

WHEN YOU WISH UPON A STAR

Situation Background

Wholesale Internet Supply House (WISH), a medium-sized broker of new and used equipment serving Internet providers and cable operators, wants to expand overseas by entering a “Big Emerging Market” (BEM) that will be a star. It would like to grow its sales which have been stable, averaging a little over \$100 million per year. Most of its twenty employees are in sales and service, and a few work in the local office handling the books and payroll. After building operations in a new country, the CEO hopes to expand into additional countries. WISH has narrowed its initial globalization choices to four possible partners, each in a different corner of the globe: Brazil Broadband, Indonesia Internet, South African SynTek, and Turk-Tri-Web (see Exhibit 1).

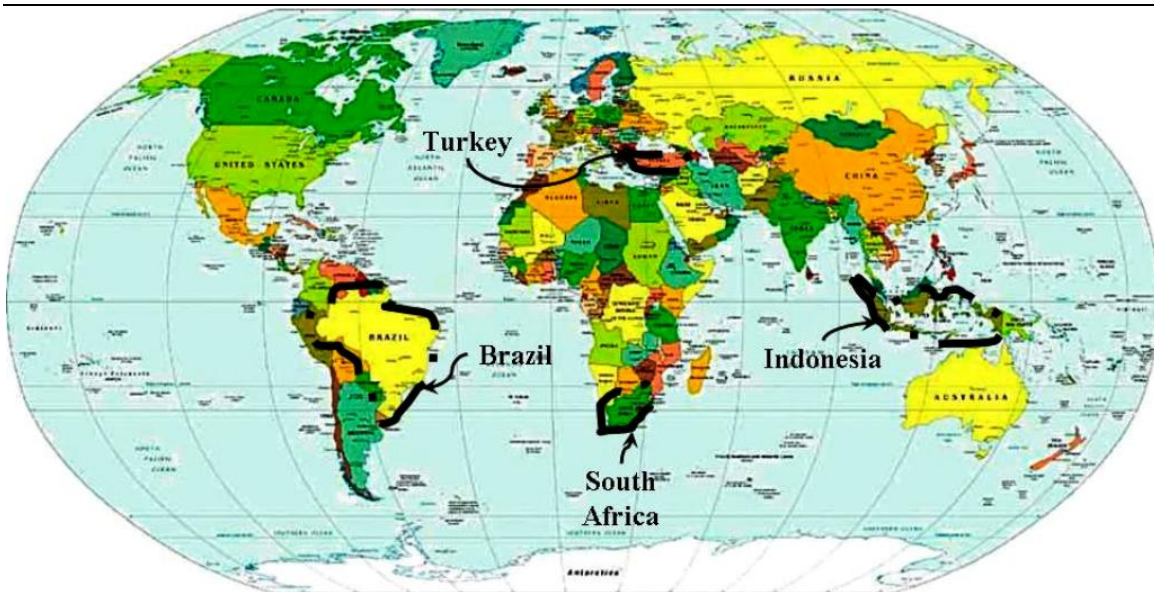


Exhibit 1: Four Alternative Markets

While the major global players include such well-known companies as Alcatel, Cisco, Ericsson, and Siemens, WISH is one of many small- and medium-sized companies supplying the hardware and components that “flatten” the world.¹ The Internet is comprised of one global network made up of tens of thousands of smaller interconnected computer networks and dozens of huge corporate networks that agree to communicate with each other and share information. In this way, every computer on the Internet connects to each other. (Exhibit 2 shows a schematic of how one service provider would assemble some of the necessary components.)

At the distribution center, a *headend* controls various centralized functions and provides access to a gateway that accepts, decrypts and re-encrypts, and routes traffic. Internet service providers (ISPs) have racks of *modems* for dial-up users that convert between analog signals and digital information. A *cable modem termination system* converts between digital and radio. Very fast cable and ADSL modems are common today. Similarly, while much of the original access to ISPs was over telephone lines, cable distribution centers increasingly connect to nodes within a neighborhood through

¹ Friedman, *The World Is Flat* (Farrar, Straus and Giroux: Release 2.0 rev. 2006)

fiber optic (glass strands) cable that transmit data very fast with little interference. Older telephone coaxial cable (copper wiring surrounded by insulation) already exists throughout many areas which continue to carry signals from the nodes to homes or businesses, although telephone and cable companies are now replacing these with fiber optic cable. Some companies also maintain their own fiber optic lines or lease space from others for their internal communications, or intranet. *Routers* are specialized computers that determine where to send information along thousands of pathways so that the right information goes to the right computer. These technologies are converging to deliver telephony and cable television along with Internet services. (Exhibit 3 shows samples from WISH's product catalog.)

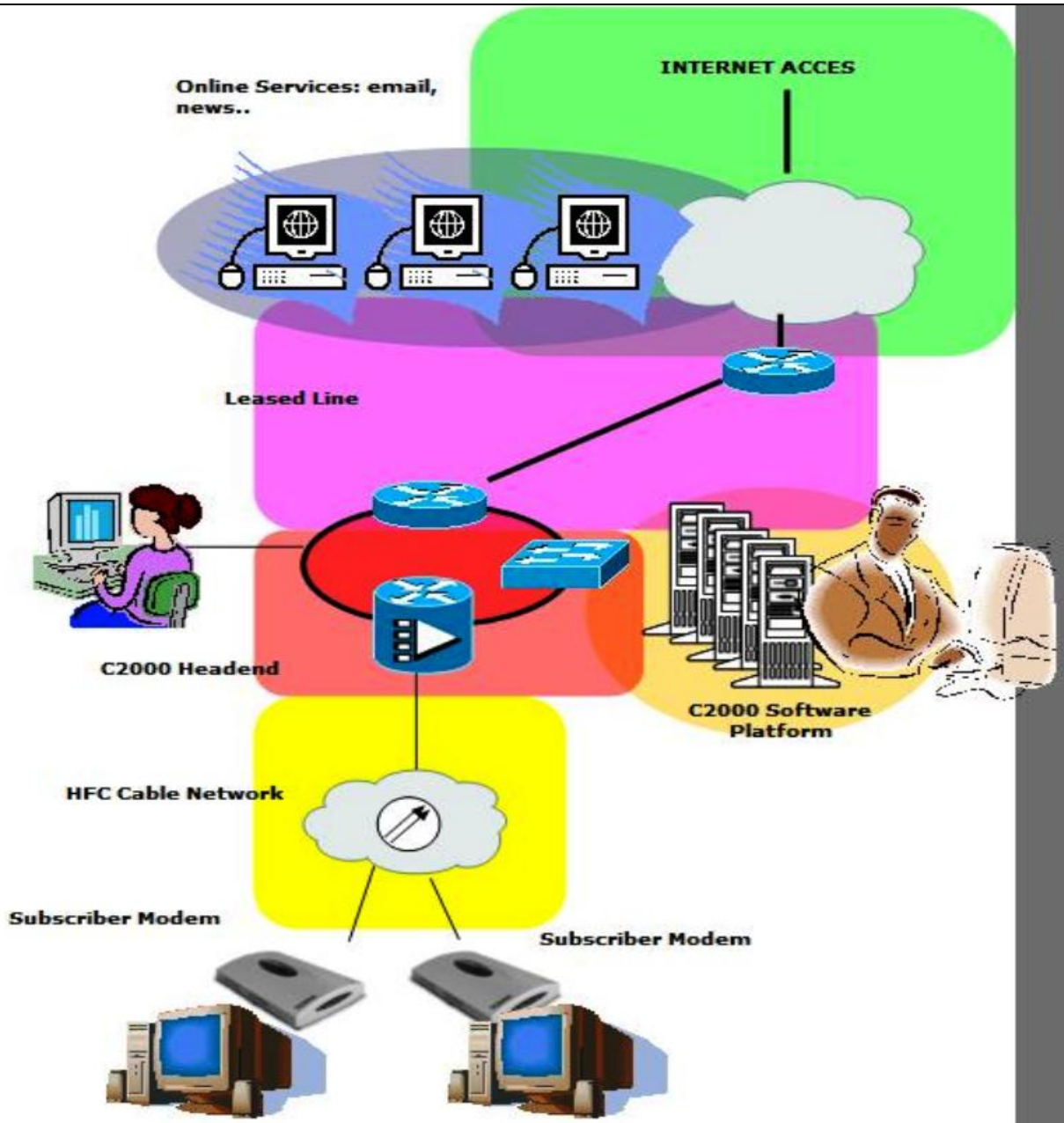


Exhibit 2: Schematic of Internet Service Provider Components

Source: http://www.tonna.net/cable100/index_e.htm



Headend



Router



Cable Modem Termination System



Ethernet DSL



Cable Modem



Analog RF/IF/RF Converter



Power Supply



RF LED Node



Fiber-Optic Cable

Exhibit 3: Product Catalog Samples

Many of these products are manufactured in China and Mexico, often under contract to an original equipment manufacturer (OEM) that brands and distributes them. These products can be sold directly to developing countries at half the price of the OEM, especially when dumping obsolete technology. In addition, many developing countries impose huge import tariffs on products from developed countries. Even worse, it is common for customs officials to prefer certain shippers because of the bribes they are given. On the other hand, some countries offer attractive incentives such as providing free land and tax exemptions to partner with domestic companies or set up shop in their development zones. The Export-Import Bank's credit terms for products that are of U.S. origin can make or break a deal if the selling price is near the competition.

There is no obvious "best alternative" as each of the four countries and partners WISH is considering looks attractive on some dimension but not on all (Exhibit 4 compares country data). The actual results will depend on an unknown future. Following brief country descriptions are possible critical events that might impact each one.² The next section presents brief company data, followed by strategic issues WISH is considering.

Brazil: France's late president Charles de Gaulle reportedly once said, "Brazil has a great future, and it always will have." Brazil is by far South America's largest economy and most populous country with vast natural resources. In fact, with the largest sugar

² The primary sources are <https://www.cia.gov/cia/publications/factbook/> and <http://news.bbc.co.uk/>.

cane crop in the world it is producing ethanol fuel from sugar cane to become the world's largest ethanol exporter. Still, its troubled past includes a long history of foreign debt defaults, Brazil overcame more than half a century of military rule in 1985 when the regime peacefully ceded power to civilian rulers. The government's largely domestic debt increased steadily from 1994. In August 2002, the IMF announced a new \$30 billion loan, its largest ever, to Brazil. Foreign investment has plunged and highly unequal income distribution remains a pressing problem, but Brazil's continued growth yields increases in employment and real wages as it expands its presence in world markets resulting in record trade surpluses. President Luiz Inácio Lula da Silva recently won a second four-year term in a landslide victory. The left-winger came to power four years ago by promising to reform the country's political and economic system. He vowed to eradicate hunger and create a self-confident, caring, outward-looking nation and has pumped billions of dollars into social programs, increased the minimum wage well above inflation, and broadened state help to the most impoverished. Although Brazil has seen steady annual growth, some business leaders argue it is losing the competitive edge against international rivals. Nonetheless, his government has quelled the initial fears of the financial markets by keeping the economy stable and achieving the budget surplus the IMF requires.

<i>Characteristic</i>	Country			
	Brazil	Indonesia	S. Africa	Turkey
<i>Population (mill.)</i>	186.4	220.6	45.2	70.4
<i>Population annual growth</i>	1.35%	1.36%	-0.70%	1.26%
<i>GDP annual growth</i>	2.30%	5.60%	4.90%	7.38%
<i>Overall market potential (rank)</i>	23	21	24	11
<i>Days required to start a business</i>	152	151	38	9
<i>Ease of doing business (rank)</i>	121	135	29	91
<i>Investor protection (rank)</i>	60	60	9	151
<i>Ease of enforcing contracts (rank)</i>	120	145	43	40
<i>Global competitiveness (rank)</i>	66	50	45	59
<i>Corruption perceptions index (rank)</i>	62	137	46	65
<i>Exports of goods and services (% GDP)</i>	22.66%	37.69%	26.57%	27.42%
<i>Imports of goods and services (% GDP)</i>	14.96%	32.56%	22.39%	33.98%
<i>Exchange rate vs. U.S.\$* ($\Delta$ past year)</i>	-5.2%	0.8%	17.0%	3.3%
<i>Telephone mainlines/1,000</i>	230	46	105	267
<i>Internet hosts (000)</i>	6,508	170.8	645.2	1,313
<i>Internet users (mill.)</i>	25.9	16	5.1	16

Exhibit 4: Country Statistics

* Larger changes suggest weakening since they require more currency that makes imports more expensive.

Sources: <http://devdata.worldbank.org/data-query/>; <http://globaledge.msu.edu/>; <http://www.oanda.com/>; <http://www.doingbusiness.org/EconomyRankings/>; http://www.transparency.org/publications/annual_report/; http://www.weforum.org/pdf/Global_Competitiveness_Reports/Reports/gcr_2006/gcr2006_rankings.pdf; <https://www.cia.gov/cia/publications/factbook/>

Indonesia: A vast polyglot nation, the world's largest archipelagic state, and the most populous Muslim country, Indonesia faces acts of terrorism, unequal resource distribution among regions, endemic corruption, the lack of reliable legal recourse in

contract disputes, weaknesses in the banking system, and a generally poor climate for foreign investment. It is trying to consolidate democracy after four decades of authoritarianism, implement financial sector reforms, stem corruption, and hold the military and police accountable for human rights violations. Indonesia had four presidents from 1998 to 2002 since the country's highest office was decided not by a popular vote but by horse-trading among Jakarta's notoriously corrupt and high-handed elite. Business groups in Indonesia have flourished by having access to state power, and resentment at the privileges they enjoyed triggered a wave of looting in 1998 as well as a resurgence of economic nationalism. Although many of the monopolies and favorable trading arrangements on which their success was founded have ended, most of these wealthy individuals are still well positioned and have adapted to the new political environment. Indonesia withdrew from its IMF program at the end of 2003, but issued a "White Paper" that commits the government to maintaining fundamentally sound macroeconomic policies previously established under IMF guidelines. Investors, however, continued to face a host of microeconomic problems and an inadequate judicial system. Declining oil production and lack of new exploration investment turned oil-rich Indonesia into a net oil importer in 2004. Natural disasters have only compounded the fiscal problem, including the 2004 tsunami and several earthquakes. President Susilo Bambang Yudhoyono won Indonesia's first-ever direct presidential elections in 2004 in what was hailed as the first peaceful transition of power in Indonesia's history. A fluent English speaker who studied for his master's degree in the U.S., he promised to fight corruption within the country's massive bureaucracy, rejuvenate the economy, and tackle separatist conflicts. Economic reformers introduced three policy packages in 2006 to improve the investment climate, infrastructure, and financial sector, but translating them into reality has not been easy.

South Africa: The discovery of diamonds (1867) and gold (1886) spurred wealth and immigration but intensified the subjugation of the native inhabitants. The Union of South Africa operated under a policy of apartheid – the separate development of the races – until the 1990s ushered in black majority rule. It is now a middle-income market with an abundant supply of natural resources; has well-developed financial, legal, communications, energy, and transport sectors; a stock exchange that ranks among the ten largest in the world; a modern infrastructure supporting an efficient distribution of goods to major urban centers throughout the region; and the lowest external debt of all the BEM countries. South Africa is the continent's major media player, and its many broadcasters and publications reflect the diversity of the population. Its economic policy has been focused on targeting inflation and liberalizing trade as a means to increase job growth and household income. But daunting economic problems remain from the apartheid era, especially poverty and lack of economic empowerment among the disadvantaged groups. For instance, with the largest unemployment rate of all the BEMs half its population remains in poverty. In fact, the United Nations has unabashedly identified South Africa as "one of the most unequal societies on the planet" where "the average income in 2001 of a white household was six times more than that of an African household," and the unemployment rate among black people was over two-and-a-half times greater than others. South African economic policy is fiscally conservative but pragmatic, targeting inflation and liberalizing trade as a means to increase job growth and household income. Thabo Mbeki, who had been involved in the struggle against apartheid from an early age, became president when Nelson Mandela stepped down in

mid-1999. He was elected by parliament in 2004 following the landslide general election victory of his governing African National Congress (ANC). His main challenge has been to improve the lot of ordinary South Africans by delivering such basic services as water, electricity, and sewers.

Turkey: Straddling the crossroads of Europe, the Middle East, and former Soviet republics bordering the Caspian Sea (and considered a gateway to North Africa as well), this secular Moslem country boasts a dynamic economy that blends East and West. Unfortunately, its twin budget and trade deficits fuel the highest inflation of the BEMs. The budget deficit is largely due to the huge burden of interest payments. It has a strong and rapidly growing private sector, yet the state still plays a major role in basic industry, banking, transportation, and communication. The automotive and electronics industries are rising in export importance. In recent years, the economic situation has been marked by erratic economic growth and serious imbalances. Perhaps because of these problems, foreign direct investment in Turkey remains low. President Ahmet Necdet Sezer won a seven-year term in 2000, the first president in modern Turkish history who was neither an active politician nor a military commander. Previously the chief justice of the constitutional court, he is regarded as a strong supporter of freedom of expression and a staunch secularist. He led an unlikely but durable three-party coalition that drew up a disinflation program with the IMF, led an effort to have Turkey accepted as a candidate for membership of the European Union, and zealously set about all manner of reforms. Nonetheless, a growing trade deficit and serious weaknesses in the banking sector plunged the economy into crisis – forcing Turkey to float the lira and pushing the country into recession. Foreign direct investment (FDI) in Turkey had averaged less than \$1 billion annually, but further economic and judicial reforms and prospective EU membership are expected to boost FDI. For instance, privatization sales are currently approaching \$21 billion and oil began to flow through its pipeline in May 2006, marking a major milestone that will bring up to one billion barrels per day from the Caspian to market.

Economic	Environmental	Geopolitical	Societal	Technological
<ul style="list-style-type: none"> • U.S. current account • Economic growth and balance of trade • Asset prices/ debt • Globalization expansion/ retrenchment 	<ul style="list-style-type: none"> • Climate change • Population • Erosion of natural resources • Natural catastrophe 	<ul style="list-style-type: none"> • Political (in)stability (e.g., Middle East) • Transnational crime and corruption • Business telecom regulations 	<ul style="list-style-type: none"> • Pandemics • Developing world infectious diseases • Developed world chronic diseases 	<ul style="list-style-type: none"> • Critical information infrastructure • R&D • Nanotechnology development

Exhibit 5: Categories of Critical Events

Source: Based on http://www.weforum.org/pdf/CSI/Global_Risks_2007.pdf

The World Economic Forum evaluates five categories of “core” global risks. Exhibit 5 highlights the primary ones of interest to WISH as possible critical events. As in any system, these potential events are interconnected and Exhibit 6 shows the interdependence of all core global risks. Its strategy must respond to the unknown combination of these critical events that determines the firm’s unique environmental

operating condition. Interestingly, the World Economic Forum lists the following common reactions which prevent a proactive approach to risk mitigation when formulating a strategic response: “Someone else will manage my risk.” “The risk is not relevant to my organization.” “Won’t taking action just slow me down?” “No one is telling me that I must act.” “What reward do I get from mitigating risk?” “It is too costly to mitigate.” “Why worry about it? It could never happen to me.” “It is too large to manage, and success is not guaranteed.”

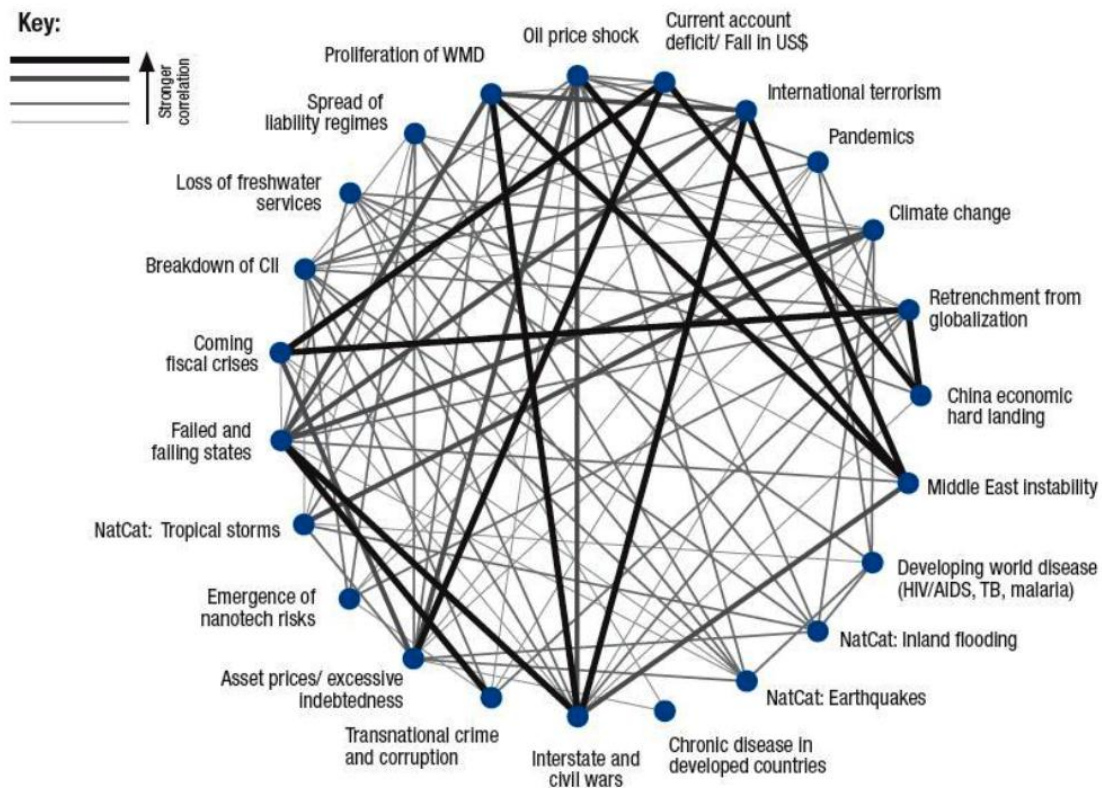


Exhibit 6: A System of Global Risks

Source: http://www.weforum.org/pdf/CSI/Global_Risks_2007.pdf

WISH intends to conduct scenario planning to overcome such inertia and stimulate new thinking. It realizes it must anticipate these risks when partnering to enter a new market as each critical event might result in a beneficial change, maintenance of the status quo, or a detrimental change. Conducting scenario planning is one method to help mitigate against such risks by evaluating unique combinations of these outcomes that form the firm’s operating environment to which the firm’s strategy must respond. Again, the World Economic Forum offers the following advantages of conducting scenario planning:

- *Improving insight:* Moving risks from the unknown to the known through research. The best mitigation strategies often derive from the changed mindset which can result from enhanced knowledge and information.

- *Enhancing information flow*: Allowing information to flow effectively between decision-makers and those experiencing the risk first-hand, to provide early warning, inform the public and exchange best practice.
- *Refocusing incentives*: Creating the incentive frameworks that will allow decisions to be made to reduce risks previously considered exogenous.
- *Improving investment*: Providing the investments necessary to mitigate risk.
- *Implementing through institutions*: Improving (or creating) the framework needed to mitigate risks for which an institutional response is required.

Selecting a Star

Besides picking a country to enter, WISH's strategy also must decide the mode of entry and type of relationship – without knowing how critical events will unfold. As a starting point, WISH has selected one company to examine in each country it is considering entering. As part of the upcoming strategic planning retreat, it will consider all possible aspects of picking the right partner. The required investment is similar for all options.

Brazil Broadband: Brazil has the most Internet users in Latin American and the 3rd highest penetration. There is growing migration from dial-up to broadband; while virtually all cable TV companies offer cable modem services, ADSL is the access technology of choice. With the widespread development of VoIP, more and more ISPs are looking to incorporate Internet telephony and pay TV services with their broadband offerings.³ While there are thousands of ISPs, Brazil Broadband (BB) is among the most aggressive players. BB is seeking a U.S. partner that would supply state-of-the-art equipment. WISH management had been considering opening a distribution center in São Paulo, the country's commercial center, to give it access to the many potential customers but has been stymied by protectionist policies. Moreover, the economic prospects are not very attractive – partnering with BB might open up the country to other sales, but WISH does not know why a partner would help it supply its domestic competitors. Moreover, most of the ISPs are not as sophisticated as BB so its potential would be limited.

Indonesia Internet: The number of Internet users in Indonesia continues to remain small in spite of its low cost due to weak infrastructure, low user confidence, and unclear public policy. Part of the problem is that the telecommunication companies – monopolized by the government through PT Telkom and PT Indosat – have not maintained their infrastructure, forcing the government to now open this area.⁴ Recent telecom deregulation has encouraged infrastructure development and further extended Internet access. As a result, several domestic portals and ISPs have recently emerged as success stories. Moreover, Southeast Asia is emerging as an attractive country for outsourcing electronics manufacturing and even some applied R&D for IT. However, progress in this sector could cease if the government chooses to again over-regulate the Internet and adopt counterproductive policies. Indonesia Internet (IndoNet) sees numerous opportunities in such a huge country with such a large population and

³ Source: <http://www.internetworldstats.com/sa/br.htm>.

⁴ Sources: <http://www.insan.co.id/indonesia-internet-statistics.pdf> and <http://www.usembassyjakarta.org/econ/Internet2001.html>.

economic growth. Founded in tourist-friendly Bali with extensive connections in Jakarta, IndoNet has approached WISH as a possible supplier of used equipment because of the low cost. Complicating matters, however, much of the lines would be underwater, a specialized business that WISH would like to enter. This contract would last for a decade and provide learning opportunities that WISH can use elsewhere.

South African SynTek: The number of Internet lines in South Africa grew quickly but user growth has come to a screeching halt. One explanation is the monopoly enjoyed by one national operator that focused on serving existing customers rather than chasing growth in users resulted in high profits despite the slowdown in user growth. The leased line market for corporate access should grow as small- and medium-sized enterprises pursue high-speed Internet connectivity. South Africa is also expected to see the biggest explosion yet of technology options available to Internet users. Finally, schools connectivity will receive a boost as a range of long-awaited projects are finally implemented.⁵ The government is licensing South African SynTek (SAST) to be the second national operator to provide high-speed broadband wireless access. This move should significantly contribute to increased access in the country. SAST, located in Johannesburg, is looking for a U.S. broker to provide the equipment needed for such a major project that would be a hybrid combining the backbone infrastructure with ISP electronics. While South Africa seems attractive, business would be contingent on growth of Internet use. The African continent has long been neglected by multinationals and so might be ripe for WISH. However, growth would not occur for years to come.

Turk-Tri-Web: Turkey boasts the 13th largest telecom market in the world and the 5th largest in Europe. The 2004 termination of fixed-line operator Turk Telekom's monopoly of Internet, voice, and data communication has resulted in mass introduction of affordable and reliable ADSL services. This sector is now one of Turkey's fastest growing as Internet users exploded. The broadband market is experiencing phenomenal growth as costs drop as a result of greater privatization (the government sold a majority stake), upcoming negotiations with the European Union for further market reform, new price control regulations, new players entering, and customers showing increased acceptance of VoIP and other new technologies.⁶ To increase Internet penetration further, Turkish Telecom will invest over 800 million US\$ in the next five years for broadband services throughout the country. Newly-established Turk-Tri-Web (TTW) is emerging as a true leader in Web technologies by providing a complete fiber optic infrastructure along with high quality Internet access services, virtual hosting, and VoIP for thousands of major and international corporate clients. Based in Istanbul, it hopes to exploit its geographical location. For WISH, partnering with a Turkish company might open a new source of fairly sophisticated equipment that can be sold in other developing countries. Moreover, many qualified European expatriates would be locally available to manage an international operation.

⁵ Source: <http://www.internetworldstats.com/af/za.htm>.

⁶ Source: <http://www.internetworldstats.com/eu/tr.htm>.

Lingering Questions and Nagging Doubts

Your team is a sub-group of WISH's twenty employees. As you prepare for the annual strategic planning retreat, keep in mind that everyone is expected to be involved in this critical decision. At the forefront of the questions you expect management to ask is which country and company will be a future star. Everyone wants to access growing markets and inexpensive supplies but cannot agree on which one; every alternative provides both opportunities and risks to consider in selecting a partner as well as the precise relationship it must forge. Maybe it is premature to be looking for a partner in a BEM – should WISH consider exporting to more developed markets that are readily accessible such as Canada or Mexico? Or perhaps WISH should search for sales representatives with technical qualifications to call upon potential clients – or in other countries that are not listed among the four BEMS?

There are other strategic considerations to ponder. For instance, WISH has been a broker between buyers and sellers but some of these relationships provide opportunities to emphasize purchasing or distribution – but not both. On the other hand, WISH has wanted for a long time to fill its extensive domestic distribution network with its own brand of equipment by contracting manufacturing to an overseas partner, but it has no design and engineering expertise. Moreover, to what extent should WISH specialize in one product, market, or activity – or should it diversify into all types of Internet products and supplies? Complicating matters is selecting the mode of entry that could range from a one-time contract to a longer-term commitment leaving open options for a joint venture or alliance. Relatedly, who should head up the overseas initiative both at home and abroad – should WISH rely on overseas agents or hire its own expatriates? Most importantly, WISH's limited resources provide no room for error. Of course, some of the risks could be mitigated by correctly structuring the relationship and payment terms.

Everyone realizes that uncontrollable events will determine the venture's – perhaps even the company's – ultimate success or failure. Then again, rewards should be commensurate with the risks. Yet the biggest fear is one of inaction, knowing that in this fragmented business numerous competitors are more than ready, willing, and able to exploit the slightest opportunity and rush in while others dream. You have the weekend to gather additional considerations in deciding which country to enter before your meeting, admittedly not much time. Given the many uncertainties WISH faces and its limited resources, the strategy must be viable regardless of what the future actually holds.