

River islands
internationalization
strategies economics
essay



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In a world of increasing global competition, companies aim to capitalize on internationalization through expansion across borders and around the globe. The main objective here is for companies to run successful businesses internationally and this is made possible through an effective mix of internationalized strategies based on core internationalization competencies (Dicken, 2010). This essay will study the possible entry modes and strategies that a UK high street fashion brand called 'River Island' could use, to start operations in India and Australia. The greater part of this essay will focus on the influences that each country's local economic environment will have on the strategies that River Island implements. Starting with the Indian market and then moving to the Australian market, comparisons will be made on how these strategies would differ and a discussion of the relevant outcomes will be provided too. Therefore, in order to anticipate future benefits and risks towards the business, it is important to know how the economic environment of the two potential countries will affect River Island's entry modes.

2. Main Body

2.1 Company background

Operating in the Retail Industry, River Island was chosen due to its immense global portfolio of over 300 stores in the UK, Russia and Singapore, etc (River Island, 2012). This Multinational Enterprise (MNE) is head-quartered in UK and though it has a huge number of outlets in its home country, it operates a global supply chain network, sourcing and manufacturing its products throughout the world. River Island has opened up its own stores in countries and has also opted for a growing number of international franchise stores

throughout the Far East, Europe and Middle East with experienced fashion retail companies (River Island, 2012) and in-house fashion designers.

More recently, Ben Lewis, sole owner of the high street fashion brand, initiated and launched an International Shipping scheme in an attempt to increase brand awareness in new markets worldwide (Internet Retailing, 2011). Though River Island undergoes international trade and delivers its clothing as far as Australia, India and South America, this will not be considered as an already existing internationalization strategy, as the company has had no previous operational outlets in these countries.

2. 2 Difference between chosen countries – Australia vs. India

A key reason for choosing these countries as the host countries is because Australia, being a First world country is developed, contrasting to India which is still a developing country. Despite the fact that both Australia and India were British colonies and are currently both Commonwealth Members, the differences that arise among them are numerous. Australia scored 83. 1 in the 2012 Index of Economic Freedom making it the 3rd freest country in the world, whereas India scored 54. 6, ranking as the 123rd freest country in the world (Heritage Foundation, 2012). This itself is a contrasting factor and naming a few others, Australia has a GDP per capita of US\$39, 699 with a population of 22. 2 million, whereas India has a GDP per capita of US\$3, 339 with 1. 2 billion people (Heritage Foundation, 2012), nearly 5 times the population of Australia.

Nevertheless, though India seems to be on a lower ranking to most of the comparatives mentioned above, it has a much higher GDP of US\$ 1, 704 billion as compared to Australia with a GDP of US\$ 1, 448 billion, released by the International Monetary Fund in 2011. Therefore, both these countries have been chosen as host countries because the potential benefits that arise from trading there, outweigh the costs of doing so, which is outlined in detail in sections 2. 4 and 2. 6.

2. 3 Entry mode into India

The most appropriate strategy that River Island could use to internationalize in India would be to create a Joint Venture with an Indian local fashion retailer. A Joint Venture (JV) is an agreement between the home and host nations to share activities, risks, expertise and profits raised in the host nation, usually on a 50: 50 partnership basis (Nagar and Enderwick, 2009). Since the JV can take advantage of India's low cost home production, this will remove the need for River Island to import its clothing from its global supply chain. However, if demand in India seems to be less, exporting from India would also be a good strategy to internationalize. However, this will not be considered to a huge extent in the essay, as India being an enormous growing market will potentially have a massive demand for River Island's fashionable clothing.

The partner company would be Globus Stores Pvt. Ltd, the local clothing retailer with stores in more than 22 cities across India (India Retailing, 2012). Globus has already developed collaborations with foreign firms through its franchising, if not through JV's. This linkage makes Globus an apt JV target since it has the much needed experience of working with a London firm <https://assignbuster.com/river-islands-internationalization-strategies-economics-essay/>

(Pepe Jeans London) as well as the technological competencies in sales, marketing and human resources (Globus, 2012). Thus, the entry mode is advantageous to River Island, as the JV can handle any regional diversity implications and facilitate smooth entry into the untapped Indian market, getting rid of cultural barriers. This can be done quickly and will lower costs in the long run, in comparison to International Shipping, with export quotas from countries potentially increasing the JV's costs.

2. 4 Critical evaluation of the entry mode

2. 4. 1 India's economic connections with the rest of the world through international trade and FDI:

The Export-Import Bank of India (2012) shows a steady increase in both inward and outward FDI. India's International Trade has also increased from US\$252 billion in Financial Year (FY) 2006 to US\$794 billion in FY 2012.

Though this portrays India to be a good host country, an increase in inward FDI also means increased competition for the JV. However, since Globus has been operating in the Indian industry for nearly three decades now (Globus, 2012), the JV will be most benefitted through Globus's competitive advantage (Porter, 1990) over new-market entrants, especially when it comes to competition against new retail firms and sourcing out a cheap and reliable supply chain.

Similarly, India's second major trading partner in terms of Top Export markets is the USA (EX-IM Bank of India, 2012) followed by China and Singapore. Since River Island already has operational bases in the USA and Singapore, this would benefit River Island, as it could then potentially export cheaper manufactured clothing from India to the USA and Singapore, using <https://assignbuster.com/river-islands-internationalization-strategies-economics-essay/>

its newly formed JV. The demise of the Multi-Fibre Arrangement in 2005 (Dicken, 2010), where quota regimes were abolished, also provides a great opportunity for India to exploit the vast unutilised potential of its textiles and clothing sectors. However, the geographical proximity of River Island's European supply chain would offset lower production costs in India (Dicken, 2010), again showcasing exporting as the second best internationalization strategy.

2. 4. 2. The role of India's government:

The Indian regulatory framework is barely efficient and has yet to overcome problems posed by corruption, excessive bureaucracy and poor infrastructure. The World Bank reported that it takes 29 days to start a business in India as compared to 13 days in UK (2012). So forming a JV in comparison to exporting through internet retailing, would only increase the legal pressures on River Island, being a disadvantage. The trade weighted average tariff rate is fairly high at 7.9% in India (Heritage Foundation, 2012) as compared to UK, making India a less open market. Thus India's obstructive investment regime creates an unfavourable environment for new investment, making it particularly hard for the government to accept River Island's JV in India. However, the inclusion of a reputed retail company such as Globus Stores Pvt. Ltd would tend to make this process quicker and hassle-free.

The Indian government's fiscal policy includes a corporate tax rate of 33.22% which is much higher compared to rate in River Island's home country, UK of 26% (Heritage Foundation, 2012). This would mean that a greater

percentage of the JV's profits in India would have to be given to the
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government in the form of taxes. This drawback could however be neutralised through the higher profits that would be earned in India as a result of lower labour costs and sourcing cheaper suppliers.

2. 4. 3 The competitiveness of relevant local industries:

Firstly, the fact that the market size in India is huge and still growing will prove extremely advantageous to River Island. India offers an enormous market, where the forecasts based on current growth rates suggest that by 2025, India will have the world's 5th largest consumer market (Nagar and Enderwick, 2009). Secondly, India has a comparative advantage (Ricardo, 1817) in producing textiles, a labour-intensive process, because it is well endowed with unskilled labour (Nagar and Enderwick, 2009). River Island scores an added advantage again, as India can manufacture clothing at a much cheaper labour-wage rate than UK or the USA. India can also then be used as the supply-chain ground, from where the readymade garments can then be exported.

Thirdly, India's rapidly growing manufacturing sector as well as its strong IT sector will provide additional sources of specialist skills, augmenting the capabilities of the JV with Globus. Therefore, growing competitiveness of the local manufacturing industry in India benefits this internationalization strategy, as low cost labour in India would increase profits in the JV.

However, since it is hard to find highly-skilled labour in India can be a huge disadvantage when it comes to financial record keeping, sales and marketing for the JV.

2. 4. 4 India's economic relations with the regional economy

Tariffs remain high by international standards in India though there are ongoing EU-India talks which aim to reduce Indian import tariffs, putting India on a more equal footing with China (Santander, 2012). In any case this would not affect River Island. Considering demand in India turns out to be low, the clothes produced can then be exported to foreign countries, where exports quotas have been removed after the GATT (General Agreement on Tariffs and Trade) Uruguay Round (Dicken, 2010). Globus would however, ensure that demand in India is at its maximum as it would know how to market and promote the JV's fashion brands. River Island would rather export from India and benefit from cheap labour, than import materials from the EU, as it is not a member-country and would consequently lose out from the high exchange rate difference.

Considering the fact that both UK and India are part of the WTO, this does provide Free Trade Area (FTA) benefits to a future export-based strategy, but does not help the JV necessarily. Since the JV would use a local manufacturer in India itself, it would not need to consider importing garments to retail. Instead, River Island could concentrate on using the Indian supply chain to export to UK, making it a much easier task as export quotas are barely prominent (GATT Uruguay round). The fact that India formed a bilateral agreement with ASEAN and its 10 member states would mean that exporting from the supply chain in India, would again incur minimal costs due to the FTA (ASEAN, 2003).

2. 5 Entry mode into Australia

The internationalization strategy here would be to set up a Franchise agreement with a Retail Franchise firm in Australia. Franchising is a specialized form of licensing, where a formal right is offered to a firm in the host country to use a home country firm's brand, technology and management know-how (Andexer, 2008). Essentially, River Island would be the Franchisor, who would allow the franchisee, to use River Island's trademark and distribute its fashion clothing. In return, the Franchisee pays River Island a royalty, and this is how River Island would build its brand awareness overseas and benefit from increased international operations, without sacrificing control to outsiders (through a JV) or incurring high labour costs (through a wholly owned subsidiary) in Australia. The Franchisee would be set up with the Australian firm, EmbroideMe (AFOX, 2012), the country's largest embroidery network, branding uniforms and promo items across the country.

2. 6 Critically evaluate the entry mode

2. 6. 1 Australia's economic connections with the rest of the world through international trade and FDI:

Australia is the 3rd freest country in the world where it takes only 2 days to open a business (The World Bank, 2012), making it one of the world most open markets, after Hong Kong and Singapore. Therefore, this consequently means that FDI in Australia is quite high due to the low trade weighted average tariff rate of 1. 9% when compared to 7. 9% in India. FDI inflows in Australia went from US\$34 billion to US\$ 65. 6 billion in 2011, being 4. 3%

(OECD, 2012) of the annual GDP, whereas UK only saw FDI to be 2.3% of GDP.

The way in which the depicted openness of the Australian market could impact River Island's Franchise, is through greater industry level competition and valuable technological advances. Though the increased competition might prove troublesome for River Island, it also results in more efficient retailing with wider consumer choice, so both parties benefit. Australia's advancement in technology and the availability of highly skilled labour will be of most benefit to River Island's franchisee, as this would mean that Point-of-sale systems are much more advanced in the EmbroideMe outlets, increasing efficiency and business profitability. Even the manufacturing processes for suppliers will be made easier and quicker. This again has been made possible through the huge amounts of FDI, filling in the technological gap.

2.6.2 The role of Australia's government:

Australia's regulatory environment is one of the most reliable, transparent, and efficient in the world, contrasting to that of India. It offers a high degree of certainty for business planning but the only problem River Island would have to face would result from the need to follow the Australian Franchising Code of Conduct. It is now made compulsory for franchisors to disclose to their franchisees, since the removal of the single foreign franchisor exemption in 2008 (International Franchise Association, 2008). Thus, although there are compliance costs, it is arguable that this creates a barrier to entry to River Island's franchise, EmbroideMe.

Under the fiscal policy, corporate tax rate is a flat 30%, which is again slightly higher to UK's 26% but lower to India's 33.22%. Australia's higher exchange rate of 1.54 AUD to 1 GBP as compared to India's exchange rate of 88.15 INR to 1 GBP (XE, 2012) would also make a huge difference in River Island's profitability, when profits are sent over to the home country, UK. However, if sales stand high in both countries, then all else is well. Australia's judicial system operates independently and impartially, with consistent application of laws (Heritage Foundation, 2012). Therefore, if an argument arose between River Island and EmbroideMe, the government would first refer back to the Franchise Agreement. This can be both beneficial as well as harmful, based on how conservative the agreement contract is.

2.6.3 The competitiveness of relevant local industries:

The retail industry in Australia has met many competitive challenges in the past. Though the intensified competition is good for consumers, it will be challenging for the Franchise, EmbroideMe to gain its market share. However, the fact that River Island is a well-known brand overseas and has experienced franchising elsewhere around the world, will give EmbroideMe the edge and thus help it reap high profits.

River Island will control everything; from how the brand is to be marketed and how management is run in the Australian franchise. Only the finance and actual implementation of these essentials will be carried out by the franchisee, being EmbroideMe. Thus, the fact that Australia is so similar to UK in its historical links, language, business and legal practices, will make it easier for River Island to establish itself in Australia, under the EmbroideMe

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Franchise. Australia has a minimum wage rate of £6. 29 per hour which is higher than the UK minimum wage rate of £5. 80 (National Minimum Wage, 2010), depicting the fact that franchising in Australia rather than opening up a wholly owned subsidiary or a JV is much better, as this would cut down on business costs to a huge extent.

2. 6. 4 Australia's economic relations with the regional economy

As Australia is part of the Asia-Pacific Economic Cooperation (APEC), importing fashion clothing supplies from within the Asia-Pacific region would be tariff free and therefore incur zero costs for River Island's Franchise. Thus EmbroideMe would benefit from importing its garments and fashion-wear from countries such as the US, Singapore and Russia, rather than India, which is not yet a member country of APEC (APEC, 2012.). However, since UK is not part of APEC, it would not benefit any transactions that River Island's franchise had with its home country, UK.

On the contrary, both the existence of the Australia-United States Free Trade Agreement (AUSFTA) and the Singapore-Australia Free Trade Agreement (SAFTA) make Australia's trade between these countries go further than the WTO itself (Australian Trade Commission, 2012), with greater reductions in tariffs. This would again have a favourable effect on River Island's franchise, as EmbroideMe would be able to import its garments for retailing from either USA or Singapore, at lower costs.

3. Conclusion

To summarize, though the OLI-framework (Dunning, 2008) of FDI is not fully satisfied through the two chosen internationalization strategies, it is still reflected to a reasonable amount. The local economic environment in India depicts a fair number of benefits and drawbacks of internationalizing using a Joint Venture; reduced uncertainty, lower costs, and enhanced revenues for the MNE, River Island, seems favourable enough. Considering Australia, its economic liberalism, its stability and judicial system transparency, combined with strong economic growth of more than 15 years, make up for the narrowness of its market and its geographical isolation, thus making it a desirable destination for a franchise. Therefore, keeping in mind that all strategies have a set of pros and cons, the chosen strategies are comparably the most appropriate ones for River Island's host countries, as the benefits indeed outweigh the drawbacks when the local economic environment is considered.