

# [Hsbc and foreign market strategies](https://assignbuster.com/hsbc-and-foreign-market-strategies/)

### 1. Introduction

With assets of US $1, 502 billion, HSBC Holdings is one of the largest banking and financial services organisations in the world. 1 It provides a comprehensive range of financial services including personal financial services, commercial and corporate banking, investment banking and markets, private banking, and other activities. HSBC’s international network comprised over 9, 500 offices in 76 countries and territories in Europe, the Asia-Pacific region, the America, the Middle East and Africa.

### 1. 2. Literature Review

What determines foreign market entry strategies? To answer this question, most existing literature has focused on the characteristics of the entering firm, in particular its resources and capabilities (Barney, 1991; Anand and Delios, 2002) and its need to minimize transaction costs (Buckley and Casson, 1976; Anderson and Gatignon, 1986; Hill, Hwang, and Kim, 1990). While resources and capabilities are certainly important (Peng, 2001), recent work has suggested that strategies are moderated by the characteristics of the particular context in which firms operate (Hoskisson et al., 2000; In particular, institutions—the ‘ rules of the game’—in the host economy also significantly shape firm strategies such as foreign market entry (Peng, 2003; Wright et al., 2005). In a broad sense, macro-level institutions affect transaction costs (North, 1990). However, traditional transaction cost research (exemplified by Williamson, 1985) has focused on micro-analytical aspects such as opportunism and bounded rationality. As a result, questions of how macro-level institutions, such as country-level legal and regulatory frameworks, influence transaction costs have been relatively unexplored, remaining largely as ‘ background.’ However, a new movement in research posits that institutions are far more than ancillary elements, and that institutions directly influence what resources a firm has at it’s disposal as it strives to develop and launch strategy. Nowhere is this point more clearly borne out than in emerging economies, where institutional frameworks differ greatly from those in developed economies (Khanna, Palepu, and Sindha, 2005; Meyer and Peng, 2005; Wright et al., 2005; Gelbuda, Meyer, and Delios, 2008). Given these institutional differences, how do foreign firms adapt entry strategies when entering emerging economies? Focusing on this key question, it can be argued that (1) institutional development (or underdevelopment) in different emerging economies directly affects entry strategies, and (2) investors’ needs for local resources impact entry strategies in different ways in different institutional contexts. In essence, we advocate an integrative perspective calling not only for explicit considerations of institutional effects, but also for their integration with resource-based considerations.

An analysis of theory developed specifically out of changes to global markets shows little development of the standard theories of market segmentation, differentiated pricing and appropriate distribution channels which underpinned local and domestic marketing theory. However, the literature over the past five years has shown a particular set of theoretical models specific to global marketing. Hollensen, S (2007) discusses the Upsalla International Model which suggests a sequential pattern of entry into international markets with an increasing “ commitment” to overseas markets as the international experience of the firm grows. He contrasts this with a traditional approach of what is termed as the Penrosian tradition which returns us to the economy of scale and a cost-led approach working from the firm’s core competencies. Dunning (1998) suggests a similar Ownership-Location-internalisation (OLI) framework identifying an “ ownership advantage” of establishing overseas production facilities, a locational advantage which builds a logistics network around the overseas production and, finally, an internalisation advantage where it must be economical for a firm to utilise the previous two advantages rather than sell them to a foreign firm.

Similar to the development of the standardisation-localisation model emerging to deal with the specific choices related to international market entry the identification of risk mitigation factors salient to international marketing has developed rapidly. Baker, M (1993) recognises the risk mitigation inherent in internationalisation, protecting the firm from adverse fluctuations in the national economic cycle. Hollensen, S (2007) concurs, outlining the ownership, operating and transfer risk in being attached purely to domestic markets. All of the literature, in short, is strong on identifying the risks of domestic-based marketing, however there is scant coverage of the specific risks of internationalisation

### 2. 1 Factors Affecting Market Entry Models

Comprehensive models are easily identifiable in the literature and cover diverse entry modes, total product offer, and maturity models, Hollensen, S (2007). Earlier literature is more product-based than market-led, as with Majaro, S (1993) who presents three approaches to entering a product onto the international market: the development of new products, the deletion of weak products and the modification of new products. Hollensen, S more or less deals with market maturity as a key consideration of entry. Two distinct models suggested here are the waterfall approach where the product is disseminated from advanced through developing to less developed countries and the shower approach where all three are simultaneously targeted where early market penetration is a goal. Overall, the literature is consensual on the fact that shorter product lifecycles are the salient feature of internationalised markets.

### 2. 2 Internal Factors

With assets of US $1, 502 billion, HSBC Holdings is one of the largest banking and financial services organisations in the world. 1 HSBC provides a comprehensive range of financial services including personal financial services, commercial and corporate banking, investment banking and markets, private banking, and other activities. HSBC’s international network comprised over 9, 500 offices in 76 countries and territories in Europe, the Asia-Pacific region, the America, the Middle East and Africa. It was a pioneer of modern banking practices in a number of countries.

A growth oriented company from it’s earliest days, in 2000, HSBC decided to launch concrete strategies to attain market leadership in all sectors it operated in. Though the company was amongst the leading players in areas such as consumer finance, personal financial services, commercial and corporate banking, it also wanted to establish its presence in areas such as investment banking, mortgage, insurance and credit card business. To strengthen its product portfolio and geographical reach, the company embarked on an aggressive acquisition strategy. The focus was on areas where HSBC was either weak or did not have a presence. Simultaneously, the company launched an aggressive branding exercise to complement its growth strategy. The geographical reach of the bank could be estimated by its presence in form of the subsidiaries and franchises. It has nearly 200, 000 shareholders in some 100 countries and territories. The shares traded on the New York Stock Exchange in the form of American Depositary Receipts. HSBC was also listed on the London, Hong Kong, New York, Paris and Bermuda stock exchanges.

In late 1998, the Group adopted the HSBC brand and the hexagon symbol as a unified brand in all the markets where it operated. The bank adopted the tagline ‘ Your world of financial services’ in 1999. With the new tagline, HSBC hoped to acquaint customers with the extent and the range of its financial services. The tagline and the unification of the business under one name emphasised the global reach of the group. In early 2000s, HSBC vigorously worked towards developing its banking and financial services to gain market leadership. In 2002, the HSBC changed the tagline to ‘ The world’s local bank’, the tagline emphasised the group’s experience and understanding of a great variety of markets and cultures. The group chairman said ‘ We are committed to making HSBC one of the world’s leading brands for customer experience.’1 as part of the ‘ Managing For Value’ Strategy

In 1998, HSBC launched the above strategy to set the conditions for future success in a fast-changing market. The company hoped to beat the total shareholder return delivered by competing financial institutions. To do so, it needed to enter areas that promised returns that were higher than the risk-adjusted cost of capital. It decided to offer wealth management services, personal asset management and insurance services to its customers. Its objective was to cross-sell a wide range of products around the globe, including mortgages, insurance, mutual funds, and credit cards.

As a first step, the company decided to eliminate bad growth strategies i. e. those which had failed to cover the cost of capital. As a part of its value-based profitability drive, it adopted several measures which targeted higher-value creation at the bank. Managers and staff adopted behavioural practices such as targeting high-net-worth customers through several prestigious credit card schemes, strengthened the sales culture of staff by ways of incentives and promoting client cross-referral across the different business divisions, running more loyalty programmes for customers to capture a greater share of creditworthy customers. Like some other companies, HSBC has also developed international programs with their own incentive and compensation systems, performance metrics, and opportunities to groom managers for global positions (Exhibit 3, on the next page). Such programs, which often provide training focused on tolerance and cultural awareness, aim to produce managers who are well versed in a company’s distinctive capabilities but flexible enough to deal successfully with novel situations. These managers learn to distinguish the nonnegotiable aspects of a business model from those that can be modified as necessary. Ranbaxy, whose current CEO is British, is one of the companies working to develop this kind of global cadre. Its country managers move to new locations as soon as they are ready to assume larger challenges.

### 2. 3. External Factors

### 3. 1 Barriers to market entry

### 3. 1. 1 Regulation

Firms in regulated industries face a significant strategic dilemma when expanding abroad. On the one hand, established theory and practice recommend following a gradual, staged model of international expansion so as to minimize risks and cope with uncertainty (Johanson and Vahlne, 1977; Chang, 1995; Rivoli and Salorio, 1996; Guill´en, 2002; Vermeulen and Barkema, 2002), that is, to overcome the so-called liability of foreignness (Hymer, 1976; Zaheer, 1995). On the other, the regulated nature of these industries tends to require a strong commitment of resources anda fast pace of entry into foreign markets. This is the case for three interrelated reasons. First, these industries tend to be highly concentrated, and they often exhibit certain features of the ‘ naturalmonopoly.’1 Second, entry may be restricted by the government, frequently under a system oflicenses. And third, the government may own significant parts of the industry. Under these circumstances, foreign entrants face strong incentives to commit large amounts of resources and to establish operations quickly, whenever and wherever opportunities arise, and frequently via acquisition as opposed to greenfield investment (Sarkar et al., 1999). Thus, the regulated and oligopolistic nature of these industries generates strong first mover advantages (Doh, 2000; Knickerbocker, 1973). Recent research in strategy argues that firms in regulated industries follow ‘ asymmetric strategies’ in that they seek to defend their home-country position by preventing rivals from competing on a level playing field while pursuing entry into foreign markets as deregulation occurs. Given that deregulation has taken place at different moments in time and to different degrees from country to country, firms in regulated industries tend to follow a multidomestic strategy of foreign expansion, namely, they pick and choose which markets to enter depending on the specific circumstances

A natural monopoly emerges when it is possible to exploit economies of scale over a very large range of output. As a result, the optimally efficient scale of production becomes a very high proportion of the total market demand for the product or service. present in each foreign country, arranging their operations with a local rather than a global logic in mind, and engaging in limited cross-border coordination (Bonardi, 2004). Another distinctive feature of regulated industries is the role of the state as a shareholder. Some of the most active firms in regulated industries expanding abroad are former monopolies in which the state has or has had a controlling stake (Doh, Teegen, and Mudambi, 2004).

### 3. 1. 2 Cultural Barriers

By September 2000, the Hong Kong operations of HSBC were falling behind in implementing the MfV strategy. The strategy set the goal of the bank doubling shareholder value over a five years through growth in its core businesses in addition to a massive reduction in operating costs. One major cost-saving initiative was the migration of the bank’s Network Services Centre (NSC) in Hong Kong to its new global processing centre in Guangzhou, a Chinese city on the mainland. Implementing this initiative which involved moving staff and resources to the Guangzhou Data Centre (GZC) came up against major operational and public relations issues. (MB)

Technically, there were no major obstacles to the bank following a global trend in financial services; seeking economies of scale by moving back-office operations to lower cost areas. The average salaries of staff in the GZC were only 20% of those in the NSC. From this angle, moving professional positions to GZC and to HSBC’s other new Indian global processing centre seemed perfectly in line with MfV objectives. Most duties were highly routine involving few important decision-making duties. Nevertheless, The staff, who were initially offered a choice to move or risk losing their positions, felt betrayed by the bank, since there was an expectation among the workers that dutiful service should be recognised with job security.

### 4. Market Opportunities available to HSBC

### 4. 1. 1. Micro-Financing

With significant operations in the emerging markets and expertise in transactional solutions, and supported by our office network, services, processes, capital, and customer relationships, HSBC are well placed to serve the micro finance sector. The bank’s approach to this sector is based on commercial viability with high social benefit, with the aim of creating self-sustaining, stable financial services to help people out of poverty. HSBC integrate micro-finance activities Global Business and Organizational Excellence DOI: 10. 1002/joe January/February 2009 17 with local business capabilities rather than as a separate business line. Following pilot projects in 2005, HSBC has engaged more closely with micro-finance enablers and MFIs on the ground to understand the principal issues facing the sector, and the findings have informed and shaped our priorities. HSBC is currently working with MFIs in Argentina, India, Mexico, the Philippines, Sri Lanka, and Turkey through our operations in those countries. The bank is at the forefront in arranging foreign investments into the country and deals for Indian companies investing overseas, and it is custodian of more than 40 percent of the foreign institutional investments (FIIs) in India, with total assets under management in India that exceed $5 billion. Although HSBC in India has 47 branches and 178 ATMs in 26 cities, it lacks a branch network and accessibility in rural areas, where the majority of India’s empoverished population lives. The rural poor need a diverse range of financial services, including credit and safe and flexible savings services, to run their businesses, build assets, stabilize consumption, and shield themselves against poverty. However, access to quality financial services in rural India is still heavily inadequate. Eighty-one percent of villages in India do not have banks within a distance of 2 km (1. 2 miles); 41 percent of the population does not have a bank account; and available credit in rural areas meets just 10 percent of the actual need. Microfinance established a foothold in India during the 1990s, but this decade has seen rapid growth, with a distinct shift away from a “ welfare” model toward a “ business model” for delivering these services. Since it is quite expensive for HSBC in India to provide services directly to the rural poor, it lends funds to microfinance intermediaries, the MFIs that further on-lend the funds to the ultimate clients. HSBC in India established a team for microfinance under its Commercial Banking division in December 2007 and plans to eventually create regional-level teams to facilitate initiatives in their respective parts of the country.

### 4. 1. 2 North America Market Entry

HSBC’s initial motivation for its acquiring retail banks in North America and the UK was to diversify away from its home in Asia. After it acquired Marine Midland Bank and Midland Bank, HSBC’s motivation may have changed subtly. It is becoming increasingly difficult for banks that are large relative to their home markets to grow at home. In many developed countries banking has become quite concentrated (Marquez and Molyneux, 2002). In response, policymakers in these countries have started to bar the banks from further domestic mergers and acquisitions. Some recent failed attempts in Canada are a case in point (Tickell, 2000). The only remaining possibility for growth then is cross-border. Interestingly, each of the owners of the largest subsidiaries of foreign banks in the US is disproportionately often the largest bank in its own home country (Tschoegl, 2002 and 2004). Assessing the viability of this strategy is the classic question of how a foreign firm competes against local firms that do not face any liability of foreignness (Zaheer, 1995), that is, costs that come from operating in a foreign environment or at a distance. One issue then is whether having operations in contiguous countries represents a competitive advantage. Tschoegl (1987) and Dufey and Yeung (1993) have argued that where markets are well developed and competitive, there is no reason to expect foreign banks in general to be better than local banks at retail banking. At the same time there is evidence for the existence of a liability of foreignness vis-à-vis the foreign banks’ host-country competitors (Parkhe and Miller, 2002). Of course, there is also evidence that suggests that the liability is minimal (Nachum, 2003) or wanes over time (Zaheer and Moskowitz, 1996). However, these last two studies examine the liability in the context of corporate and wholesale banking markets. The liability may be more salient in the retail markets, where national differences between the home and host market are likely to be more profound. Demirgüç-Kunt and Huizinga (1999) and Claessens et al. (2001) found that foreign banks tend to have higher margins and profits than domestic banks in developing countries, but that the opposite holds in industrial countries. Similarly, Dopico and Wilcox (2002) found that foreign banks have a greater share in under-banked markets and a smaller presence in mature markets. The implication is that one should not expect much in the way of cross-border mergers in commercial banking within developed regions. We can speculate that on the production side, differences in products across markets and privacy laws appear to be limiting parents’ ability to consolidate processing. As far as depositors are concerned, there seems to be little value to having an account with a bank that operates in other countries, especially now that travelers can draw cash from networked automated transaction machines (ATMs). HSBC does have a service for wealthy individuals-HSBC Premier-that provides for such crossborder advantages as transfer of an individual’s credit rating when they relocate, and some other services. However, these facilities are not available to ordinary accounts. The literature on trade flows is instructive here; the evidence on NAFTA has shown that borders have a substantial damping effect on trade flows (McCallum, 1995). In North America HSBC is even poorly positioned to take advantage of the one form of cross-border retail banking that is currently drawing attention: remittance flows from Mexican workers in the US. Although HSBC now has a strong presence in Mexico, it has almost no offices in California or other US states with large populations of Mexican immigrants.

By contrast, Bank of America, which is the largest bank in California and is present in many other US states, in 2002, bought a 25 percent stake in Santander-Serfin, Santander’s subsidiary, which has amalgamated Mexico’s oldest and third largest bank. If there is little reason to believe that HSBC benefits from cross-border demand or production effects, what is left as a source of advantage?

One candidate is what Kindleberger (1969) has called “ surplus managerial resources.” When a bank such as HSBC can no longer grow at home, it may find itself with a management team that is underemployed in terms of the demands on its time. The bank may then choose to grow abroad when it can combine these surplus resources with what Berger et al. (2000) call a global advantage. Berger et al. argue that some US banks succeed in the competition with local banks elsewhere in the world simply by being better managed. In their survey of the literature on productivity, Bartelsman and Doms (2000) draw several stylized lessons, among them that firms differ in their productivity and that this difference may persist for years. Obviously, not all US banks necessarily partake of the advantage of better management and by contrast some non-US banks may. HSBC may simply be one of these. As Nachum et al. (2001) point out, the competitiveness of firms depends on the kind of assets that firms can transfer internally from country to country, but that are difficult to transfer from one firm to another, even within a country. Still, it is, unfortunately, extremely difficult to measure an intangible asset as subtle and hard to define as better management (Denrell, 2004), especially when, as recent events have shown, stock market performance or accounting measures are of doubtful reliability.

HSBC began its growth in North America by acquiring failed and weak banks. In effect, shareholders lacking a comparative advantage relative to HSBC, with respect to owning and governing given banks or branches (Lichtenberg and Siegel, 1987), sold them to HSBC. Generally, growth by acquisition is difficult to execute and as a strategy it is vulnerable to problems of over-reach due to managerial hubris (Roll, 1986; Baradwaj et al., 1992; Seth et al., 2000). Peek et al. (1999) found that generally the US subsidiaries of foreign banks have not done well. The poor performance of foreign bank subsidiaries was a result of the foreign banks acquiring poorly performing US banks and being unable to improve their performance sufficiently within the period that the authors examined. (One cannot arrive at strong conclusions from studies of the profitability of subsidiaries. Banks transfer profits across borders (Demirgüç-Kunt and Huizinga, 2001), and foreign banks may prefer to book some business from their headquarters (Peek and Rosengren, 2000).) Still, HSBC’s operations in the US and Canada are survivors of a winnowing process that saw other banks from Canada, Japan, the UK and the US sell their Canadian or US subsidiaries, in some cases to HSBC. As Mitchell and Shaver (2003) show with respect to firms in the US medical sector, firms differ in their ability to absorb and manage business on a continuing basis. They use the biological metaphor of predation and their evidence is consistent with the idea that some predators are better able to target desirable prey and better able to overpower the prey they target. HSBC appears to have found that it is one such successful predator. One may surmise that HSBC initially chose to acquire weak banks as much out of necessity as design. For any given size, a profitable bank will cost more than an unprofitable one, and to achieve its goal of diversifying, HSBC needed to acquire large banks. Now that HSBC is one of the world’s largest banks, whether one measures by market capitalization or total assets, it has more leeway.

### Conclusion

Assuming that there is a positive relationship between marketing spend and market share, marketing activities, if well-targetted should have a incremental impact on market share. However, this does not always seem to hold true within the “ big four” banks. Barclays and HSBC both developed their market share by 1% between 1995 and 2000, in spite of greatly varied levels of investment in marketing. Lloyds TSB market share fell by 2% although the bank spent significantly more than either Barclays or HSBC while NatWest and RBS have both declined by 4% despite having a collective expenditure of more than double Barclays. This perhaps, at least partly, explains why HSBC has adopted a highly acquisitive strategy, realising that, although the core brand is strong, customer recognition may have saturated, therefore integrating both fresh brands into subsidiaries in tandem with launching new, retail-focussed services, keeps the proposition fresh.

### Recommendations

With the disproportionate focus on retail banking, HSBC has yet not come over as a major player in investment banking. However, with the wave of recent milestone deals during over the last three years, the bank is beginning to emerged as an investment banking brand. HSBC played a central role in two of Europe’s biggest-ever merger and acquisition deals i. e. Mittal Steel’s hostile bid for France’s Arcelor and German utility company E. On’s offering for Spanish rival Endesa. However, the development in the direction of investment banking requires some acceleration as the retail ban king sector continues to be heavily impacted by the sub-prime mortgage fallout and credit tightness. The bank has been planning to further enhance its business in the UK by investing £400m in retail and commercial distribution network and setting up 500 new ATMs, 250 new Express terminals, however this is has not yet materialised and may be badly-timed if implemented within the year.

HSBC has considered the Asian region as its major focus area and it can expect a bigger share from the Asia-Pacific region in the future. In early 2007, Asia-Pacific, the Americas (including South America) and Europe each contributed one third in HSBC group’s overall bottom line.

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