

Emerging Multinationals: Manufacturing In a Rapidly Changing Global Landscape

How Powerhouses from Emerging Markets are Reshaping
Global Manufacturing



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Introduction

In recent years, considerable publicity has been given to the acquisition of some well-known Western companies by companies from emerging nations. Examples include: from China, Lenovo's acquisition of IBM's Personal Computing Division and SAIC's takeover of Rover; and from India, Tata Steel's acquisition of Corus and Tata Motors' acquisition of Jaguar and Land Rover. However, the trend is much broader than these high-profile examples. It is clear that some of these acquiring companies are becoming global players and it is therefore noteworthy to look at the processes by which they have emerged onto the world stage and their impact on the manufacturing industry.

Predictions indicate that the BRIC economies (Brazil, Russia, India and China) will together be more than half

the size of G6 economies (United States, Japan, Canada, the United Kingdom, Germany and France) by 2025 and will overtake them by 2040; so, in all probability, the new MNC (multinational corporation) giants of tomorrow will emerge from these economies. Currently, the outward investment from these countries is relatively small compared to that from developed countries such as the US and UK; but this investment is growing, fuelled largely by inward investment and by the strong growth in their economies. This paper examines the internationalisation path of companies from each of these emerging economies with the aim of identifying common themes and significant differences among them, as well as the implications they pose for Western companies.



Executive Summary

Emerging economies are playing a greater role in global trade aided by the process of “globalisation.” As they evolve, a new breed of companies with ambitious internationalisation objectives is appearing. These “emerging multinationals” (EMs) are changing the configuration of global industries. This report examines the growth of some of these companies to understand their behaviour and the implications for existing multinational corporations.

Key Findings

Global Level: A Shift in the Global Economy

The globalisation of markets has resulted in dramatic changes in the patterns of supply and demand around the world. One indicator of these changes is the amount of foreign direct investment (FDI) i.e. the sums invested in one country from another. Global FDI has generally increased more rapidly than global GDP, but it is more variable. An apparently irresistible rise from the mid 1990s was reversed at the beginning of the new century, but growth picked-up again and by 2006 global FDI had reached levels comparable to the 2000 peak.

The growth in FDI reflects many factors and a large part of this investment flows between developed countries as industries become more global, however the newly emerging economies such as Brazil, Russia, India and China, the BRICs, are attracting increasing levels of FDI as companies in developed nations attempt to access their rapidly growing domestic markets and/or to take advantage of the low local cost of production. A more recent, and less reported, trend is the growth of FDI from these emerging economies, which is examined in this report.

National Level: Overseas Investments from Emerging Economies are Increasing

The “break-out” point at which outward FDI from the BRICs started to take off varies slightly from country to country. For Brazil, Russia and China, it seems to have been 2003-04, whilst for India growth was relatively modest from 2000, followed by dramatic acceleration in 2006.

Outward investment from the BRICs now approaches the global GDP average, although China lags in this respect. As these are potentially major future markets for MNCs, inward investment has generally exceeded outward investment. The gap is closing, but China’s outward investment remains significantly less than inward investment.

A substantial part of this outward FDI is in the form of mergers and acquisitions (M&A). Over the period 2004-06 more than half of the FDI from Brazil, India and China was in the form of M&A, but so far Russia has used M&A less extensively.

Company Level: Early Growth in Protected Environments

The majority of the companies studied experienced their earlier growth in market conditions that either encouraged local monopolies or sheltered them from intense competition from Western MNCs. Each was located in a large country with a huge domestic market. As a result, they gained scale and experience before facing formidable international competition.

Partnerships: Learning from Others

Several of these companies engaged early in significant collaborations, which helped them develop their competencies. In some cases, this was with a Western joint venture partner hoping to penetrate their home market (e.g. Ranbaxy-Lapetit, Embraer-Piper Aircraft, MTS-T-Mobile, Birla-Kaiser Aluminum and Chemicals, TCL- Luk’s Industrial and Thomson Electronics). In other cases, the competence was developed as a contract manufacturer for an established company (e.g. Wanxiang-Zeller, Haier-Liebherr and Welbilt). The Chinese companies, in particular, seem to have actively sought out competencies to help them grow.

Strategic Leadership: Long-term Vision

Most of the Brazilian, Russian and Chinese companies started as state-owned enterprises (SOEs). The others were privately held companies of one form or another. The Indian companies were primarily family-owned with a dominant equity holder. As a result, all were free to take a longer-term view of strategy.

In the Indian and Chinese cases, a key leader, who was often but not necessarily the founder, can be identified as the person behind the company's strategy and internationalisation (e.g. Birla-Aditya Birla, Ranbaxy-Parvinder Singh, Haier-Zhang Ruimin, Wanxiang-Lu Guanqiu, TCL-Li Dongsheng)

Early International Experience: Methods and Motives Were Varied

Most of these EMs studied gained international experience well before the respective economic break-outs in their countries. There is no single pattern to explain this early internationalisation and their methods and motives appear to have been varied, including:

- Exports to new markets (all companies)
- International investment greenfield facilities, joint ventures or mergers and acquisitions to facilitate access to new markets (virtually all of the companies)
- Upstream investment to secure raw materials (e.g. Petrobras, Vale and Aditya Birla)
- Downstream investment to improve value capture and secure routes to market (e.g. Aditya Birla, Norilsk Nickel)
- Escape from restrictive legislation in the home market (Aditya Birla)

Many of the companies made their early international investments in other developing markets often with cultural or political links to the home economy (e.g. Birla, Haier and TCL in Southeast Asia, Ranbaxy in sub-Saharan Africa, and MTS in the former Commonwealth Independent States). Those companies seeking raw materials had to invest where the resources were located (e.g. Vale in Canada

and Birla's Hindalco in Australia). Wanxiang is an exception in that its first international investment was in the USA, but this is explained by its earlier position supplying this market as a subcontractor. Many of the companies have subsequently invested in North America and/or Western Europe as a means of penetrating these rich markets.

Growth Strategy and Tactics: Reliance on M&A Grows

All of these companies benefit from a cost advantage over companies operating in the West. This has enabled them to be profitable in countries or market segments that were unattractive to Western companies. For example, the Indian and Chinese companies have sought to exploit their cost advantage by attacking low-margin segments from textiles (Birla) and generic pharmaceuticals (Ranbaxy) to cardan universal joints (Wanxiang) - sometimes with unbranded products, but often as subcontractors for Original Equipment Manufacturers (OEMs). The profits earned have been invested in product development to move up into higher profitability segments in developed economies.

The cases demonstrate all the modes of international expansion (greenfield, joint ventures and M&A), with the companies selecting that which was expedient at the time. One clear trend, however, is the recent reliance on mergers and acquisitions; this fits with the companies' increasingly strong financial positions, their increasing access to capital and the global surge in M&A activity. Recent examples (in 2007) include Brazil's Vale purchase of Inco for US\$17bn and India's Hindalco (Aditya Birla Group) purchase of Novelis for US\$6.4bn.



Implications

As the developing economies grow and as their level of outward FDI increases, we can expect EMs to become an even more potent force in the world economy. The cases in this report suggest that existing MNCs will have to pay special attention to the threats posed by these aggressive new competitors.

The case studies suggest that EMs are internationalising rapidly, partly as a result of using M&A, so established MNCs may soon expect to find themselves confronted by new competitors in both developed and developing markets. They should explicitly consider the possibility that competitors in emerging markets may expand much more rapidly than might be anticipated.

Most EMs have a cost advantage over established MNCs. Strategies to combat an attack on price must be developed. Concentrating on innovation and premium sectors at the expense of lower-margin products and markets, may be dangerous on two counts. Firstly many EMs have used these low-margin sectors to establish their “beach-head” and, secondly, they have gone on to develop innovative, premium products of their own.

The scale of recent M&A activities is such that MNCs should consider whether they or their subsidiaries may become a target for such activity and, if so, whether this could fit with strategic objectives. Many MNCs are already considering their global footprint strategy particularly as a means to penetrate emerging economies or to gain access to local talent pools and low-cost resources. They may themselves evaluate growing companies in emerging markets as potential targets both to achieve these aims and also to eliminate potential future global competitors. The growth of some EMs suggests that MNCs should be very careful in using JVs or other collaborations as temporary tools to penetrate emerging, and possibly protected, markets and in using third-party manufactures to reduce production cost. Both approaches have helped create EM competitors.

However it is not only the MNCs that will face a new competitive environment. The EMs will increasingly find themselves in competition with other EMs from their own

home bases and from even more newly emerging economies. These EM competitors will have the same cost advantages and appetite for growth, so competition will be fierce and their growth may falter. At the same time many of the EMs have turned to the capital markets to fuel their aggressive growth plans. They may find that these markets are less tolerant of low returns and long paybacks if growth starts to falter.

In the pages that follow, we take a close-up look at each of the BRIC countries in terms of economic trends and the manufacturing industry and provide sample case studies to illustrate the rise of emerging multinationals and their growing global impact.



Countries and Companies in Study

		Sector	Foundation	Turnover (US\$bn)	Employees
Brazil 	Petrobras	Oil/energy	1953	96	69,000
	Vale	Mining/metals	1942	33	55,000
	Embraer	Aircraft	1969	5	24,000
Russia 	Norilsk Nickel	Mining/metals	1935	12	84,000
	MTS	Telecommunications	1993	6	
India 	Aditya Birla	Conglomerate	1857/1919	24	100,000
	Ranbaxy	Pharmaceuticals	1937	2	12,000
China 	Haier	White goods	1984	14	50,000
	TCL	Electronics	1980	7	60,000
	Wanxiang	Automotive components	1969	4	40,000

Study Methodology

In this study, we developed case studies of significant firms and examined these in the context of political and economic developments in their home economies and in their target markets. Our purpose was to gain an understanding of their growth patterns and the developments that allowed them to expand beyond the boundaries of their home countries and into the global arena, and how these were in turn influenced by the context in which they grew. The information used was primarily from secondary sources, which are acknowledged at the end of this report, and the analysis is qualitative rather than quantitative. The objective was to examine companies that were broadly in the manufacturing sector since this is an area where overseas investment is at it most tangible. After an initial scan, case companies were chosen because of their success at internationalisation and to provide contrasts in approach.

Brazil: M&A Activity and Privatisation

Drive Growth

Country Overview

Brazil has a land mass only slightly smaller than the United States, with a population of 190 million. By constitution, it is a federal republic of 26 States, Federal District and 5,564 Municipalities. Brazil is the largest market in Latin America and the world's fifth most populous country. It is the eighth largest economy in terms of purchasing power and the tenth largest at market exchange rates. Its 2006 GDP was \$1.07 trillion at current market exchange rates and purchasing power parity, \$1.71 trillion. The growth rate has averaged 3% since 1993. Its GDP comes mainly from services (64%), followed by industry (31%) and agriculture (5%).

The internal economic environment has improved modestly in recent years. The economic turbulence in the early 1990s has been stabilised due to the improvement of macroeconomic conditions. The government carried out programmes to combat inflation, poverty rates and income inequality. The implementation in 1994 of the Plano Real – a set of measures taken to stabilise the Brazilian economy –

successfully reduced the inflation rate from 66% in 1995 to 4% in 2006. According to a forecast by The Economist, Brazil's inflation rate will average 4% between 2008 and 2012. Brazil joined the World Trade Organisation (WTO) in 1995.

Manufacturing Industry

Currently 12 Brazilian firms are on the list of the top 100 emerging multinationals from the BRIC nations. There are more than 40 Brazilian firms operating all over the world; most are from the manufacturing industry and tend to share some similar characteristics. Historically, these firms were formed as state-owned enterprises, with full support from the government. Many, but not all, have since been privatised.



Economic Trends

Brazil's GDP grew fairly steadily from 1980 to the late 1990s after which it went into decline for about five years. However, growth restarted in 2003 and by 2005, Brazil's GDP had outstripped its previous peak in 1997.

Inward FDI was flat until 1995, and then it grew strongly until the end of the century, reflecting the impact of the Plano Real and the liberalisation of the economy. It subsequently fell back until about 2003, reflecting the difficulties in the economy, after which it began to grow again.

Most of this outward FDI has been in the form of mergers and acquisitions. The number of cross-border M&A agreements had been increasing, reaching a historic high of 57 deals in 1998. Since then it has stabilised at around 30 deals, but the total value of M&As has surged, reflecting the magnitude of the deals being made.

The following case studies provide examples of growing emerging multinationals in Brazil.

Case Studies

Petrobras

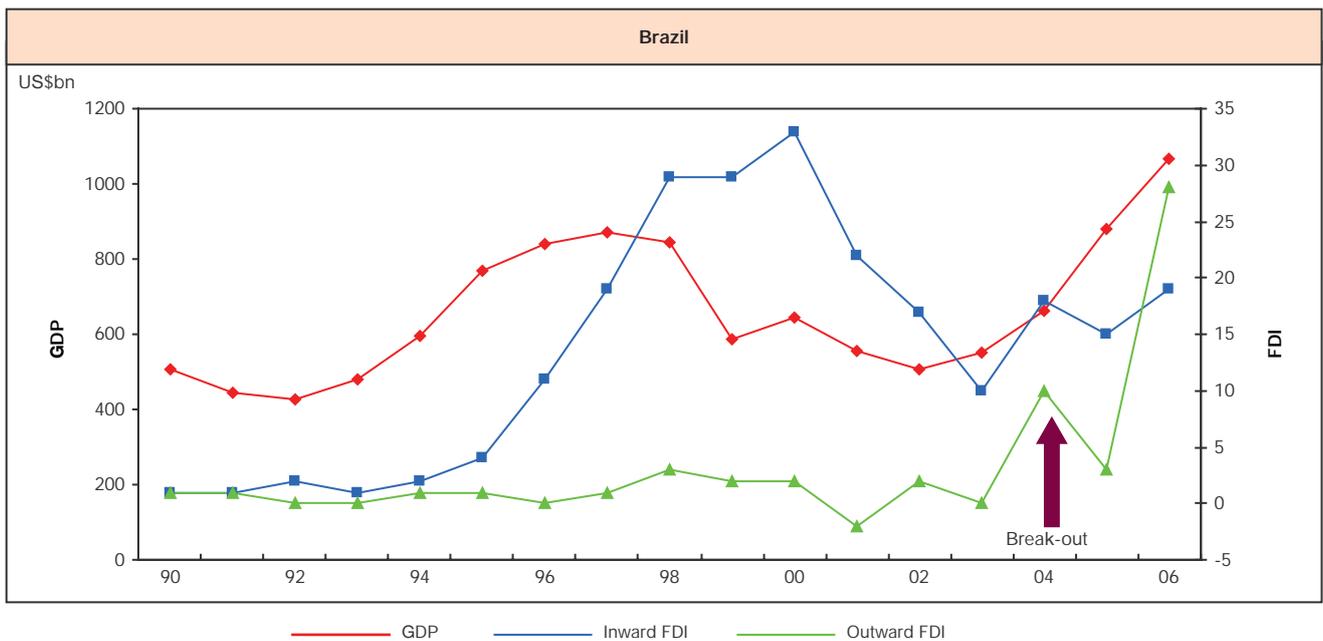
Overview

Petrobras is Brazil's state-owned oil company (32% of equity and 56% of voting shares are owned by the Brazilian government) and is the largest industrial firm in Brazil. It has an integrated business matrix including oil and oil derivative exploration, production, refining, marketing and logistics service, both in Brazil and overseas markets, represented in 27 countries across five continents (South America, North America, Africa, Asia and Europe). Petrobras is a world leader in deep-water oil exploration and production. It was among the world's top 10 firms in the latest Platts global energy performance rankings in 2006.

History

Founded in 1953 by the Brazilian government, Petrobras has enjoyed strong political and financial support, receiving oil resources and refinery facilities from the National Petroleum Council (CNP). At the time, oil production was 2,700 barrels a day (representing 27% of Brazilian demand), but oil products were imported. Petrobras enjoyed a monopoly role in the domestic petroleum industry until 1997.

Economic Trends - Brazil



Initially, the firm's operations focussed on increasing domestic oil production and exploration of domestic oil reserves in accordance with a self-sufficient strategy for energy. In this development stage, Petrobras' international activities focussed on seeking oil supplies. It started exploration abroad to access additional oil reserves and open new refineries. It sourced oil supplies from Saudi Arabia and Venezuela and then gradually expanded to eight countries/regions including Colombia, Argentina, Middle East and North Africa. The diversified oil supply fit well with its goal of meeting oil demand for the domestic market. The growth of its refinery capability changed the structure of imports. At the start of the company, 98% of imports were oil products while 2% were crude oil; however, by the end of 1967, 92% of imports referred to crude oil and only 8% comprised oil-products. Petrobras became self-sufficient in producing gasoline, diesel fuel and kerosene. Meanwhile, the government also gave Petrobras exclusive rights in oil and oil products imports.

In 1968, Petrobras developed innovative offshore drilling techniques that helped the company become a global player with access to more reserves. In 1970, 34% of the oil production came from offshore explorations and approximately 65% of the area blocks were in water with depths of more than 400 metres. Consequently, the company has increased its drilling activities in deeper water and has become a leader in offshore deep-water drilling technology. This has given Petrobras a competitive advantage in its international plans for expansion, allowing it to partner with other oil firms such as Shell, Texaco and Pemex.

After the oil crisis in the 1970s, Petrobras changed its strategy from relying heavily on imports to looking at exploring overseas oil supplies and focusing on both developing domestic sources and on foreign projects as a means of hedging its energy bets. In the middle of the 1980s, Brazil exceeded 500,000 barrels of oil a day to become the third largest producer in Latin America, behind Mexico and Venezuela. Without steering from its goal to supply the domestic market, Petrobras began to export oil to other countries. Oil production rates and oil reserves surged to nearly 2 million barrels per day in 2006.

The event that significantly affected Petrobras' development strategy was the Oil Law in 1997, which ended Petrobras' legal monopoly, opening the oil industry to private initiatives. The government also set up an independent agency to award exploration rights, making Petrobras just another competitor in the oil sector. Big names such as Shell, Exxon

Mobil, BP and Texaco appeared in the various oil and oil-derivatives sectors in Brazil. The new competitive landscape forced Petrobras to adapt its strategy and look to the international markets to survive. In its business plan for 2008 to 2012 and the Petrobras' Strategic Plan 2020, the firm intends to invest \$15 billion abroad. Investments mainly flow to the United States, Argentina and Africa, and 70% focuses on international exploration and production activities. Now, its foreign oil projects can provide 10% of Petrobras' output and the share soon could increase. A recent discovery in Nigeria could add another 100,000 barrels a day to the company's international oil output.

Petrobras' next moves are into the Asian markets by purchasing 87.5% interest in the Japanese refinery Nansei Sekiyu K.K. for approximately US\$50 million from TonenGeneral Sekiyu Kabushiki Kaisha (TGSK), a subsidiary of ExxonMobil. Petrobras intends to use this opportunity as a foothold in the Asian markets and strengthen its global presence.

In January 2007, Petroleum Intelligence Weekly (PIW), one of the most respected power sector publications, rated Petrobras the eighth biggest listed oil company in the world and the 14th largest out of 125 companies in terms of overall classification

Vale

Overview

Vale, known as Compendia Vale do Rio Doce (CVRD) until 2007, was founded by the Brazilian government in 1942, and later privatised in 1997. Currently, it is the world's largest iron ore miner, operating on five continents with over 100,000 employees. Vale's main business, iron ore and pellets used in steel production, accounts for more than half of the company's sales. It also represents a third of the world's ocean-shipped iron ore. Vale also mines bauxite, nickel, kaolin and potash. Other products include steel, ferroalloys, copper and aluminium. Vale has holdings in hydroelectric power generation and in rail and shipping businesses, primarily to support its mining activities.

History

Vale's initial purpose was to explore Brazil's vast mineral resource deposits; by 1949, it was recognised as a worldwide mineral supplier accounting for 80% of Brazilian

iron ore exports. In 1953, it sent its first shipment of iron ore to Asia. In the same year, it used a Brazilian ship to transport minerals to the United States for the first time. To improve its export practice, it began to restructure its logistics by introducing its own fleet of cargo ships. Vale then signed and secured long-term exporting contracts with Japanese steel firms and German mills. Up to this point, Vale's internationalisation focussed on expanding its overseas export business. In 1974, Vale became the largest iron ore exporter with 16% of the transoceanic iron ore market.

In 1989, Vale released a strategic plan, specifically focusing on globalisation. Previously, its investments were concentrated within the Brazilian borders and international business was limited to exports. Vale restructured its capital, risk prevention and corporate governance during the 1990s. The firm launched its American Depositary Receipts programme; tradable in the United States' over-the-counter markets, in 1994 and in 1997, the firm privatised. In the second year after privatisation, Vale's corporate governance moved to a decentralised model. Vale achieved a profit growth of 46% in 1996, and in 1999 attained record high profits.

Entering the new millennium, Vale restructured its business to align with a global scope by spinning off operations such as steel and wood pulp to focus on mining and logistic services. Globalisation in the new century actually makes domestic and overseas environments more closely integrated.

To maximise their benefits, Vale consolidated its domestic iron ore business by acquiring local iron ore producers to control 85% of Brazil's 300 million tonnes annual iron ore production, while at the same time, it began diversifying its product portfolio by moving into the non-ferrous metals market in order to reduce its dependence on iron ore through acquisitions. In 2001, Vale bought Sossego Mine (copper); in 2003, it announced a partnership with Mitsui, a Japanese logistics company, for intermodal shipping services; and in 2006, it acquired Caemi (Kaolin). Also in 2006, Vale offered an all-cash takeover worth US\$17 billion to acquire Canadian firm Inco and was the largest purchase by a Latin American firm overseas. By taking over Inco, Vale became the second-largest mining company in the world after BHP Billiton. Meanwhile, Vale also acquired Canico Resource for about \$800 million. In 2007 Vale entered the coal mining business by purchasing the Australian coal mining company AMCI Holdings for \$656 million.

Vale is expanding both horizontally and vertically, to become more global. Now Vale has an integrated business matrix that spans the world, with activities in mining, production and logistics. Its international business is closely linked to its domestic operations. In overseas projects, Vale focuses on R&D activities, dedicating 64% to mineral research and production activities. It has operations in the United States, Bahrain, France, Belgium and Norway.



Embraer

Overview

Embraer, a Brazilian aerospace corporation, produces commercial, military and corporate aircraft, and offers aerospace-related services. It is the third-largest commercial aircraft manufacturer in terms of annual delivery volume, after Boeing and Airbus, and the fourth largest in terms of workforce, after Boeing, Airbus and Bombardier.

History

Embraer was founded in 1969 as a state-owned company, with a military leader as its chairperson. Its formation resulted from the Brazilian government's desire to commercialise its Bandeirante aircraft project. In 1975, Embraer started to export the Bandeirante, selling 500 planes to 36 countries, and establishing Embraer in the aviation industry. Since then, Embraer has manufactured and designed aircrafts for both domestic and overseas markets. Its first pressurised aircraft (the Xingu) took flight in 1976 and made its debut at the Paris International Air Show in 1977. The French Air Force was its primary customer.

Following a request from the Ministry of Aeronautics, Embraer moved into combat aircraft. Tucano was its most successful turboprop military trainer, with more than 650 units sold around the world. In the late 1970s, Embraer developed the Brasilia, a turboprop aircraft with a 30 to 40 passenger capacity, as an export product. The quick market penetration of Brasilia was largely due to the trust that Embraer gained in international aviation. It established a cooperative relationship with Piper Aircraft, an American firm, to assemble many general aviation products by licence. This relationship was crucial for Embraer, helping it create an international services network.

In military products, Embraer was chosen to join the AMX Program, co-initiated by the Italian Air Force. The company was responsible for key components like fuselage design and development. From this project, Embraer gained access to new technologies that were important in its further product development capability.

In the early 1990s, Embraer suffered a financial crisis with the failure of the product Vector, co-developed with an Argentinean partner, and because of the implementation of the Constitution of 1988, which reduced the key support provided to the aviation industry by the government. The end of the Cold War also reduced the demand for defence products. In 1994, privatisation began and Embraer, still in a financial predicament, changed its organisation structure to be more market-oriented. Embraer shifted its global

strategy to partnerships and technical alliances with global suppliers to control development cost and risks. This new business model was applied to the development of a 45-seat regional jet. Embraer partnered with suppliers from Chile, Spain, Belgium and the United States, gaining technology and investments. The international partners set up subsidiaries and offices in Brazil to achieve production and logistic efficiencies. The successful E model is a derivative of this approach and directly pushed Embraer to become a competitor to Boeing and Airbus. Embraer thus was able to move up its product range.

The booming low-cost airline operators also laid a solid ground for the regional jet market. Embraer was Brazil's largest exporter from 1999 to 2001, and the second largest in 2002 to 2004, after Vale.

Country Discussion

All the case companies started as state-owned enterprises and enjoyed state funding and monopoly conditions in the early stages of their growth. Both Vale and Embraer were privatised in the mid-1990s when the economy was being liberalised and the government faced growing debt. Privatisation have led to growth strategies, which has improved profitability. Although Petrobras was not privatised and remains state-owned, it lost its monopoly position in 1997, however, the strategic importance of oil and refining has led to strong growth.

Petrobras developed its core competence, deep-water offshore drilling, internally; however, offshore drilling projects are high risk and require cooperation and partnerships with other international firms, such as Shell and Chevron, to reduce cost and risk, and have additional opportunities for learning. Embraer was able to learn through its joint venture partnership with Piper and later with other international partners.

Vale started exporting—while still a state-owned enterprise—in 1953, under the Vargas administration, but it did not invest abroad until 2006, well after privatisation, to gain access to resources. Petrobras initially invested offshore for the same reason, but earlier in 1970, sought after strategic oil resources during the international oil crisis. More recently, it has invested to penetrate new markets. Embraer has remained focussed on its export model as its products are easy to deliver.

Both Vale and Petrobras have recently made very large acquisitions contributing significantly to the large outflow of FDI from Brazil in the last two to three years.

Russia: A New Generation of MNCs Emerges

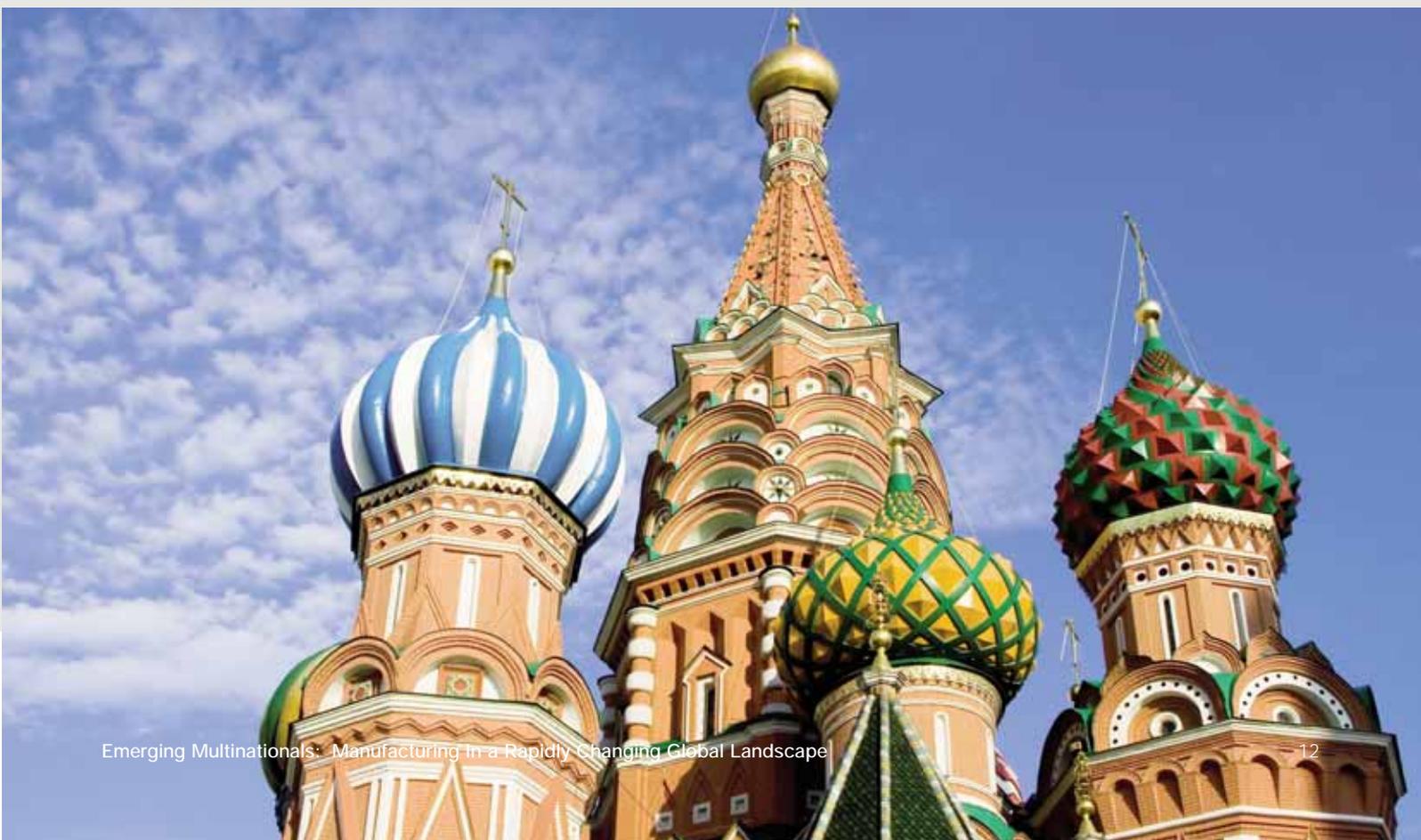
Country Overview

A territory spanning 11 time zones and covering one-eighth of the world's land surface, Russia is the largest country in the world and the richest in terms of natural resources. Russia is the most populous country in Europe with over 143 million people. Russia consists of 89 federal entities including 16 autonomous republics, 5 autonomous regions, 10 national regions and many provinces and metropolitan areas.

Russia was one of the two superpowers in the world in terms of military capacity—from the 1950s to early 1990s. The military-oriented industry development strategy helped Russia establish its heavy industries and manufacturing capabilities. Its metallurgy/metal, energy and machine building accounts for more than 40% of total industry outputs, whereas the consumer industries only make up about 16%. This imbalance in its industrial structure not only caused serious economic shortages in the USSR era but also continually and strongly affects current Russian foreign investments and the behaviours of emerging Russian multinational corporations.

Despite being hit by hardships and crisis in the last century, Russia has always managed to emerge as a survivor, and stronger. In the last ten years, after radical reforms and turbulent transformation of society, Russian economic growth has been substantial and sustainable. GDP has increased more than 5% on average and inflation has been controlled at 9%. Although this has been largely attributable to higher global prices for Russian export commodities, a much more stable political and macroeconomic environment has transformed Russia towards a market economy. Russian GDP in 2006 was \$979 billion, ranking 11th globally – after Brazil.

Russia has experienced steady economic growth since the turn of the century and both Inward Foreign Direct Investment (IFDI) and Outward FDI (OFDI) have increased. In 2006, it was in the fourth place for highest OFDI amongst all developing nations. A new generation of Russian multinational corporations is emerging.



Manufacturing Industry

Russian industrial production is dominated by heavy industries. The energy, machinery building and metal and metallurgy industries account for more than 40% of total industrial production in the country. Industries serving end customers such as food processing and fast moving consumer goods (FMCG) only comprise 16% of total industrial production. The others are mainly chemicals, forest products and construction materials.

Russian companies usually are very vertically integrated- from early-stage raw materials preparation and component fabrication to final product assembly or integration. Oligopoly has replaced the state monopoly in many strategic industries. However, free competition, lower barriers for entry and exit, and especially grass-roots entrepreneurship are still needed in all industries.

Russian small- and medium-sized companies were mostly privatised during 1992 and 1994. However, the change of ownership does not make every company develop better. SME managers urgently need management and innovation training to enhance their capabilities to survive and grow.

Larger Russian companies have widely adopted corporate governance reform to build new institutions and satisfy shareholders' requirements. The privatisation of these larger companies happened later and took much longer. During the early years of the new century, many corporate reorganisations took place as well as mergers and

acquisitions between large companies. The Russian government has a new policy to develop national flagship corporations in strategic industries through M&A and corporation governance enhancement.

International Activity

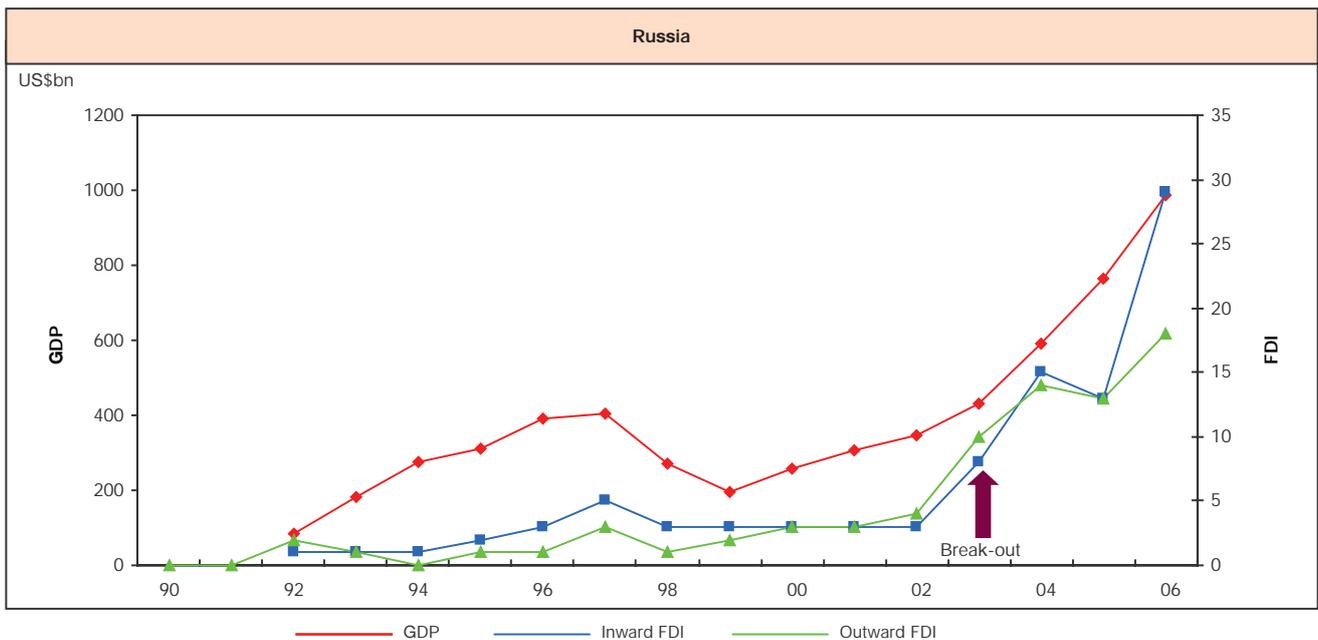
The former USSR had strong trade and industrial integration with Eastern communist countries. During the 1990s, the Russian Republic "externalised" trading relationships with the Commonwealth Independent States (CIS) countries. As a result of Russian industrial structure, resource-oriented commodities, which include oil, gas, ores and metallurgy products, comprise more than 70% of total exports; in contrast, machinery, equipment, transportation and agricultural raw materials and food products, account for more than 60% of total imports.

In the last seven years, Russia has emerged as a major FDI player in both outward and inward directions. International interactions, especially international operations, have promoted Russian industry's competitiveness in terms of best practices, strategic capabilities and business performance.

Economic Trends

Following the decline and break-up of the USSR, Russia's economy grew from 1992 to 1996/97. Thereafter it declined for a couple of years, but strong growth restarted from 2000 with GDP surpassing the previous high in 2003 and doubling again in 2006.

Economic Trends - Russia



Inward FDI grew steadily until 2002 and then grew explosively increasing by a factor of five by 2006.

Outward FDI levels are broadly comparable to inward FDI levels. Like inward FDI, they grew steadily but accelerated dramatically from 2003. M&As accounted for most of the outward FDI in 2003, but the importance of M&As has since decreased significantly.

The following case studies seek to explore why, and how, Russian companies have started to internationalise.

Case Studies

Norilsk Nickel

Overview

Mining and Metallurgical Company (MMC) Norilsk Nickel is an Open Joint Stock Company (OJSC). It is the largest mining company in Russia, as well as the world's largest producer of several strategic metals. For example, its world market share of palladium measures about 60%, platinum and nickel 20%, cobalt 10% and copper 3%. The company also produces a large number of by-products, including metallic cobalt, rhodium, silver, gold, tellurium, selenium, iridium and ruthenium.

The company's sales in 2006 were US\$11.550 billion, increasing 61% from 2005 mainly driven by the price increase in most raw materials. Its gross and net profit margins reached 73% and 43% in 2006.

The company has a very vertically integrated value chain—from exploration, mining, enrichment, metallurgical production and sales, to transportation. The company has also achieved complete power support for its own usage in Russia in order to increase its autonomy.

The processes and operations are very complex. For example, the company's largest production site in Taymyr Peninsula has three main different types of product families, starting from seven mines to two main concentrators, and four key plants or workshops.

Taking a snapshot of the company's global footprint in 2006, it owns its main mines and production sites in Russia, US and Australia. Its R&D Institute is located in St. Petersburg and downstream sales offices are distributed in London, Zug, Pittsburgh and Hong Kong.

The company's headcount was 83,600 people in 2006, more than 97% of whom are located in Russia (56% in Taymyr Peninsula, and 18% in Kola Peninsula and St. Petersburg regions).

History

The company was originally built upon a rich copper-nickel ore mining field discovered in the Taymyr Peninsula during the 17th century. In June 1935 the Council of Peoples' Commissars of the USSR passed a resolution "On Building the Norilsk Combine" leading to the country's biggest mining and metallurgical complex. By 1953, the combine was producing 35% of the Soviet Union's total nickel output, 12% of its copper, 30% of its cobalt and 90% of its platinum group metals.

In the last 20 years, the company has experienced a series of radical ownership restructurings resulting from the Russian privatisation programme. It is evident from the company's evolution that it has one clear strategy: to ensure that it can control the entire value chain from the Russian mining sites to the global end customers. This strategy can be traced back to 1997 when the corporation formulated its long-term development plan. To fulfil this plan, the company undertook a series of strategic actions including:

2000: Acquisition of Involvement Norimet Ltd, a London-based metal trading company, to facilitate trading on the London Metal Exchange

2002: Acquisition of SUA Stillwater Mining in the US.

2002-03: Investments in transportation: port, energy etc.

2004: Setting up internationally dispersed sales offices through M&A and organic development

2005-06: Upstream vertical integration to secure sources of raw materials

2007: Acquisition of OM Group Nickel Business Division in US.

The company's strategic objectives seem to have been:

- To grow while exploiting its existing strong production capabilities – for example, the acquisition of Polus in Russia and the OMG Nickel Business acquisition, a horizontal expansion that gave the company ownership of four additional sites in Finland and Australia.
- To penetrate new geographic markets and earn foreign currency. The purchase of Norimet, a London-based metal trading firm, gave it access to the London Metal exchange and thus supported foreign sales. The Stillwater acquisition captured some key international customers, including customers from the United States automotive industry and buyers of palladium jewellery.
- To secure routes to market for its metals and to undertake higher-margin activities downstream of its traditional activities. The Stillwater Mining acquisition in 2002 is a clear example of this. Stillwater brought some downstream conversion activities into the company's control, thus providing an opportunity to trap further value. By converting the metals from commodities to fabricated products, these also tended to "lock-in" customers.
- To secure control of its extended supply chain: Investments in South African gold fields, a joint venture with Rio Tinto for exploration in Southern Siberia and the Far East, and an alliance with BHP Billiton for geological exploration in Western Siberia provided enhanced access to raw materials.
- Logistics control was extended by acquisition of the Yenisey River Shipping Co and the Arctic Circle transportation group.
- Investments in supporting infrastructure included a gas condensation facility.

Thus, the company has been pursuing a very aggressive strategy. Although it has concentrated on M&A, it has also used a range of other options from JVs to alliances and licencing. Unlike many Western companies, Norilsk Nickel currently seems to prefer direct control of the whole supply chain rather than concentrating on core competencies and relying on the market for other activities.

MTS

Overview

Mobile TeleSystems (MTS) is an Open Joint Stock Company traded in New York, Russia and Europe. Serving over 81.97 million subscribers in a total population of more than 230 million, MTS is the largest mobile phone operator in Russia and the Commonwealth Independent States

(CIS). Through a very aggressive internationalisation after 2002, the company serves the regions of Russia, as well as Armenia, Belarus, Turkmenistan, Ukraine and Uzbekistan, in which MTS and its associates and subsidiaries are licenced to provide both fixed line and GSM mobile services. The company's total sales reached about US\$6.4 billion in 2006, increasing more than 27%.

MTS is owned by the largest Russian private consumer service company – Sistema, which is a diversified investor. Sistema works in two fundamental areas – the first is a "core foundation business," which includes telecommunication, high technology and real estate. The second is a "high potential business," which comprises retail, financing, mass media and venture capital. Sistema has driven MTS with a very aggressive and rapid growth strategy empowering it to move into the faster growing mobile phone services arena, and enabling it to pursue a succession of M&As. MTS has floated approximately 47% of its shares; 53% are still controlled by Sistema.

History

MTS was established as a Closed Joint Stock Company (CJSC) by the Moscow City Telephone Network (MGTS), T-Mobile Deutschland GmbH (T-Mobile) and several other shareholders in October 1993. Four Russian companies collectively held 53% of the original share capital, while the German shareholders retained the balance of 47%. In late 1996, Sistema JSFC bought out the Russian shareholders and the Deutsche Telekom affiliate bought the remaining stake from Siemens. On March 1, 2000, CJSC MTS and CJSC RTC merged to form an Open Joint Stock Company, Mobile TeleSystems. On April 28, 2000, the Federal Commission for Securities of the Russian Federation registered the initial issue of OJSC MTS shares. That same year, MTS became the second Russian company to trade on the New York Stock Exchange. Since 2003, MTS' local shares have also been listed.

MTS restructured its corporate governance to transform the old stated-owned management style to a more market-oriented enterprise in its early stage of development. The subsequent internationalisation of MTS has been to expand its customer base and pursue market growth. Growth of the mobile business heavily depends on regional coverage and penetration rates, and subscriber growth is critical. In 2002, MTS started its internationalisation through M&A in the former CIS states. Now, it has operational services in six countries: Russia, Belarus, Ukraine, Uzbekistan, Turkmenistan and Armenia. Although it is a young company with a business legacy of providing classical fixed-line services, MTS is growing its international mobile

service rapidly. It acquired a foreign company every year between 2002 and 2007. Consequently, MTS has emerged as the largest mobile services provider in Russia and the CIS region.

Following its success in CIS, MTS adopted a global benchmarking programme against its main global competitor. It identified brand name development and the development of global strategy as the key requirements for further expansion.

MTS' motivation for internationalisation appears to have been the exploitation of its existing core business model. Its new corporate governance and operational excellence were key enablers in its international expansion. It has concentrated on the former CIS states because these are strongly linked to Russia by culture and heritage. As a result, the expansion to these countries was probably less risky than attempting to penetrate far-off markets.

Once again the company has used M&A as its primary method of internationalisation. MTS started its domestic M&A in 1998 by acquiring Russian Telecom. Afterwards, it conducted successive domestic acquisitions in different regions. These provided practical experiences for additional M&As internationally. However, it also used other collaboration forms such as joint ventures, sharing licences and long-term collaborative agreements. Launching its own network to achieve organic growth is also an approach to grow its business when the infrastructure is not sophisticated.

In summary this is a young company with about 15 years of total operations experience and a decade in international business that has expanded quickly and aggressively through M&A. The transformation of its management structure is thought to have been key to its success in acquiring and integrating its acquisitions in a consistent way. Experience in pursuing domestic M&A targets and then integrating their operations, equipped MTS with the skills to pursue a similar approach abroad.

Country Discussion

Norilsk Nickel has a long history whereas MTS was created fairly recently; yet both have begun to internationalise very recently – in 2002 – as the country began to grow rich on oil revenues and just before the explosion in outward FDI that started in 2003.

Norilsk Nickel had a chance to grow under the command economy of the Soviet Union and was well placed to compete globally as the Russian economy opened up. When it did internationalise, it did so aggressively by upstream and downstream vertical integration to secure resources and routes to market. It used M&A and other mechanisms to secure its targets in widespread countries.

By contrast, MTS was formed as a CJSC as late as 1993, with German companies bringing technology and capital, lured by the prospects of new market opportunities following Boris Yeltsin's reforms. Its internationalism has been largely restricted to seeking new markets and these efforts have thus far been mainly confined to the CIS states.



India: Family Businesses Emerging as International Giants

Country Overview

India has a population of 1.130 billion spread over an area of 3.3 million square kilometres (approximately one-third of the area of the United States). It is composed of 28 states and seven union territories.

India's GDP is only US\$0.9 trillion at market exchange rates, but US\$4.2 trillion at Purchasing Power Parity (both 2006 figures). Growth rate has averaged 7% since 1996 and has risen to about 9% since 2006, partially because of a significant expansion in manufacturing.

In recent years, the economy has benefited from a growth in service industries serving more developed markets. Exports of goods and services now account for 23% of GDP and the country is now a major exporter of software services and software workers. Services now account for 55% of GDP, compared with 28% for manufacturing and 18% for agriculture.

Recently, the government has begun to prioritise manufacturing—both high technology, to provide exports/growth, and traditional industries, to provide employment. A significant expansion in manufacturing has been reflected in a GDP growth rate of 8.5% since 2006.

Manufacturing Industry

Despite the recent emphasis on services, there is a long tradition of industrial manufacturing in India. Many of these longer-standing firms tend to have similar characteristics. They often started as traders broadening into manufacturing later as opportunities presented themselves. Historically, companies tended to be controlled by the families of “promoters” (owners) rather than by independent professional managers. Often, many businesses are linked by complicated cross-holdings with ultimate ownership widely dispersed among an extended family or closely linked sets of families. These groups of companies typically were conglomerates of many types of businesses and it is difficult, or rather



misleading to define the boundaries of the group. It seems this behaviour was encouraged partially by culture, but also by the actions of government in trying to limit the size (and power) of individual companies.

By contrast, some companies have recently emerged with a much more focussed approach. Factors influencing this behaviour include a cadre of sons returning to their country armed with a Western business education, and pressures from capital markets for transparent structures and explicit strategies. This has been reinforced by liberalisation of the economy, which has increased exposure to global markets and competition.

The two types of company are illustrated in the case studies.

Economic Trends

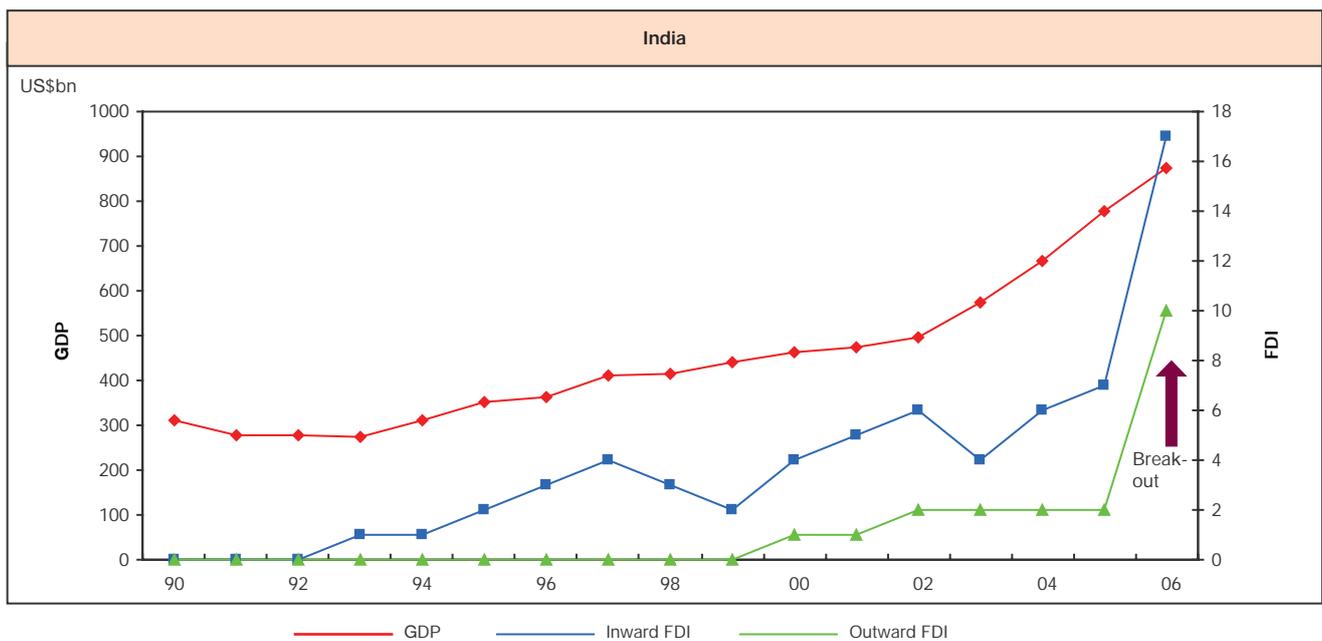
India's GDP has grown steadily since the 1980s, with most of the growth taking place after the mid-1990s, and particularly rapid growth setting in from 2003.

Inbound FDI grew in the mid to late 1990s, but fell back in 1998-99 despite the growth in global FDI. However, it recovered from 2000 onwards and growth has been particularly strong since 2005, reflecting both the global growth in FDI and the improved conditions for investment in India.

So far, outbound FDI levels have been substantially lower than inbound FDI. Outbound FDI effectively started from around 2000 and continued to grow through the subsequent world downturn in FDI. As global FDI began to rise again, outflows from India began to grow strongly and increased markedly in 2006. A substantial portion of this FDI has funded M&As with most of the targets being in Europe or the United States (about 75% for 2000-06). The main driver for this recent international M&A activity seems to be access to foreign markets in industries that are being rapidly globalised. The pharmaceutical sector has been particularly active here.

However, it is significant that Western companies are currently often priced at considerably lower multiples of earnings than Indian companies, making such purchases potential bargains as well as being strategically sound. Most deals are cash, rather than stock-based, which is consistent with the strong cash positions of many successful Indian companies and the strong emphasis on family/promoter ownership in the Indian industry.

Economic Trends - India



Case Studies

Aditya Birla

Overview

In aggregate, Aditya Birla is a Fortune 500 company with a turnover of US\$24 billion, a market capitalisation of US\$31.5 billion and 100,000 employees in over 20 countries. The group coordinates its activities under three main businesses:

- Grasim has total sales of US\$4 billion from Viscose Staple Fibre (VSF) and cement – its core businesses – plus sponge iron, chemicals and textiles. UltraTech Cement Limited (a Grasim subsidiary) handles cement with gross sales of around US\$1.25 billion.
- Hindalco has gross sales of around US\$5 billion in aluminium and copper.
- Aditya Birla Nuvo Ltd (formerly Indian Rayon and Industries Ltd.) has a consolidated gross income of around US\$2 billion from Viscose Filament Yarn (VFY), carbon black, branded garments, fertilisers, textiles and insulators, plus life insurance, telecom, Business Process Outsourcing (BPO), IT services, asset management and other financial services.

The Aditya Birla Group is controlled by The Birla Family whose business holdings extend beyond the Group itself. Their approach to business has been characterised by an emphasis on control by family relationships and the use of “padtha” (free cash flow) as a major business control.

Despite recent restructuring, the ownership of the international operations remains complex. The origin of this complexity may have resulted from the way the company has evolved, with family members starting new companies as well as inheriting stakes in existing ones, however it may also have been a means to avoid some of the restrictions the Indian government placed on very large companies especially during the 1970s. This case study focuses on major product groups that are manufactured internationally without too much emphasis on how they are coordinated within the group. However, it must be remembered that at times these similar activities may have been controlled by different family companies that had different ownership structures and which might even have been in competition with each other.

History

The Birlas' industrial empire can be traced back to Seth Shiv Narayan Birla who set himself up as a cotton trader in 1857. The first manufacturing operation (jute milling) was set up by Ghanshyamdas Birla (a grandson) in 1919. Partition at Independence left most of the cotton growing areas in Pakistan and provided an opportunity for the Birlas to establish a textile business based on weaving rayon fibre (viscose staple fibre, VSF). The first steps to industrial expansion occurred in the 1950s under the leadership of BK Birla, but all efforts were internally focussed. Key investments were setting up an Indian plant to produce VSF and replace imports for the textile spinning operations, and the establishment of Hindalco to manufacture alumina, aluminium and aluminium fabricated products. This company was an (temporary) alliance between the Birla group and the American company Kaiser Aluminium and Chemicals Company (KACC), which provided technical expertise.

Internationalisation started first in textiles in the 1970s. Two major factors appear to have driven this. Firstly, AV Birla was very active in this area and was in favour of building overseas businesses. Secondly, during this period, the government began to place increasingly difficult restrictions on Indian businesses. Although setting-up yarn and then fibre production in South East Asia may have been in part to secure yarn for the Indian weaving business, the main motive seemed simply to find investment opportunities in countries with a more congenial legislative environment. The result of these moves was that by the late 1970s Grasim was one of the world's largest producers of VSF.

The picture is different in the 1980s and early 1990s. The metals group diversified into copper in India, with technical collaboration from Outokumpu (Finland) and MIM (Australia), taking advantage of a large differential between the import duties for ore and metal. During this period, carbon black plants were built in both India and Egypt and by 1992, the group was the largest producer of carbon black in India and sixth largest in the world. More dramatically, a major series of investments in South East Asia was made by the chemicals business. Most of these were in Thailand, where the group had first internationalised in textiles. Anecdotal evidence suggests the investments in Thailand were made to be free of home country restrictions. Familiarity with the country and good business/government relations appear to be major factors in selecting it for new investment. That these investments continued through the 1990s, even after reform had started, probably reflects some scale/scope economies of co-locating similar operations.

As Indian business conditions improved from 1995 to 2005, investment in India became a priority. By 1997, Hindalco had become the largest integrated aluminium producer in the country – overtaking Indal (an Alcan subsidiary), and it went on to acquire major stakes in Nalco and Indal – taking advantage of privatisation programmes to build scale and to become the largest aluminium business in Asia. Only a few significant overseas investments were made. Another carbon black plant in China was presumably an attempt to benefit from the expected explosion in the Chinese automotive industry. Copper mines were acquired in Australia to replace expensive Chilean ore for its Indian smelters, and for similar reasons, pulp mills were acquired in Canada for the textiles business. Clearly, both the Australian and Canadian investments were driven by the location of the raw materials rather than by market or labour-cost considerations.

Finally, as business began to boom in India post 2005, an explosion of activity took place. In the textiles group, fibre plants were set up in Egypt and China and a pulp facility was acquired in Laos to secure raw materials. In the chemicals group, investments were made in Indonesia, China and the Philippines. These seem to be the result of the company looking for good places to invest its cash. In the metals group, the company made a spectacular purchase of Novelis (which operated in 11 countries, bought primary aluminium from Alcan and processed it into rolled products), allowing Hindalco to extract more value from its aluminium operations and giving it routes to market in many developed countries. Such an acquisition no doubt signals the group's financial strength, but it is doubtful that it could have made such a purchase at an earlier stage in its history, since a number of factors needed to be in place, for example:

- The relaxation of restrictions on Indian companies making overseas investments
- The inflow of funds to the country as a result of economic policies
- The restructuring of the company by K.M. Birla to make it more intelligible and credible to overseas investors.

Ranbaxy

Overview

Ranbaxy Laboratories Limited is India's largest pharmaceutical company, producing a wide range of generic medicines. The company ranks among the top ten global companies in the generic medicine business and has a presence in 23 of the top 25 pharmaceutical markets. Turnover was US\$1.607 billion in 2007. It operates in 49 countries, has manufacturing facilities in 11, and employs 12,000 people.

Although it focuses on generics, Ranbaxy has placed a lot of emphasis on research in the areas of novel drug delivery systems and new chemical entities, and employs 1,200 research scientists

Although they did not start the company, the Singh family has been central to its success and owns most of the equity. Bhai Mohan Singh joined the company as a partner in 1951 when it was a distributor and led it through its early growth and subsequently into manufacturing. His son, Parvinder Singh, joined the company in 1967 becoming managing director in 1982 and chairman in 1993. It was his vision to transform Ranbaxy into an international company based on research rather than simply carrying on with local low-cost manufacturing. When he died suddenly the company was led by non-family members, D.S Brar and then Brian Tempest, a European. Malvinder Singh, one of Parvinder's two sons, was appointed President (pharma) and an Executive Director at the time of Tempest's appointment. Tempest then became Chief Mentor & Executive Vice Chairman of the Board and Malvinder the CEO whilst another European, Peter Burema, is President of the Global Pharmaceutical Business.

History

The company's history contains three intertwined threads stemming from Parvinder Singh's policy: the growth of its business at home and abroad, its policy of challenging patents to gain sales in rich markets, and its attempts to develop its own intellectual property and transform itself into a research-led organisation.

Growth

The company started in 1937 as a distributor for Japanese vitamins and anti-tuberculosis drugs. The company's manufacturing history was triggered by an alliance in 1951 with the Italian company Lapetit under which Ranbaxy distributed Lapetit's products in India. In 1961, Lapetit assisted Ranbaxy to set up some limited local manufacture. This was the first example of Ranbaxy's use of alliances to gain technical expertise. The association with Lapetit ended in 1966, due to Ranbaxy's determination to formulate more products locally. Faced with an ensuing product shortage, Ranbaxy "reverse-engineered" Lapetit's products by 1969. At the same time, it also expanded its product range by developing Calmpose, its own version of Valium. At that stage, there was nothing to prevent Ranbaxy copying others' products, but Ranbaxy was very small compared to the foreign multinationals (MNCs) and Indian public sector firms, such as Hindustan Antibiotics Ltd and IDPL, which dominated the local market.

The Indian government introduced patent legislation in 1970; however, this only protected processes. Competitors were free to imitate products as long as they used a different process. This created a disadvantage for MNCs compared to local imitators, and they were further discouraged by the introduction of price controls on drugs and later (in 1973) by restrictions on the amount of equity they could hold in local companies. This clearly provided a spur for the development of local pharmaceutical companies such as Ranbaxy, which established its bulk drugs facility at Mohali, Punjab, in 1971 and went public in 1973. Over subsequent years, it has continued to invest in its Indian manufacturing operations, which still form the core of its operations.

Initially the company concentrated on the local market; however, given the low-cost Indian labour, the low capital cost of setting up a pharmaceutical plant in India (one-third the cost of Europe or United States), and the high-value density of pharmaceuticals, exporting either generic products, which were out of patent, or “copies” of patented drugs to countries which were prepared to accept them was an obvious strategy for Ranbaxy, and indeed this is what it started in 1975.

From 1980, the company transformed from a local to an international company. The driving forces were Parvinder Singh’s vision, the extension of price controls in the Indian market, and some encouragement from the government to companies to invest abroad. In 1993, reflecting the growing importance of its overseas operations, Ranbaxy restructured into four regions – India and Middle East; Europe CIS and Africa; Asia Pacific; and North and South America – setting up regional headquarters in the US and UK in the following year.

In 1992, Ranbaxy expanded its operations via a joint venture with Eli Lilly to manufacture Lilly products in India and market them throughout South Asia; in 1994, when it looked as if the US healthcare reforms would trigger an explosion in the generic drug market, Lilly also contracted Ranbaxy to make generics for it.

By 1997 the Indian economy was beginning to slow down and drugs exporters, facing competition by the Chinese, began to increase focus on generics, and in the same year Ranbaxy engaged in a spate of alliances and acquisitions to gain scale domestically. Although Parvinder Singh died in 1999, the company continued along the same course, but after 2004 its international activities seem to have accelerated (see table below) slightly anticipating the acceleration of

outward FDI from the country as a whole. It is interesting to note that M&A increasingly appears to have become the dominant expansion mode, perhaps driven by increasing levels of inward FDI, the growth in the Indian economy, and relaxation of the constraints on Indian companies, which wanted to expand overseas.

Ranbaxy: Recent International Activity

2004	<ul style="list-style-type: none"> ■ Began operations in France ■ Increased equity stake in Brazil, China, Peru and Thailand
2005	<ul style="list-style-type: none"> ■ Set up joint venture in Japan ■ Acquired 18-product generic portfolio from EFARMES of Spain ■ Set up a new manufacturing facility in Malaysia ■ Set up a manufacturing facility in Brazil ■ Agreed plans for joint venture in Mexico ■ Entered Italy with wholly owned subsidiary ■ Opened third R&D facility at Gurgaon, India ■ Launches operations in Canada
2006	<ul style="list-style-type: none"> ■ Acquired Be Tabs South Africa ■ Acquired unbranded generics business of GSK in Italy and Spain ■ Acquired Terapia in Romania ■ Signed a deal to form a joint venture with South Africa’s Community Investment Holdings to sell low-cost generic AIDS drugs in Africa ■ Signed strategic alliance with Zenotech to market basket of Oncology products in various global markets ■ Renewed and expanded its alliance with GlaxoSmithKline (GSK)

Ranbaxy: Manufacturing Operations and M&A

	Approximate %age of Global Sales (2007)	Number of Countries with Operations	Number of Countries with Manufacturing	Year Established		Year of Acquisition	Examples of M&As in Last Decade
India and Middle East	21	3	1				
India	20		Yes			1997	Increased stake in Vorin Laboratories
						1997	Merger with Crosland Research
						1997	Acquired substantial part of Gufic Group
Europe CIS and Africa	38						
Europe	24	16	2				
Romania	5		Yes	2006	↔	2006	Terapia, the country's largest independent generic pharma company
France	5					2004	RPG (Aventis) SA
Germany	3					2000	Basics, Bayer's generics business
United Kingdom	3						
Italy and Spain	2					2005	Acquired 18-product portfolio of generics from EFARMES (Spain)
						2006	Unbranded generics business of GSK (Italy and Spain)
Ireland	-		Yes	1996	↔	1996	Rima Laboratories
CIS	6	2	0				
Russia	3					1997	Natco Pharmaceuticals
Ukraine	3						
Africa	8	10	2				
South Africa	4		Yes	2006	↔	2006	Be Tabs fifth largest generics company in RSA
Nigeria	2		Yes				
Asia Pacific	7	10	4				
Japan	2		Yes	2004			
Malaysia	2		Yes	1987			
China	1		Yes	2004			
Vietnam	3		Yes	2001			
North and South America	33						
North America	28	2	1				
United States			Yes	1995	↔	1995	Ohm Laboratories
						2002	Signature Pharmaceuticals (liquids syrup manufacturing)
Latin America	5	3	1				
Brazil			Yes	2005			

Challenging Patents

Originally, the company's business was in generic drugs (i.e. those out of patent) or selling copies of patented drugs in countries that permitted this. However, in 1984, the US Hatch Waxman Act was passed and this allowed generic manufacturers to challenge existing patents and, if successful, to have 180 days free of competition from other generics manufacturers. This made the United States a prime target market prompting Ranbaxy to enter the US market. By 1995, the US was Ranbaxy's largest market outside India. This aligned with Ranbaxy's strategy of copying and emphasised the need to develop skill in challenging patents that it has deployed to great effect in recent years, for example by invalidating Pfizer's US patent for the anti-cholesterol drug Lipitor in 2006 and gaining US FDA approval for its generic equivalent, Simvastatin.

Research

However, the company decided that it needed to create its own Intellectual Property (IP) to compete in the longer term. Indian drugs companies had some natural competitive advantages in research. Not only was there a good supply of highly skilled and comparatively cheap research chemists, but, thanks to the huge population, it was easier and

quicker to conduct clinical trials there than in the West. In 1985, the Ranbaxy Research Foundation was established. By 1990, Ranbaxy had acquired its first US patent. By 1993, the company had formalised the emphasis on research by declaring its vision to become a research-based international pharmaceutical company, and its new research facility at Gurgaon (near Dehli) was operational the next year. In 1994-95 (when the capital cap on foreign MNCs was relaxed, the number of drugs under DPCO was reduced, and an agreement was reached that product patent laws would be fully introduced by 2005), the Indian market became more attractive to foreign competitors, thus confirming the wisdom of Ranbaxy's strategy of emphasising research, rather than relying solely on low-cost production.

Its research programme began to show results in 1998, when it filed its first investigational new drug application and by 1999, Ranbaxy was selling exclusive development and worldwide marketing rights for its anti-anthrax product, Ciprofloxacin, to Bayer AG. In 2003, Ranbaxy entered a global alliance with GSK for drug discovery and development (renewed and expanded in 2006). By 2005, it had developed RBX 11160, an anti-malarial compound.

Nevertheless, it appears that Indian companies became concerned by the “winner takes all” nature of drug discovery and by 2004 it was noted that they were also focusing on lower-risk types of research such as devising new ways of delivering established drugs. For example, Ranbaxy developed a once-a-day version of Bayer’s antibiotic, Cipro, for which it received royalties from Bayer, and its development of a three-in-one combination anti-retroviral drug gained it the first approval from the FDA under the President’s Emergency Plan for Aids Relief.

More recently, the company appears to have become more concerned at the risks implicit in research. In 2007, it indicated it wanted to dilute its stake in its research company by up to 60% by hiving it off into a separate entity in 2008.

Summary

The overriding rationale for Ranbaxy’s expansion seems to have been the exploitation of economies of scale and scope in R&D, product approval, and possibly bulk drug synthesis.

Ranbaxy has only established manufacturing operations in 11 of the 45 national markets in which it has sales operations. Given the low cost of manufacturing in India and the high value density of the products, it seems unlikely that gaining overseas manufacturing sites was driven by the need to acquire capacity or skills. Most likely, the overseas manufacturing facilities were primarily established to facilitate market entry and/or as part of acquisition. In most cases, the synthesis of active chemicals has been retained in India when the formulation and packaging has been transferred. Local packing also makes it easier to comply with local regulations regarding packaging and labelling.

Country Discussion

Indian businesses have traditionally been run by families. Even as they have grown into substantial businesses, and in some cases turned into public companies, control has been kept by the family, usually represented by a dominant family member with a very large personal stake in the business (the promoter). Although the degree to which family issues may interfere with the business may vary, genealogy remains a major factor and can lead to “wobbles” when one generation passes over the reins to another.

Traditional Indian businesses have typically started as traders of one form or another, and expansion into manufacturing has been a means to expand the business. As a result, business decisions seem to be highly pragmatic. Longer-

term strategies are becoming more evident as the government opens up the economy and local companies have to compete with global competitors and attract investments.

Some of these businesses benefited in their formative years from protectionist policies and later from the divestment of publicly owned companies by the Indian state, but now there is little state interference with company policies; hence, one tends not to see the “grand gesture” investments seen in other emerging countries such as China.

The early expansion of a few Indian businesses was to escape restrictions on growth at home. Alternative motivations were to exploit the advantages offered by India’s cheap skilled labour. However, of late some of these companies have begun to emerge as global players looking for scale in an increasingly globalised marketplace.

The recent trends have been driven by more enlightened economic policies, which have both encouraged investments in India and also relaxed restrictions on Indian companies investing abroad. The recent government emphasis of manufacturing as a means to promote growth and provide employment will most likely accelerate this trend. Although both case study companies emerged as international players well before the norm, both made substantial overseas investments since 2005 when the government relaxed the US\$100 million cap on annual foreign investment by Indian companies. Both companies have used M&A as a means of rapid expansion, although not exclusively.

Although it is now firmly established in service and retail operations in the segments we have already discussed, Aditya Birla seems to regard itself as a manufacturing company, and its early expansion ventures have led to a wide manufacturing footprint centred on East Asia. However, as the company has grown and rationalised, there have been investments that fit in with the more usually cited motives for international manufacturing such as securing resources (copper ore in Australia or wood pulp in Canada and Laos) and downstream vertical integration to capture value (fatty-acid production in Malaysia and Philippines, and more spectacularly the acquisition of Novartis). By contrast, although Ranbaxy manufactures in 11 countries and some of the locations in low-cost countries have been driven by considerations of supply chain efficiency, it seems that most of these operations have been acquired through M&As aimed at securing brands and/or routes to market.

China: Factory for the World

Country Overview

With 1.321 billion people, China has a slightly larger population than India spread over an area roughly three times as large: at 9.6 million square kilometres it is slightly smaller than the United States.

China's GDP is US\$3.2 trillion at market exchange rates and US\$7.2 trillion at Purchasing Power Parity (both 2007 figures). Growth rate has averaged steadily from around 10% in 2003 to over 11%, although this is thought to be unsustainable and is expected to drop back to 8-9%.

Despite still being a communist nation, only a third of the economy is directly state controlled. In 2007, merchandise exports were worth US\$1.2 trillion and imports stood at US\$0.96 trillion (according to customs data), resulting in a trade surplus of nearly US\$0.3trillion.

Manufacturing Industry

China has become the factory for the world. Manufacturing takes place in wholly owned foreign enterprises, joint ventures between foreign companies and local companies,

and in independent purely local companies. As in most economies, these local companies may be owned by the state, by private individuals, or they may be listed on a stock exchange.

Many of the old, inefficient state-owned enterprises from the former command economy have collapsed or reformed, yet some still remain, supported by cheap or free finance.

Co-location is an intriguing characteristic of manufacturing in China. In some cases, whole cities seem to specialise in a small product range – in some cases, a significant proportion of world demand is produced within a very small radius. Also, certain industries tend to concentrate in certain regions. Not only do the major industries vary by region in terms of their location, but the characteristics of manufacturing firms also tend to vary from region to region. For example, there are distinct differences between the types of companies predominating in the Pearl River Delta and those within the Yangtze River Delta. Such is the scale of the country that there are also distinct differences between companies in different sub-regions.



Although many Chinese companies export and others act as contract manufacturers for international OEMs, Chinese companies have only begun to internationalise their operations comparatively recently, seeking either markets for their goods or raw materials to support manufacture.

Economic Trends

China's GDP was reasonably flat until the late 1980s, since then it has grown geometrically influenced by the reforms introduced by Deng Xiaoping. Since 1990, there has only been one year in which the GDP was slightly lower than the previous year.

Inbound FDI has also been growing strongly since 1992 as companies have sought to establish themselves in this strategically important market. The slight dip in 1999 and 2000 actually anticipated the global downturn in FDI; however, the recovery from 2002 also anticipated the global recovery, and growth has been very strong since, albeit with a suggestion of possible softening in the latest figures.

From 1980 to 2000, Chinese firms were allowed to invest abroad under restriction, making China's outward FDI considerably lower than inward FDI. Since China's admission to the World Trade Organisation in 2001 and the Chinese government's strategy of "Going Out" (policy to raise China's global economic profile by encouraging

Chinese firms to invest abroad), China's outward FDI surged. Much of this outward FDI has been in the form of M&As. By the end of 2007, more than 5,000 domestic Chinese enterprises had established direct investments in 172 countries and regions around the world. Most of China's outward FDI stock has accumulated in Asia, with Hong Kong as the hottest destination. Some of this outward FDI was undoubtedly "round tripping," that is, a large portion of the investment re-entered China as "foreign investment" to take advantage of incentives and benefits granted to foreign-invested enterprises. Nevertheless, Chinese companies are beginning to expand overseas and the following case studies provide examples of China's emerging multinationals.

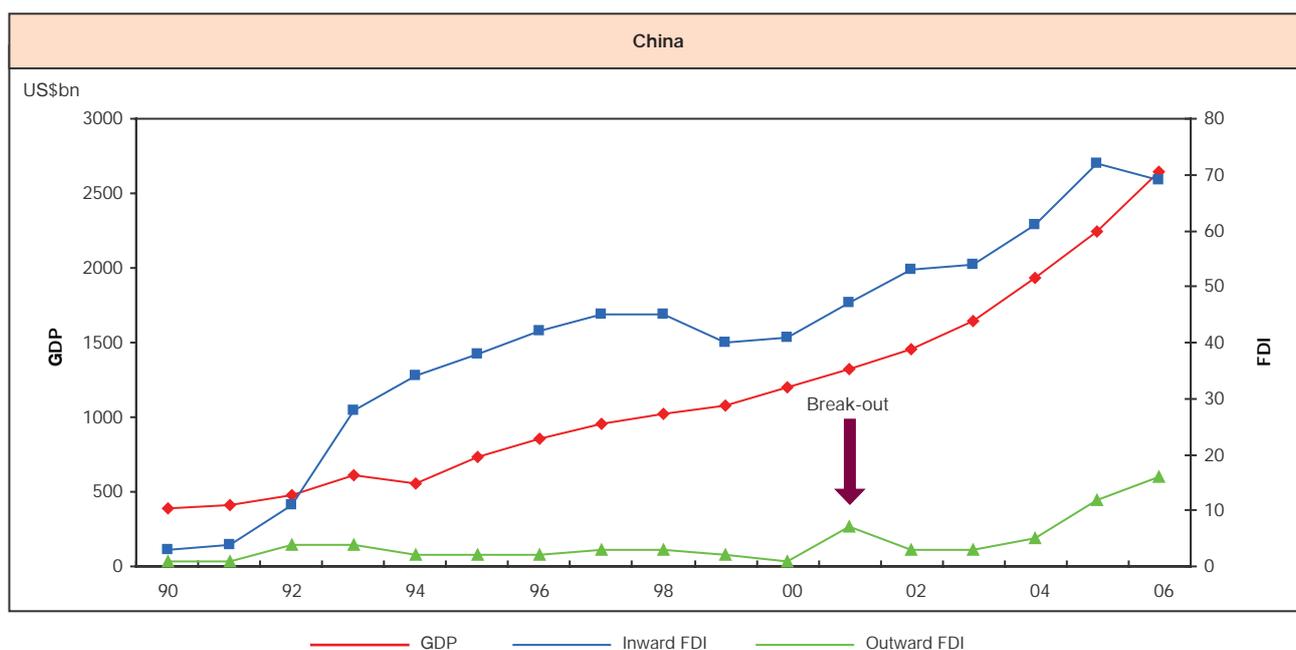
Case Studies

Haier Group

Overview

Haier's 2006 global revenue was US\$13.1 billion, 21% of which came from overseas markets. In its domestic market, it holds more than 30% market share in the white goods market having dominant positions in refrigerator/freezer, washing machine and air conditioner markets. Globally, Haier ranks third in white goods revenues, and is the second largest refrigerator manufacturer with 6% global market share, behind Whirlpool and ahead of Electrolux, Kenmore

Economic Trends - China



and GE. It has 240 subsidiary companies employing more than 50,000 people. Its global business platform comprises nine overseas regions, six overseas R&D centres, ten information centres and thirteen overseas factories (principally in the United States, Italy, Syria, Iran, Pakistan, Jordan and Nigeria).

History

Haier started with a defunct refrigerator factory in Qingdao, Shandong Province in 1984 and has developed in three stages: Branding (1984-1991), Diversification (1991-1997) and Internationalisation (1997-present). It took seven years to build a strong local brand name in the domestic refrigerator market, but by 1991, Haier had become China's leading refrigerator manufacturer. From 1992 to 1997, it acquired 15 companies becoming a manufacturer of a wide range of household electrical appliances. In 1997, Haier developed its formal global expansion strategy called "three one-third": the objective was to produce two-thirds of total output in China and to sell two-thirds in overseas markets. At the time the strategy was first outlined, Haier's overseas sales accounted for less than 3% of total sales. An Overseas Business Promotion Division was established in 1999 to manage export business, overseas sales subsidiaries and overseas factories.

Exports

Haier started to venture into overseas markets as a contract manufacturer starting exports to United Kingdom, Germany, France and Italy in 1991, Asia and the Middle East in 1993 and the United States in 1994.

In Germany, Haier's refrigerator was marketed by a German appliance firm, Liebherr, under the "Blue Line" brand. A blind quality test by a German magazine gave Haier's Blue Line refrigerators eight top rankings, beating Liebherr's seven. In the United States its compact refrigerators were marketed by a New York import company, under the Welbilt brand and captured 10% of the compact refrigerator market in the first year. These successes prompted Haier to establish its own brand in these markets. In 1997 Germany became the first export market for its own brand of refrigerators and in 1999 Haier decided to sell own-brand products in all overseas markets.

Internationalisation of the Manufacturing Function

Haier began to pursue international production as early as 1996 and now has manufacturing facilities in all six regional markets. Overseas factories are managed by product divisions and this study focuses on the refrigerator/freezer division, because refrigerators and freezers are the core products of Haier and because the refrigerator/freezer division was the first to engage in cross-border production.

The internationalisation of manufacturing in Haier's refrigerator/freezer division followed three steps:

- Entry into nearby developing countries (South East Asia); America and Europe.
- Establishment of a manufacturing plants in North America and Europe;
- Exploring other developing countries (South Asia, Middle East and Africa).

Haier: Internationalisation of the Manufacturing Function

Region	Division (Number of sites)			
	Refrigerators/ Freezers (11)	Washing Machines (6)	Air Conditioners (8)	Televisions/ Mobile Phones (3)
South East Asia	Indonesia JV (1996) Philippines JV (1997-2000) Thailand JV (1999) (bought Sanyo plant in 2006) Vietnam JV (2000)	Malaysia (1998)		
North America			USA (2000)	
Europe	Italy (2001)			Slovakia (2006)
South Asia	Bangladesh JV (2001)		Bangladesh (2001)	
	Pakistan Industrial Complex (2002)			
Middle East	India (2008)			India (2008)
		Iran (1999)		
		Syria JV (2002)		
Africa		Middle East Industrial Complex in Jordan (2003)		
	Nigeria JV (2001)		Nigeria (2001)	
		Tunisia (2002)		
		Algeria (2004)		

1. Entering Nearby Developing Countries

The initial stage of manufacturing internationalisation of the refrigerator/freezer division focussed on South East Asia. The primary motives were to avoid import tariffs and to increase sales in host markets. South East Asia was chosen as the first destination for two reasons. Firstly, there cultural synergies between South East Asian countries and China, so some of Haier's accumulated production and marketing experience in its domestic market was applicable and transferable. Secondly, since millions of Chinese live in South East Asia, Haier could expect to find suitable partners for their joint ventures (JVs) – in which Haier provided the production line, technology and semi-knocked down (SKD) parts, while local partners took care of renting land and buildings, hiring labour and developing the local distribution network. In some cases the match was not as good as expected and the JV in the Philippines was shut down in 2000. In Thailand Haier subsequently acquired Sanyo's refrigerator plant to supply the local market and to export to North America and the Middle East.

2. Establishing Factories in North America and Europe

Haier began construction of its plant in South Carolina in 1999. At first this acted as a "receiver," being highly dependent on Haier's factories in China for everything from parts sourcing and manufacturing processes to new product development. However, it has subsequently become an important innovation source for large-size refrigerators in the entire manufacturing network. Haier also has a trading company in New York and a design centre in Boston. A second trading company in Miami deals with the Latin American market.

In 2001, Haier invested US\$8 million to acquire a refrigerator plant in Padova, Italy, from Meneghetti SpA, one of the largest built-in appliances manufacturers in Italy. The plant produces built-in refrigerators and freezers for the expanding built-in sector. In the near future, it will become an essential innovation centre for built-in refrigerators and freezers in the manufacturing network. A second trading company was established in 2002 to separate air conditioners business from white goods business to reflect the different requirements for the distribution channels and aftersales service. Logistics in Europe are coordinated by the headquarters in Italy through four distribution centres in Italy, Spain, the United Kingdom and Holland.

3. Exploring Other Developing Countries

Haier's market and production presence in the United States and Europe supported its investment and operations

in other developing countries through technology spin-off and brand reputation. Initially it formed JVs to set up small plants to pilot plants to test the markets. Then it established industrial complexes to serve a range of markets. The Pakistan industrial park is the production base for the whole South Asian market except India. Similarly, the Jordan industrial park is for the whole Middle East market. In India, Haier formed an alliance with Whirlpool and Voltas to produce refrigerators and air conditioners in 2004. It also announced that a refrigerator factory and an R&D centre would be established in India in 2008.

TCL Corporation

Overview

TCL Corporation is a consumer electronics company. Currently, TCL operates six business units: multimedia, telecommunications, home appliances, personal computers, consumer electronics and electronics components. Of these, multimedia is the largest unit and the television category has been TCL's largest segment since 1999, partially dependent on its internationalisation strategy.

TCL's global revenues amounted to US\$6.7 billion in 2006. It employs over 60,000 employees in more than 80 countries and regions worldwide covering Asia, America, Europe and Australia.

History

Founded in 1980 as a cassette manufacturer, TCL became the number one telephone producer in China by 1986. In 1992, TCL entered the television market, first as a distributor, selling colour televisions produced by its Hong Kong based joint venture partner Changcheng, under TCL's brand "King." In 1996, TCL moved into production by forming a joint venture with Hong Kong manufacturer Luk's Industrial to produce televisions in Shenzhen. By 2001, TCL had become the largest television producer in China. Afterwards, TCL started to expand its production capacity to cover the entire China market. In 2006, TCL's annual television sales in China increased to 14 million sets, which maintained its number one position.

TCL Corporation's Internationalisation Process

TCL's international experience began in 1997, when it started to export Cathode Ray Tube (CRT) television sets first to the United States and then to South East Asia. In 1999, TCL took over Luk's factory in Vietnam with the intention to fulfil local demand and further expand the South East Asian market. By 2006, TCL held 22% of

Vietnam's CRT television market, ranking second behind Samsung Electronics. Reaching global prominence in January 2004, TCL and Thomson Electronics signed an agreement to create TTE, a joint venture that combined the CRT television assets of each. TCL dominated the joint venture, with 38% of the shares, while Thomson holds 30%. Five Regional Business Centres (RBCs) – China, Europe, North America, Strategic OEM (S-OEM) and Emerging Markets – were established to manage the sales and marketing function of TTE's CRT television products in a global scope. Each RBC took charge of a specific market, each with a different market focus and brand.

Under the joint venture agreement worldwide, TTE owns ten manufacturing plants, including six in China, one in Vietnam, Thailand, Poland and Mexico. Thomson previously owned the latter three factories. Combining the annual production of all ten plants, TTE is capable of producing 23 million televisions each year, the highest in the world.

In 2006, TTE sold 9 million television sets in overseas markets and 8.85 million sets in the domestic market. On average, the same television model, priced in overseas markets is higher than that in China; therefore, in 2006, TTE's foreign sales to total sales were over 50%. Currently, there are 5,822 employees working in TTE's overseas subsidiaries and factories accounting for 13% of total employment. In the near future, TTE plans to reduce overseas employees to 5,200 by to reduce overseas costs.

Wanxiang Group

Overview

Wanxiang Group Corporation is one of the top 500 companies in China. It is a supplier of universal joints, bearings and CV joints to automotive customers in over 40 countries. It has a turnover of US\$4.2 billion and employs 40,000 employees.

History

Wanxiang Group began as a town-village (collective) enterprise in 1969. Starting as a low value-added automotive parts supplier, Wanxiang has grown into a multinational conglomerate, with business portfolios in automotive components production, hotel and restaurant management, bridge/road construction and development, as well as international trade, leasing, financial services and property development.

As early as 1970, Wanxiang entered the automotive parts industry and began to produce cardan universal joints. By now, it has specialised in the production of four series of automotive components – transmission shafts, brakes, suspension systems and exhaust systems. In 2005, its sales revenue of automotive components in the domestic market reached US\$3.15 billion, making it the seventh largest automotive components supplier in China, and number one in local enterprises.

Wanxiang's Internationalisation Process of Automotive Components Division

Export

Wanxiang began exporting in 1984. At that time, automotive component orders were centrally planned, distributed primarily to state-owned enterprises (SOEs) for production, and afterward procured by the government. In the highly protected industry dominated by state-owned enterprises, it was very difficult for Wanxiang – as a town-village enterprise – to increase market share in the domestic market. Therefore, in 1984, it began to export cardan universal joints to the United States, as a contractual manufacturer for Zeller Corporation. At the beginning of 1985, Wanxiang signed a new contract with Zeller to export 200,000 sets of cardan universal joints each year for the following five years. This is how Wanxiang stepped on the road to internationalisation.

In 1991, Zeller Corporation decreased its order quantity because Wanxiang refused to export cardan universal joints exclusively through Zeller. Although it caused a backlog of hundreds of thousands of universal joints stocked in Wanxiang's warehouse, it triggered Wanxiang's determination to expand its export product categories as well as the overseas market coverage. Wanxiang began to export drive shafts in 1991, bearings and constant velocity shafts in 1993; by 2001, ball bearings, suspension products and brake components all joined Wanxiang's product categories for export. Overseas markets were expanded to North America, Europe, South America and Japan.

Establishment of Sales Subsidiaries

In 1993, Wanxiang created its first overseas subsidiary, Wanxiang American Corporation, in Kentucky and then relocated it to Chicago in 1994. The American subsidiary was active in building and extending the marketing and sales network for Wanxiang's automotive components across North America, South America and Europe. Then, Wanxiang Europe and Wanxiang South America were

established as affiliates to Wanxiang American Corporation in 1997, to take charge of Wanxiang's overseas business in Europe and South America. In July 1997, Wanxiang bought 60% shares of AS Company, a sales company in the United Kingdom, and established the Wanxiang Europe Bearing Company to market and sell all kinds of bearings in the European market.

Worldwide, Wanxiang has built an international sales network that covers over 60 countries. In 2005, its overseas sales revenue of automotive components exceeded US\$800 million – 20% of total annual sales.

Involvement in Cross-Border Production

Since 2000, Wanxiang entered the stage of international production, mainly through acquisitions. In April 2000, Wanxiang acquired Zeller Corporation, a top three automotive part supplier in the American market, and obtained its equipment, brand, technology patents and distribution channels. In October 2000, Wanxiang purchased 35% shares of LT Company, the number one supplier of hub units in America, and became its largest shareholder. Wanxiang, henceforward, had its own manufacturing and assembly capabilities in the United States.

In August 2001, Wanxiang bought 21% shares of UAI Company; a NASDAQ listed company, and became its largest shareholder. UAI specialised in production of brake components and was the top brake components supplier in America. The acquisition provided a good technology platform to transfer technology capabilities to the newly launched brake system line in Wanxiang China. However, UAI's global distribution networks facilitated Wanxiang China to export brake products to the global market. In September 2003, Wanxiang successfully bought 33% shares of Rockford Powertrain Corporation and become its largest shareholder. Rockford Powertrain was the largest supplier of wing-type drive shafts in the American market, accounting for 70% market share. The acquisition enhanced Wanxiang's drive shafts business in North America. In April 2007, Wanxiang announced its decision to acquire a pro-shaft plant from Ford Motor's Automotive Component Holdings to produce shafts, half-shafts, driveline products and catalytic converters.

Wanxiang operates seven specialised manufacturing plants in the United States. In all factories, some capital-intensive production processes such as tooling production were transferred to China to achieve economy of scale; most labour-intensive production processes such as component production were also transferred to China to make use

of low labour cost and achieve economy of scale. All plants in the United States stay in the front and bottom of the value chain, in other words, product design/customisation and assembly, testing and packaging, respectively.

Country Discussion

As might be expected, two of these three companies – Haier and TCL – started as state-owned enterprises, but Wanxiang was a town-village enterprise. All received some favourable treatment from the government.

All three moved globally through exports – TCL exported its own products whereas Haier and Wanxiang were contract manufacturers. Wanxiang started exporting quite early (1984 during a time when China's exports were beginning to climb) because its orders for automotive components were centrally planned, and primarily supplied by SOEs. In this highly protected industry, the village enterprise found it hard to grow. By contrast, Haier and TCL were busy fulfilling domestic consumer demand. Subsequently, in the early 1990s, Haier gained further scale through exports as a contract manufacturer and in the late 1990s TCL began to export directly.

All three seem to have learned from partners, whether JVs or customers. Haier supplied products for established OEMs in Europe and the States, Wanxiang for an American OEM (which it subsequently purchased) and TCL had some Asian partners followed by a JV with Thomson Electronics.

Conclusion

Although the economies of these countries were all being liberalised in the late 1990s and all were experiencing an increase in inward foreign direct investment (FDI) – albeit mild in Russia – none took part in the global explosion in outward FDI that culminated in 2000. Subsequently however each is participating in the current surge in outward FDI influenced by recent economic growth, strong inward FDI and the continuing liberalisation of their economies.

Specific factors to explain this change in behaviours may include each country, for example:

- Brazil: Held back by the currency crisis of 1999-02 and then encouraged by further liberalisation.
- Russia: Held back by the financial crisis of 1998, but subsequently benefiting from an emphasis on free markets and company autonomy and supported by increases in oil prices.
- India: Although outward FDI started to increase following the reforms in the mid-1990s, the progressive removal of the restrictions on outward investment in the mid-2000s seems to have removed the brakes on outward FDI.
- China: China's outward FDI has lagged behind inward FDI, but joining the WTO in 2001 and the government's "going out" policy seems to have triggered growth in this field.

This FDI has been made by emerging multinationals that have grown up in these emerging economies. Our study has illustrated a number of similarities, whilst not universal, in the history and behaviour of several of the companies we have examined. These include:

- A period in which the company was protected from local and especially foreign competition. A significant number were originally state-owned enterprises (especially in China, Brazil and Russia) and the Indian companies, whilst emphatically not state owned, were protected by policies that discouraged foreign competition and granted effective local monopolies. As a result, each had a chance to gain scale in its home market before being exposed to more stringent competition.

- Several companies – particularly in China and India – had visionary leadership that was free to pursue long-term strategies, because the company's ownership was restricted in some way (e.g. state ownership closed-stock companies or family control). In the case of China, the growth has been comparatively recent and each of these key leaders is still in place (e.g. Zhang Ruimin in Haier and Lu Guanqiu in Wanxiang), whereas in India, family ownership has passed through several generations. Nevertheless, it is possible to identify the leader who initiated international expansion, for example, A.V. Birla in Aditya Birla and Parvinder Singh in Ranbaxy.
- For nearly all these companies early international growth preceded the recent expansion on FDI. The triggers that prompted this have been varied. Many started looking for growth via exports, but other motivations included the search for raw materials and even a desire to escape domestic restrictions. As a result of this early international experience, these companies were able to develop capabilities in international business before the recent acceleration in international competition.
- When moving abroad many of these companies used their low-cost advantage, and possibly their different expectations of ROI, to target low-margin sectors that were relatively unattractive to established players. Initial growth was usually gained through direct investment, joint ventures or by acting as contract manufacturers. Once established, several have used the earnings and experience to move upmarket and to penetrate more sophisticated markets. In several cases it is possible to identify early collaborations that have provided the key technology for their future growth.

Although outward FDI has generally lagged inward FDI (with Brazil being a recent exception), outward investment as a percentage of GDP is increasing and is now comparable to the global average (with China lagging). Since the economies of these countries are growing significantly faster than those in developed countries, we can expect this outward FDI to grow even more rapidly. Put in less abstract terms, we can expect to see even more aggressive

international expansion of the emerging multinationals, which will grow in size and number, transforming the competitive environment.

The growth of the EMs will make life even more uncomfortable for any companies concentrating on a national or regional market. As Zhang Ruimin, CEO of Haier, puts it, "In the globalisation era, there are two categories of companies. One is the international company, and the other is the one taken over by the former group. There isn't a third choice." As a result, further rationalisations within industries are likely with the emerging multinationals often in the role of acquirer, but the targets will include MNCs (or parts of MNCs) as well as national and regional players. Recent examples of such acquisitive behaviour include:

- Brazil: Vale's purchase of Inco for US\$17bn
- Russia: Norilsk Nickel's purchase of OMG for US\$0.4bn
- India: Hindalco's (Aditya Birla Group) purchase of Novelis for US\$6.4bn
- China: Haier's unsuccessful bid of US\$1.3bn for Maytag

The expansion of the EMs has implications for competing MNCs in that the entry of new players will put pressures on margins, especially if they are able to operate with a

lower cost base – for example by using the "home" resources to carry out many of the labour-intensive activities from component assembly to research.

To compete with these new players, established MNCs will have to learn to be more cost competitive or find ways to out-innovate the new competition. However, we can expect the new players to catch up rapidly in innovation given the high levels of technical education in their home countries. MNCs will also have to re-think their approach to market segmentation: a low-margin segment that was formerly of little interest to incumbents may have a different significance if it offers a point of entry to a new competitor.

However, there will most likely also be challenges for the EMs themselves. As they expand and grow in number they can expect fiercer competition from the established players and also additional competition from other companies in emerging economies. Growth will therefore become more difficult. Some have already sought capital for expansion from the capital markets and this may restrict their freedom to forgo short-term profitability especially if their rate of growth declines.



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