9 July 2008

International Business

Jopie Coetzee

Welcome to my world!!

RSA-Angola Chamber of Commerce

Using Vector Analysis to Mitigate Investment Risk

**Structuring cross-border FDI projects
upfront for success**

Jopie Coetzee ©
082 336 8118; jopie@global.co.za

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Agenda

Unique feature
A case study of a
FDI project in China

- **Achilles' heel of cross-border projects**
- **Statement of IB dilemma**
- **Approach taken to address IB dilemma**
- **The *Vector Model for Global Venture Creation***
- **The management process**
  - **Flow of management activities**
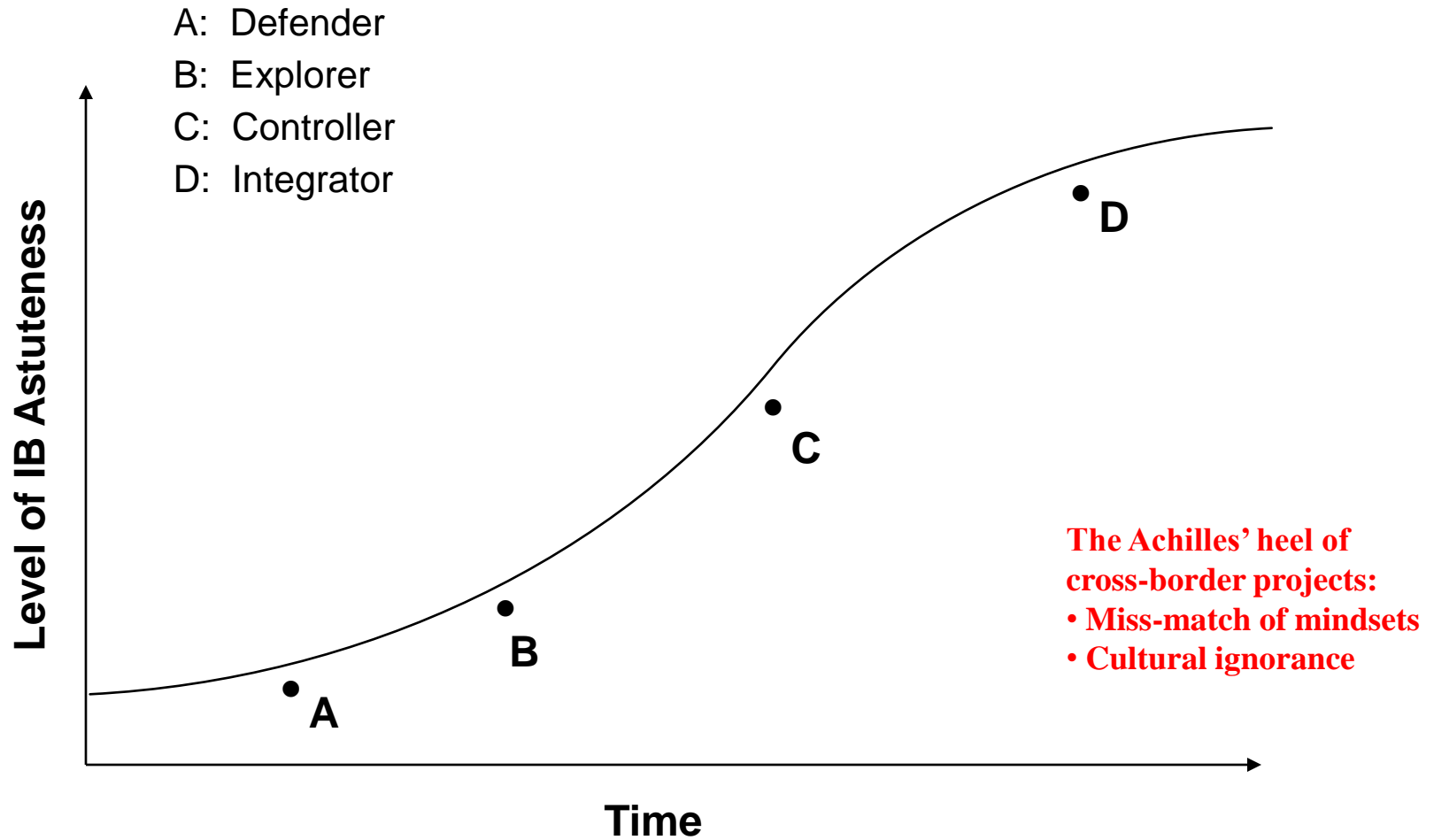 - **Executive decision making**
- **Conclusion & way forward**

Pitch

Corporate level of strategy making & implementation

Global mindset & IB Maturity Curve

- Source: Kedia & Mukherji (1999), and Coetzee (2006) -

A: Defender
B: Explorer
C: Controller
D: Integrator

Level of IB Astuteness (y-axis)

Time (x-axis)

• A
• B
• C
• D

The Achilles' heel of cross-border projects:
- **Miss-match of mindsets**
- **Cultural ignorance**

Statement of IB dilemma

- **IB theory:**
  - No one model/theory fully captures complexity of FDI
- **IB practice:**
  - Increasingly complex & competitive contexts for FDI
- **Approach to IB dilemma:**
  - This IB research aims to close gap between theory & practice
  - "Vector model for global venture creation", or
    - An epistemological, systems thinking approach to global venture creation, or
    - An integrated theoretical approach to global venture creation

FDI: purchase [project development] of physical assets, such as plant and equipment, or business operations in a foreign country, to be managed by the parent corporation. FDI is in contrast to foreign portfolio investment (Dictionary of International Investment Terms, 2001

Approach taken to address the IB dilemma

How to operate across borders?

How to implement strategy?

KPA 1:
Optimise the firm's positioning in a host country

What entry mode?

What global opportunity?

KPA 2:
Optimise a specific venture in that host country

What global strategy?

Why outside home country?

$D_{phenomenon} = 1 < n < \infty$; $D_{Vector\ Model} = n = 80\ [\Sigma(16\ vectors\ x\ 5\ global\ best\ practices/vector)]$

What is a vector?

- **A vector = the resultant of a set of forces**
- **It's a practical term to explain hidden dynamics within selected global venture creation models**
- **For the IB manager:**
  - **A vector is a strategy dynamic, a competitive advantage to add, or to defend value….**
  - **It is the resultant of a set of company competences….**
  - **It is a strategic thrust….**
- **It's what a MNC do to acquire, develop or leverage to get certain competencies to implement its global strategy, e.g.:**
  - **How to get & apply "Experience" in the host country (V13)**
  - **How to get & apply "Control" over a cross-border venture (V14)**
- **The 16 vectors also serve as an agenda for strategic and tactical conversations regarding global business development**

80 Global Best/Next Practices — FDI context-specific

16 vectors — IB theory-specific

2 mutually exclusive success criteria for successful strategy implementation — Context right? Implementation right?

6 models — IB body of knowledge (theory and practice)

Structure of models & vectors (2)

KPA 1: Optimise the firm's positioning in host country

- CAGE model (V1-4)

- Capability & opportunity space model (V5)

- Global opportunity selection 3-D model (V6-8)

KPA 2: Optimise a specific venture in that host country

- Conceptual framework of entry mode selection (V9-12)

- Evolution of entry modes (V13-15)

- Hierarchical model of entry modes (V16)

Presentation of ranked vectors (1 & 2)
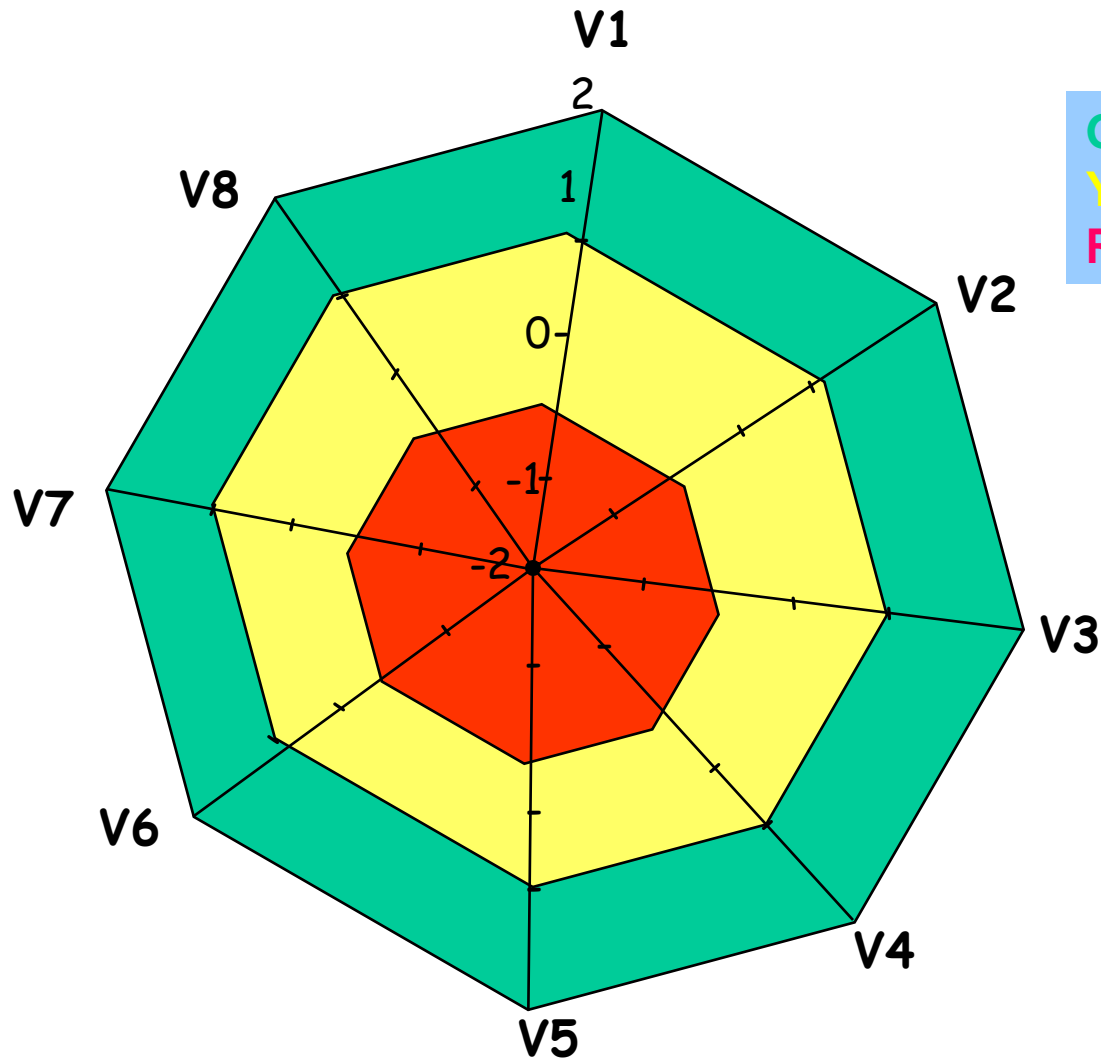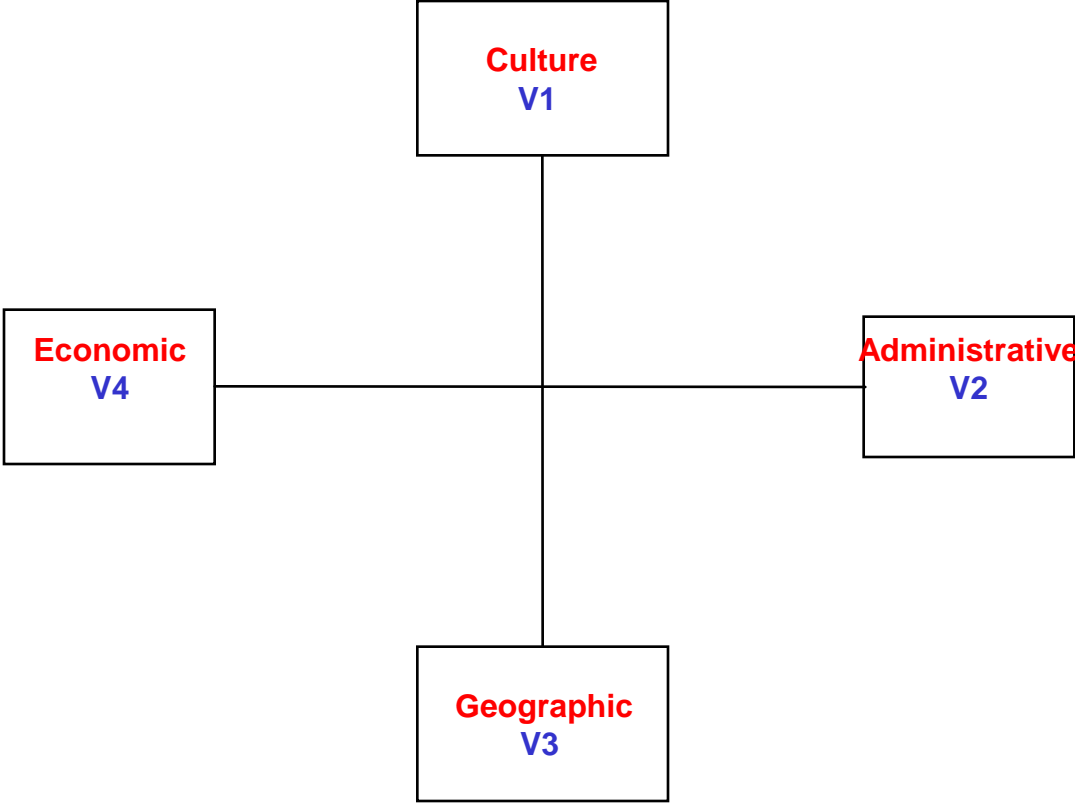

Green = acceptable
Yellow = caution
Red = fatal flaw

Legend:
- Stop/Abort
- Discretion
- Go-ahead

INPUTS TO THE VECTOR MODEL
&
SYSTEMS THINKING

Ghemawat proposes that 4 new measures of distance should be used in the evaluation of the attractiveness of foreign markets. Many failures are due to an overestimation of the attractiveness of markets. Firms become dazzled by the sheer size of a new market. They loose sight of the difficulty of entering new, difficult territory.

```
                    ┌─────────────┐
                    │   Culture   │
                    │     V1      │
                    └──────┬──────┘
                           │
  ┌─────────────┐          │          ┌────────────────┐
  │  Economic   │          │          │ Administrative │
  │     V4      ├──────────┼──────────┤      V2        │
  └─────────────┘          │          └────────────────┘
                           │
                    ┌──────┴──────┐
                    │  Geographic │
                    │     V3      │
                    └─────────────┘
```

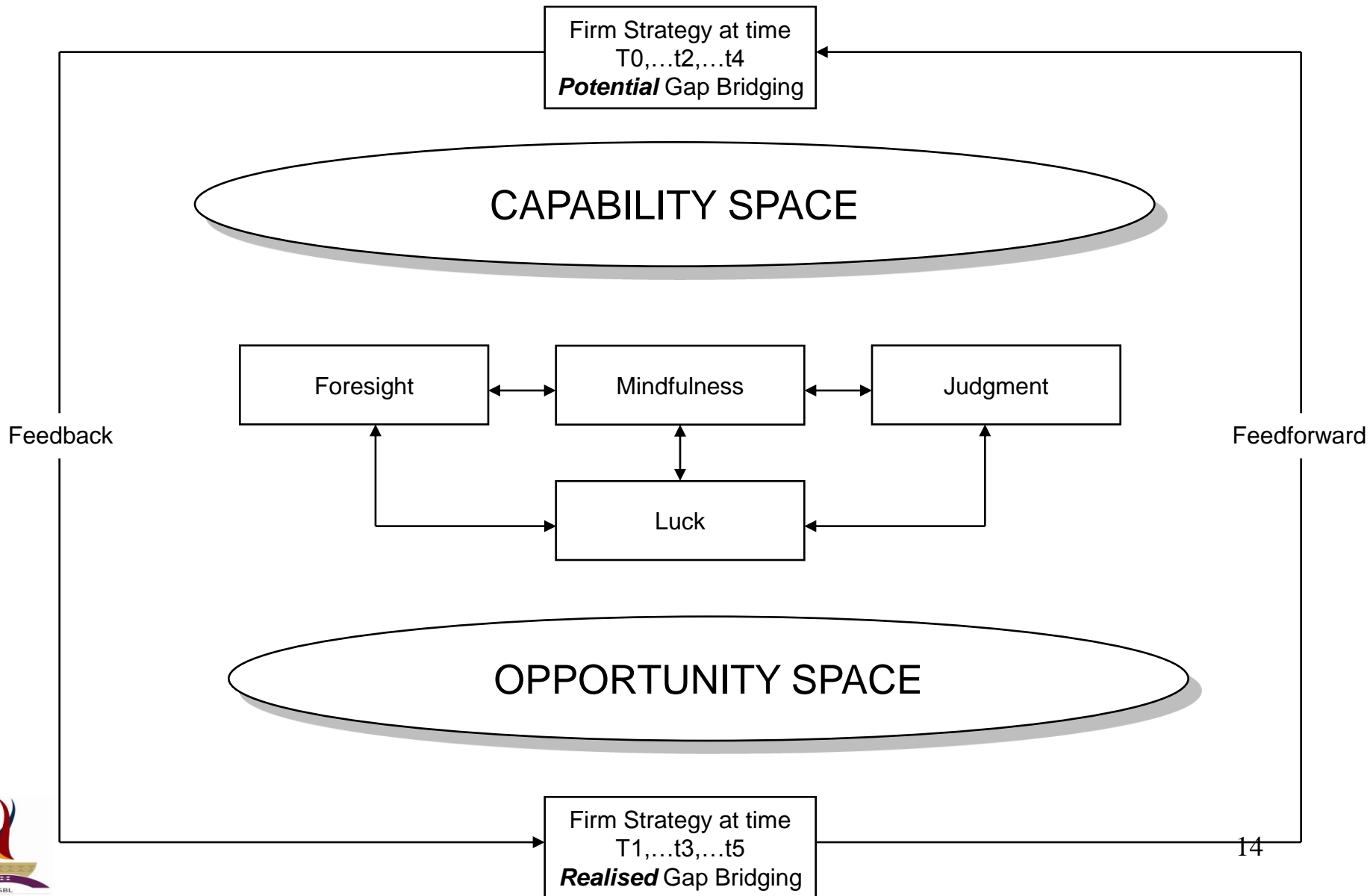**The CAGE model**

(Ghemawat, 2001)

Vector 1: Cultural distance

The degree to which people interact with one another and with companies and institutions. Differences in language, religion, race, social norms and values can contribute to business inefficiency, or even become deal breakers

1. **The Chinese culture and doing business through guanxi is effectively applied by XYZ-personnel in Beijing**

2. **The Chinese culture and doing business through guanxi is effectively applied by XYZ-personnel in Johannesburg**

3. **XYZ's business processes and decision-making criteria can accommodate doing business in China**

Capability and Opportunity Space Model

**(Dagnino, 2003) (V5 = crafting your own luck)**

```
┌─────────────────────────┐
│   Firm Strategy at time  │
│       T0,…t2,…t4         │
│ Potential Gap Bridging   │
└─────────────────────────┘
```

CAPABILITY SPACE

| Foresight | ↔ | Mindfulness | ↔ | Judgment |

Feedback   Feedforward

Luck

OPPORTUNITY SPACE

```
┌─────────────────────────┐
│   Firm Strategy at time  │
│       T1,…t3,…t5         │
│  Realised Gap Bridging   │
└─────────────────────────┘
```

14

Vector 5: Crafting a firm's luck

The extent to which a firm positions itself in a host county to participate in future growth prior to any knowledge of a specific business opportunity

1. **XYZ operates within the guidelines of board approved opportunism**

2. **XYX has a superior network of business intelligence within China – real time information and guanxi relationships**

3. **XYZ has the ability to exercise entrepreneurial creativity and judgment**

Global Opportunity Selection 3D-Model

(Jopie Coetzee, University of South Africa's SBL (2006) - unpublished)
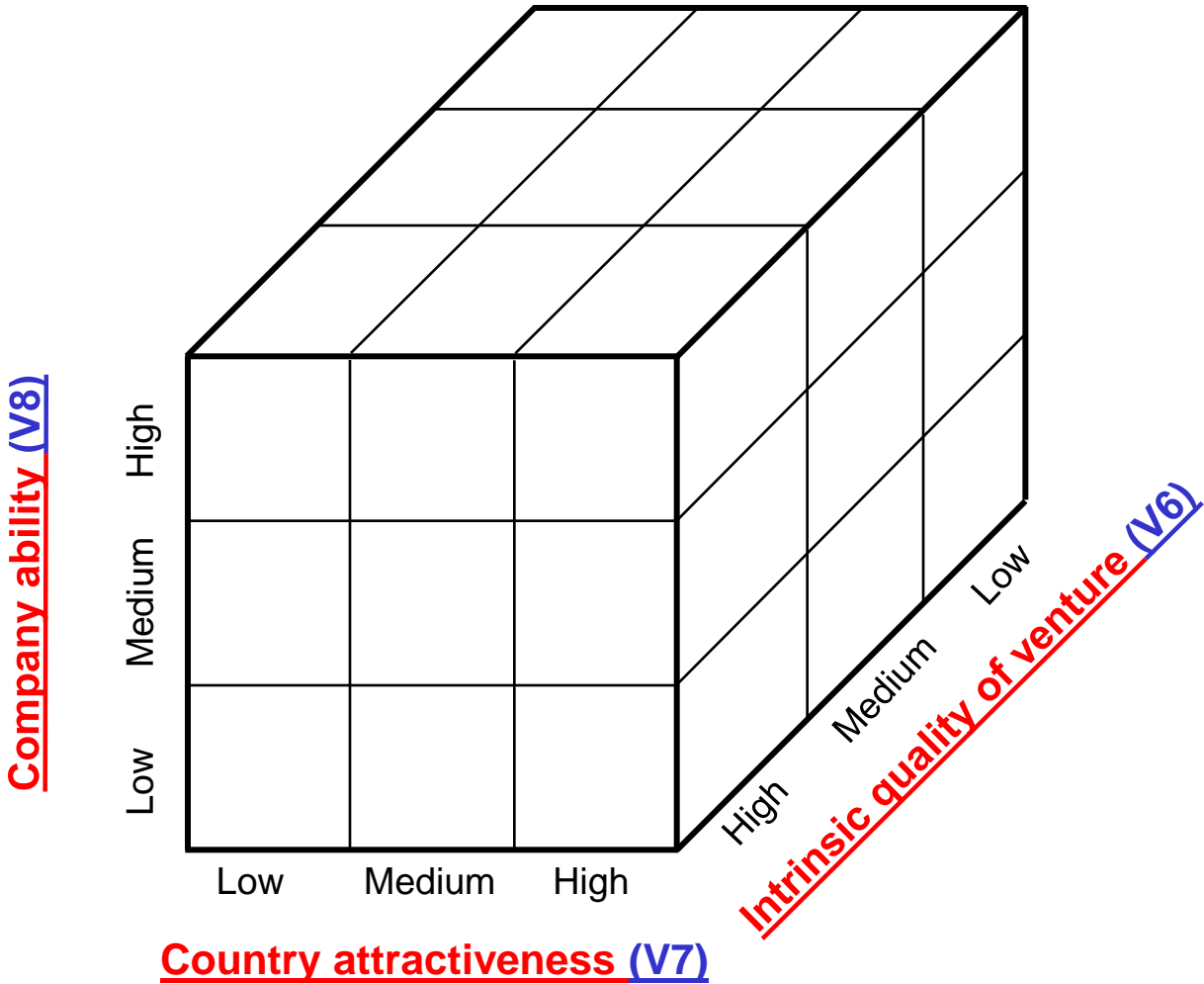
Vector 8: Firm's ability to implement
The extent to which a firm is able to pursue an opportunity in the host country

1. **XYZ has the capacity for delayed returns**
   - **Financial and patience!**

2. **XYX has a board-approved "country & culture leverage business plan"**

3. **XYZ has a done a credibility check on its local representative (s)**

Conceptual framework of entry mode choice
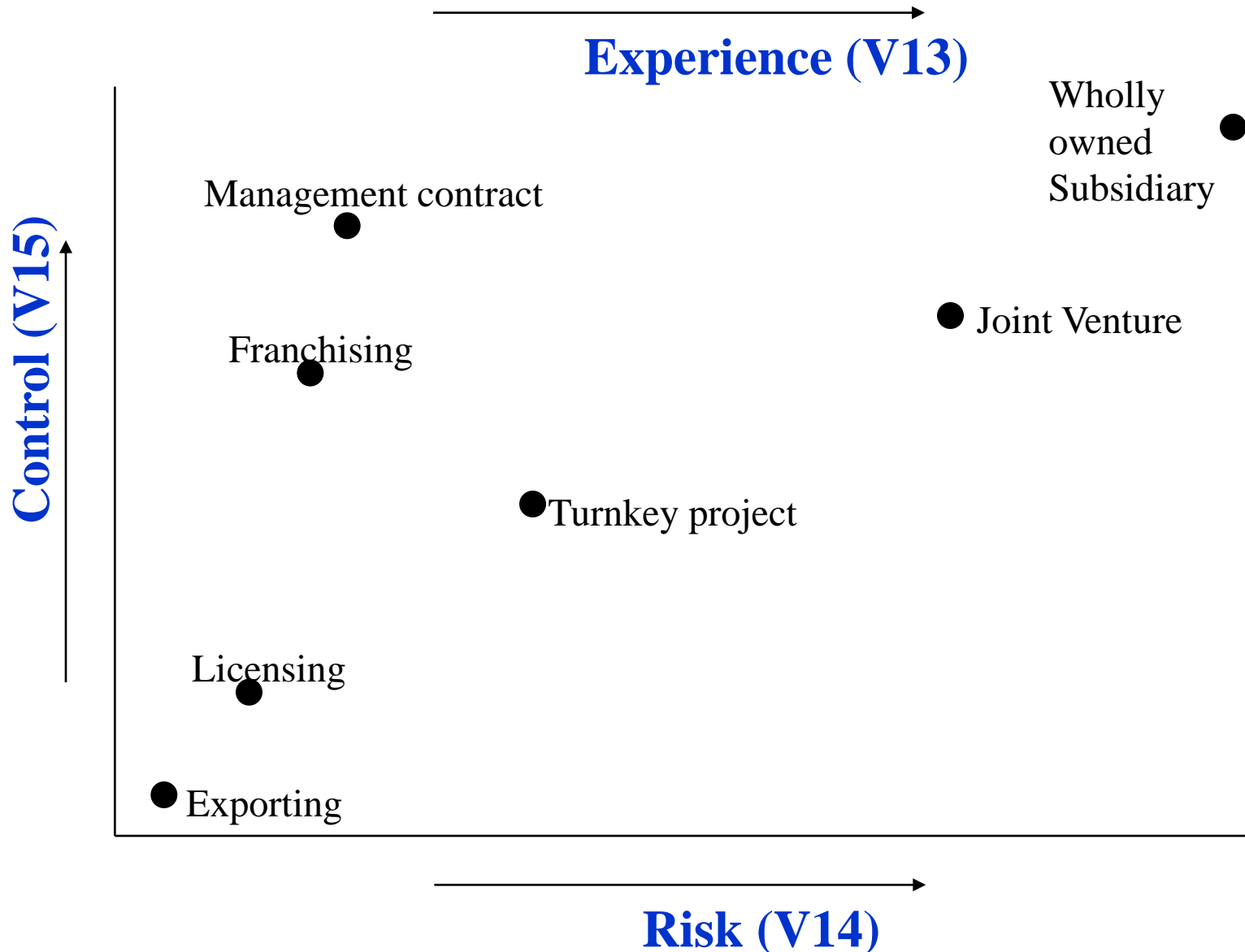
(Shi, Siu & Ho, 2001)

Strategic Variables (V9)
Export-orientation
Market-seeking

Firm specific Variables (V12)
Firm size
International experience
Host country experience
Relationship

ENTRY MODE CHOICE

Location-specific Variables (V10)
Market potential
Production costs
Host government policy
Location of investment

Transaction-specific Variables (V11)
Contractual risk
Asset specificity

Vector 11: transaction-specific variables
This vector deals with the specific transaction

1. **The contract has been subjected to a cross-cultural audit, on a clause-by-clause basis**
   - **Alignment of roles, responsibilities and expectations?**
   - **The engineers, technicians and scientists can communicate?**
2. **XYZ can protect its intellectual property**
3. **XYZ has a due process to resolve conflict**

Evolution of the Entry Mode Decisions

(Wild, Wild & Han, 2003)

Experience (V13)

Control (V15)

Wholly owned Subsidiary

Management contract

Joint Venture

Franchising

Turnkey project

Licensing

Exporting

Risk (V14)

Vector 13: experience to participate in a JV entry mode
This vector confirms the choice of entry mode

1. **XYZ has participated in a similar JV outside China**
   - **XYX can leverage from it's own experience curve**
2. **XYZ has drawn on experiences from other firms in similar ventures**
   - **XYZ draws from global learnings**
3. **XYZ's experience is enterprise-wide, and not vested in a few individuals**

The Hierarchical Model of Entry Modes

(Pan & Tse, 2000) **(V16 = increasing financial commitment)**
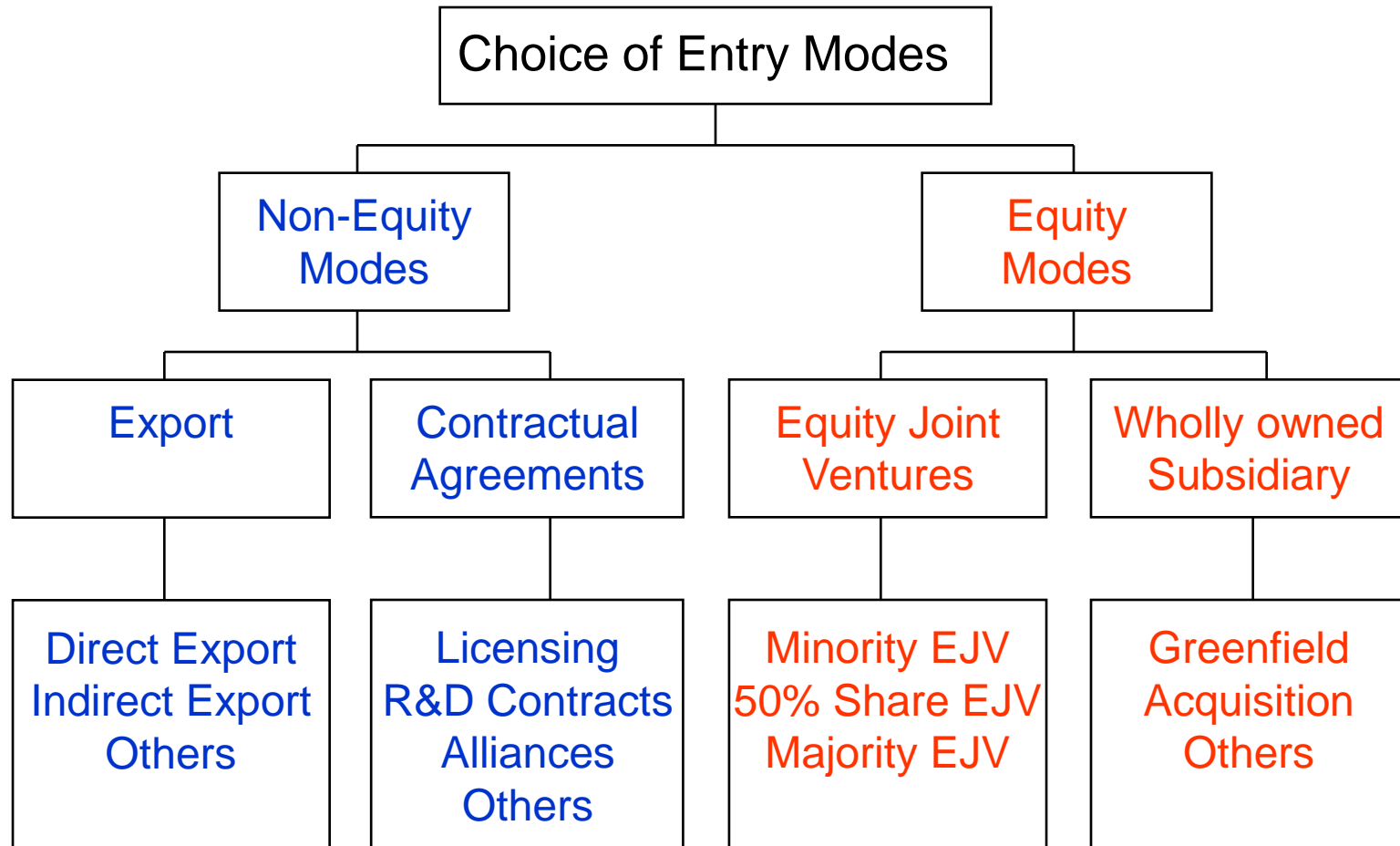
OUTPUTS OF THE VECTOR MODEL

Firm's positioning in host country – go ahead!

Legend:
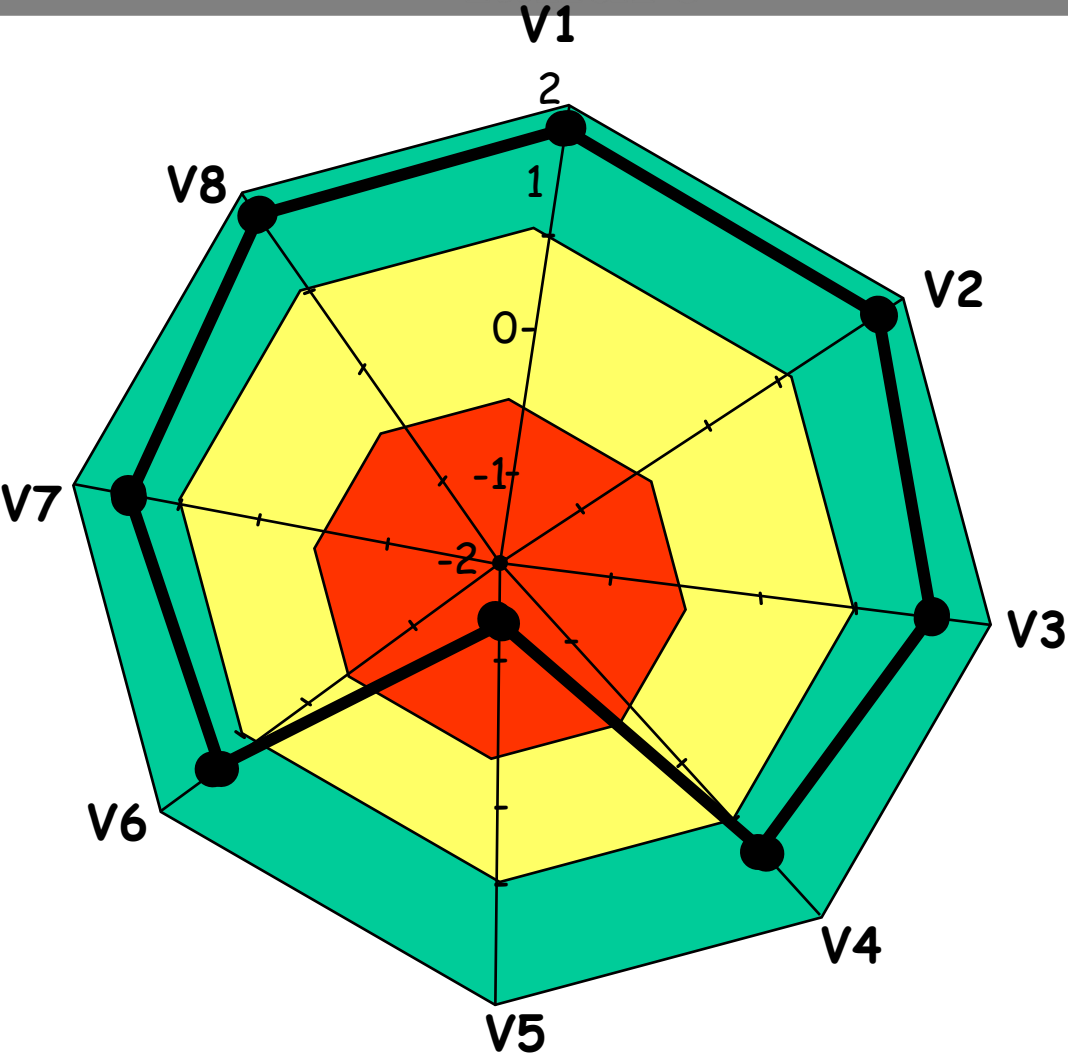- **Stop/Abort** (red)
- **Discretion** (yellow)
- **Go-ahead** (green)
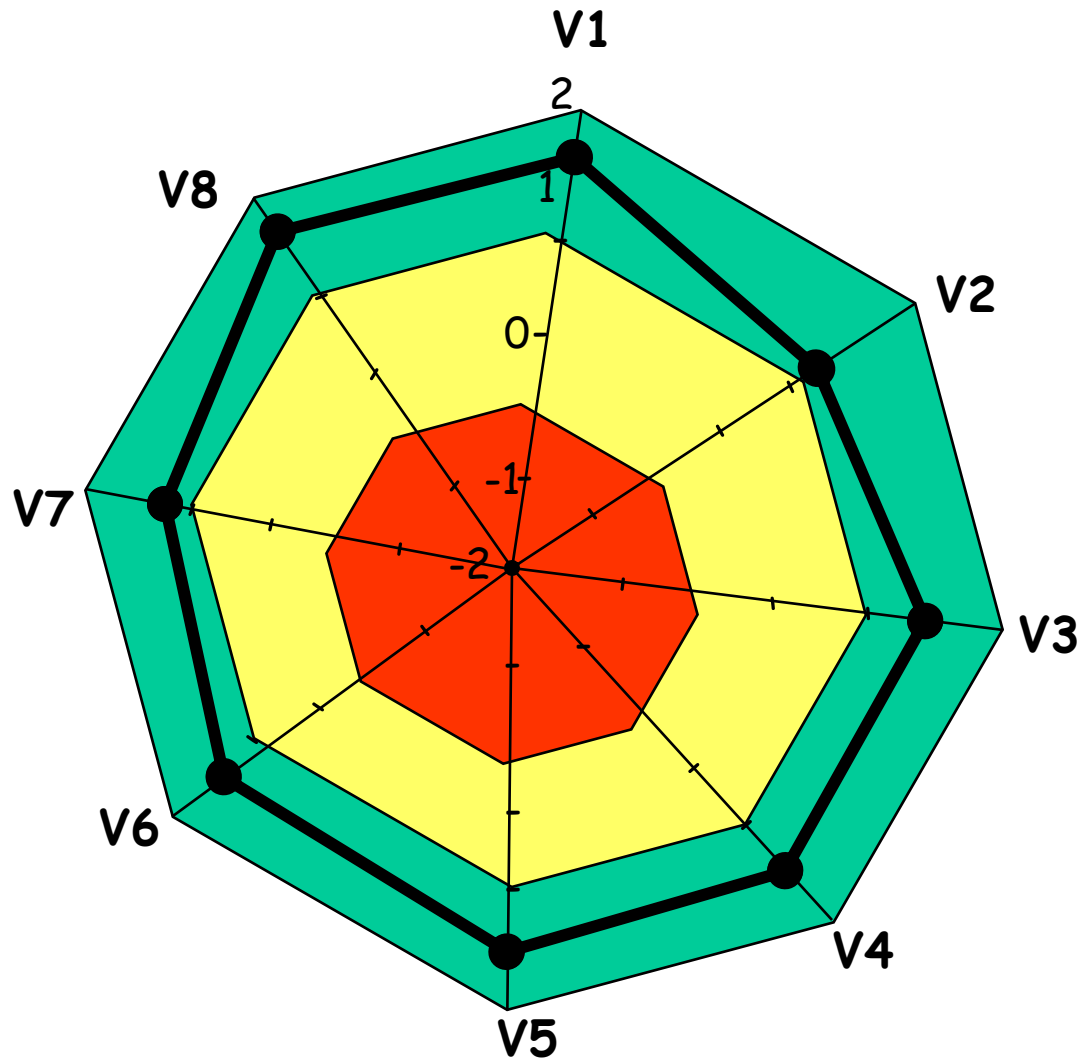
Firm's positioning in host country - structured for long-term suffering and sub-optimal returns
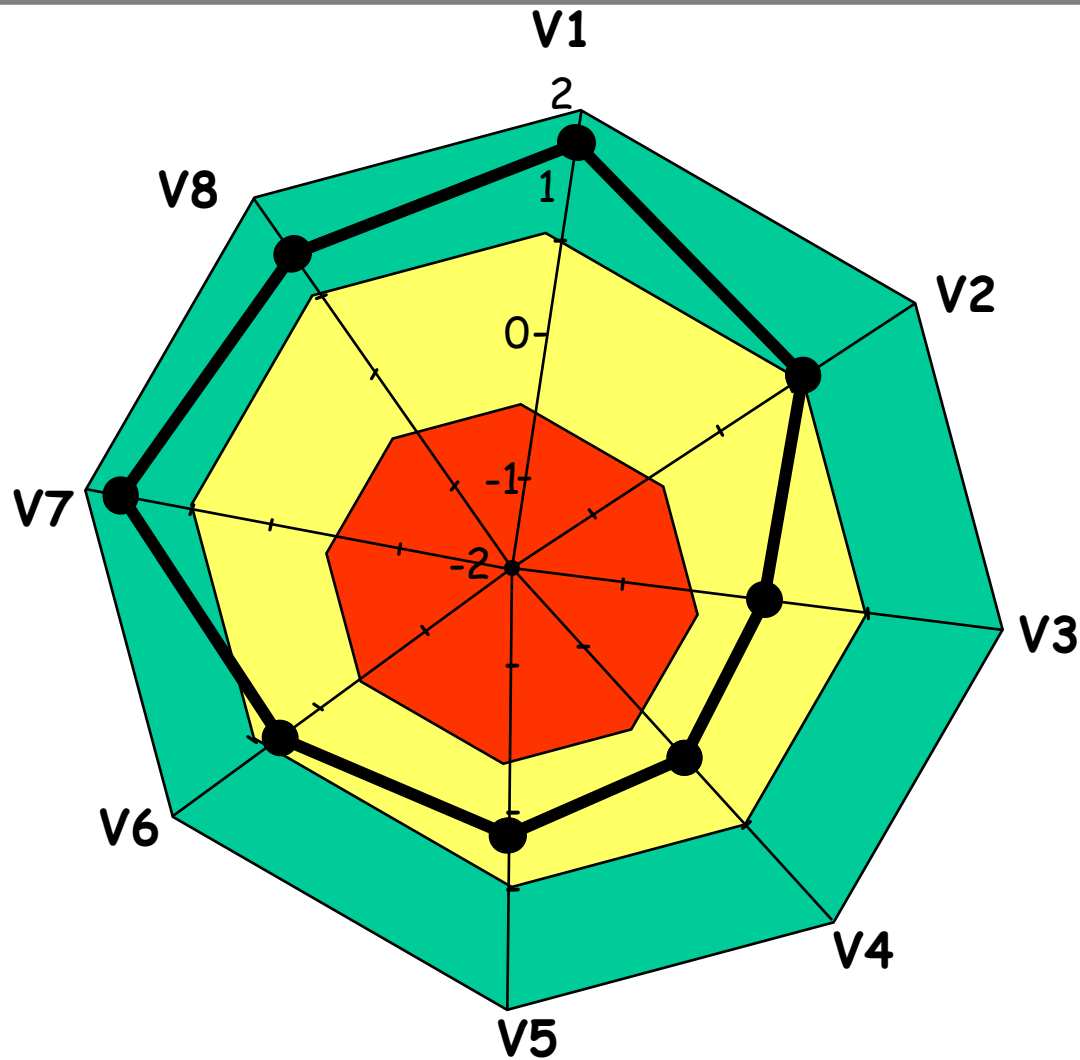
Firm's positioning in host country - structured for failure
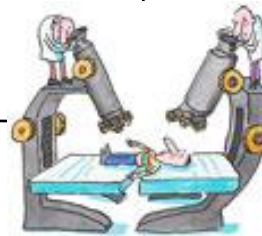
Flow of management actions (1)

Identify 80 global best/next practices, which is context-specific

Identify
80
global
best/next practices,
which
is context-specific

→

Ranking the 80

• 2 management teams
• 1 independent team

Tools

• nominal group
• delphi

→

Analysis

• systems thinking
• q & q analysis
• root cause of Δ

Ongoing
monitor
&
control

←

Implement corrective actions
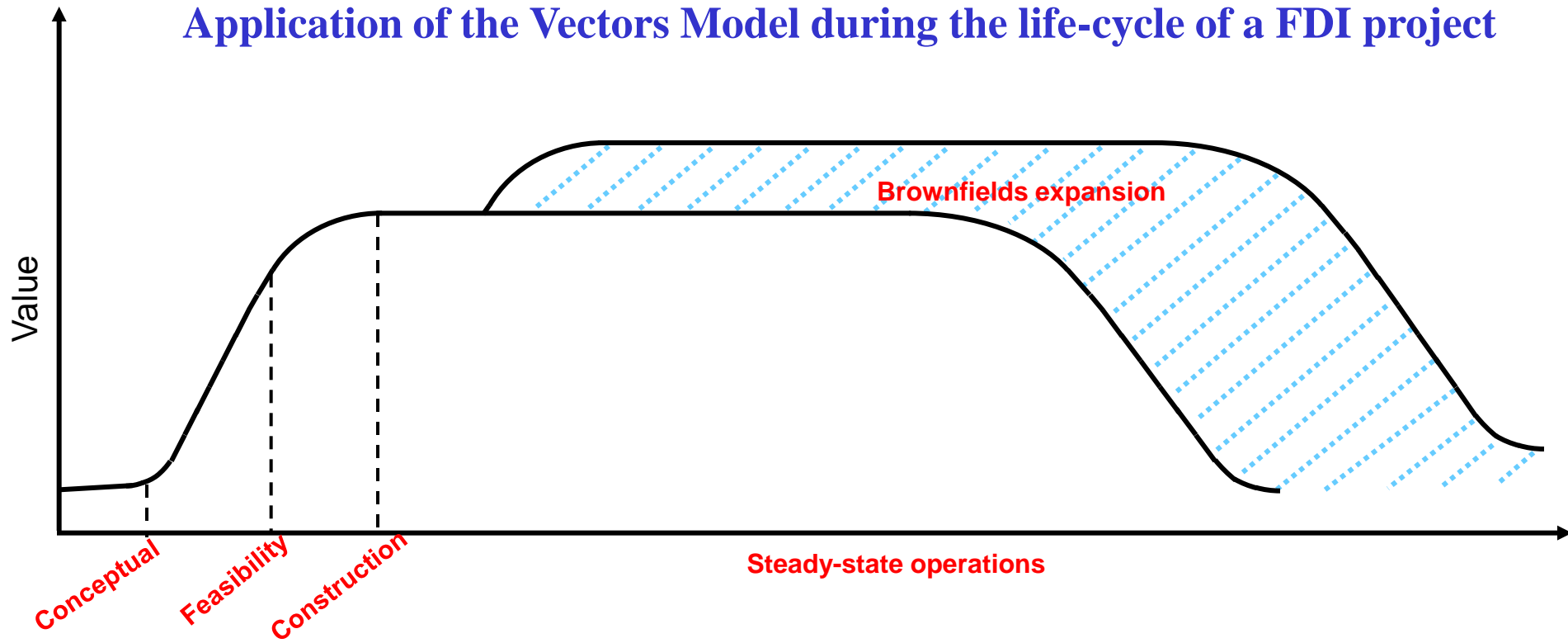
• maintain
• upgrade
• intervention

←

Feedback

• risk profile
• Δ
• corrective options
• optimality
• way forward

Flow of management actions (2)
Application of the Vectors Model during the life-cycle of a FDI project

Value

Brownfields expansion

Conceptual

Feasibility

Construction

Steady-state operations

Legal: LOI → MOU → JV agreement

Management level: Strategy "war room" → Board

Control: pre- → concurrent- → post control

Executive decision making (1)

- **Positioning of each Vector:**
  - Green: Upgrade to "next practice"
  - Yellow: Upgrade to global best practice
  - Red: Strategic intervention
    - Upgrading through:
      - Increased resources, research, re-planning, re-negotiation…
      - While project remain on fast track, or start slow tracking…
    - Put project on hold, while upgrading the Vector in distress
    - Seek partner to upgrade Vector
   - Stop, on hold until conditions improve, sell out..

Executive decision making (2)

- **Dealing with ranking Δ's between management teams:**
  - Joint visioning building: business model, global mindset…
  - Exchange of information, experience…
  - Fundamental re-design of implementation…
  - Management rotation…
- **Entrench delivery of 80 global best practices:**
  - Negotiations
  - Planning
  - Implementation
- **Guide global learning towards a focused search**
- **Presentations – promote; plan; promise; defuse..**

Executive decision making (3)

- **Provides balanced agenda to guide strategic thinking**
- **Integrates various parts of the whole**
- **Structures venture for success upfront or at key milestones**
- **Aligns corporate resources towards a focused pursuit**
- **Allocates corporate resources to strengthen success drives**
- **Provides dynamic management tool for ongoing monitoring**
- **Provides a simple yet powerful presentation tool**

Thank you!
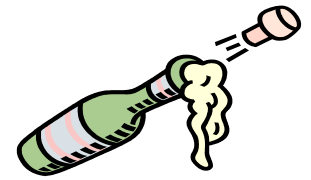
Acknowledgement: my MBL3 research students

Class of 2006 & 2007	Industry sector	Type of research
Tracy Davis	Manufacturing	Multiple case analysis
Clasina Stofberg	IT	In-house case analysis
Stefan Boshoff	Mining	In-house case study
Soovi Hurgobin	Chemicals	In-house case study
Liezel Keyter	Banking	In-house case analysis
Werner Kapp	IT	In-house case analysis
Christo Prinsloo	Biofuel	Multiple case analysis
Thembi Masekela	Banking	Multiple case analysis
Judith Mahaule	Banking	In-house case analysis
Andries Wilken	US philanthropy	Multiple case analysis