10

Export modes

Contents

Learning objectives

After studying this chapter you should be able to do the following:

- **Distinguish between indirect, direct and cooperative export modes.**
- **Describe and understand the five main entry modes of indirect exporting:**
  - **export buying agent;**
  - **broker;**
  - **export management company/export house;**
  - **trading company; and**
  - **piggyback.**
- **Describe the two main entry modes of direct exporting:**
  - **distributor;**
  - **agent.**
- **Discuss the advantages and disadvantages of the main export modes.**
- **Discuss how manufacturers can influence intermediaries to be effective marketing partners.**

10.1 Introduction

With export entry modes a firm's products are manufactured in the domestic market or a third country and then transferred either directly or indirectly to the host market.

Export is the most common mode for initial entry into international markets. Sometimes an unsolicited order is received from a buyer in a foreign country, or a domestic customer expands internationally and places an order for its international operations. This prompts the firm to consider international markets and to investigate their growth potential.

Exporting is thus typically used in initial entry and gradually evolves towards foreign-based operations. In some cases where there are substantial scale economies or a limited number of buyers in the market worldwide (e.g. for aerospace), production may be concentrated in a single or a limited number of locations, and the goods then exported to other markets.

Exporting can be organized in a variety of ways, depending on the number and type of intermediaries. As in the case of wholesaling, export and import agents vary considerably in the range of functions performed. Some, such as export management companies, are the equivalent of full-service wholesalers and perform all functions relating to export. Others are highly specialized and handle only freight forwarding, billing or clearing goods through customs.

In establishing export channels a firm has to decide which functions will be the responsibility of external agents and which will be handled by the firm itself. While export channels may take many different forms, for the purposes of simplicity three major types may be identified: indirect, direct and cooperative export marketing groups.

1 *Indirect export*. This is when the manufacturing firm does not take direct care of exporting activities. Instead another domestic company, such as an export house or trading company, performs these activities, often without the manufacturing firm's involvement in the foreign sales of its products.
2 *Direct export*. This usually occurs when the producing firm takes care of exporting activities and is in direct contact with the first intermediary in the foreign target market. The firm is typically involved in handling documentation, physical delivery and pricing policies, with the product being sold to agents and distributors.
3 *Cooperative export*. This involves collaborative agreements with other firms (export marketing groups) concerning the performance of exporting functions.

In Figure 10.1 the different export modes are illustrated in a value chain.

Partner mindshare

Partner mindshare
The level of mindshare that the manufacturer's product occupies in the mind of the export partner (e.g. agent or distributor).

No matter which of the three export modes the manufacturer uses in a market, it is important to think about what level of 'mindshare', that the manufacturer 'occupies' in the mind of the export-partner. **Partner mindshare** is a measurement of the strength of a relationship in terms of trust, commitment and cooperation. There is a strong and proven correlation between mindshare levels and how willing an export intermediary is to place one company-brand in front of another, or how likely the intermediary is to defect. Mindshare also expresses itself very clearly in sales performance. Intermediaries who have high mindshare will, typically, sell more than those with low mindshare.

Mindshare can be broken down into three drivers (Gibbs, 2005)

1 commitment and trust;
2 collaboration;
3 mutuality of interest and common purpose.

Good mindshare is going to depend upon scoring well across the board. For example, there are manufacturers, who are good communicators, but are not trusted.

As well as these three mindshare drivers there is a fourth group we need to measure – product, brand and profit. This fourth measures the perceived attractiveness of the supplier's product offering to the intermediary. The manufacturer can think of this as a hygiene driver. Broadly speaking, the performance of the manufacturer needs to be as good as the competition for him to garner the full benefit from strong mindshare.

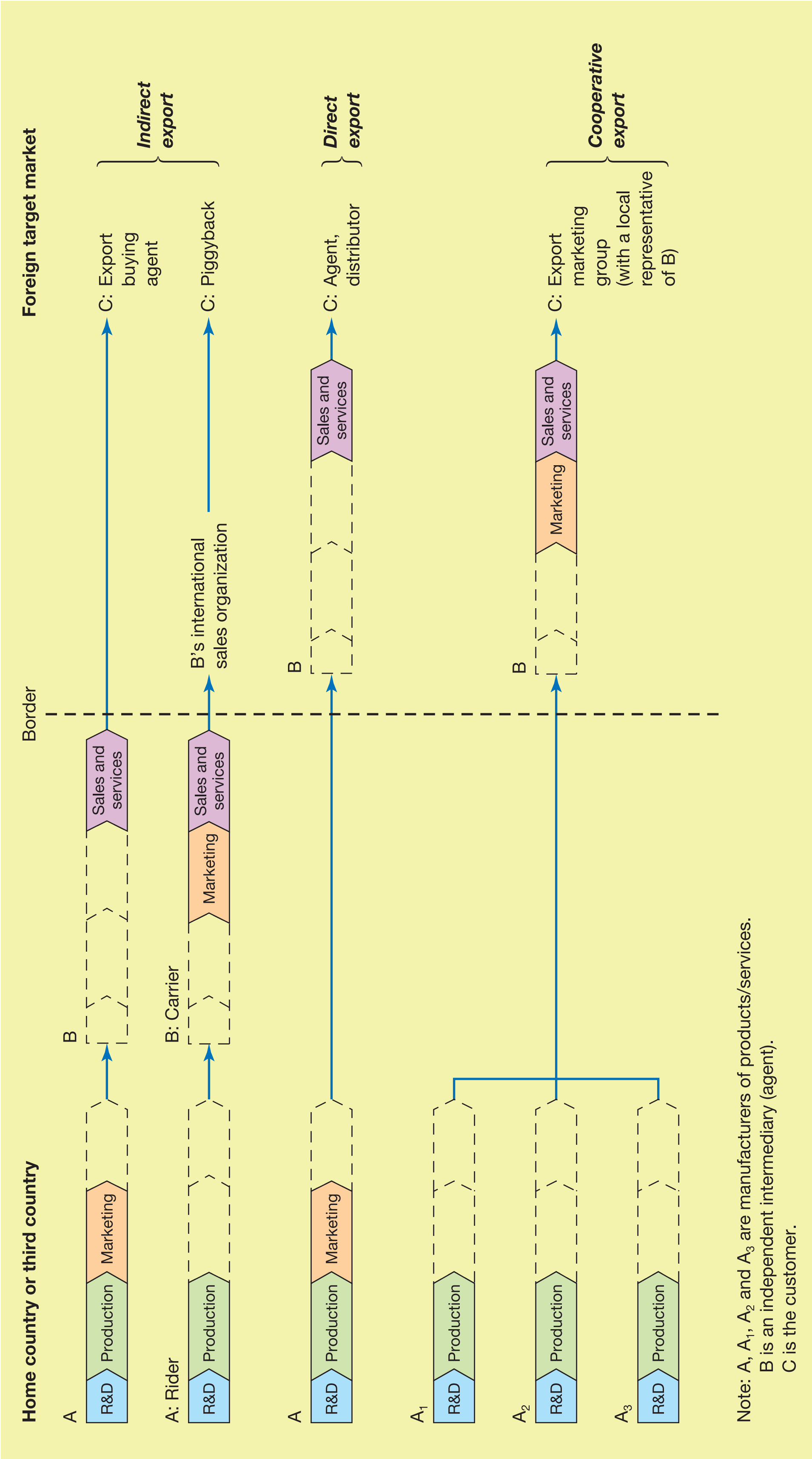


Figure 10.1 Export modes

Many manufacturers with excellent products and strong brands which offer good profits, struggle precisely because they are seen by the export partner as arrogant, untrustworthy and unhelpful. In other words, they have low mindshare at the export partner.

Each of the three drivers can be broken down further. For instance, collaboration is based partly on a measure of how good the manufacturer is at cooperating on sales. Another constituent of collaboration measures its ability to cooperate on marketing. Other constituents measure whether it is perceived as communicating relevant information in a timely way, how much real joint planning takes place and how valuable the export intermediary finds this process.

Mindshare is severely damaged when suppliers refuse to share resources with partners. Partners may feel excluded – not part of the family. If the intermediary has no long-term stake in manufacturer, and has more mindshare with a competitor, then one could choose to simply wind down activities with that intermediary. Alternatively, the manufacturer can fight back by integrating its products and campaigns into the intermediary's business plan and going out of its way to show commitment to the intermediaries. At Oracle they are doing that by saying: 'Our approach is to give marketing materials to our partners. Give them the things they would get if they were internal employees' (Hotopf, 2005).

Manufacturers need to understand the partners' business models, goals, their value to the manufacturer and what it would cost to replace them. But the manufacturer also needs to look at the long-term value of the relationship (life time value = year-on-year value multiplied by the number of years that the manufacturer typically does business with export intermediaries). This can be used to justify investments in the relationship.

10.2 Indirect export modes

Indirect export occurs when the exporting manufacturer uses independent organizations *located in the producer's country*. In indirect exporting the sale is like a domestic sale. In fact the firm is not really engaging in global marketing, because its products are carried abroad by others. Such an approach to exporting is most likely to be appropriate for a firm with limited international expansion objectives. If international sales are viewed primarily as a means of disposing of surplus production, or as a marginal, use of **indirect export modes** may be appropriate. This method may also be adopted by a firm with minimal resources to devote to international expansion, which wants to enter international markets gradually, testing out markets before committing major resources and effort to developing an export organization.

Indirect export modes
Manufacturer uses independent export organizations located in its own country (or third country).

It is important for a firm to recognize, however, that the use of agents or export management companies carries a number of risks. In the first place the firm has little or no control over the way the product or service is marketed in other countries. Products may be sold through inappropriate channels, with poor servicing or sales support and inadequate promotion, or be under- or overpriced. This can damage the reputation or image of the product or service in foreign markets. Limited effort may be devoted to developing the market, resulting in lost potential opportunities.

Particularly significant for the firm interested in gradually edging into international markets is that, with indirect exporting, the firm establishes little or no contact with markets abroad. Consequently the firm has limited information about foreign market potential, and obtains little input to develop a plan for international expansion. The firm will have no means to identify potential sales agents or distributors for its products.

While exporting has the advantage of the least cost and risk of any entry method, it allows the firm little control over how, when, where and by whom the products are sold. In some cases the domestic company may even be unaware that its products are being exported.

Moreover, an SME that is already experienced in traditional exporting may have resources that are too limited to open up a great number of export markets by itself. Thus, through indirect export modes the SME is able to utilize the resources of other experienced exporters and to expand its business to many countries.

There are five main entry modes of indirect exporting:

1 export buying agent;
2 broker;
3 export management company/export house;
4 trading company;
5 piggyback (shown as a special case of indirect exporting in Figure 10.1).

1 Export buying agent (export commission house)

Some firms or individuals do not realize that their products or services have potential export value until they are approached by a buyer from a foreign organization, which might make the initial approach, purchase the product at the factory gate and take on the task of exporting, marketing and distributing the product in one or more overseas markets.

Export buying agent
A representative of foreign buyers who is located in the exporter's home country. The agent offers services to the foreign buyers: such as identifying potential sellers and negotiating prices.

The **export buying agent** is a representative of foreign buyers who resides in the exporter's home country. As such, this type of agent is essentially the overseas customer's hired purchasing agent in the exporter's domestic market, operating on the basis of orders received from these buyers. Since the export buying agent acts in the interests of the buyer, it is the buyer that pays a commission. The exporting manufacturer is not directly involved in determining the terms of purchase; these are worked out between the export buying agent and the overseas buyer.

The export commission house essentially becomes a domestic buyer. It scans the market for the particular merchandise it has been requested to buy. It sends out specifications to manufacturers inviting bids. Other conditions being equal, the lowest bidder gets the order and there is no sentimentality, friendship or sales talk involved.

From the exporter's point of view, selling to export commission houses represents an easy way to export. Prompt payment is usually guaranteed in the exporter's home country, and the problems of physical movement of the goods are generally taken completely out of its hands. There is very little credit risk and the exporter has only to fulfil the order, according to specifications. A major problem is that the exporter has little direct control over the global marketing of products.

Small firms find that this is the easiest method of obtaining foreign sales but, being totally dependent on the purchaser, they are unlikely to be aware of a change in consumer behaviour and competitor activity, or of the purchasing firm's intention to terminate the arrangement. If a company is intent upon seeking longer-term liability for its export business it must adopt a more proactive approach, which will inevitably involve obtaining a greater understanding of the markets in which its products are sold.

2 Broker

Another type of agent based in the home country is the export/import broker. The chief function of a broker is to bring a buyer and a seller together. Thus the broker is a specialist in performing the contractual function, and does not actually handle the products sold or bought. For its services the broker is paid a commission (about 5 per cent) by the principal. The broker commonly specializes in particular products or classes of product. Being a commodity specialist there is a tendency for the broker to concentrate on just one or two products. Because the broker deals primarily in basic commodities, for many potential export marketers this type of agent does not represent a practical alternative channel of distribution. The distinguishing characteristic of export brokers is that they may act as the agent for either the seller or the buyer.

3 Export management company/export house

Export houses or export management companies (EMCs) are specialist companies set up to act as the 'export department' for a range of companies. As such the EMC conducts business in the name of each manufacturer it represents. All correspondence with buyers and contracts are negotiated in the name of the manufacturer, and all quotations and orders are subject to confirmation by the manufacturer.

By carrying a large range EMCs can spread their selling and administration costs over more products and companies, as well as reducing transport costs because of the economies involved in making large shipments of goods from a number of companies.

EMCs deal with the necessary documentation, and their knowledge of local purchasing practices and government regulations is particularly useful in markets that might prove difficult to penetrate. The use of EMCs, therefore, allows individual companies to gain far wider exposure of their products in foreign markets at much lower overall costs than they could achieve on their own, but there are a number of disadvantages, too:

- The export house may specialize by geographical area, product or customer type (retail, industrial or institutional), and this may not coincide with the supplier's objectives. So the selection of markets may be made on the basis of what is best for the EMC rather than for the manufacturer.
- As EMCs are paid by commission they might be tempted to concentrate upon products with immediate sales potential, rather than those that might require greater customer education and sustained marketing effort to achieve success in the longer term.
- EMCs may be tempted to carry too many product ranges and as a result the manufacturer's products may not be given the necessary attention from sales people.
- EMCs may carry competitive products that they may promote to the disadvantage of a particular firm.

Manufacturers should therefore take care in selecting a suitable EMC and be prepared to devote resources to managing the relationship and monitoring its performance.

As sales increase the manufacturer may feel that it could benefit from increased involvement in international markets, by exporting itself. However, the transition may not be very easy. First, the firm is likely to have become very dependent on the export house and, unless steps have been taken to build contacts with foreign customers and to build up the firm's knowledge of its markets, moving away from using an EMC could prove difficult. Second, the firm could find it difficult to withdraw from its contractual commitments to the export house. Third, the EMC may be able to substitute products from an alternative manufacturer and so use its existing customer contacts as a basis for competing against the original manufacturer.

4 Trading company

Trading companies are part of the historical legacy from colonial days and, although different in nature now, they are still important trading forces in Africa and the Far

East. Although international trading companies have been active throughout the world, it is in Japan that the trading company concept has been applied most effectively. There are thousands of trading companies in Japan involved in exporting and importing, and the largest firms (varying in number from nine to 17 depending upon source of estimate) are referred to as general trading companies or *Soge Shosha*. This group of companies, which includes C. Itoh, Mitsui & Company and Mitsubishi Shoji Kaisha, handle 50 per cent of Japan's exports and 67 per cent of its imports. While the smaller trading companies usually limit their activities to foreign trade, the larger general trading companies are also heavily involved in domestic distribution and other activities.

Trading companies play a central role in such diverse areas as shipping, warehousing, finance, technology transfer, planning resource development, construction and regional development (e.g. turnkey projects), insurance, consulting, real estate and deal making in general (including facilitating investment and joint ventures). In fact it is the range of financial services offered that is a major factor distinguishing general trading companies from others. These services include the guaranteeing of loans, the financing of both accounts receivable and payable, the issuing of promissory notes, major foreign exchange transactions, equity investment and even direct loans.

Another aspect of their operations is to manage counter-trade activities (barter), in which sales into one market are paid for by taking other products from that market in exchange. The essential role of the trading company is to find a buyer quickly for the products that have been taken in exchange. Sometimes this can be a very resource-demanding process.

Counter trade is still a very widespread trading form in Eastern Europe and developing countries because of their lack of 'hard' currency. One of the motivations for western firms to go into counter trade is the low-cost sources of production and raw materials for use in the firm's own production (Okoroafo, 1994).

Piggyback
An abbreviation of 'Pick-a-Back': i.e. choosing a back to ride on. It is about the rider's use of the carrier's international distribution organization.

5 Piggyback

In piggybacking the export-inexperienced SME, the 'rider', deals with a larger company (the 'carrier') which already operates in certain foreign markets and is willing to act on behalf of the rider that wishes to export to those markets. This enables the carrier to utilize fully its established export facilities (sales subsidiaries) and foreign distribution. The carrier is either paid by commission and so acts as an agent or, alternatively, buys the product outright and so acts as an independent distributor. Piggyback marketing is typically used for products from unrelated companies that are non-competitive (but related) and complementary (allied).

Sometimes the carrier will insist that the rider's products are somewhat similar to its own, in view of the need to deal with technical queries and after-sales service 'in the field'. Branding and promotional policies are variable in piggybacking. In some instances the carrier may buy the products, put its own brand on them, and market them as its own products (private labels). More commonly the carrier retains the brand name of the producer and the two work out promotional arrangements between them. The choice of branding and promotional strategy is a function of the importance of brand to the product and of the degree to which the brand is well established.

Piggybacking has the following advantages/disadvantages for the carrier and the rider.

Carrier

Advantages

A firm that has a gap in its product line or excess capacity in its export operation has two options. One is to develop internally the products necessary to round out its line and fill up its exporting capacity. The other option is to acquire the necessary products outside by piggybacking (or acquisition). Piggybacking may be attractive because the firm can get the product quickly (someone already has it). It is also a low-cost way to get the product because the carrier firm does not have to invest in R&D, production facilities or market testing for the new product. It can just pick up the product from another firm. In this way the firm can broaden its product range without having to develop and manufacture extra products.

Disadvantages

Piggybacking can be extremely attractive for the carrier, but some concerns exist about quality control and warranty. Will the rider maintain the quality of the products sold by another firm? This depends in part on whose brand name is on the product. If the rider's name is on the product the quality incentive might be stronger. A second concern is continuity of supply. If the carrier develops a substantial market abroad, will the rider firm develop its production capacity, if necessary? Each of these items should be a subject in the agreement between the two parties. If the piggybacking arrangement works out well there is another potential advantage for the carrier. It might find that the rider is a good acquisition candidate or joint-venture partner for a stronger relationship.

Rider

Advantages

Riders can export conveniently without having to establish their own distribution systems. They can observe carefully how the carrier handles the goods and hence learn from the carrier's experience – perhaps to the point of eventually being able to take over its own export transactions.

Disadvantages

For the smaller company this type of agreement means giving up control over the marketing of its products – something that many firms dislike doing, at least in the long run. Lack of commitment on the part of the carrier and the loss of lucrative sales opportunities in regions not covered by the carrier are further disadvantages.

In summary, piggyback marketing provides an easy, low-risk way for a company to begin export marketing operations. It is especially well suited to manufacturers that either are too small to go directly into exports or do not want to invest heavily in foreign marketing.

10.3 Direct export modes

Direct exporting occurs when a manufacturer or exporter sells directly to an importer or buyer located in a foreign market area. In our discussion of indirect exporting we examined ways of reaching foreign markets without working very hard. Indeed, in the indirect approaches, foreign sales are handled in the same way as domestic sales: the producer does the global marketing only by proxy (that is, through the firm that carries its products overseas). However, both the global marketing know-how and the sales achieved by these indirect approaches are limited.

As exporters grow more confident they may decide to undertake their own exporting task. This will involve building up overseas contacts, undertaking marketing research,

Direct export modes
Manufacturer sells directly to an importer, agent or distributor located in the foreign target market.

handling documentation and transportation, and designing marketing mix strategies. **Direct export modes** include export through foreign-based agents and distributors (independent intermediaries).

The terms 'distributor' and 'agent' are often used synonymously. This is unfortunate because there are distinct differences: distributors, unlike agents, take title to the goods, finance the inventories and bear the risk of their operations, whereas agents do not. Distributors are paid according to the difference between the buying and selling prices rather than by commission (agents). Distributors are often appointed when after-sales service is required, as they are more likely than agents to possess the necessary resources.

Distributors

Distributor (importer)
Independent company that stocks the manufacturer's product. It will have substantial freedom to choose own customers and price. It profits from the difference between its selling price and its buying price from the manufacturer.

Exporting firms may work through **distributors (importers)**, which are the exclusive representatives of the company and are generally the sole importers of the company's product in their markets. As independent merchants, distributors buy on their own accounts and have substantial freedom to choose their own customers and to set the conditions of sale. For each country exporters deal with one distributor, take one credit risk, and ship to one destination. In many cases distributors own and operate wholesale and retail establishments, warehouses and repair and service facilities. Once distributors have negotiated with their exporters on price, service, distribution and so on their efforts focus on working their own suboperations and dealers.

The distributor category is broad and includes more variations, but distributors usually seek exclusive rights for a specific sales territory and generally represent the manufacturer in all aspects of sales and servicing in that area. The exclusivity is in return for the substantial capital investment that may be required on the part of the distributor in handling and selling products.

Agents

Agent
Independent company that sells on to customers on behalf of the manufacturer (exporter). Usually it will not see or stock the product. It profits from a commission (typically 5–10%) paid by the manufacturer on a pre-agreed basis.

Agents may be exclusive, where the agent has exclusive rights to specified sales territories; semi-exclusive, where the agent handles the exporter's goods along with other non-competing goods from other companies; or non-exclusive, where the agent handles a variety of goods, including some that may compete with the exporter's products.

An agent represents an exporting company and sells to wholesalers and retailers in the importing country. The exporter ships the merchandise directly to the customers, and all arrangements on financing, credit, promotion, etc., are made between the exporter and the buyers. Exclusive agents are widely used for entering international markets. They cover rare geographic areas and have subagents assisting them. Agents and subagents share commissions (paid by the exporter) on a pre-agreed basis. Some agents furnish financial and market information, and a few also guarantee the payment of customers' accounts. The commissions that agents receive vary substantially, depending upon services performed, the market's size and importance, and competition among exporters and agents.

The advantages of both agents and distributors are that they are familiar with the local market, customs and conventions, have existing business contacts and employ foreign nationals. They have a direct incentive to sell through either commission or profit margin, but since their remuneration is tied to sales they may be reluctant to devote much time and effort towards developing a market for a new product. Also, the amount of market feedback may be limited as the agent or distributor may see itself as a purchasing agent for its customers rather than as a selling agent for the exporter. If the agent or distributor is performing well and develops the market it risks being replaced by a subsidiary of the principal. Therefore a long-term strategy is needed whereby it might be useful to include the agent in any new entry mode decision (e.g. advent of a subsidiary) to avoid the disincentive of being replaced.

Choice of an intermediary

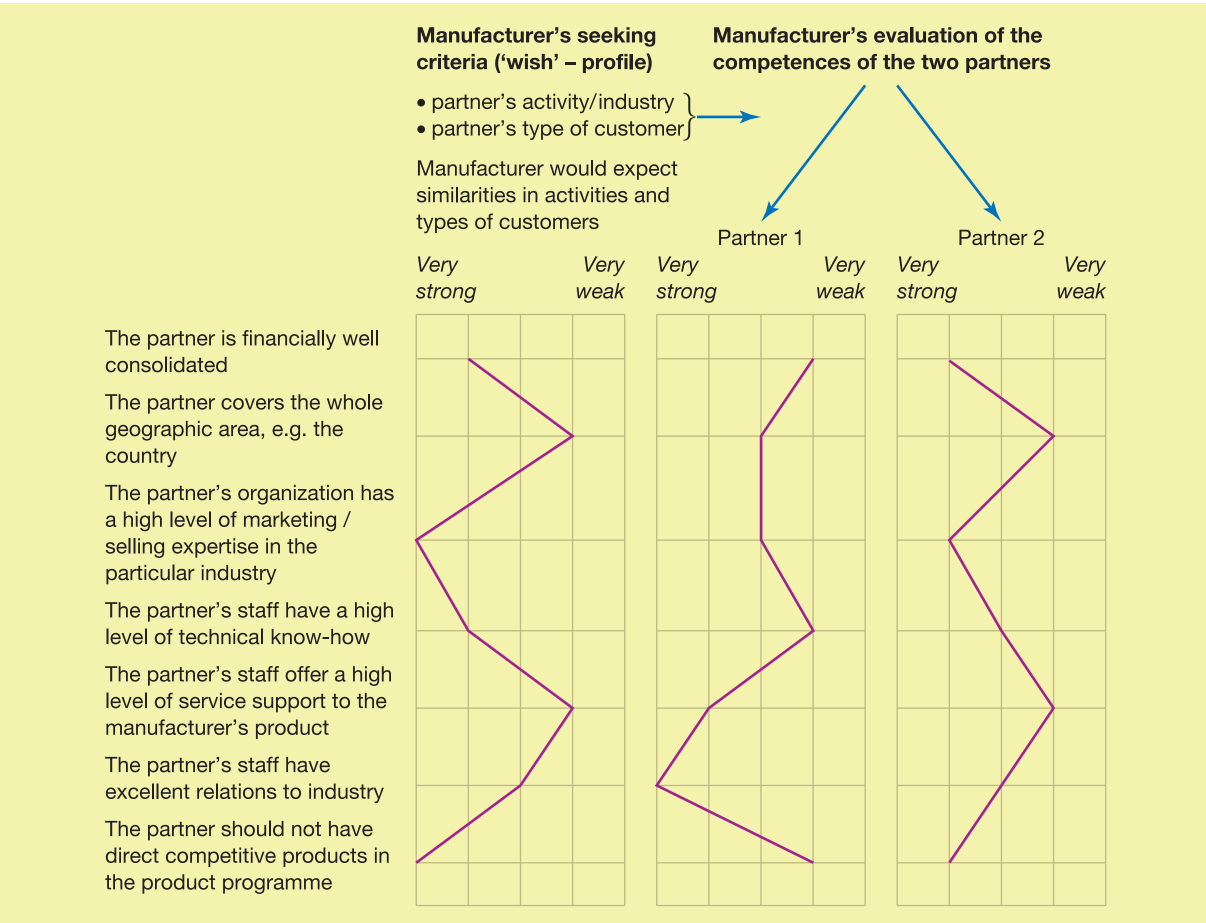
The selection of a suitable intermediary can be a problematic process. But the following sources may help a firm to find such an intermediary:

- asking potential customers to suggest a suitable agent;
- obtaining recommendations from institutions such as trade associations, chambers of commerce and government trade departments;
- using commercial agencies;
- poaching a competitor's agent;
- advertising in suitable trade papers.

In selecting a particular intermediary the exporter needs to examine each candidate firm's knowledge of the product and local markets, experience and expertise, required margins, credit ratings, customer care facilities and ability to promote the exporter's products in an effective and attractive manner.

Figure 10.2 shows the matchmaking of a manufacturer and its 'wish'-profile, and two potential intermediaries and their performance profiles in a particular market.

Figure 10.2 An example of matchmaking between a manufacturer and two potential distribution partners



If Partners 1 and 2 were the only potential candidates for the manufacturer, Partner 2 would probably be chosen because of the better match of profiles between what the manufacturer wants on the market ('wish'-profile) and the performance profile of Partner 2.

The criteria listed in Figure 10.2 would probably not be the only criteria in a selection process. Some other specific desirable characteristics of an intermediary (to be included in the decision-making process) are listed below (Root, 1998):

- size of firm;
- physical facilities;
- willingness to carry inventories;
- knowledge/use of promotion;
- reputation with suppliers, customers and banks;
- record of sales performance;
- cost of operations;
- overall experience;
- knowledge of English or other relevant languages;
- knowledge of business methods in manufacturer's country.

When an intermediary is selected by the exporting manufacturer it is important that a contract is negotiated and developed between the parties. The foreign representative agreement is the fundamental basis of the relationship between the exporter and the intermediary. Therefore the contract should clearly cover all relevant aspects and define the conditions upon which the relationship rests. Rights and obligations should be mutually defined and the spirit of the agreement must be one of mutual interest. The agreement should cover the provisions listed in Table 10.1.

For most exporters the three most important aspects of their agreement with foreign representatives are sole or exclusive rights, competitive lines and termination of the agreement. The issue of agreeing territories is becoming increasingly important, as in many markets distributors are becoming fewer in number, larger in size and sometimes more specialized in their activity. The trend to regionalization is leading

Table 10.1 Contracts with intermediaries

1 General provisions	
Identification of parties to the contract	Definition of territory or territories
Duration of the contract	Sole and exclusive rights*
Definition of covered goods	Arbitration of disputes
2 Rights and obligations of manufacturer	
Conditions of termination	Inspection of distributor's books
Protection of sole and exclusive rights	Trademarks/patents
Sales and technical support	Information to be supplied to the distributor
Tax liabilities	Advertising/promotion
Conditions of sale	Responsibility for claims/warranties
Delivery of goods	Inventory requirements
Prices	Termination and cancellation*
Order refusal	
3 Rights and obligations of distributor	
Safeguarding manufacturer's interests	Customs clearance
Payment arrangements	Observance of conditions of sale
Contract assignment	After-sales service
Competitive lines*	Information to be supplied to the manufacturer

* Most important and contentious issues.

Source: Root, F.R. (1998) *Entry Strategies for International Markets: Revised and Expanded Edition*, pp. 90–91. Copyright © Jossey-Bass 1998. Reprinted with permission of John Wiley & Sons, Inc.

distributors increasingly to extend their territories through organic growth, mergers and acquisitions, making it more difficult for firms to appoint different distributors in individual neighboring markets.

In general there are some principles that apply to the law of agency in all nations:

- An agent cannot take delivery of the principal's goods at an agreed price and resell them for a higher amount without the principal's knowledge and permission.
- Agents must maintain strict confidentiality regarding their principal's affairs and must pass on all relevant information.
- The principal is liable for damages to third parties for wrongs committed by an agent 'in the course of his or her authority' (e.g. if the agent fraudulently misrepresents the principal's firm).

During the contract period the support and motivation of intermediaries is important. Usually this means financial rewards for volume sold, but there can also be other means:

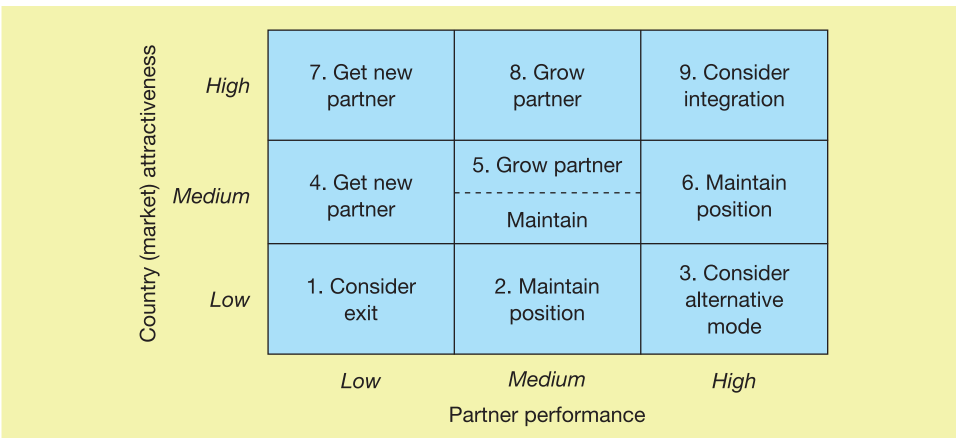
- significant local advertising and brand awareness development by the supplying firm;
- participation in local exhibitions and trade fairs, perhaps in cooperation with the local intermediary;
- regular field visits and telephone calls to the agent or distributor;
- regular meetings of agents and distributors arranged and paid for by the supplying company in the latter's country;
- competitions with cash prizes, free holidays, etc., for intermediaries with the highest sales;
- provision of technical training to intermediaries;
- suggestion schemes to gather feedback from agents and distributors;
- circulation of briefings about the supplying firm's current activities, changes in personnel, new product developments, marketing plans, etc.

Evaluating international distribution partners

Even if the firm has been very careful in selecting intermediaries a need can arise to extricate oneself quickly from a relationship that appears to be going nowhere.

In the process of evaluating international distribution partners Figure 10.3 can be used:

Figure 10.3 International partner matrix



According to Figure 10.3 the two most important criteria for evaluation international distributor partners are:

1 the performance of the distributor partner;
2 the general attractiveness of the market where the partner operates.

Performance can be evaluated by using criteria like achieved turnover and market share, profits generated for the manufacturer, established network to potential customers, etc. The country (market) attractiveness can be evaluated by using criteria like the ones discussed in Chapter 8 (Table 8.2 and Figure 8.5), for example, market size and market growth.

If the partner performance is low combined with a low attractiveness of the country (Cell 1), then the company should consider an exit from that country, especially if the low attractiveness seems to be a long-term phenomenon.

If the partner performance is high, but the country attractiveness is low (Cell 3), then the company could consider a shift to another entry mode (e.g. a joint venture). In this way the company can prevent dissatisfaction on the partner's side by rewarding it with a bigger part of the created profit pool in such a difficult market (low attractiveness).

If the partner is doing badly on a very attractive market (Cell 7), the partner should be switched with another (and better) one.

If the market is very attractive and the partner is doing a good job (Cell 9), then the company could consider forward integration, by turning the existing entry mode (distributor) into a subsidiary and promoting the distributor as the new CEO of the subsidiary, provided he or she has got the necessary competences for such a position and is endowed with sufficient management talent

The other cells of Figure 10.3 are mainly concerned with maintaining current position or 'growing' the existing partner. This can be done by offering training in the company's product/service solutions at HQ, or visiting the partner in the local market in order to show it that you are committed to its selling efforts in that local market.

Termination of contracts with distribution partners

Cancellation clauses in distribution partner agreements usually involve rights under local legislation and it is best that a contract is scrutinized by a local lawyer before signature, rather than after a relationship has ended and a compensation case is being fought in the courts.

Termination laws differ from country to country, but the European Union situation has been largely reconciled by a Directive regarding agents that has been effective in all EU member states since 1994. Under the Directive, an agent whose agreement is terminated is entitled to the following:

- full payment for any deal resulting from its work (even if concluded after the end of the agency);
- a lump sum of up to one year's past average commission;
- compensation (where appropriate) for damages to the agent's commercial reputation caused by unwarranted termination.

Outside western Europe some countries regard agents as basically employees of client organizations, while others see agents as self-contained and independent businesses. It is essential to ascertain the legal position of agency agreements in each country in which a firm is considering doing business. For example, laws in Saudi Arabia are extremely strong in protecting agents.

10.4 Cooperative export modes/export marketing groups

Export marketing groups are frequently found among SMEs attempting to enter export markets for the first time. Many such firms do not achieve sufficient scale economies in manufacturing and marketing because of the size of the local market or the inadequacy of the management and marketing resources available. These characteristics are typical of traditional, mature, highly fragmented industries such as furniture and clothing. Frequently the same characteristics are to be found among small, recently established high-technology firms.

Figure 10.1 shows an export marketing group with manufacturers A_1, A_2 and A_3, each having separate upstream functions but cooperating on the downstream functions through a common, foreign-based agent.

One of the most important motives for SMEs to join with others is the opportunity of effectively marketing a complementary product programme to larger buyers. The following example is from the furniture industry.

Manufacturers A_1, A_2 and A_3 have their core competences in the upstream functions of the following complementary product lines:

A_1 Living room furniture
A_2 Dining room furniture
A_3 Bedroom furniture.

Together they form a broader product concept that could be more attractive to a buyer in a furniture retail chain, especially if the total product concept targets a certain lifestyle of the end customers.

The cooperation between the manufacturers can be tight or loose. In a loose cooperation the separate firms in a group sell their own brands through the same agent, whereas a tight cooperation often results in the creation of a new export association. Such an association can act as the exporting arm of all member companies, presenting a united front to world markets and gaining significant economies of scale. Its major functions are the following:

- exporting in the name of the association;
- consolidating freight, negotiating rates and chartering ships;
- performing market research;
- appointing selling agents abroad;
- obtaining credit information and collecting debts;
- setting prices for export;
- allowing uniform contracts and terms of sale;
- allowing cooperative bids and sales negotiation.

Firms in an association can research foreign markets more effectively together, and obtain better representation in them. By establishing one organization to replace several sellers they may realize more stable prices, and selling costs can be reduced. Through consolidating shipments and avoiding duplicated effort firms realize transportation savings, and a group can achieve standardization of product grading and create a stronger brand name, just as the California fruit growers did with Sunkist products.

Considering all the advantages for an SME in joining an export marketing group, it is surprising that so few groups are actually running. One of the reasons for this could be that the firms have conflicting views as to what the group should do. In many SMEs there are strong feelings of independence inspired by their founders and entrepreneurs, which may be contrary, for example, to the common goal setting of export marketing groups. One of the major tasks of the export group is to balance the interests of the different stakeholders in the group.

10.5 Summary

The advantages and disadvantages of the three main types of export mode are summarised in Table 10.2.

Table 10.2 Advantages and disadvantages of the different export modes for the manufacturer

Export mode	Advantages	Disadvantages
Indirect exporting (e.g. export buying agent, broker or export management company)	Limited commitment and investment required. High degree of market diversification is possible as the firm utilizes the internationalization of an experienced exporter. Minimal risk (market and political). No export experience required.	No control over marketing mix elements other than the product. An additional domestic member in the distribution chain may add costs, leaving smaller profit to the producer. Lack of contact with the market (no market knowledge acquired). Limited product experience (based on commercial selling).
Direct exporting (e.g. distributor or agent)	Access to local market experience and contacts with potential customers. Shorter distribution chain (compared to indirect exporting). Market knowledge acquired. More control over marketing mix (especially with agents). Local selling support and services available.	Little control over market price because of tariffs and lack of distribution control (especially with distributors). Some investment in sales organization required (contact from home base with distributors or agents). Cultural differences, providing communication problems and information filtering (transaction costs occur). Possible trade restrictions.
Export marketing groups	Shared costs and risks of internationalization. Provide a complete product line or system sales to the customer.	Risk of unbalanced relationships (different objectives). Participating firms are reluctant to give up their complete independence.

CASE STUDY 10.1

Lysholm Linie Aquavit: International marketing of the Norwegian Aquavit brand

Aquavit, which translates as ‘water of life’, a slightly yellow or colourless alcoholic liquor, is produced in the Scandinavian countries by redistilling neutral spirits such as grain or potatoes and flavouring them with caraway seeds. It is often consumed as an aperitif.

The alcohol content in the various aquavits varies somewhat, starting at 37.5 per cent. Most brands contain about 40 per cent alcohol but Lysholm Linie Aquavit has an alcohol content of 41.5 per cent. (‘Lysholm’ is the name of the distillery in Trondheim where the aquavit is made, and from this point on the name 'Linie Aquavit' is used.)

The history of Aquavit

Originally, aquavit was used for medicinal purposes, but from the 1700s stills became commonplace in Scandinavian homes.

The definition of aquavit gets slightly complicated when you try to draw the line between it and other spirits popular in the northern climate. The term 'schnapps', for instance, is widely used in Germany, Switzerland and Scandinavia (the Danish say 'snaps') to mean any sort of neutral spirits, flavoured or otherwise. Then there's 'brannvin' a term used similarly in Sweden. (Like the Dutch word 'brandewijn' from which we derive the word 'brandy' it means 'burnt wine'.) The famous Swedish vodka Absolut began life in 1879 as a product called 'Absolut Renat Brannvin' which might be translated as 'absolutely pure schnapps', said to have been distilled ten times. However, when the Swedish government's alcohol monopoly launched Absolut's descendant as an international brand in 1979, it labelled it vodka.

Making Linie Aquavit

Caraway is the most important herb in aquavit, but the mixture of herbs varies from brand to brand. Linie Aquavit is derived from Norwegian potato alcohol blended with spices and herbal infusions, and caraway and aniseed predominate. After the alcohol and the herbs have been mixed the aquavit is poured into 500-litre oak barrels, the choice of which has not been left to chance. Norwegian specialists travel to Spain for the express purpose of selecting the best barrels, from those used in the production of Oloroso sherry for several years. Sherry casks are used because they remove the rawer, more volatile aspects of the liquor; the aquavit takes on a golden hue, and the residual sherry imparts a gentle sweetness.

Many theories have been put forward to explain how the man behind Linie Aquavit, Jørgen B. Lysholm, came up with the idea of sending aquavit around the world on sailboats in order to produce a special flavour. History tells us that, in the early 1800s, his family tried to export aquavit to the West Indies, but the ship 'Trondheim's Prøve' returned with its unsold cargo. That is when they discovered the beneficial effects that the long ocean voyage and the special storage had had on the aquavit: the length of the journey, the constant gentle rocking of the boat and the variation in temperature on deck, all helped give Linie Aquavit its characteristic taste. Jørgen B. Lysholm subsequently commercialized his maturation method and this is still how things are done today.

Linie Aquavit has one of Norway's long-established shipping companies as its steady travel partner. The first Wilhelmsen liner vessel carrying Lysholm Linie Aquavit set sail in 1927. Since that time, Wilhelmsen has been the sole carrier of this distinguished product. The barrels are tightly secured in specially designed cribs before being loaded onto containers, which remain on deck during the entire journey. The journey from Norway to Australia and back again takes four and a half months and crosses the equator (or the line, as sailors prefer to call it) twice. In fact, this is where Linie Aquavit gets its name. On the back of each label is the name of the ship and the date that it first crossed the equator.

International sales of Linie Aquavit

Arcus AS is Norway's sole manufacturer of hard liquor and it is this company which produces Linie Aquavit. The company also taps wine from wine producers all over the world and imports a select range of bottled wines. With a market share of about 30 per cent, Arcus AS is the leading player in the Norwegian wine and spirits market.

The international aquavit markets (primarily Sweden, Norway, Denmark, Germany and the United States) are dominated (except the last) by local Aquavit brands. At present Linie Aquavit is the market leader in Norway with a 20 per cent market share. In Denmark and Sweden the market share is 3–5 per cent. Germany is the most important export market, where Linie Aqavit holds 12 per cent of the aquavit market in competition with brands like Malteserkreutz and Bommerlunde.

Arcus is using export modes (foreign-based intermediaries) in all export markets. In 2000 the main distributors in Germany (Berentzen-Gruppe) and Denmark (Hans Just) became part-owners of Arcus AS, because they wanted to be sole distributors of Linie Aquavit in their countries. In the German market Berentzen offers a whole range of different types of alcoholic drinks. The company ranked number three in spirits in 2001, with a volume share of 7 per cent. Berentzen aims to expand its international spirits business during the next few years, in order to achieve long-term growth.

Sources: www.arcus.no/english/; Christian Brink, Head of Marketing, Sales and R&D at Arcus AS.

Questions

1. What are the main advantages and disadvantages for Arcus of using export modes, compared to other entry modes, for its Linie Aquavit?
2. What are the advantages for Arcus of having distributors as part-owners?
3. What should be Arcus' main criteria for selecting new distributors, or cooperation partners, for Linie Aquavit in new markets?
4. Would it be possible to pursue an international branding strategy for Linie Aquavit?

CASE STUDY 10.2

Parle Products: An Indian biscuit is seeking agents and cooperation partners in new export markets

A long time ago, when the British ruled India, a small factory was set up in the suburbs of Mumbai city to manufacture sweets and toffees. The year was 1929 and the market was dominated by famous international brands that were freely imported. Despite the odds and unequal competition the company, called Parle Products (**www.parleproducts.com**), survived and succeeded, by adhering to high quality and improvising from time to time.

Today, Parle enjoys a 40 per cent share of the total Indian biscuit market and a 15 per cent share of the total confectionary market in India. The Parle Biscuit brands, such as Parle-G, Monaco and Krackjack, and confectionery brands, such as Melody, Poppins, Mangobite and Kismi, enjoy a strong image and appeal among consumers.

If you thought that a typical family-run Indian company could not top the worldwide charts, think again. The homegrown biscuit brand, Parle G, has proved the belief wrong by becoming the largest selling biscuit brand in the world. However in most European markets Parle Products has to fight against a particular competitor, United Biscuits (producer of McVitie's). In all European markets the market share of Parle Products is very small.

United Biscuits (UB)

United Biscuits was founded in 1948 following the merger of two Scottish family businesses – McVitie & Price and McFarlane Lang. In 1960 UB added to its portfolio with the acquisition of Crawford's Biscuits and MacDonald's Biscuits.

In 2000 UB was bought by Finalrealm, a consortium of investors, and reverted to private limited company status.

Brand muscle

UB's brands rank number one or two in seven countries, they have five of the top ten biscuit brands in the United Kingdom, France and Spain, and four out of the top ten leading snack brands in the United Kingdom. More than 89 per cent of UK households bought McVitie's products in 2001. Anyone would agree that it has 'brand muscle'.

Consumer insight

UB's unique position as the largest UK snack food player, with a balanced portfolio of both sweet and savoury brands, gives it a unique understanding of how to respond effectively to changing consumer needs and wants.

Parle Products

Parle Products is the leader in the glucose and salty biscuit category but does not have a strong presence in the premium segment, with Hide-n-Seek being its only brand.

The extensive distribution network, built over the years, is a major strength for Parle Products. Its biscuits and sweets are available to consumers even in the most remote places and in the smallest of villages in India, some with a population of just 500.

Parle has nearly 1,500 wholesalers, catering to 425,000 retail outlets directly or indirectly. A 200-strong dedicated field force services these wholesalers and retailers. Additionally, there are 31 depots and customs and freight agents supplying goods to the wide distribution network.

The Parle marketing philosophy emphasizes catering to the masses. The company constantly endeavours to design products that provide nutrition and fun for everyone. Most Parle offerings are in the low and mid-range price segments. This is based on understanding the Indian consumer psyche. The value-for-money positioning helps generate large sales volumes for the products.

The other global biscuit brands include Oreo from Nabisco and McVitie's from UK-based United Biscuits. According to market reports Parle Products commands (with Parle G as the market leader) a 40 per cent market share in the R3,500 core biscuit market in India. In the confectionery segment the company enjoys a mere 15 per cent market share. The Parle G brand faces competition from Britannia's Tiger brand of biscuits, amongst others.

The company's flagship brand, Parle G, contributes more than 50 per cent to the company's total turnover. The other biscuits in the Parle Products' basket include Marie, Cheeslings, Jeffs, Sixer and Fun Centre.

Source: adapted from Jain and Zachariah, 2002; http://www.bsstrategist.com/archives/2002/mar/.

Questions

1 Which region of the world would you recommend Parle Products to penetrate as its first choice?
2 What kind of export mode would be most relevant for Parle Products?
3 How could Parle Products conduct a systematic screening of potential distributors or agents in foreign markets?
4 What would be the most important issues for Parle Products to discuss with a potential distributor/agent before final preparation of a contract?

VIDEO CASE STUDY 10.3

download from www.pearsoned.co.uk/hollensen

Honest Tea

Honest Tea is a tea company based in Maryland, USA. Honest Tea was founded in 1998 to sell 'bottled iced tea that tastes like tea'. They are best known for their line of bottled organic tea products, but they also produce tea bags and other bottled drinks. Honest Tea has a strong focus on social responsibility. Honest Tea has become a role model of philanthropic business practices. The CEO believes a social mission is not only socially responsible but also financially sustainable because it enhances customer loyalty. The hope is that Honest Tea will become a well-known national brand and will have impact around the world.

Questions

1 Please discuss how its policies regarding social responsibility helps Honest Tea in its exporting efforts?
2 What research method would you recommend for selecting the most suitable agent in Germany?

For further exercises and cases, see this book's website at www.pearsoned.co.uk/hollensen

Questions for discussion

1 Why is exporting frequently considered the simplest way of entering foreign markets and is thus favoured by SMEs?

2 What procedures should a firm follow in selecting a distributor?

3 Why is it difficult – financially and legally – to terminate a relationship with overseas intermediaries? What should be done to prevent or minimize such difficulties?

4 Identify the ways to reach foreign markets by making a domestic sale.

5 What is the difference between direct and indirect exporting?

6 Discuss the financial and pricing techniques for motivating foreign distributors.

7 Which marketing tasks should be handled by the exporter and which ones by its intermediaries in foreign markets?

8 How can the carrier and the rider both benefit from a piggyback arrangement?

9 When a firm begins direct exporting, what tasks must it perform?

10 Discuss the various ways of communicating with foreign distributors.

11 'When exporting to a market, you're only as good as your intermediary there.' Discuss.

12 The international marketer and the intermediary will have different expectations concerning the relationship. Why should these expectations be spelled out and clarified in the contract?

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