

5.4: Globalization and Industry Structure

Yoffie suggests 5 propositions that help explain how the structure of an industry can evolve depending on, among other factors, the dynamics that shape competition in the industry and the role governments play in stimulating or obstructing the globalization process. (Yoffie (1993), chaps. 1 and 10. The reader is encouraged to consult this excellent book for further details).

Proposition 1 is that when industries are relatively fragmented and competitive, national environments (factors of production, domestic market and domestic demand, and so forth) will largely shape the international advantage of domestically headquartered firms and the patterns of trade. A correlate to this proposition is that in emerging industries, country advantages also play a dominant role in determining global competitive advantage.

In other words, in fragmented industries relative cost is a key determinant of global success, and since countries differ in terms of their factor costs, as long as entry barriers remain low, production will gravitate to the lowest cost, highest efficiency manufacturing location. Another way of saying this is that the presence of multinational firms, by itself, should not influence the pattern of international trade in globally competitive, fragmented industries; other things being equal, country factors determine the location of production and the direction of exports. Oligopolistic global industry structures define a very different strategic context, as the next proposition illustrates.

Proposition 2 stipulates that if an industry becomes globally concentrated with high barriers to entry, then location, activity concentration, export, and other strategic decisions by multinational companies are determined to a greater extent by the nature of the global oligopolistic rivalry. Thus, while in concentrated industries country characteristics remain important, the dynamics of the global, oligopolistic competitive climate become the principal drivers of global strategy. This is intuitive. In global oligopolies, more so than in fragmented market structures, the success of one firm is directly affected by that of a few, immediate competitors. Entry into the industry is often restricted in some way—by factors such as economies of scale or scope, high levels of capital investment, and the like, or by restrictions imposed by governments. Furthermore, in many global oligopolies, participating firms earn above-average returns, which may make the difference in cost between producing locally and exporting a less critical determinant of strategy. Opportunities to cross-subsidize businesses and geographies further reduce the importance of geography in production or export decisions. As a consequence, the moves and countermoves of direct, global competitors heavily influence company strategies. For example, it is quite common for companies to enter some other firm's home market, not just because that market is likely to generate additional profits but mainly to weaken its global competitive position. This line of reasoning directly leads to a third proposition, which relates organizational and strategic attributes of global competitors to global strategic choice.

Proposition 3 suggests that in global oligopolies, specific firm characteristics—the structure of ownership, strategies employed, and organizational factors, to name a few—directly affect strategic posture, the pattern of trade, and, sometimes, the competitiveness of nations. In global oligopolies with a relatively small number of competitors, issues such as *who* owns the resources necessary for creating value and *who* sets the global priorities take on a greater strategic significance. Executives from different cultures approach strategy differently—state-owned enterprises are often more motivated by public policy considerations, employment, and other nonprofit concerns. These differences can have a direct impact on the relative attractiveness of global strategy options. The influence of governments in global markets is captured further in the fourth proposition.

Proposition 4 suggests that extensive government intervention in global oligopolistic industries can alter the relative balance between firms of different countries—even in fragmented industries, it can alter the direction of trade and affect major corporate trade decisions. The degree and influence of government intervention varies from industry to industry. Whereas in fragmented industries the influence of governments is naturally somewhat limited by market conditions, government intervention can have a pronounced influence in industries with significant economies of scale effects or other market imperfections. For example, governments can protect “infant” industries with such characteristics. While a case can be made for the temporary protection of strategically important industries, in reality, such protection is rarely temporary. This can create a global strategic environment in which anticipating and capitalizing on the actions of governments become the driving forces of global strategy.

Proposition 5 suggests that in industries where firms make long-term commitments, corporate adjustments and patterns of trade tend to be “sticky.” This fifth and final proposition addresses the issue of corporate inertia. Although the global competitive climate changes every day, choices made by multinational companies and governments tend to have an enduring impact on the industry environment. This proposition has at least two implications. First, the study of how industries evolve globally and what decisions different competitors made and how they made them is relevant to understanding what drives strategy in a particular global context. Second, the commitments already made by industry participants and governments may spell opportunity or impose constraints for years to come.

These 5 propositions define 2 important dimensions for classifying globalizing industries according to the nature of the strategic challenge they represent: *the degree of global concentration and the extent to which governments intervene*. In industries with a relatively low degree of concentration and little government intervention, the classical economic laws of *comparative advantage* are the primary drivers of international competition. Here, factor costs are a primary determinant of global competitiveness. It would seem natural, therefore, to focus on a global strategy aimed at minimizing costs. But this can be extremely difficult in a fast-changing world. Comparative country costs change continuously. In cars, semiconductors, and computers, among other industries, the comparative (cost) advantage has shifted a number of times since World War II from the United States to Japan to East Asia to Southeast Asia. What is more, there is good reason to believe it will shift again, perhaps to Africa or Latin America. And, with new technological breakthroughs, Western nations may once again become the low-cost production centers. So what should companies do? While companies should definitely take advantage of opportunities to minimize costs, especially in their initial investments, Yoffie suggests that long-term global strategic choices should emphasize *commitments to countries that are likely to act as the best platforms over time for a broad array of activities*. (Yoffie (1993), 432).

In globally concentrated industries where the role of governments is limited, characterized by *oligopolistic competition*, company strategies are often heavily influenced by the moves and countermoves of direct competitors. Strategies such as making significant investments in competitors' markets, regardless of their short- or medium-run profitability—which would not work in highly competitive markets—can only be explained in terms of a strategic posture aimed at maintaining a long-term global competitive balance between the various participants. Caterpillar invested heavily in Japan while Komatsu and European construction equipment manufacturing moved into the United States at a time when such moves offered limited immediate returns. In this kind of competitive environment, the potential for overglobalization—the globalization of different aspects of strategy well in advance of proven benefits—exists as the relatively small number of competitors and high barriers to entry encourage “follow-the-leader” competitive behavior. On the other hand, not responding directly to major competitors can be equally dangerous. Komatsu's challenge to Caterpillar, in part, was made possible because, early on, Caterpillar focused its strategy on keeping John Deere, International Harvester, and Dresser Industries at bay rather than on beating Komatsu. This suggests a number of strategic implications. First, while imitation cannot be the sole basis for developing strategy, in oligopolies, it may be necessary, at times, to match a competitor in order to reduce the risk of competitive disadvantage. A related implication is that in global oligopolies, companies cannot allow their competitors to have uncontested home markets in which profit sanctuaries can be used to subsidize global competitive moves. This explains Kodak's extraordinary efforts to pry open the Japanese market—it knew Fuji would be at a considerable advantage if it remained dominant in Japan. Finally, the use of alliances can make such global moves more affordable, flexible, and effective. Alliances can be powerful vehicles for rapidly entering new countries, acquiring new technologies, or otherwise supporting a global strategy at a relatively low cost. (Yoffie (1993), 433, 434).

Dealing effectively with governments is a prerequisite for global success in oligopolistic industries such as telecommunications, where extensive government intervention creates a global competitive climate known as regulated competition. Here, nonmarket dimensions of global strategy may well be as important as market dimensions. Political involvement may be necessary to create, preserve, or enhance global competitive advantage since government regulations—whether in infant or established industries—are critical to success. As a consequence, strategy in global, regulated industries should be focused as much on shaping the global competitive environment as on capitalizing on the opportunities it offers.

Political competition, characteristic of fragmented industries with significant government intervention, also calls for a judicious mix of market and nonmarket-based strategic thinking. In contrast to regulated competition, in which government policy has a direct impact on individual companies, however, government intervention in political competition often pits one country or region of the world against another. This encourages a whole range of cooperative strategies between similarly affected players and strategic action at the country-industry level.

Finally, it is worth remembering that patterns of competition are not static. Industries evolve continuously, sometimes dramatically. Similarly, the focus of government action in different industries can change as national priorities change and the global competitive environment evolves.

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