



Competition between Local companies and Multinationals

MIBA-THESIS



DECEMBER 25, 2014

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ACKNOWLEDGMENT

I owe all the gratitude to **God** for putting me on the MIBA road and helping me finish it.

The journey was short in time but rich in personal and technical experience, thanks to my all **Father** and **Mother**, my **Wife** and my little **Seif, Mariem** and **Alia** for their love, patience and support before and through the MIBA time.

Thanks to **Dr. Ahmed Shalaby**, his extra ordinary support, patience and advice enlightened my way and made this thesis possible; I think he is simply the best supervisor.

Finally, warm thanks to all professors teachers and assistants at **ESLSCA**, whom with their support during the past years, I broadened my spectrum of business knowledge.

Abstract

Competition between local companies and multinationals is an important as in battles for emerging markets; big multinationals do not hold all the advantages. This model has succeeded in North America, Europe and few Asian countries but it is not significantly present in the Gulf and North Africa region, and not in Egypt specifically.

The research uses a model based on strategies that local companies can adapt to encounter the multinationals (Dawar, 1999)

The case study concludes that Strategic alliance with the multinationals help to pacify the competition and results in leading the market vis-à-vis the multinationals.

Further strategic alliance and pacify competition needs to be applied in different industries

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List of Abbreviations

ESLSCA	École supérieure libre des sciences commerciales appliquées
OECD	Organization for Economic Cooperation and Development
KSA	Kingdom of Saudi Arabia
MIBA	Master of International Business Administration
MNCs	Multinational companies
SPIMACO	Saudi Pharmaceutical Industries & Medical Appliances Corporation

I. Chapter 1: Introduction

Being global brings clear strategic benefits: the ability to access new customer markets, new suppliers, and new partners. These immediate benefits can also create secondary ones. Building a customer base in a new market, for example, provides familiarity and relationships that may enable additional investments. (Dewhurst, 2012)

However, being global also brings strategic challenges. Many companies find it increasingly difficult to be locally flexible and adaptable as they broaden their global footprint. In particular, processes for developing strategy and allocating resources can struggle to cope with the increasing diversity of markets, customers, and channels. (Dewhurst, 2012)

In battles for emerging markets, big multinationals do not hold all the advantages.

Benefits from competition have been driven growing attention to productive efficiency and dynamic efficiency (Ahn, 2002)

I.1 Productive efficiency: productivity improvement throughout innovations, which let in new and superior production techniques, and effective innovations will lastly expand the level and growth rate of productivity in the long term. (Ahn, 2002)

I.2 Dynamic efficiency: links between market frame and industry performance. (i.e., birth and death, growth and decline of individual firms) is an important component of innovation and aggregate productivity growth. Dynamic efficiency gains from product market competition, however, can hardly be achieved without well-functioning factor markets, which reallocate labor and capital of shrinking/exiting firms to entering/growing firms. (Ahn, 2002)

Multinational companies are dashing in to discover fresh chance for evolution as they have fundamentals financial resources, sophisticated technology, outstanding products, robust brands, and seasoned marketing and management skills

I.3 Strategies to decrease competition? Managers postulate they can abide by one of only three ways:

I.3.1 By calling on the government to cut back trade barriers or provide some other form of back up

I.3.2 By becoming a subsidiary partner to a multinational

I.3.3 By simply selling out and layoff the industry

I.4 Analysis of current situation in competition every manager in emerging markets needs to address:

First, how robust are the pressures to globalize in your industry?

Second, how internationally transferable are your company's competitive properties?

1.4.1 Strategic thinking types: (Dawar 1999)

1.4.1.1 Defender. If globalization pressures are weak and a company's own assets are not transferable, the company needs to concentrate on defending its sector against multinational raid.

1.4.1.2 Extender. If globalization pressures are weak but the company's properties transferred, then the company may be able to stretch its success at home to a limited number of other markets

1.4.1.3 Dodger. If globalization pressures are strong, the company will pan bigger challenges. If its assets work only at home, then its constant independence will hang on its ability to dodge its new rivals by restructuring around specific links in the value chain where its local assets are still valuable

1.4.1.4 Contender. If its assets are transferable, although, the company may actually be able to compete head-on with the multinationals at the global level

Figure 1.1 illustrating the four strategies to position the company in an emerging market



I.5 Strategies, which can invade the others: (Ghemawat, 2007)

I.5.1 Exploit evolving market conditions by anticipating the changes and leveraging your knowledge of customers, can point opportunities to pack services and products where you have a particularity.

I.5.2 Manage convergences in costs Governments in emerging markets are put aside barriers to outside MNCs, thus dropping their costs. In addition, market demand is forcing local players to offer advanced products, which cost more to produce. Result: a more level playing field for emerging and established MNCs. Both types of companies can work around or enrich on this convergence.

I.5.3 Rework value chains emerging and established MNCs alike can find competitive opportunities by carefully examining what customer needs not served by existing industry value chains. Some companies succeed by specializing

As more countries open their markets to foreign competition, local firms are facing increasing pressure to build, integrate, and reconfigure their resources in response to rapidly changing environments (Ghemawat, 2007).

Gaining a competitive advantage, and more importantly sustaining a competitive advantage, is dependent upon a firm's competitive environment, its institutional environment, and its resources and capabilities (Ghemawat, 2007)

I.6. Research questions:

I.6.1 How local firms in emerging markets create and implement successful competitive positioning strategies?

I.6.2 How competition will affect performance of local and multinational companies?

I.6.3 Which factors will enhance competition efficiency of firms in emerging markets?

II. Chapter 2: Theoretical Background

We will cover the factors influencing competition (Ahn, 2002)

II.1 Competition and incentives

Competitive pressure may lessen such carelessness by granting more incentives to the stakeholders of the firm (i.e., managers and workers) for rising their efforts and enhancing efficiency. In other words, one can rationally anticipate that product market competition would self-control firms into efficient operation

Three different channels taken into consideration in this regard (Ahn, 2002)

II.1.1 Competition form utmost opportunities for comparing performance under information asymmetry and hence makes it convenient for the owners or the market to monitor managers.

II.1.2 Cost-reduction improvements in productivity could create greater increase in revenue and profit in a more competitive environment where price elasticity of demand head for higher. In other words, a cost-reducing innovator will be capable of raising revenue more dramatically by reducing price in a more competitive market with higher price elasticity of demand.

II.1.3 The likelihood of bankruptcy is higher in a more competitive environment, which will pressurize managers to work strictly to avoid bankruptcy. In the sense that product market rents coming from lack of competition shared with workers in the form of higher pays or reduced effort, the grade of competition affect the grade of workers' effort in similar ways.

Theoretical predictions on the impact of competition on incentives are “delicate and vague” (Ahn, 2002). In the models of the market mechanism as an incentive scheme under information asymmetry, for example, product market competition among firms can lessen managerial,

careless as far as there is significant correlation among the firms' costs due to common external shocks (Ahn, 2002). However, by modifying model assumptions about managers' responsiveness to fiscal incentives, (Ahn, 2002) showed that competition exacerbate the incentive problem. Similarly, while higher demand elasticity under competition boosts the relative rewards from a cost reduction, greater scale of operations for a monopolist head for an increase his absolute reward from a similar cost reduction. Depending on the setting of the model, competition shown to enhance efficiency in many, but not all, circumstances.

II.2 Competition and innovation

The potential trade-off between static and dynamic efficiency earn special concerns in considering the links between competition and innovation. According to (Ahn, 2002), for example, the organization of firms and markets most useful to solving the static problem of resource allocation is not necessarily most conducive to rapid technological progress. The positive effects of market power on innovation in his view summarized under the following two themes (Ahn, 2002).

II.2.1 The expectation of some form of transient *ex post* market power is required for firms to have the incentive to invest in research and development.

II.2.2 The possession of *ex ante* market power also favors innovation. When capital markets are imperfect, the rents from market power provide firms with the internal fiscal resources for innovative activities. Market power also helps reduce uncertainty associated with excessive opposition, which tends to undermine the incentive to invest.

Is competition helpful to innovation? In the Schumpeterian view of market power and innovation, competition seems to be rather detrimental to innovation and technological progress. If more monopolistic firms were more active in innovative activities because of less market uncertainty, competitive pressure would lessen their incentives to invest in research and development. On the other hand, competition will head for firms to innovate to survive. In fact, recent empirical studies report positive correlation between product market competition and productivity growth. (Ahn, 2002) offer several theoretical cases where competition is actually useful to innovation and growth:

II.2.3 Darwinian effect: Intensified product market competition could pressurize managers to boost the adoption of new technologies to avoid loss of control rights due to bankruptcy (Ahn, 2002). Firms should innovate to survive under competitive pressure (Ahn, 2002).

II.2.4 Neck-and-neck competition: In a simple model of “creative destruction”, the support firms unlike new entrants have no incentives to innovate. Under a more gradualist technological progress assumption with support firms engaged in systematic innovative activities, competition could increase innovation. It is because more intensive product market competition between firms with “neck-and-neck” technologies will increase each firm’s incentive to acquire or increase its technological lead over its oppositions.

II.2.5 Mobility effect: In the learning-by-doing model of endogenous growth, the steady-state rate of growth increased if skilled workers become more adaptable in switching to newer production lines (namely, Lucas effect). In this case, more competition between new and old production lines (parameterized by increased substitutability between them) will induce skilled workers to switch from old to newer lines more rapidly (Ahn, 2002).

II.3 Competition and selection

Firm dynamics (i.e., birth and death, growth and decline of individual firms) make an integral part of dynamic competition. An increasing number of theoretical and empirical studies focused firm level or plant-level dynamics show that overall productivity of an industry significantly affected by compositional changes in the industry due to firm dynamics. Dynamic competition continuously weeds out less efficient firms from more efficient ones and reallocates productive resources from shrinking/exiting firms to entering/growing firms. In this context, well-functioning labor markets and capital markets are very important.

Schumpeter. Dynamic competition is a process in which innovators with new technology enter a market and compete with current conventional technology can find a theoretical framework for dynamic competition and firm dynamics in the notion of “creative destruction”. If the innovation is successful, the entrants will be able replace the current. If not, they will fail to survive, such dynamic competition “from the new commodity, the new technology, the new source of supply, the new type of organizations” strikes “not at the margins of the profits and the outputs of the existing firms but at their foundations and their very lives” (Ahn, 2002).

When current, which have already accumulated substantial experience with conventional technology, are less enthusiastic about taking risks of adopting new technology, new entrants aggressively experimenting with new technology can be a driving force of innovations. Current are also forced to innovate themselves by the competitive pressure coming from the existence of actual and/or potential entrants. Overall productivity evolves with successive innovations through selection process of firm dynamics under competitive pressure.

II.4 New modes of competition

In some high-tech industries such as information and communication technology (ICT) sectors where technological changes are very rapid and competition centers on Schumpeterian innovation, “dynamic” competition *for the market* is arguably more important than static price/output competition *in the market* (Ahn, 2002). In the static sense, competition in such high-tech industries appears far from being rigorous. A few dominant firms have significant market power and they set prices well above marginal costs. In the Schumpeterian view, however, the *expectation* of short-run market power is a necessary condition for dynamic competition and the *existence* of short-run market power does not necessarily imply lack of competition. In such industries, competition between different systems/networks to become the standard in the market is fierce.

II.4.1 Network effects: “Positive feedback effects” and “systems competition” are keywords in understanding new features of dynamic competition. In markets with “network effects”, users want to buy products, which are compatible with those bought by others because the value of a product is an increasing function of the size of the network of compatible products (Ahn, 2002). Network effects are indeed pervasive, and can take different forms:

II.4.1.1 Direct network effects: found in communications networks (e.g., telephone, fax, mobile phone, etc.). As an extreme case, a fax machine would be of no use if one’s counterparts do not have a compatible fax machine.

II.4.1.2 Indirect network effects: found in a system of hardware/software. A larger base of hardware owners implies a larger market for compatible software products. If software production has scale effects, consumers belonging to a larger network of a hardware/software

system will be able to buy software at a lower price and they will have more variety in choosing software products. In general, indirect network effects exist in any situation where the availability of complementary goods increases as the number of users of the good increases. Systems competition based on such indirect network effects observed in various areas: computer hardware and software; credit-card networks; durable equipment and repair services, and the typewriter keyboard.

When more than one network are competing with one another, buyers want to get more benefits from network effects by joining a larger or winning network. Therefore, a larger network has advantage in competing with smaller ones and hence can grow even faster. In other words, network effects create “positive feedback effects” or “snowball effects”.

III. Chapter 3: Empirical Methods

III.1 Major empirical issues

Two important empirical issues deserve special attention the one is on the relations between market structure and technological progress. The other is on evaluating effects of regulatory reform.

III.1.1 Schumpeterian hypothesis on competition and innovation

Focused on the relationship between firm size and innovation. Some arguments for a positive effect of firm size on innovation are as follows (Ahn, 2002):

III.1.1.1 The returns from R&D are higher where the innovator has a large volume of sales over which to spread the fixed costs of innovation (*economies of scale* in research and development).

III.1.1.2 Large diversified firms can benefit from positive spillovers between the various research programs (*economies of scope* in research and development).

III.1.1.3 Large firms can undertake many projects at one time and hence diversify the risks of research and development.

III.1.1.4 Large firms with market power have an advantage in securing finance for risky research and development, because size and market power can increase the availability and stability of external and internal funds.

However, one can also find counter-arguments in the spirit of Schumpeter (1942), namely, the bureaucratization of inventive activity (Ahn, 2002).

III.1.1.5 As firms grow large, efficiency in research and development undermined through loss of managerial control.

III.1.1.6 As firms grow large, the incentives of individual scientists and entrepreneurs attenuated as their ability to capture the benefits from their efforts diminishes.

In many empirical studies, Schumpeter's claim that large firms in concentrated markets have advantage in innovation interpreted as a proposition that innovative activity increases more than proportionately than firm size (Ahn, 2002). Alternatively, some other studies examined the relationship between market concentration and innovative activities measured by innovative inputs research and development expenditures.

III.1.2 Effects of regulatory reform

Economic regulation (e.g., regulation of pricing, entry and exit) would deprive consumers of the benefits from price competition. Market distorting regulations would also create allocative inefficiencies by making prices deviate from marginal costs. Even though regulation could benefit protected firms by insulating them from competition, it would also restrict their operations and thus create dynamic inefficiencies as indicated by low productivity growth, slow technological innovation, and the poor quality of management (Ahn, 2002). In fact, the United States and many other OECD Organization for Economic Cooperation and Development. Countries have made considerable progress in regulatory reform in some sectors during the last two decades, and the available evidence suggests that progress in regulatory reform has been beneficial for efficiency and consumer welfare (Ahn, 2002)

IV. Chapter 4: Research Proposal

IV.1 Research question (Business problem):

Success of a local pharmaceutical company (SPIMACO ADDWAEAH) in leading the KSA pharmaceutical market (the largest Middle-East market) vis-à-vis the multinationals.

This problem is important to all pharmaceutical companies operating in the Middle East and North Africa region as the KSA market is the largest and the most attractive market to operate in due to high profitability

.IV.2 Variables: (Kotler, 1975)

IV.2.1 Independent variable: Competitive pacification

IV.2.2 Dependent variable: Market Share

IV.3 Variables (definitions):

IV.3.1 Competitive pacification: the high-share company may attempt to reduce the risks associated with its position by cultivating better relations with its competitors. This done in numerous ways.

- Organizations may help find supplies of raw materials, or even sell the material outright.
- They may conduct advertising campaigns that promote the product category rather than their specific brands.
- They may refrain from reacting strongly to the strategy changes of their rivals.
- They may supply valuable research data and other assistance to smaller competitors through trade association activities.

- They may provide price umbrellas.
- In addition, they may hold back the rate of new product introduction. (Of course, the company that chooses to use competitive pacification strategies must be careful to avoid behaving in what considered a collusive manner.)

IV.3.2 Market share: capturing a dominant share of a market is likely to mean enjoying the highest profits of any of the companies serving that market. It can also mean winning the leadership, power, and glory that go with such dominance

IV.4 Variables (measurements):

IV.4.1 Competitive pacification: wider variety of products to choose.

IV.4.2 Market Share: Sales (SAR)

IV.5 Variables (relationship):

IV.5.1 Competitive pacification is directly increasing market share

IV.6 Hypothesis:

IV.6.1 If competitive pacification is applied the market share of the high market share company will go up

IV.7 Research design:

IV.7.1 In-depth Interviews with top management to determine which competitive pacification tactics led to growing up the market share

V. Chapter 5: Case Study

Success of a local pharmaceutical company (SPIMACO ADDWAEAH) in leading the KSA pharmaceutical market (the largest Middle-East market) vis-à-vis the multinationals.

V.1 Data needed:

V.1.1 Annual reports of (2010-2013)

V.1.2 Strategic audit report 2013

V.1.3 Business plans 2014

V.1.4 Strategic alliances contracts copy

V.2 Data sources:

V.2.1 Global marketing director

V.2.2 Strategic planning manager

V.2.3 Business development manager

V.3 Data analysis:

V.3.1 Focus group (marketing team, sales field force, business development team)

V.4 Conclusion:

V.4.1 Strategic alliance with the multinationals help to pacify the competition and results in leading the market vis-à-vis the multinationals.

V.5 Recommendation:

V.5.1 Further strategic alliance and pacify competition needs to be applied in different industries.

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