

International Marketing
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Lecture – 25
International Business Case Analysis

Hello, good morning welcome back. Today, we will discuss international business case analysis. So, I have prepared two cases and these are actually real-life cases, but I have made some changes in the name of the company and all those details are not shared. But the problem is most important for you to understand the problem and what are the ways to resolve the problem, so that is the way how we will proceed. There is no unique solution.

So, there is nothing like $(a + b)^2 = a^2 + 2 ab + b^2$ is not that type of a simple solution in business. There can be various solutions, one manager might look at one solution which will be more fit for the company. Another manager will think some other strategy should be correct fit for the company. So, it varies from manager to manager. It varies from various financial analysis. So, there is no unique solution.

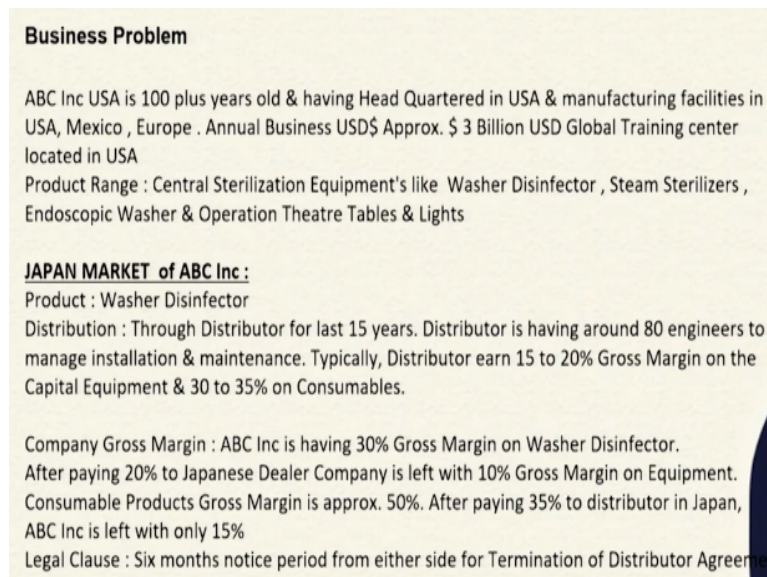
So, there is no such simple formula that you put that formula or put some theory to resolve in a business case, any business case typically can have multiple solutions. So, here I will present two business cases, international business cases and this may not; I have providing one shot of a solution, I am giving one shot of a direction. Some other manager may not accept the strategy what I am proposing, may propose something different which may be correct from his point of view.

So, that is the thing. So, it is not always $1 + 1 = 2$, so no such formula is there in strategy. It all depends on the company and the executive and the board of directors and the shareholders. There are so many stakeholders in the company who has to accept that. So, as an international marketing manager, you try ways and you have to constantly try to look at various options and analyse various option that is the one.

And then it is up to the board of directors to select which is the correct strategy for the company for that period of time. So his time is very important, entry time is very important.

There are so many other dimensions there. So, let us go first simply address the problem. Okay.

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Business Problem

ABC Inc USA is 100 plus years old & having Head Quartered in USA & manufacturing facilities in USA, Mexico , Europe . Annual Business USD\$ Approx. \$ 3 Billion USD Global Training center located in USA

Product Range : Central Sterilization Equipment's like Washer Disinfector , Steam Sterilizers , Endoscopic Washer & Operation Theatre Tables & Lights

JAPAN MARKET of ABC Inc :

Product : Washer Disinfector

Distribution : Through Distributor for last 15 years. Distributor is having around 80 engineers to manage installation & maintenance. Typically, Distributor earn 15 to 20% Gross Margin on the Capital Equipment & 30 to 35% on Consumables.

Company Gross Margin : ABC Inc is having 30% Gross Margin on Washer Disinfector.
After paying 20% to Japanese Dealer Company is left with 10% Gross Margin on Equipment.
Consumable Products Gross Margin is approx. 50%. After paying 35% to distributor in Japan, ABC Inc is left with only 15%

Legal Clause : Six months notice period from either side for Termination of Distributor Agreement

So here, I am now sharing a business problem. So the company is ABC Inc US which is 100 plus year old company and having head quartered in USA and manufacturing facilities in USA, Mexico, Europe. Annual business turnover is around 3 billion US dollars and they have their global Training Centre in United States so that is about the company. So, the product range is central sterilization equipment like washer disinfector, steam sterilizers, endoscopic washer, operation theatre tables and lights, these are the products.

So as I need to explain you about this product, so I will give you a very simple explanation, you need not be an expert to understand these products. I will give you a heads up on that so that very simply you understand what is a product and what for it is used that is all, there is no need for you to really go in depth to understand at this point of time. For you it is very important to understand which strategy should be correct fit.

And what are the challenges you will face and which strategy you have to adopt, so that is more important for you as a marketing manager, not really the product at this point of time, though product is definitely very crucial. But at this point, we are more discussing on an entry strategy in a market. Now, the company is having an operation in Japan and the Japan market the product, they sell the washer disinfector.

So, currently they are distributing through a distributor who is there for last 15 years and distributor is having around 80 engineers to manage the installation and maintenance and typically the distributor earns around 15 to 20% gross margin on the capital equipment and 30% to 35% on the consumables. So this machine, when I will explain you about this machine this is a capital equipment.

So, this requires some consumables just like in washing machine it requires a detergent, here also the washer disinfectant needs the consumables to clean and disinfect. The segment of the customers are basically the hospitals, they are the main user for this product. Now, about the company the ABC Incorporation is having around 30% gross margin on the washer disinfectant. So, this is at gross level, the margin is 30%.

After if they pay the 20% to the Japanese dealer, they are left only with 10% gross margin. So, imagine the company is a manufacturer. They made huge investment in R and D to design a product and then get RIAs, regulatory approvals and then came up with a new technology and then the company at the end of the day from Japan market is only earning 10% and Japan as you know is a very important healthcare market for the company.

And for all companies Japan is a very, I will come to that Japan market a little bit more on the healthcare segment how big is the market and all those. So, the situation at the end of the day, it is only 10% the company is earnings the parent company and distributor is earning 20%. And the consumable products which are the essentials for that and which is locked with the equipment that means you have to use only the consumables of ABC Incorporation USA there.

You cannot use any other detergents there for your cleaning and disinfection. So, you cannot use, it is locked with that. So, that means the consumables also, the customer has to buy the consumable also from you and also the equipment from you. It is just like a washing machine with the detergent also you have to buy from the washing machine company. Suppose you buy Bosch washing machine, you have to use only Bosch detergent.

You cannot use say Surf Excel or Ariel or any other that type of situation in this healthcare segment. So, that means if you are using ABC Incorporation's washer disinfectant you have to use only their consumables for cleaning and disinfection. In consumables the margins are

very high. As you know, everyday there will be huge use and then every month there will be huge use and it is locked with the equipment, so the company starts earning.

So, more than equipment the; model here is earning from the consumables. So, here the company's actual gross margin of the company ABC Incorporation is 50%, but they have to pay 35% of the Japan distributor. So, they are left only with 15%. So in equipment they are left only with 10% and in the consumable products they are left only 15%.

There is a legal clause with the distributor that anyone if the termination either the ABC Incorporation can terminate or the distributor also can terminate from his end, but the termination notice period is 6 months. So that is a legal agreement as per the laws and this has been accepted signed by ABC Incorporation and their dealer which is there for last 15 years and maybe some modification of that paper agreement must have happened.

But the most important part is that you need to give a clear 6 months' notice to the distributor to terminate the distributor or on the vice versa distributor has to also give ABC Incorporation 6 months' notice if they want to terminate the agreement with ABC Incorporation, so that is the clause.

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PROBLEM
ABC Inc is not happy with very low Gross Margin both from Equipment Sales & Consumable sales

Current revenue is around \$50 Million USD per year.

ABC Inc is having two Managers stationed in Japan to oversee the Business After adjusting all the expenses like Salary/ Travel /Office rent , ABC Inc is gross margin takes a further hit.

CEO of ABC Inc is interested to have direct operation at Japan Market to improve Gross margin .
In order to Initiate the actions , ABC Inc must ensure smooth transition from Distributor to Direct Model without loss of Business & creating any dissatisfaction with large existing customer base

The problem: The problem statement here is that ABC Incorporation is not happy with the very low gross margin both from equipment sales and consumables, very low gross margin, 10% only on the equipment. So if 100 dollars they sell, they only earn 10 dollars and in the

consumables they are only earning 10 to 15% that is all. So current revenue of Japan market for your analysis is around 50 million dollars.

So that is the size of the revenue coming for ABC Incorporation by selling the equipment as well as the consumables. So ABC Incorporation is selling in Japan both the equipment and consumables of washer disinfectant and the revenue sizes for your calculation it is around 50 million US dollar. ABC Incorporation is having two managers stationed in Japan or to oversee the business.

And after adjusting all the expenses like salary, travel, there is a small subsidiary office there or representative office you can consider maybe a representative office to be very clear because it cannot function as a full fledged legal entity, it is a representative office that means the office will have an entity where it cannot run any business just a representative office and there are 2 or 3 people there, one secretary there and that expense is also there.

And ABC Incorporation has to spend the salary of the people and these people basic job is to manage the distributor, meet the customers and do some promotional activity, conduct various seminars and all those things at the customer places all those things and also resolve any issue, any conflict between the distributor and customer, so, that is their job. So, they are not essentially doing any sales, but they are facilitate a letter of the sales and so they will help the distributor to sell their equipment.

Now, there is a huge cost for them because their salary, their travel, there is a small office and the rent and all those things. So further there, it all goes from the gross margin what the company earns 10%, it goes also from there. So, actual gross margin may fall down to around 6% or 7% or maybe 5% depending on the investment or promotional activity. So look, the problem here is 50 million dollars, actually 5 to 6% is the earnings coming to the ABC Incorporation being a manufacturer, so that is big problem.

So, CEO of ABC Incorporation is very unhappy. He says that I want to have a direct operation in Japanese market to improve my gross margin. Why I should walk away work only on 5 to 6% or maybe 7% where my distributor is working on 20% why that should happen? I should have my own operation, I should improve my overall gross margin and he

is very much interested for the most lucrative business of the consumables where the margin is very high.

So, here he says that I will earn 50% of the gross margin for those detergents, so why I should lose and why I should earn only 10 to 15% for that, why distributor will earn so much of money and when we have so much of expenses in developing that product, to get the various efficacy test and all those why we should earn that. So, the he has told his management that he wants to go ahead in the direct operation.

So, the problem here is removal of a distributor who is in the; market for more than 15 years, sizable business 50 million dollars approximately the business in a year and have large installations already in the Japan. So, in order to initiate the action, ABC Incorporation must ensure a smooth transition from the distributor. So, CEO said nothing doing you just go ahead and you implement and we will have a direct operation there and remove the distributor.

So, smooth operation from distributor to direct model without loss of business and creating any dissatisfaction with large existing customer base which is very important. When you remove a distributor and then you have large customers, the customers who are using large number of large hospitals and they must be using around 10-20 of these equipments there should not be any hard feeling or there should not be any short of an annoyance created for the customer.

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So, what are the challenges? Now for the manager, what are the challenges? Before that I will take you through the product first. So, let me first explain you so that you understand what exactly the product is. So, this is typically the product. So, there is the product this is washer disinfectant. This is a capital equipment This is used in the hospital. So, what is the purpose of this equipment? You know when the surgery takes place, so there will be the knives and scissors and all the surgical instruments.

After the surgery it will be with lot of blood, tissues and everything and that needs to be cleaned first because they will not throw away those surgical instruments. They are not disposable. They are very costly surgical instruments. So, they want to use for the next patient. So now suppose a surgeon is doing a surgery, a general surgery or a cardiac surgery or neurosurgery any surgery this surgeon is conducting.

After the surgery is over those huge amounts of surgical instruments will now come with blood stains, tissues, and everything will be there and that needs to be first cleaned and disinfected and then it has to be sterilized. So, there is a big difference between disinfection and sterilization. At this point, let us not go into those details. At this point for you as a manager, for you is most important to understand the basics of the product.

So, it just like in washer at your home. You put all the equipment which are coming from the operation theatre these are manually cleaned at a scrub station. So, this is just like a basic where it is manually cleaned. And after cleaning these equipment's are put in the trays there. You can see the trays there. And these are the typically the trays, here you can see the tray and you put or you load all the equipment here.

Once you put the equipment you close the door and then the equipment will draw this liquid and it will start washing and there will be various cycles, 3-4, 4 cycles as far as I remember, 4 cycles to clean and then disinfection that is a high level disinfection. And then there will be other side one door. In a typical home washing machine, there is only one door. So, you open one side and put all the dirty clothes and after washing your clothes, take out the clean clothes from the same door.

But in this case, there are two doors, why two doors? Because in one door if you open this side is a dirty side of the hospital where all infected products like means all the surgical

instruments which are not cleaned and disinfected are in one side of the equipment. And then the other side there is a door after the cleaning is over, you take out the clean and disinfected products on the other side of the washer disinfectant.

So, if I want to show you this, so this is the washer disinfectant, so you start loading from this side. There is a wall here and the equipment is kept in between a physical barrier there. So, this side is known as a dirty side and this side is known as a clean side. So, from dirty side you put the equipment in the dirty side and then you close this door and then you start the cycle. After the cycle is over, unfortunately I have only one door here, but you hypothetically just assume there is another door other side and there is a physical barrier wall this side.

Once this is over, the machine will tell that it is over and then you open this side in the clean side, take out all the surgical instruments and then you put it in a steam sterilizer or we call it autoclave where you just sterilize the product. So, the objective of this product is to clean and disinfect. And you can see for in this photograph, there are various sizes. Some hospitals need large, some hospitals need small, so there are various sizes.

And this is very essential. Why this is very essential in the hospital? Suppose in an hospital, there are 20 different operation theatres. So 20 surgeries are going on in the morning, 20 surgeries in the afternoon, 40 surgeries. So imagine 40 surgeries, there will be huge surgical instruments will come for washing and disinfection. So, these 40 has to be cleaned and disinfected. So, you need this machine to be on to be available 24 into 7, 365 days.

If this one machine is down, please understand if the one machine is down that means you will not be able to clean and disinfect the surgical instruments. What will happen that? If you cannot do that, these surgical instruments if it is not cleaned due to failure of the machine or some problem in the machine, then you will not be able to sterilize. If you are not able to sterilize that product will not go in the operation theatre.

So, the patient who is in the queue for the next surgery will not have the surgery because the surgeon will not get the equipment if the machine is down. So, this is very crucial equipment in the hospital. So, from the manufacturer or the distributor side it has to be maintained 24 into 7, so that typically there is no breakdown of this machine. If there is a breakdown in the late afternoon, late evening, some technician has to rush to the hospital to rectify the units.

To put the steams or spares if required or cleaning the required whatever is problem they have to resolve. So, these products are kept inside the hospital, any hospital in the world whether it is in India, whether it is in US, whether it is in Japan, these are all in the CSS department, which is central sterile services department. In that department, this is a very crucial equipment.

And the ABC Incorporation makes this product for United States and is one of the 100 years old company and enjoys a largest market share of this product or maybe a huge market share in United States and throughout the world including the Japan.

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So, this product it looks like that, I am showing you another close up view. So, this looks like this. Here you can load the; on one side you load the dirty products, dirty equipment, surgical equipment, on the other side you take out the surgical products from there which is clean and disinfected.

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Detergents Revenue : Consumables



And this is the detergent or the consumables which you need to buy from the hospital which is locked with instruments that is you can use the equipment only with the manufacturer's detergent, you cannot buy detergent from the market and use it.

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Challenges :

Critical Issues which needs to be addressed:

1. Washer Disinfector is very critical equipment at CSSD department. In case the unit is down due to non availability of service technician or spares, entire days plan for Surgeries will go hay wire.
2. Huge disruption will create issues for Hospital Administration & Patients
3. In case Service cannot be provided , hospital will loose revenue / bad reputation
4. Establishing wholly owned subsidiary requires time & compliance to several legal requirement
5. Recruitment & training of 50 to 60 engineers will require long time. No revenue generation during project implementation period
6. Training Center is in USA. All freshly recruited engineers has to go through training in USA HQ.
7. There will be two different types of customer in Japan
 1. New installations at hospitals
 2. Customers having service contract (CMC) with Distributor
8. All new sales contracts & all existing CMC will be transferred to ABC Inc from distributor
9. Management of Spares Inventory
10. Warehouse for storage for Washer Disinfectors & building inward & outward logistics.

So, here now, so, I have explained you as simple as possible this product for your understanding. This is a washing machine with two doors, in one side dirty clothes or put, another side open the door and you take out the clean cloth, it is same like that you understand that terminology. There is no need for you to go into the detail about the cycles, about various standards and other things.

Because you are a manager here who has to take a decision which is to improve the CEO's decision to go into the market and increase your gross margin. So, the first one as I said the

washer disinfect is very critical equipment at central sterilization services department. In case the unit is down due to nonavailability of service technicians or spares entire day span for surgery will go haywire.

Huge disruption will create issues for the hospital administration and patients. So, imagine there is a very critical patient and he has to be done surgery as planned for next morning say around 8 o'clock in the morning, but due to the washer disinfect failure his surgery will get postponed. So, what will happen? It is a threat for the patient. There is a life risk for the patient and huge amount of hospital administration issue.

Because they have to redo the entire queuing of the patients and in large hospitals if you look at; any large hospitals in the country like Apollo, Fortis or Global or any of the large hospitals in the country, they have series of operation all lined up. So, if one operation is disrupted due to some reason, all the operations setup in the queue will have an issue. So, that is very crucial. So, the failure of this equipment is extremely crucial.

So, for you as a manager what you have to think that when I shift from the distributor to direct model, the transfer of the equipment smooth transition has to happen. So, as if it is not smooth transaction, then you will have a big problem with the hospital, with the patients, everybody will suffer. In case the service is not provided as I said hospital will lose revenue, bad reputation.

Now the next point is the challenge is that establishing in wholly owned subsidiary requires time, compliance and several legal requirements. So, currently the company is having only a representative office. So, there is a big difference between a representative office and if fully wholly owned subsidiary entity. Representative office cannot do any business in the country. So, there can be some managers who can facilitate the business but they have no license to conduct the business.

That means they cannot participate in a tender, they cannot quote, they cannot submit an official quotation from that address, they cannot have any tax registration there or they cannot generate invoice, they cannot import any spares, they cannot export anything, so they are just a representative office. So representative office is the first entry in any country the company makes.

So, that typically in a distributed driven market for any company if the operation is large like this, 50 million dollars operation, they will put a representative office where typically they will put one or two people to manage the business. Establishing the wholly owned subsidiary requires time compliance and there is some time required for this. And recruitment, so what you have to do in this case the distributor is having 80 engineers.

So, when you start your direct operation, you should have at least 50 to 60 engineers you need the day when you take it over. So, imagine apart from setting up the office, you have to recruit 50 to 60 engineers there. And when you are recruiting, the recruiting process is going on, these engineers will not generate any revenue, they will be sitting in your payroll but they will not have any revenue because distributor is still that time managing the business.

So, before you terminate the distributor or server notice, you should have these engineers ready with you. Then another big bottleneck is here. The training of these engineers. The training centre of the company of ABC Incorporation is in United States, so all the engineers whomever you recruit, they have to go through the training in United States. So, there is no training centre in Japan, so that is one of the bottlenecks here.

So, everybody you recruit and these engineers after recruitment have to go to Japan. So, we will discuss up to this point now. And in the next session, we will take it forward, right. Thank you very much.