White Paper

Expanding into International Markets

7 Key Questions to Achieve Success

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Overview

The old adage, “if you’re not growing, you’re dying,” is often cited by business leaders as the motto that has helped drive their success. The statement is rooted in common sense and can be a rallying point for a whole organization. Many successful business owners also use the phrase, “failure to plan is planning to fail.” In our sound byte world, these two statements are right on target when businesses consider expanding into international markets.

Business owners considering international expansion are often overwhelmed with questions and anxiety about the mystery of doing business internationally. Consequently, business owners can get stuck in place not knowing where to begin. In this document, we explore the seven key questions business owners should ask before pursing international expansion.

Why Businesses Expand Internationally

All business environments are dynamic; changes in markets, supply lines, or consumer behavior are just a few challenges businesses encounter on a regular basis. In this dynamic environment, many business owners look to international expansion as a strategy to achieve their goals. Businesses choose to expand internationally to:

- Achieve market diversification or implement growth strategies;
- Enhance profit margin;
- Serve key supply chain customers;
- Gain geographic proximity to supply sources;
- Gain market edge through streamlining the supply chain;
- Develop or maintain a relationship with foreign customers.

International expansion is similar in many ways to domestic expansion, and a variety of influences continue to bring international opportunities closer to the front door. They include:

- Technology that allows easy connection to end-users;
- Economies that are interdependent and rely on each other for expertise and specialization to produce reliable goods and services; and
- Delivery mechanisms that allow interaction during and after the sale.

7 Key Questions to Achieve Success

If you are considering international expansion, you should ask yourself seven key questions.

1. Have we completed a readiness assessment?

Exploration is broadly defined as a systematic consideration. For many, international expansion is a new adventure and, as such, the enterprise needs to analyze and assess skills in areas such as:

- Internal capabilities and experience to develop an international strategy. It is very common to encounter enterprises where internal personnel have prior individual international experience. However, it is also very common that businesses have not grouped their internal abilities to form a team charged with exploring international opportunities.

- Due diligence conducted internally or with the assistance of an advisor can be priceless. Areas to consider include:

    - ♦ Operational obstacles
        - ◊ Will the company make or buy in the foreign country?
        - ◊ How much market intelligence has been gathered and how much additional information is necessary to make informed good decision?
        - ◊ What talents are in the labor force?
        - ◊ Will US personnel be required for management or is there sufficient local staff?
        - ◊ What other crucial areas that are unique to my business should I consider?
    - ♦ Financial
        - ◊ How much capital will be required to start up and fund the operation?
        - ◊ What do projections and forecasts indicate about profitability and cash flow?

- ◊ How long does the organization expect to financially support the expansion?
- ◊ Does the organization have internal personnel who can address currency differences, local compliance reporting, and local country payroll issues?
- ◊ Does the organization include personnel to address financial and tax reporting in the local country?
- ◊ Is the company in a position to take advantage of any incentives offered by government bodies, including the United States?

Let's consider an example of the importance of due diligence. It is a common misconception that a strong market demand for a product in the United States indicates demand will also be strong in another region. Many executives have made the error of not considering the appeals and pitfalls of a market prior to advancing. The fact is, market diligence is crucial to success in a foreign market. Successful executives utilize all resources available to them to explore a market, including the following:

- Organizations or individuals with local market experience and expertise; (such as consultants, accountants, and lawyers) can be a great asset and well worth the investment;
- Trade organizations that deeply understand the operation and approaching changes within a market;
- Referrals from friends and colleagues in the industry who trust the organization or an individual's skills and integrity as assets to move the company into the market;
- Government organizations (local and United States) with information or a skill base that can assist in the exploration of the market.
- The return recognized from the energy, effort, and cost expended in this area is rarely immediate. However, in the long run, the benefits outweigh the costs many times over.

2. Have we defined success and do we have a sound business plan?

Take a minute to think through your business' standard procedures for developing a new market in the United States. For many companies, expansion is a process developed and perfected over a long period. The process is likely well defined and honed through years of corporate development. Whether greenfield development or acquisition, most companies have a developed plan to analyze operational, financial, and market data for the benefit of a successful venture.

Companies seeking international expansion often make the mistake of simply replicating their domestic plan and applying it to their international endeavor. For many reasons, this approach is fraught with difficulties and obstacles. For instance, the financial metrics of an international venture are rarely the same as those domestically encountered. The business planning process must be reconfigured, sometimes as far back as the initial introduction of a domestic product. And market development costs tend to be overlooked. The baseline costs of market development are likely buried in the fixed costs of the domestic organization. It is not uncommon for executives to underestimate these types of fixed costs needed in an expanded market. Often, underpricing the costs of expansion, even to the smallest detail, can make or break a foreign endeavor.

Expansion into an international market may require infrastructure investments for the new organization. Costs in this area include: basic marketing, brand awareness, location development, market start-up costs, and product modifications.

For example, careful assessment of the new target market may reveal that some level of change to a product or service will be needed in order to attain market acceptance. The degree of modification will depend on the product or service and the specific country or region of entry. Name changes are a common modification. Readers may have heard of some of the classic brand name faux pas; such as that endured by Irish Mist, a golden whiskey liqueur produced in Dublin, Ireland, by C&C Group. While the beverage has a lovely sounding name in English, when C&C Group launched it in Germany, they were perplexed as to why sales weren't going well. "Mist," you see, is the German word for "manure."

Alternatively, planning for market needs when launching in the Philippines has paid off for three consumer products companies. In the market, an 80% share of shampoo sales to men belongs to Unilever, Colgate, and Procter & Gamble. These consumers do not follow the traditional bottle-level purchases of product for a variety of market- and region-specific phenomena, including pay frequency and residential space considerations. Unilever, Colgate, and Proctor & Gamble have thus modified the inventory carried in Philippine stores into single use packets and attained market acceptance.

The Irish Mist and shampoo cases illustrate the considerations that must be taken into account when expanding into new markets. It is critical that enterprises examine all aspects of its product in the continuing effort to ensure the company is optimally positioned and establishing a basis for success in the new markets.

Product characteristics can present unique logistical challenges that must be addressed by an enterprise seeking new markets. For instance, precision equipment or construction-level products may be typically re-constructed on sight. However, the distance to the project, size of the project, and level of skilled personnel may render the typical method unusable for international projects. Therefore, the enterprise must consider whether the typical processes used for delivery of the product or service are viable or require significant changes.

International expansion requires executives and entrepreneurs to embrace a comprehensive plan, using all that has been learned and developed in the domestic market. These individuals need to avoid the trap of attempting to "bolt on" without detailed consideration and planning.

3. Are we flexible and able to adapt?

Internationally, the fundamentals of doing business are rarely impacted. That is, businesses are established throughout the world to provide products and services to consumers in exchange for cash or other property in payment. There is, however, a wide variation of country-specific factors that impact the business. For instance, method of product delivery is a common adaptation required for international expansion. Manufacturing, wholesale, and service delivery are common industries where modifications must be made. For instance, service delivery commonly completed over an extended period of time in the clients' offices may need to be modified to include a single trip to client offices and expanded delivery from off-site or over computer connection. Manufactured product that requires final assembly by company personnel may need to be modified to allow third party contractors to complete delivery and installation.

A common need that often creates difficulty is the amount of control that home office management is able to exert over a foreign job or operation. Time and time again, entrepreneurs find the obstacle of not being on-site for part or all of a delivery or installation to be the most difficult aspect of a foreign transaction. Companies and executives must make the determination early on about how much involvement will be necessary from the home office. It is crucial that consideration be given to the cost and benefits of an international transaction or business expansion and how much time and effort will be needed to achieve the desired customer experience.

4. How well do we accommodate cultural differences?

United States executives and entrepreneurs can become frustrated and upset with the business environment of a foreign market. Many is the time that financial and operational projections are over-optimistic because management has overestimated the speed of a market. Each foreign market -- from developed, sophisticated locations all the way to the outer reaches of the world -- have well-developed business cultures. In many cases, the cultures are at odds with traditional practices of United States enterprises and business people. Many cultures have less of a “get it done now” attitude than that of the United States.

Furthermore, communication styles differ from country to country, sometimes immensely. In some locations, a handshake is all one needs to carry on business in the millions of dollars. Meanwhile, other cultures have a more hierarchical structure that requires the development of a personal relationship prior to conducting any business.

In addition, it is very common for business people and consumers in other cultures to conduct their affairs in a very provincial manner. The myriad situations where business to business or business to consumer commerce will be politely or impolitely avoided unless the out-of-town business person represents an enterprise that has a business in the country. United States businesses may need local personnel to represent or man a local operation if the company wishes to do business locally.

Investing time and energy in understanding and catering to local market cultural differences and the similar desires of consumers is often a price of entry into a new market.

5. Have we considered the tax and regulatory environment?

Proper arrangement of legal and tax affairs according to local and worldwide needs is an a crucial procedural requirement; this is because proper arrangement ensures the legal and tax affairs of the new organization mesh with the needs of the worldwide enterprise while maintaining local country protection and flexibility.

As an example, an enterprise looking to expand into Asia has a myriad of decisions regarding the desired operational structure in the foreign country. Some key operational questions include:

- Does the local enterprise need to manufacture, distribute, or provide services?
- Will sales be conducted in the country? Or will the product be sourced or produced in the country for sales outside the country?
- Will services be delivered into our out of the country?

Other considerations include:

- choice of currency,
- local labor issues,
- expatriate needs, and
- the long-term strategy of the business.

Professional advice is critical to ensure the operational requirements of the enterprise work in concert with the legal and tax goals of management and the enterprise.

Business owners are well aware of how regulation impacts commerce. Regulatory compliance is a cost to the business that must be addressed and planned. Domestic business practice encounters all types of regulation in day-to-day business. For instance, wholesale and retail enterprises must contend with state and local sales tax requirements. For most businesses, state and local process and procedure has been built into the business practice and is commonplace. When expanding into new markets, however, the local jurisdiction may have a variety of additional regulatory requirements that are new to the enterprise.

Custom and duty have a grand history and go down as one of the earliest forms of tax. Custom, duty, and other forms of tariff are used between trading partners to ensure local suppliers are protected from unfair trade practices. The collected amounts are also used to fund public services in most countries. However, the custom and duty system is complicated, as there are differing rate schedules based on the type and amount of product coming into a country. Enterprises that do not consider the additional administrative and carrying costs of products or services in a new market are overlooking a cost that can hinder or eliminate profit.

Another important concept often overlooked by enterprises is the “arm’s-length” transaction rules, which are included in almost every country’s regulations. The rules, commonly referred to as “transfer pricing,” require transactions between related parties to be completed at “arm’s length." That is, transactions are completed at comparable prices to market prices. Often overlooked, the audit and adjustment of a related party sale can be significant and devastating to the ongoing viability of the business. In many countries, the amount of regulation and compliance can be shocking. Budding enterprises must include all potential costs in their analysis of the business climate.

Enterprises must also be aware of a country's statutory reporting requirements, as an audit is legally required in some countries. It is also a requirement of some nations that a citizen of that country share in ownership of the business.

Business regulation and tax are business facts that are well known by United States businesspeople. It is important to recognize the differences and unique requirements that exist from market to market. Professional assistance is crucial to ensure compliance and a full understanding of additional costs that must be borne by the new market.

6. Have we fully considered the market and business environment?

Exploration, planning, and regulation are important components to understanding and playing in any new market. However, with the number of details confronting a business in a new market it is important that the business step back and understand the overall market and business environment. For instance, if a business were planning to expand into the European market in 2010, a critical piece of intelligence would have been to understand how the new market fit into the pending financial difficulties of the European Union. While one is involved with the planning and development of a new project, it is difficult to maintain an objective viewpoint at a macro level.

Executives and entrepreneurs tend to rely on their own business legend to provide a perspective in the new market. However, this can be a dangerous pitfall because the facts and circumstances in the new market are rarely the same as the domestic experience. Furthermore, factors such as cost, consumer desire (or lack of) for different features and benefits, and overall economic conditions can indicate that a product or service other than the most popular in the United States will be more successful in the new market.

Many have fallen victim to the “not invented here” syndrome, refusing to listen to the voice of the market and pushing on into a failing strategy. Businesses have resources that can assist in listening to the voice of the market and help establish an objective viewpoint. If a business is having a hard time finding resources, experienced professionals can provide assistance and referrals to navigate the landscape.

7. Are we committed to investing in labor and talent to tilt the odds in our favor?

The success of a new venture is credited to those who devoted the time and effort to make the expansion a reality. Talent and labor are critical to the success of an international venture. Some approach such a venture with an eye toward the important items to make a business success: market demand, product acceptance, quality, delivery, and maintenance of the product, and client relationship before and after the sale. It is easy to rely on the current management and sales team to undertake a foreign venture. After all, they know the business and clients better than anyone. But this approach can be a critical pitfall.

Current management, sales, and service personnel have filled their days with current business needs. Overloading any individual with the responsibility of an international expansion is likely to create one of two outcomes: failure at home or failure of the new venture. It is important to find the right person for the assignment. Perhaps the person currently exists in the structure of the company; if so, it is critical that an allocation of current responsibilities be made to allow enough time for he or she to spearhead the expansion. The expansion will need an individual or individuals to navigate the expansion, motivate the organization, and cheerlead the project. The organization needs to select the individual and provide him or her with the tools to succeed.

Another critical decision for the business is the determination of whether the organization needs “feet on the ground” in the new market. Recruiting the right person can mean success or failure of the project. Will the individual be assigned from the United States office or be local to the new market? How much outside labor will need to be included? Will they be employees or outside contractors?

Businesses must invest in labor and talent and it may require a completely different viewpoint than traditional hiring practices. The importance of finding the right person to lead the project and be responsible for its success will produce long-term achievement and return on investment.

Conclusion

Looking for a place to start? We have the experience and expertise to guide you through the process. We have a multi-disciplined team devoted to working with businesses that are looking to enter international markets. We use a unique, hands-on approach to help businesses evaluate, plan and execute an international strategy.

To Learn More, Contact Us

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