at least half of their annual output is exported or if the nature of their operations relies heavily on advanced technology and the application of this high technology is beneficial to the African country. Approval to establish a wholly foreign owned enterprise is granted much more sparingly when compared to joint ventures.

As a local legal entity they may sign separate contracts with the appropriate government authorities or local business entities to acquire land use rights, rent buildings, and receive utility services. Wholly foreign owned enterprises enjoy exclusive management control of their business activities and have autonomy in their operation and management with less interference from the local government.

But these positive points are counterbalanced by some critical factors: the first is that, because there is no local partner to guide the project through the approval process and through the other regulatory issues associated with construction and operation of the enterprise, the logistics of establishing a wholly foreign owned enterprise can be difficult and costly. Enterprises must establish relationships and contact with the local actors relying only on their own resources. In the same way, enterprises must have a perfect knowledge of the legislation and of the procedures to be able to conduct their business. A wholly foreign owned enterprise is considered a local legal entity and must abide by all local laws. They must employ local labour in accordance with local and central government labour laws and are encouraged to establish trade unions (but not required to do so). So, the independence offered to the foreign investor is often outweighed by the lack of direct links to the domestic economy.

Traditionally the wholly foreign owned enterprise has rarely been the chosen method. For all the previous mentioned reasons, European enterprises that want to use this method to penetrate in the African market must have years of business experience in this continent, and must have a deep knowledge of the local usages and customs. An enterprise that wants to penetrate the market with this strategy should start with export, franchising or licensing strategies; through these practices, the enterprise can deep its knowledge of the local market with minor risks.

5.4 Joint Ventures

Joint Ventures are collaborations between companies, sometimes competitors, to exchange or share some value activities". Examples include Joint R&D, shared manufacturing, and distribution alliances. Joint Ventures involve capital investment and the creation of a new corporate unit jointly with a foreign partner.
Joint Ventures have long been common especially in countries such as India where government mandates participation by locals and in countries such as Japan where market access is difficult for outsiders.
Joint Ventures are type of strategic alliance in which partners create an equity-based new unit. The Joint Venture involves the transfer of capital, manpower, and usually some technology from the foreign partner to an existing local firm, whose main contribution tends to be expertise and understanding of the local market.

This way of collaboration will be developed more in details in the following chapter.

6 JOINT VENTURES

6.1 Advantages and disadvantages of Joint Ventures

Advantages	*Inconvenient*
• Synergy effects can be achieved through the utilisation of complementary know-how – e.g., technology, management, country-specific know-how	• Dependence on co-operation partners
• Existing networks can be used - markets are reached without a long Build-Up of relationships in channels - to government, customers, suppliers etc.	• Transaction costs (preparation, arrangements, control and adaptation costs)
• Risk distribution ("pooling" of risk), lessened risk exposure	• Risk of losing control of the firm's know how
• Distribution of costs (above all concerning fixed costs)	• Concerns over intellectual property protection: there is little protection for foreign technology
• Possibility to increase the number of simultaneous projects	• Obstruction of own initiative/creativity

6.2 Forms of Joint Ventures

There are two types of joint ventures - Equity Joint Ventures and Cooperative Joint Ventures.

6.2.1 Equity Joint Venture

Is the older type, which provides less flexibility. An Equity Joint Venture always takes the form of a limited liability company. This shields the personal property and wealth of the responsible individuals from corporate loss. The allocation of profits is the most significant difference between Equity Joint Ventures and Cooperative Joint Ventures. In Equity Joint Ventures, the ratio of capital contributions made by the partners determines how profits are allocated. If one party contributes 40% of the total capital investment, they will receive 40% of total profits. Most manufacturers prefer Equity Joint Ventures as an investment vehicle. Before making a decision which type of joint venture to choose, the purpose of the investment must be clear.

6.2.2 Cooperative joint ventures:

Cooperative Joint Ventures offer more flexibility. They can be organized either as a limited liability company or as a non-legal person, in which the partners are subject to unlimited liability and thus entirely liable for any losses the joint venture may incur. Most Cooperative Joint Ventures are established as limited liability companies. Unlike Equity Joint Ventures, Cooperative Joint Ventures allow for profits to be allocated according to the partners' discretion. One party may recover its investment through an accelerated repayment structure, and the other party may become the owner of the joint venture's assets after termination of the joint venture.

6.3 Acquisition of an existing plant

A company can consider the acquisition of an existing company for the Joint Venture plant.

Advantages	***Inconvenient***
• Speed of penetration is high: An existing plant will already have a product line to be exploited, a distribution and dealer network - the company can get on with marketing its new product(s) in conjunction with the existing line.	• Existing product line and the new products be introduced might not be compatible
• Low investment costs	• Prunings and adjustments that have to be made require re-educating the working force
	• Burden from former operation
	• Long-lasting contracts for the employees and management, which cannot be cancelled

6.4 Greenfield Venture

A Greenfield Venture is a Joint Venture, which is set up on the so-called “Greenfield”. It means that instead of the adaptation of an existing plant, a completely new plant is constructed.

Advantages	***Inconvenient***
• Newest technology	• High investment costs
• New management	• Long period for the set up
• No burdens from former operations (obsolete fixed assets, liabilities, mortgage on real estate etc.)	• Connections to official institutions must be build up
• New, motivated manpower, which meets the specific needs, can be hired	• No experience of the management and labour force
	• Long period until the first revenues can be gained

6.5 Identification of an appropriate partner

The key decision in JVs is the selection of a partner. Very few hard and fast rules apply here, apart from the obvious one of picking a partner who is willing and able to share company resources and skills and whose skills complement those of the partner.

First of all the term “appropriate partner” has to be specified. The target of co-operations is to gain synergies. The partner should supply resources – technological know-how, know-how about the market (country-specific information), human and financial resources - the company does not own itself, but which are necessary for the optimised entrance into the new market. Normally a “win-win” situation should result, that means, that every participating company will gain advantages out of this co-operation.

The analysis of potential partners involves study of individual companies in an industry. It is necessary to analyse the capabilities of potential partners.

6.5.1 General qualifications

Above all standing of the potential partner among experts res. his social network, which is the base for interaction between social, political and economic institution, as well as the location.

6.5.2 Economics

Here the question in the centre of interest is how the co-operation partner is leaded financial. The lack of available financial resources clearly acts as a constraint to being an effective partner. Firm level financial ratios are key pieces of information.

6.5.3 Management

The ability of managers to develop strategies, to observe the market, to encourage research and development, to negotiate with governmental organisations, trade unions etc. provide information about the capability of potential partners to meet future aims. Another important aspect of potential partner analysis focuses on the processes and procedures used. A major trend has been the development of quality programs such as Total Quality Management (TQM).
The ability to manage is also related to the quality of a firms' new product and/or process development efforts. A firm with a high ability to develop new products/processes is in the long run a more appropriate partner than a company that has not been innovative. The use of such procedures as TQM generally improves product and/or process design capabilities.
The technical capabilities of potential Joint Venture partners can be analysed by using the following framework:

- Technology selection or specialisation
- Level of competence
- Sources of capability: internal versus external
- R&D investment level
- R&D organisation and policies

Another factor in this category is the production capabilities of the firms. For a service business, this category might be termed ability to deliver the service. The aspect of ability to produce involves the productive capacity, the quality, and commitment of suppliers of crucial parts and services.

6.5.4 Distribution and marketing

As the knowledge and possibilities the local partner can bring in this field of the partnership determine the success of a JV substantially, this point is very important. The market share of the potential partner should be checked, as well as their marketing strategy - how aggressive or inventive are the firms in marketing their products? Do they have a strong presence in key distribution channels? Figure 6 summarises specific bits of information that would be useful to know about potential partners.

Figure 6: Qualification Profile of Potential Partners

Characteristics	**+ +**	**+**	**+ / -**	**-**
General Qualification				
Standing				
- in social network				
- among experts				
Ability to communicate				
Trustworthiness				
Entrepreneurial consciousness				
Strategic conception				
Location				
Economical				
Ability to finance				
Turnover				
Profit before taxation				
Financial management				
Cost management				
Company structure				
Ability to create value increase				
Controlling Management				
Management				
Quality Management				
Productivity				
Leadership qualification of leading management				
Qualification of middle management				
Education level of technical personnel				
Age structure of labour force				
Ability to innovate				
Human Resource Connection				
Working discipline				
Waste control				
Organisation				
Logistics				
Procurement				
Characteristics	**+ +**	**+**	**+ / -**	**-**
Distribution and Marketing				
Marketing knowledge				
Market share				
Sales planning				
Product management				
Market knowledge				
Distribution infrastructure				
After sales and clients service				

6.6 Identification of the optimum location

On principle, there are four major elements, which play an important role for the identification of the optimum location in a country (Porter, 1991).

6.6.1 Factor conditions

In general four different factors can be distinguished: human, physical, know-how and capital resources and infrastructure.
These factors can be divided into Basic Factors and Advanced Factors, whereby the later mentioned play an important role for the future. Basic factors are: natural resources (quantity, quality, costs), human capital (education and qualification of man power, wages), geographic conditions and infrastructure (telecommunication, transport, energy supply – availability, costs, quality). Technology is an example for advanced factors.
Additionally, General and Special Factors can be distinguished. General factors are e.g., infrastructure, to which all industries have access to, supply with outside capital or motivated manpower with university degrees. Special factors can be specialists, an infrastructure with special features etc.

6.6.2 Demand conditions

Two features of demand are important:
- Structure and nature of consumer needs: Demand of consumers on quantity and quality of products or services, availability, utility, and the price-performance ratio.
- Size and growth structure: the bigger the market, the easier is it, to gain economies of scale and/or learning-curve-effects and the break even point can be reached faster.

6.6.3 Supporting and related branches

Suppliers, who are able to deliver high quality products, in sufficient quantities, at moderate costs in time, have positive effects on the efficiency of companies. A high market intern competition in the branches of suppliers has positive effects on the above-mentioned factors.
Supporting branches can also be universities, research institutes, and other institutions.

6.6.4 Competition intensity

The last point can be described through the number, structure and strategy of competing companies. It has to be examined, how firms developed, how they are organised and lead. For example, the behaviour of management and employees, trade policy or anti-trust laws play important roles.
The level of competition is of great importance. If there is a high competitive market, firms are forced to engage in R&D, to lower the costs and to produce efficiently for staying competitive on the market. On the other side, if a company is a quasi-monopoly, it has a strong position on the market, what makes the entry more difficult.

6.7 Profitability analysis

The profitability analysis of foreign activities depends on quantitative and qualitative factors. Quantitative factors can be analysed with the aid of the Capital Value. The not calculable qualitative factors, which have influence on the type of foreign activity, can be judged by means of a Pattern Analysis.

6.7.1 Quantitative analysis - Capital Value

With the help of the capital value, it can be assessed, if a certain form of foreign activity is profitable (economical).

6.7.1.1 The Capital Value in general

In general, the capital value can be calculated as follows:

$$C_S = -\sum_{t=0}^{T} \frac{I_{s,t}}{(1+i)^t} + \sum_{t=1}^{T} \frac{E_{s,t}}{(1+i)^t} + \frac{L_S}{(1+i)^T}$$

C_s: Capital value for organisation form s
$I_{s,t}$: Necessary investment for organisation form s in period t
$E_{s,t}$: Payment surplus in period t for organisation form s
T: Planning period
L_s: Liquidation revenue from organisation form s at the end of planning period T
i: Interest on capital rate

6.7.1.2 Capital Value for foreign direct investment

Six categories of payment surplus from foreign investment, which could be relevant for the determination of the capital value:

a. Payment surplus from continuous business

The following considerations come from the standard theory for international companies (Busse von Colbe, W./Ordelheide, D., 1984, p. 37) and assume, that retained profits must be considered in the evaluation of the capital value. As the parts of the Cash Flow, produced abroad, which represent no profit, as for example depreciation, cannot be transferred easily, they should be left out of consideration.

b. Additional profit from the acquisition of an existing company through synergy-effects

Several synergy-effects can arise if a foreign company is bought or an co-operation contracted. Synergy-effects must be converted into national currency, and such which emerge in the home country. The whole tax burden is also taking under consideration national and foreign taxes. Further it is assumed that the purchase price for the foreign company is paid in foreign currency so that it must be converted with the currency exchange rate.

c. Additional payment surplus from exports of pre-material and/or other products

Three different types of export goods must be distinguished:

- Capital goods (items of equipment)
- Pre-material
- Finished products

Export Revenue can emerge through the export of pre-material of the national company to the foreign subsidiary. Taking under consideration the **Export of End Products**, two domains have to be distinguished: end products, which shall be now manufactured abroad, and products, which are sold complementary to those mentioned above through the foreign company. If end products, which up to know have been manufactured in the home country, are manufactured now abroad, this fact must be taken into account. Assuming that the now free capacities cannot be used further in the home country, the decrease of exports of these displaced products must be taken into account as negative component.

In general it is assumed, that in the domestic country free capacities are available, that the returns lead to payments in the same year and that the variable costs in the same year lead to disbursement. The following restrictions have to be also taken under consideration:

- The import of capital goods can be limited
- Import restriction for pre-material supply can exist abroad
- Governmental fixed exchange rates could exist
- Price controls (maximum and minimum price) could exist

d. Additional payment surplus from technology contracts with foreign companies

Regardless which international technology contract, for the evaluation of the capital value of payment surplus, the height of the technology fee must be determined.
The value of a technology for the technology taker depends on the liberty, which is granted to him for the utilisation of the new technology. For the determination of payment surpluses the following restrictions have to be taken into consideration:

- **Restrictions concerning the contractual territory** - it has to be distinguished between restrictions which refer to the country of the technology taker and such, which refer to foreign countries from the point of view of the technology taker (e.g., export ban). A geographic restriction for the export of products, for which a licence agreement has been concluded, emerges. The restriction can limit the amount of exported goods and the price.
- **Restrictions concerning the home country of the technology taker** - they must be examined regarding to anti-trust laws. If the restrictions are outlaw the enterprise can try to get an exemption from the anti-trust-office. For international technology contracts it is occasionally possible to find clauses, which are equal to price fixation (e.g., vertical price fixing clause).
- In technology transfer agreements often **Purchase Obligations** have to be undertaken. According to them the technology taker has to obtain raw material, accessories, fixtures, intermediate products, or a equipment from the technology provider.
- **Grant-Back-Clause** - if the technology taker succeeds in improving a licensed process, it can be agreed that he has to transfer the improvement to the technology provider.
- For the protection of his interests the technology provider can claim in the technology transfer agreement that the partner agrees upon a **Competition Prohibition**. Two types of prohibition have to be distinguished: first the prohibition of production, utilisation and distribution of rival products and in the second place the prohibition of technology contract agreements referring to the same technical contractual territory.
- It also can be arranged, that the licence taker is allowed to sell the licensed products only through the licence provider or through certain distributors (the individual case has to be examined concerning anti-trust-legislation).

e. Additional payment surplus and/or disbursement decrease caused by the import of products from the foreign corporation

Besides export profits domestic companies can, when involved into foreign direct investment, gain import profits for example that initial products can be obtained cheaper as from other foreign companies or on the domestic market or that the end products of the foreign subsidiary are distributed through the domestic company on the home market. The capital value of import profits from foreign investment gained from supply with cheaper initial products.

f. Existing payment surplus, which would be lost, if no foreign direct investment is realised.

Foreign direct investment can become necessary for a company. A direct investment can be carried out for maintaining competitiveness because of costs or provision reasons. In such a case the company has to calculate, for assessing the profitability of the FDI (Foreign Direct Investment), the payment surplus, which would be lost, if no FDI is carried out.

6.7.2 Qualitative analysis

For the final decision - if the company goes abroad, which type of co-operation is chosen, which co-operation partner etc.,- an analysis of the qualitative factors is needed. These factors can be subdivided into:

6.7.2.1 Country-specific qualitative factors:

Can be derived from the analysis of the country-situation, therefore concentrates mainly on political, economical, legal and social risk-factors.

6.7.2.2 Product-specific qualitative factors:

An example for a product specific risk-factor is “needed observance of secrecy” concerning the product technology, process technology etc.

6.7.2.3 Strategy-specific qualitative factors:

Can be derived from the general company policy of the partners, e.g., attitude of the management towards social groups like trade unions, actual company situation (financial shortage, free capacities) and determination of priority markets.

6.7.3 Model for the combination of quantitative and qualitative analysis

Joint Ventures is based upon the separation of decision processes in a profitability analysis and the analysis of qualitative factors with the help of the Pattern Analysis.
After a combination of alternative forms of Joint Ventures, profitability criteria are developed and an analysis of qualitative factors in form of a Pattern-Analysis is concluded. Therewith for each form of co-operation a value of profitability, measured against the capital value “C” and the significance of qualitative factors, measured against the relevance number “R”. Following, the alternative forms of Joint Ventures are transferred in a diagram (C-R-Diagram), which ordinate states for profitability and which abscissa stands for the relevance number. All potential forms of Joint Venture, which compared to the others have not only a lower C- but also a lower R-value, are dominated and will be eliminated.

After the analysis of the C-R-Diagram, only such Joint-Venture organisation types remain, which have either a higher C-value or a higher R-value as the other alternatives. This organisation types now must be compared individually against each other. As the relevance numbers and results of the profitability analysis have different dimensions an immediate comparison is not possible.

6.8 Negotiations with the Joint Venture Partner

Four sequential stages that characterise information exchange in most business negotiations.

6.8.1 Nontask sounding:

This is an initial period when the conversation consists mainly of small talk, designed to get the partners to know each other better.

6.8.2 Task-related exchange of information:

An extended period when the main issues are brought out, facts are presented, and positions clarified.

6.8.3 Persuasion:

This is the stage when there is further explanation and elaboration of positions, and questioning of the other side's evidence.

6.8.4 Concessions and agreements:

Toward the end of most negotiations is a period when mutual concessions might be made, when there is some yielding of fixed positions in order to reach an agreement.

In most negotiations, knowing something about the cultural background of the opposite partner is considered a must. The length and the importance of the stages can differ between two countries. The possibility of discrepancies between what the manager thinks (s)he is communicating and what is actually received by the other party must be taken in consideration.

It shall always be kept in mind that the relationship between the two contract partners should not be a zero-sum game, but a win-win proposition.

6.9 Governmental Agreement

When it comes to government regulations of business - involving questions ranging from "Who can start a business?" to "Can free product samples be sent in the mail?" - the foreign firm can do little but to adapt to them. Some assistance from the home government might be available from services of government offices (foreign ministry, chamber of foreign trade, consulate abroad), or from supra-national authorities like the European Commission or WTO.

As a member of a Joint Venture or some other collaborative alliances, the native partner can be assigned the task of carrying out negotiations with government authorities and local regulators. The most pressing problem, getting building codes, retail regulations, or negotiate extra-conditions, like subventions, special conditions concerning environmental and labour regulations, the ownership structure requires a strong local presence. Once in, the firm became an insider with claims on the same local protection as domestic firms.

Negotiations with the government play an important role, especially if governments' guarantee is a necessary condition, which must fulfill when applying for certain kinds of financial support. It would give a public character to the project. For instance the World Bank Group demands the guarantee from government.
Depending on the country enough time must be included in the time table for the negotiation phase. In some cultures it is necessary to build up long-term relationships before it is possible to come to any agreement. In addition, it has to be taken into consideration that the project has to be partially changed; adaptations have to be made to fulfil country-specific conditions or to get support from the government of the host country.

6.10 International Financial Management

Compared to the national financial management, the international financial management has to consider a vastly heterogeneous field. There from additional chances and risks emerge and connected therewith arises the necessity to adapt the international financial policy to national circumstances.
Foreign subsidiaries are subject to special legal and economic regulations from their local position. The particular company law influences for example the equipment with own capital, the rendering of accounts, the distribution of profits and the rights of shareholders. Besides it, in order of the raising of capital, different local financing regulations and the performance of local capital markets have to be considered.
Problems, which arise because of missing or only insufficient equipped capital markets, make an international financial management necessary just the same way as local foreign exchange and/or credit restrictions. An international financial management offers simultaneously the chance to distribute the risk, to benefit from currency and interest rate variations, as well as taxation advantages and subventions.

6.10.1 Raising of capital

International companies can take advantage of several financing possibilities. They have access to national and international financial markets. The decision which mode of financing is chosen, depends on the efficiency of the capital markets (e.g., in less-developed countries they are less efficient), possible restrictions for the turnover of capital, differences in interest rates and taxes, expectancy of inflation development, and currency risks (e.g., in countries with high inflation rates).
Additionally they have because of the involvement in different countries abroad in most cases easier access to foreign local financial markets. They have the chance to receive governmental credits and/or credits with a reduced interest rate, as well as subventions and other financial supports, which are only given to local companies.

6.10.1.1 Financing on the foreign local market

Local financing capital can reduce transfer costs and risks as well as currency risks, and the integration of the subsidiary in the host country advances. Joint Ventures are advantageous in self-financing because the own capital resources of the foreign subsidiary is enforced through the corporation with a local partner. In addition the flexibility and sovereignty of the subsidiary in the host country will be enforced, because local creditors and own capital suppliers are interested in good earning and profits, respectively in a continued existence of the enterprise. However it must be taken into consideration, if self-financing abroad is conducted through the emission of shares or through the foundation of a Joint Venture, externs have influence on the management and a homogeneous company policy may be threatened.

6.10.1.2 Financing on the international market

International financial markets are hardly subject to national restrictions and regulations. As on this market exists strong competition, several new forms of financing emerged which in most cases allow a less cost-intensive financing, compared to the local capital or credit market. Several forms of loans are adapted to the needs of investors and borrowers. The following financing forms should be mentioned:

- Loans bearing fixed interest
- Zero-coupon loans
- Loans bearing variable interests
- Convertible loans
- Double currency loans, where the raising of capital as well as interest and amortisation rate are made in different currencies
- Revolving Underwriting Facilities, where the creditor has the right to claim flexibly the repeated emission of short-term loans
- Fixed rate credits
- Roll-over-credits

The foreign exchange rate risks can be reduced by, for example, Dual Currency Issues or Currency Option Bond.

Special problems occur for long-term capital raising in foreign currencies of countries with high interest rates, because of the fact, that besides a high exchange rate risk a high risk of interest rate changes exist. In order to avoid high capital costs if interest rates are sinking, a so-called “Escape-Clause” can be included into the loan-conditions.

In the area of short-term liquidity-securing, a company can become active on the Euro-Money-Market, where important international currencies are traded without national regimentation.

6.10.1.3 Financing with the help of Supra-National Organisations

Another source of capital is development banks as the World Bank, EBRD (European Bank for Reconstruction and Development), special investment programs of the European Community, or private investment funds.

6.10.1.4 Criteria for Financing Decisions:

Which kind of financing is best depends on the objectives of the company. For the subject profitability the height of financing costs is an important determinant. The financing costs depend on:

- Interest costs
- Commissions for financing institutes
- Taxes
- Costs for capital turnover
- Costs for currency risk

Companies try, considered from the profitability point of view, to finance in those countries, where the interest costs and the burden of taxation cause low financing costs.

Security is also taken into consideration – the interest change risk and exchange rate risk shall be covered as well as possible.
In addition the attempt to be independent influences the choice of the financing method. To avoid the obligation of information, decision restrictions, and the right of co-determination of others in business companies can disclaim certain financing methods abroad.

6.10.2 Capital Structure Policy

The term capital structure can be understood simplistically as relation own-/outside capital (static indebtedness grade). The capital structure has strong impact on the risk position, the credit-worthiness, the potential liquidity of a company, and the leverage-effect of the own capital profit.
Special problems concerning the capital structure policy arise in the case of Joint Ventures. An increase in the own capital through company outside, local own-capital is conducive to the integration in the host country; however the local partner can have other targets. Several points of view have taken into consideration when developing the capital structure.

6.10.2.1 Own capital quota and foreign risks

A low own capital quota is especially relevant for foreign subsidiaries, operating in countries with high political instability and high currency risk. Exists the threat of expropriation, or is capital transfer and/or revenue repatriation limited a low own-capital quota would be appropriate for reducing the risk.

6.10.2.2 Own capital quota and country-specific conditions

An adaptation of the capital structure to country-specific conditions often is explained by the argument that an autonomous credibility of the foreign subsidiary must be secured. Taxation and risk political considerations are further reasons why foreign subsidiaries have different own capital quotas. An increase of the own-capital quota results inevitably through capital turnover restrictions, if, for example, revenues cannot be transferred to the headquarter - in this case the own capital will increase automatically.

6.10.3 Organisation of international financial management

In the case of capital market transactions a central financial management can exploit international differences, gain increasing scale-revenues, realise synergy effects, and undertake an international compensation of risk and liquidity. But on the other side regional adaptations are necessary.
In particular capital turnover restrictions, lacking convertibility of currency, restrictions on local money and capital market, taxation as well as restrictions in owner ship structure make it necessary that international companies choose a structure, which allows an adequate relation between centralisation and decentralisation in the financial area. As a consequence financing corporations and project financing corporations can founded.

Financing Corporations take over the task to carry out cash management, foreign exchange management and raising of capital. Frequently, they are legal independent corporations, which in many cases are established in countries having a favourable legislation concerning foreign currency, private law and taxation (e.g., Cayman Islands, Jersey, Curaçao). With the establishment of financing corporations, firms try to increase their financial flexibility, to improve credit conditions world-wide as well as to take advantage of international capital market imperfections and taxation advantages.

Special cases are Project Financing Corporations. They are founded for particular large-scale projects. It is tried to reduce the risks connected to the project through the utilisation of adequate financing and contract arrangement techniques. For this purpose current interest- and redemption payments are made from the cash flow of the project and the project is offered to the investor as security. Project financing corporations are founded in most cases for the financing of energy and raw material supply, where in general long term sales contracts exist. Also project financing corporations are very often founded in tax haven res., Off-Shore-Financial centres to benefit from legal and taxation advantages.

6.11 The Joint Venture Contract

The effective formation of Joint Venture contracts is all over the World an important basic requirement for the economic success. Following the most important points are mentioned.

- Description of partners
- Applicable right
- Governmental agreement and registration of Joint Venture co-operation
- Target and business of Joint Venture
- Responsibilities of contract partners
- Credits
- Foreign Exchange Balancing
- Management
- Liability
- Duration and termination of JV
- Regulation of lawsuits

It is important that the JV contract is in accordance with the economic law of the host country, and that a contract adaptation clause is included, which makes it possible to adjust the contract to changing legal conditions.
Besides the economic and legal point of view, it is important that all co-operation partners agree absolutely to the contract content. In the long term, as experience shows, only equivalent partnerships, where all partners can take advantages from, can guarantee the necessary stability. If partners or even countries are cornered and they are indoctrinated with their own values and methods, this will lead to dissatisfaction. The aim of intercultural management has to be understanding and peace, because only the last mentioned one guarantees in the long run good business.

6.11.1 Organisation of foreign activities

6.11.1.1 Factors having influence on the organisation structure abroad

- **Socio-cultural factors**: like style of leadership, company philosophy, company culture, demographic structure, education, mentality, creativity, motivation and religion of employees, and the nationality of the JV partner.
- **Technical-economical factors**: for example, used technology, size of the Joint Venture, development status of the market.

- **Political-legal factors**: possible legal form, local control-requirements, and local influence on the management structure.

6.11.1.2 Efficiency requirements on the organisation

The efficiency of the subsidiary depends among other things on the capability of the foreign subsidiary to react flexible to changing national and international conditions. This subject can best be reached through the implementation of a simple, transparent organisation structure. It should be possible to reach synergy effects, and to overcome communication barriers that control, distribution of tasks and a mutual understanding of the different participants can be secured.

The organisation elements to be considered are:

- **Co-ordination:** to reach synergetic effects between headquarter and subsidiary, activities must be co-ordinated. The answer is: Which decisions should be centralised, which decentralised? Too much autonomy involves the danger of loosing synergy effects, too less autonomy can on the other side direct to inefficiency of the local company. The decentralisation of decisions has the advantage, that the Joint Venture company can develop a strategy which is oriented on local circumstances. A well-aimed product strategy, better allocation of resources, and a better identification of market chances on the foreign market can be reached. In the case of centralisation all foreign activities are controlled centrally by the headquarter. The whole organisation process is oriented ethnocentrically, whereby the attempt is set to transfer the organisation structure of the headquarter to the subsidiary. A rigid leadership is the aim. In practice a mixture of central and decentral co-ordination is used in most cases.
- **Control:** the task of control is to control the realisation of given subjects through the headquarter. The performance of the foreign subsidiary has to be analysed taking into consideration the local environment. Control is conducted with the aid of budget and/ or index number systems, as well as through a comparison of ideal and actual performance.

6.11.1.3 Communication

Different cultural, legal, economical, and social conditions make it more difficult to develop a homogenous communication system.
In practice it is tried to overcome this problem by a cross-country standardisation of the information system, periodical discussion groups, and co-ordination groups, but also through the advancement of informal communication channels.

- **Ethnocentric Co-ordination and Communication Structure**: co-ordination and communication take place bilateral between headquarter and subsidiary, whereby the headquarter plays the dominant role.
- **Polycentric Co-ordination and Communication Structure**: also in this case co-ordination and communication take place bilateral, however a transfer of competences and activities to the subsidiaries is effected. Co-ordination and communication are directed concerning local requirements, nevertheless a harmonising with the headquarter is more difficult.

6.11.1.4 Human resources for Joint Ventures

With the decision to employ staff for a company, the cycle of personnel management begins. In consideration of personal demand of Joint Ventures the following three questions have to be responded:

- Which basic qualifications are imparted by the school system in the host country?
- Where are recruitment markets?
- How does recruitment look like?

Subsequently placement, remuneration, and labour legislation, solution of inner company conflicts and continued education are discussed.

a. Characteristics of personnel placement planning in Joint Ventures

The demand for staff members from the headquarter can be derived from the targets of the company. In general the following targets are aimed at:

- Execution of know how transfer
- Development of management capabilities of expatriate
- Compensation of missing national leaders
- Securing of an uniform leadership
- Development of national potential leaders
- Uniform reporting guaranteed

The demand of headquarter delegates in the foreign subsidiary depends on the state of internationalisation of the company, the education level of staff, the size of subsidiary, the activity field of the subsidiary, the organisation structure, the necessary know-how transfer as well as legal regulations.

b. Placement strategy in Joint Ventures

The demand for personnel in a Joint Venture can be covered by external or internal personnel acquisition.

➢ **Internal personnel acquisition**

Includes all measures for the satisfaction of personnel demand inside the company with or without change of existing employment contracts. The advantages of internal acquisition are that firm-specific know-how must not be built up, the judgement of performance is easier, and therewith the risk for miscast can be decreased.

➢ **External personnel acquisition**

Plays an important role concerning casual workers. Concerning leading position external acquisition is in most cases applied, if there is a shortage of internal employees, which do not meet the needed qualification profile.

c. Ethnocentric placement strategy

The ethnocentric placement strategy proceeds on the assumption that a superior company culture is transferred from the headquarter to the subsidiary. A relatively high share of headquarter employees is employed in the foreign subsidiary.
The company leadership is endeavoured to fill leading and key positions with employees from the home country. This strategy allows a realisation of an uniform enterprise policy, communication and co-ordination with the headquarter without problems, better know-how transfer of technical and management know-how, and the gaining of experience for employees of the headquarter.

Disadvantages are that the employees from the host country may be unmotivated, and because of frequent changes in the management in the subsidiary, the effects on the working climate as well as on the continuity of the company policy may be negative. The time limited delegation may also involve the risk of a short time optimisation of success instead of the long term targets of the subsidiary.

d. Polycentric placement strategy

In a polycentric oriented company the different conditions between the countries are considered as being so important that in every country an individual to the country-specific conditions adapted leadership is necessary.

The consequence is a far-reaching disclaim to the delegation of headquarter employees. Leader and key positions are observed almost exclusively by local employees.

Advantages of a polycentric placement strategy:

- The personnel demand exceeds partly the number of people from the headquarter who are qualified for the foreign employment
- Lower costs
- The integration of the subsidiary is facilitated - local staff have better knowledge concerning business and branch customs and in most cases already existing contacts to market partners and governmental offices
- Motivation of local staff because they can reach leading positions
- Continuity of style of leadership

A problem of the polycentric placement strategy is the co-ordination between local management and headquarter, but also loyalty problems, lack of subordination willingness, higher communication costs, lacking know-how transfer, conflicting aims of headquarter and foreign subsidiary. Above all, in developing countries, a lack of qualified local leaders is often noticeable.

e. Problems concerning expatriates

➢ **Selection**

An employee who shall be sending to a foreign subsidiary has to fulfil several criteria. Besides the professional and technical qualification, the expatriate must also have certain personal qualification.

Concerning the professional and technical qualification, understanding of leadership and organisation, as well as knowledge of the products and the headquarter policy are necessary.

High adaptability and flexibility are demanded from an expatriate in the meaning of that (s)he can relativise his (her) own expectations, norms, and behaviour pattern for being able to accept new forms of life and methods of working. Without this adaptability the expatriate will suffer a “culture shock”.

Another important element is the ability to communicate. If (s)he does not know the language of the country at the beginning of the sending it, it is indispensable in the long run. Besides the verbal communication in the long run non-verbal communication (patterns of behaviour, mimic, gestures) are important.

Health and psychical endurance are other necessary characteristics. And of great importance is the expectation attitude of the expatriate.

Regarding selection technics, personal recommendation, potential judgement, and showing of interest of employees are popular technics for the selection. In addition assessment centres are used, biographic questionnaires and interviews, and of course long-term continuous personnel observation.

- **Preparation**

The necessity for a good preparation emerges from the fact, that abroad in many cases tasks are taken upon, which require independent working and at the same time high responsibility under changed environmental conditions. Moreover it has to be considered that a know-how transfer shall occur.
[Lanier, 1979] proposes a 7-stages-plan:

- Short visit to the country
- Language preparation
- Lessons in geography
- Private studies of country-specific literature
- Procurement of special literature, which is relevant for the company
- Experience exchange with people, who already worked in this country
- During the initial working period support from the headquarter

During the delegation the employment contract is maintained. Special features concerning revenue, social insurance, taxation, change of residence etc., are regulated in a special delegation contract. The foreign revenue consists of a basic salary and different extra payments. Such extra payments concern costs of living, taxation compensation, housing costs, and education grants. The basic salary depends on the requirements of the position and is the basis for offered extra payments. The payment can be made in:

- in the currency of the home country
- in the currency of the host country
- partly in currency of host and home country
- in a third currency

Generally it is fixed in the delegation contract that the employment relationship with the headquarter revives after the end of the delegation.

- **Employment Abroad**

In this stage the duration of the employment abroad and the maintenance of human relationships play important roles.
Usually the **Duration** of delegation is between 3 and 5 years. Longer employments abroad lead to better knowledge about the environment, but at the same time the knowledge about headquarter policy decreases. Moreover the risk emerges that a strong assimilation with the conditions in the host country occurs and the expatriate and his(her) family refuses a repatriation.
During the delegation the expatriate should always have a **Contact** to someone in the headquarter, get regularly company news, take part at continued education in the headquarter and should have the possibility to get paid the holidays in the home country by the headquarter.

- **Reintegration**

The success of reintegration depends on the duration and the frequency of delegation, the cultural differences between the countries, as well as the contact to the headquarter during the delegation, and the planning of reintegration.
Many problems can be reduced, if early on the planning of the date of return and of the re-entry-position is started.

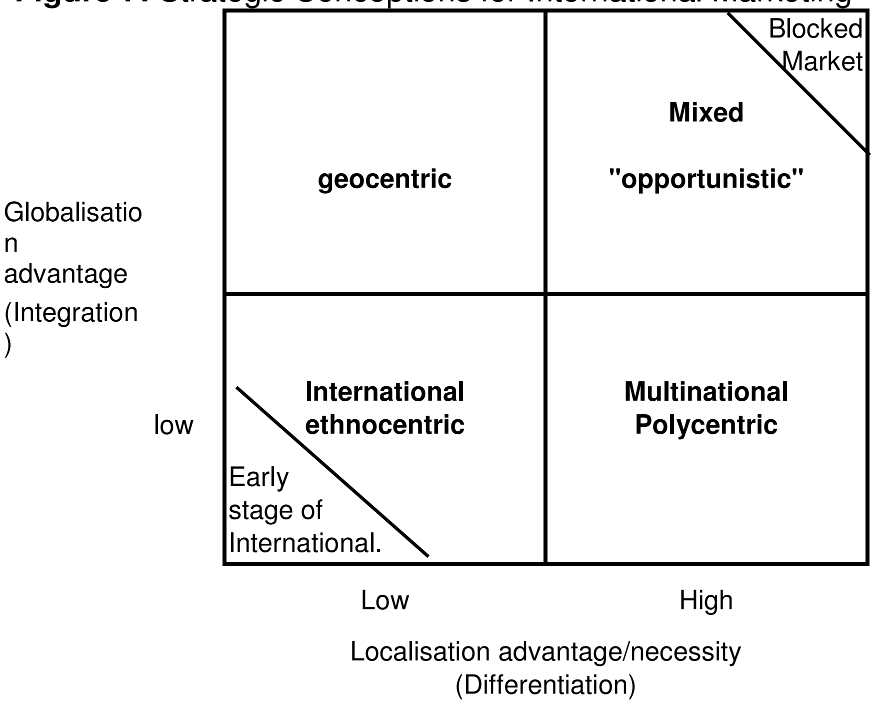
f. Influence of social and labour laws

In international personnel management differences in labour and social regulations between the host and home country must be taken into consideration as well as differences in co-operation between management and employees. Different management structures involve a personnel management adopted to local requirements.
The achievements of national trade unions concerning working time, working rhythm, security and social services must be examined with regard to transferability to the host country.

6.11.1.5 Marketing Management

The strategic marketing concept for the organisation of foreign activity includes international product, price, distribution, and communication policy.
In the literature among strategic conceptions international, multinational and global marketing can be distinguished. The definition results from two criteria: **Globalisation Advantages** and **Localisation Advantages** as can be seen in the following figure.

Figure 7: Strategic Conceptions for International Marketing



6.11.1.6 Product Policy

The product policy includes decisions about **Product Innovation, Product Variation**, and **Product Elimination.** When selecting a product, it is first of all necessary to determine the internationalisation potential of the product for the specific market and the following questions must be examined:

- Who shall buy the good abroad?
- Who shall use the good abroad?
- How shall the good be used abroad?
- Where shall the good be used abroad?
- How shall the good be used abroad?
- Why shall it be bought abroad?
- When shall it be bought abroad?

From the responses to these questions it can be concluded, if the company should follow a standardised or differentiated product policy.

a. Standardised Product Policy:

If product adaptation is not absolutely necessary, the company can strive for a standardisation of its goods. In the case of standardisation of the product policy companies try to take advantage of cost degression and experience curve effects through, for example, mass production, reduction of stock keeping, and advantages in supply with replacement parts. A standardisation is often the aim in the area of mark policy - "**Global Branding**".

b. Differentiated Product Policy:

A differentiated product policy is adjusted to country-specific requirements. This adjustment can be crucial for the market success because of differences in the structure of needs and wants, purchase power conditions, utilisation and consumption habits, but also because of legal restrictions. Starting point for differentiated product policy are *physical properties* of a product (e.g., size, material, weight), *functional features* (e.g., quality, functioning), *aesthetic attributes* (e.g., design, colour), *packing* (e.g., colour, design, protection, imprint of the brand name etc.,) and *services* (e.g., operating instructions, installation requirements, warranty, etc.,). Figure 8 shows starting points for product adaptation.

Figure 8: Product Adaptation Abroad

Components of a Product Strategy	Different Ways to Market Acceptance
Performance based product characteristics	Size, capacity, additional equipment
Product security	Target market, utilisation training, operating instructions, safety device, product design
Product quality	Expected utilisation time, recycling. materials (design, production process)
Product design/styling	Colour, materials, size, form, weight, practicality
Packing design	Colour, size, material, form
Packing imprint	Language, operating instructions, statement of contents, warning indications
Warranties	Legal liability, time period, percentage of overall lifetime
Service policy	Repair service, repair training, repurchase
Positioning	Target market, performance or not performance based characteristics, marketing mix
Repurchase policy	Repurchase
Brand policy	Languages, licenses, trade mark protection

In connection with product innovation and variation the question of product replacement cycles is relevant. Long product replacement cycles make low demands on flexibility of production technology and lead in general to a potentially high cost degression. At the same time they impede the integration of new technology elements, give weak innovation impulses, and lead to a poor innovation image. In the case of short product replacement cycles the danger exists that a “image anchor” is missing. Marginal product improvements and a lack in continuity could be regarded as negative. It is important to consider different attitudes in different countries.

6.11.1.7 Pricing Policy

Subjects of pricing policy are decisions about the remuneration for the service offered, about possible discounts, as well as about terms of delivery and payment. Several factors having influence on prices:

- The price strategy
- Terms of payment and delivery
- Costs
- Competitive situation
- Demand
- Governmental regulation
- Foreign exchange rate and inflation development
- Form of foreign market entry

a. Price Strategies

Three different pricing strategies can be distinguished:

- **Price Standardisation**

  Complete price standardisation (all over the World the same price) is hardly to put through and does not seem to be very efficient. Country-specific costs and conditions, as well as demand and competition structures are quite different in foreign countries.

- **Price Differentiation**

  The company adapts to the specific market conditions. It can be effectuated according to consumer-specific, temporal and local criteria.

  The aims of price differentiation can be oriented exclusively towards price elasticity and the price-sales-function. Besides taxation aspects can guide to price differentiation - different taxation burden in different countries lead to different sales prices - with the aim to optimise taxation. Another aim can be fast market development res. carefully directed fight against competitors.

- **Price Corridor Strategy**

  This is the compromise between price standardisation and differentiation. General Price guidelines are given with the aim to have a homogeneous price-performance-ratio. The headquarter sets centrally prices in the form of a price range and the local management can fix the end price.

  It has to be considered, that in some countries a price corridor strategy is not admissible, because vertical price fixing is not allowed.

b. Cost based price determination

Because of the foreign activity additional costs may occur and lead to higher prices abroad (*Price Escalation Effect).* Such additional costs emerge through:

- The foreign business activity itself. Specific foreign manufacturing costs (e.g., for specific product requirements), export costs (e.g., for the export of equipment, initial products) like transport and insurance costs, shipping documents; distribution costs, costs for market research.
- Different cost structures on the home and the host market. It is important, when for example a wholly owned manufacturing plant or a licensed production takes place abroad. Depending on the production location different labour, material, and capital costs emerge.
- Specific risks of foreign activity. To mention are: increases in costs for currency and deficiency risks, inflation compensation.
- Governmental measures. These can include custom duties, foreign taxes, etc. But costs can also arise because of governmental regulations, like product liability.

For a cost based price determination different methods exist, the “Full-Cost Pricing”, usually used by US-American companies, the price results from full costs. The problem is, that this method contradicts to profits maximisation and, because it does not take into consideration demand, competition. Another method is “Profit-Contribution Pricing”. Hereby the demand function is taken into account when determining the price. First of all it is determined how high demand for certain products is at different prices (determination of the price-sales-function), afterwards the price is searched that can maximise the profit.

c. Competition Based Pricing

The competitive analysis might be as simple as finding out what global and domestic competitors in the particular country market charge for their products. If the company has to compete with many competitors, it will set the price and react as quantity adapter.

This situation is common in commodity markets, where the consumer does not perceive product differences; the price will be the critical decisive factor.

The market position of the company abroad will influence on a considerable scale the feasibility of a differentiated pricing policy. Such a policy serves for the attainment of strategically competitive aims of the company, like e.g., increase in market share or profit maximisation. While the strategy of Cost (or correct: price-) Leadership demands the consequent undercutting of the concurrence prices, a Differentiating Strategy allows, because of a quasi-monopoly competitive advantage, a high price policy.

Two types of differentiating strategies can be distinguished: “Skimming” and “Penetration”.

The “Skimming Strategy” tries by charging relatively high prices to gain high cover margins per unit. Following the high price phase the enterprise decreases the price step by step with the aim to prevent potential competitors from market entry. The advantage of this strategy is, that companies can regain fast their costs and investments for the foreign activity. The disadvantage is, that because of the high price, competitors can be attracted within a short time. The “Penetration Strategy” gives the possibility to gain with the help of low prices a high market share in a relatively short time, whereby cost degression and experience curve effects can be achieved. This could serve as a market entry barrier for other competitive enterprises. A disadvantageous effect of penetration is that in the beginning the company has to accept low profit margins or even loss. In the long term this strategy can be useful, if the market potential is very high (economies of scale, experience curve effects).

d. Customer Oriented Pricing

Customers of the home and host market perhaps have different ideas about product benefit and therewith different ideas about the price for the product. The prestige benefit can also influence the price.

e. Governmental Influence on Pricing

Tariff and **Non-Tariff Trade Barriers,** and **Anti-Trust** determine foreign pricing. In addition price controls, including minimum and maximum prices, price stops, price maintenance or discount regulations, are possible. Discriminating taxation regulations can also influence pricing determination, as well as dumping and export or import regulations.

f. Influence of Mode of Entry on Pricing

The pricing policy abroad depends on the market entry strategy. Two extreme cases can be distinguished:

- The enterprise has to behave like a quantity adapter, because the price is given
- The enterprise has competitive advantages on the foreign market, which provide a quasi-monopolistic position.

In the following paragraphs it is analysed, which influence the market entry strategy of FDI has on the price and sales policy of a company for the foreign market.

The height of the maximum available capacity is crucial for the maximum reachable market share.

g. Transfer Pricing

An additional problem of pricing is the regulation of transfer prices for shipments between headquarter and subsidiary. The basic reason for transfer pricing is simple: There has to be a price paid for the products shipped between units of the same organisation when the shipment crosses national borders so that the correct duties and related fees can be paid.

In general, three basic approaches can be distinguished for the determination of transfer prices:

- The company uses the same transfer price system as in the home country, if it corresponds to the requirements of the foreign financial administration.
- The company develops an own transfer pricing system for their foreign activities.
- The company forms transfer prices corresponding to the Resale Price Method.

However, since the transfer prices charged directly affect the amount of purchases in the cost accounting of a foreign subsidiary, they have a direct influence on the subsidiary’s financial performance. Because of this fact transfer prices became a mechanism for multinational companies to shift profits from one country to another. If the headquarter of a company sets a high price on the shipment of a subsidiary in an for example African Country, this subsidiary will have trouble showing a profit - and if the price is set low, the subsidiary will be very profitable.

In practice international enterprises refer to the following defining quantities for the calculation of transfer prices:

- Transfer prices based on market price oriented list prices
- Transfer prices based on full costs
- Transfer prices based on full costs plus a certain profit margin
- Transfer prices based on negotiated prices

6.11.1.8 Communication Policy

The communication policy of a company, active on the international market, has the target to influence opinions, attitudes, behaviour of consumers abroad for the purposes of the company. A communication takes place between the sender (company) and the receiver (actual and potential consumers). Following communication barriers may occur:

- Differences in the language,
- Differences concerning governmental regulations,
- Differences concerning the availability of media,
- Economic differences,
- Differences concerning the local trade structures,
- Differences in taste and behaviour patterns,
- Differences in the availability of advertising agencies.

a. Communication Strategies

The communication mix includes advertising, sales promotion, public relation, and sponsoring. The main question is to define which kind of strategy applying: a world-wide identical communication policy (Standardisation) or a country specific communication policy (Differentiation).

The “Standardised communication” policy is distinguished by a world-wide identical strategy without consideration of eventually emerging national wants. It is assumed that the cost advantages of standardisation are more important than advantages of differentiation.
In the centre of standardised communication strategies are observable similarities between countries, the markets in different countries are regarded as one homogeneous market. Several communication activities are controlled by the headquarter.
Advantages of standardised communication policy:
- Cost reductions
- Improvement of total performance efficiency through know-how transfer and synergy-effects
- Efficient use of the advertising budget
- Development of an uniform product and company image

Inconvenient of a standardised communication policy:
- No target group is focused precisely
- Sometimes relevant, existing differences are ignored
- Conflicts may arise between the management of the headquarter and the local management

The “Differentiation of the communication strategy” policy offers the possibility to react flexibly and fast to changes in competition and customer structure and to take into consideration different country or segment specific circumstances. The country and segment specific conditions to be considered are:
- national traditions, values, conventions, customs
- different cultural, legal, economic structures and development stages
- established habits and tastes
- prejudices, attitudes, preferences towards foreign companies and their offers
- language, symbols and colours as culture factors

The advantage of country-specific communication strategies is the limited risk if a communication strategy fails.

6.11.1.9 Distribution Policy

The distribution policy of a company includes all decisions and measures which concern the way of a company’s product go to the consumer. The task is to decide which distribution channels to use, and how the logistics of the sales should be organised.

a. Selection of Distribution Channels

The enterprise can adapt to the existing distribution channels (Adaptation), modify existing distribution channels (Modification), or create own channels (Innovation).
Different distribution channels can be distinguished according to the directness of the relationship between national government and foreign end-consumer. Direct Distribution Channels are e.g., own subsidiary, franchising; Indirect Distribution Channels are for example supply to independent trade companies.
The distribution channels abroad are also influenced by availability, co-operation willingness of middlemen, costs, and general conditions. There are relevant, among others, climatic conditions, transport media, legal particularities (e.g., local content or export regulations), and the infrastructure.

b. Selection of Middleman

The middleman can be commercial agents, brokers, commission agents, travelling salesmen, trade companies, sales agency, or retailers.

c. Distribution Logistics

Logistics include questions about delivery costs, time, readiness for delivery, the availability, flexibility, custom duties, security of transport and warehousing.

The costs of logistic play an important role because of the distances. For minimising transport and warehousing costs the transport infrastructure in the target country, which differs world-wide, must be considered. The warehousing can be problematic not only because of security aspects but also because of the climate. In some countries there are no adequate public warehouses, what increases the costs.

6.12 Summary

Considering what has been written in the previous paragraphs about the analysis that an enterprise wishing to expand in a foreign country should effectuate, we can affirm that the entry strategy is affected both by company factors (firm-specific advantages) and by market factors (opportunities and threats).

6.12.1 Company factors

The company factors can be grouped into three strategic postures. The market factors are different in advanced and emerging economies and in high-growth and mature markets.

- ***Incremental***: only few resources can be dedicated to entry (the usual case when entry is the first step in the internationalisation).
- ***Protected***: a second strategic posture is when the firm possesses a well-protected trade secret or patentable know-how whose potential abroad is clear, but needs to learn about the market and develop more local familiarity. In such cases there are usually real or self-imposed limits to the resources (manpower, operating capital) allocated to the entry.
- ***Control***: in this strategic situation the company has well-established firm-specific advantages, is large enough to encounter relatively few resource obstacles to expansion, and offers a product definite potential abroad.

6.12.2 Product/Market situation

The various product/market conditions that might prevail in the market country can be grouped into three different categories.

- ***Emerging Markets***: emerging markets are those recently opened up because of political changes, and which show generally weak infrastructure, difficulty in accomplishing market-based exchanges, lack of distribution alternatives, and risk of default on payments.
- ***High-Growth Markets***: a second situation is high-growth markets, such as some high-technology markets in advanced economies and markets in many fast-growing countries, including the newly industrialised countries. The main marketing issues tend to be to quickly establish presence in the country and to support the product sufficiently in the marketplace so as not to lose out against competitors.

- ***Mature Stage***: a third situation is the market in the mature stage, when the aim is to achieve market share, including dominance in at least a niche in a well-differentiated marketplace. The emphasis in entry in mature markets is not so much on speed of penetration as on the total amount of marketing expenditure needed to establish presence and maintain loyalty.

The following figure summarises the possible types of market entry.

Figure 9: An Optimal Entry Mode Matrix

Company strategic posture	**Product/Market Situation**		
	Emerging	***High growth***	***Mature***
Incremental	Indirect exports	Indirect exports	Direct exports
Protected	Joint Venture	Indirect exports	Alliance/Licensing
Control	Wholly owned subsidiary	Acquisition/ Alliance	Wholl owned subsidiary

7 CONCLUSIONS

Joint Venture seems to be the best way for a European enterprise to do business in the African market. Using equity joint venture is, however, fraught with difficulties. A Joint Venture is only as strong as the combined expertise and resources of its two parent companies.

It is important to have a deep knowledge of the local market and of the cultural and legislative substrate; greater expertise and experience doing business in Africa is an important asset for successful Joint Venturing. On the other hand, exporting strategies and licensing and franchising practices are to be preferred by those enterprises that see this market as a very risky market and do not wish to invest big amounts of capitals.

It is difficult for foreign companies to use wholly owned strategies because without a well established and well connected local partner, it is very challenging for the foreign company to swim through the local bureaucracy.

However, there are many risks for foreign companies. These include frequent policy changes, lack of reinforcement of existing policies concerning foreign companies, foreign exchange problems. Human resource and labour issues, raw material supplies from Africa, multi-layer government bureaucracy are some of the other problems that foreign companies have to deal with on an ongoing basis.

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