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The difficulties in using a cost leadership strategy in emerging markets

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Abstract

Purpose – Strategic contingency theory maintains that a successful strategy should fit the features of the environment in which it is implemented, suggesting that different strategies are required in different world markets. In contrast, Porter posited three generic strategies, and asserted that to be effective firms should consistently use only one of the three. This paper aims to address this apparent disagreement by discussing the transfer, by developed-country multinational companies (MNCs), of a cost-leadership strategy to emerging markets.

Design/methodology/approach – Presenting theoretical arguments, based on deductive reasoning and examples reported in business publications, the authors focus on why firms from developed countries may find a cost-leadership strategy ineffective in emerging markets. This focus on both emerging markets as a group and on the ease of the transfer of the cost-leadership strategy fills a gap in the international management literature.

Findings – It is argued that implementation of a cost-leadership strategy by developed-country MNCs is rarely effective in emerging markets, and that MNCs may benefit from using different strategies in different markets.

Originality/value – The paper provides at least a partial explanation as to why developed-country firms may struggle when they apply a generic competitive strategy across countries. The contribution of this paper is two-fold. First, it explores the question of emerging market strategies by focusing on developed-country MNCs that use a cost-leadership strategy in these markets. Second, the paper contributes an important critique of the claims made by some business strategy theorists that MNCs need to use a single generic strategy globally in order to achieve high performance.

Keywords Competitive strategy, Multinational companies, Emerging markets

Paper type Research paper

Introduction

The last two decades have seen an increased focus by both academics (Luo, 2003) and multinational companies (MNCs) on emerging market economies (London and Hart, 2004). These markets represent a substantial growth opportunity for MNCs based in developed countries and will be a primary strategic focus in the foreseeable future (Arnold and Quelch, 1998). While a source of potential growth, these markets also present a unique set of environmental features and challenges for firms from developed countries (Hoskisson, Eden, Lau, and Wright, 2000). An important challenge for multinationals from developed economies operating in, or interested in, emerging markets is choosing and implementing a suitable competitive strategy.

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Strategic Contingency Theory maintains that effective strategies should fit the specific features of the environment in which firms do business (Kim and Lim, 1988). Researchers have noted that MNCs often fail to successfully adapt their strategies to the unique environments of emerging markets and, as a result of this lack of "fit," have generally been less than fully successful (Dawar and Chattopadhay, 2002; Meyer and Estrin, 2001). It is evident that many firms are not successfully choosing and implementing the best strategies for developing markets (Mammarella and Hisey, 1997; Nakata and Sivakumar, 1997).

In the following pages, we provide at least a partial explanation as to why developed-country firms may struggle when they apply a generic competitive strategy across countries. The contribution of this paper is two-fold. First, it explores the question of emerging market strategies by focusing on developed-country MNCs that use a cost-leadership strategy in these markets. In presenting theoretical arguments, based on deductive reasoning and examples reported in business publications, we focus on why firms from developed countries may find a cost-leadership strategy ineffective in emerging markets. This focus on both emerging markets as a group and on the ease of the transfer of the cost-leadership strategy fills a gap in the international management literature. Second, the paper contributes an important critique of the claims made by some strategists (Porter, 1980) that MNCs need to use a single generic strategy globally in order to achieve high performance. In closing the paper suggests directions for future academic research and presents practical managerial implications.

Theoretical background

Strategic contingency theory has its roots in the structure-strategy-performance paradigm associated with institutional economists (Bain, 1956; Caves, 1980) but focuses less on structure and more on strategy. Its focus is on the "fit or match between strategy and environment," (Lee and Miller, 1996, p. 730). Many theorists have explored the relationship between environment and strategy, but much of the early work was completed by Porter (1980, p. 3), who states: "The essence of formulating competitive strategy is relating a company to its environment."

In Porter (1980), three generic strategies are introduced: cost leadership, differentiation, and focus, which Porter divides into cost focus and differentiation focus. These strategies are a result of many various environmental features but are rooted in the firm's decision to pursue a broad or narrow target market and a uniqueness or cost competency (Figure 1). All three of these generic strategies have motivated much research (Murray, 1988; Gopalakrishna and Subramanian, 2001; Hill, 1988). This paper focuses on the effectiveness, globally, of one of these strategies, cost leadership. More specifically, the question is asked: "How effective is this generic strategy for MNCs from developed nations operating in emerging market economies?".

In his book, Porter (1980, p. 41) states that: "the firm failing to develop its strategy in at least one of the three directions – a firm that is "stuck in the middle" – is in an extremely poor strategic situation,". This "stuck-in-the-middle" scenario is discussed by Porter (1980) on a global level with the use of example firms that compete in multiple foreign markets. Porter's rigid view of the appropriateness of utilizing one generic strategy, and one only, regardless of environmental conditions, has been criticized (Hill, 1988; Wright, 1987). There is some empirical evidence that a hybrid or "middle" approach may be usefully applied (Hlavacka *et al.*, 2001; Kim and Lim, 1988).

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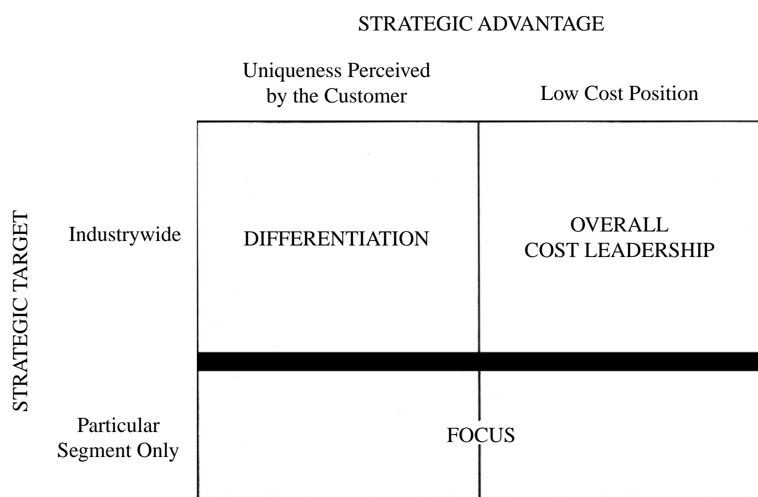

Source: Porter (1980, p. 39)

Figure 1.
Porter's generic competitive strategies

To quote Lee and Miller (1996, p. 730): "studies have found that strategies have varying utility in different settings,". In contrast to this position, other scholars have supported Porter's idea that competing with an exclusive, single strategy is most effective. Overall, the literature is generally supportive of Porter's claim (Douglas and Rhee, 1989; Green *et al.*, 1993; Miller and Friesen, 1986).

This paper challenges Porter's generally accepted approach by identifying a particular context – MNCs from developed nations operating in emerging markets that use a cost-leadership strategy in their developed markets – in which applying a single generic strategy across heterogeneous markets can be expected to produce disadvantageous outcomes. We argue that MNCs from developed nations that use a cost-leadership strategy in their home market will generally find its implementation in emerging markets more challenging and, perhaps, ill-considered. One might infer from our arguments that an alternative generic competitive strategy (focus, differentiation) or multinational strategy (e.g. licensing, political) is therefore preferable, but we make no explicit claim in support of a particular alternative strategy. Instead, we focus on the environment-based difficulties of moving a cost leadership strategy to emerging markets.

Environmental conditions necessary for cost leadership

Porter (1980) defines cost leadership as the achievement of "overall cost leadership in an industry through a set of functional policies aimed at this basic objective. Cost leadership requires aggressive construction of efficient-scale facilities, vigorous pursuit of cost reductions from experience, tight cost and overhead control, avoidance of marginal customer accounts, and cost minimization in areas like R&D, service, sales force, advertising, and so on," (p. 35). Essentially, "low cost relative to competitors becomes the theme running through the entire strategy," (p. 35). It is worth noting that Porter does not focus on the possible pricing tactics related to cost leadership, instead focusing on overarching strategic considerations and the importance of achieving lower costs than rivals, regardless of pricing method used.

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Researchers have associated cost leadership with mass merchandisers such as the retail firms K-Mart and Wal-Mart or fast food restaurants such McDonald's and Kentucky Fried Chicken (Helms *et al.*, 1992). In the discussion below, we use examples focusing on these firms and others to help illustrate our theoretical arguments.

There are some environmental conditions that form the foundation of cost leadership. First, the target customers need to be industry-wide; i.e. demand should be market wide, not segmented (Porter, 1980). Also, the customers demanding the product(s) need to be price sensitive (Murray, 1988). To meet this broad and substantial demand, considerable resources are needed. This generally prevents small firms from successfully following a cost strategy (Wright, 1987).

A high degree of price sensitive demand alone is not enough for cost leadership to be effective. Consider the example, from Murray (1988), of the gasoline retailing business. In this industry, consumers are price-sensitive and there is enormous demand. Unfortunately for gas companies, the cost structure of firms is fairly homogeneous. This prevents any one firm from being able to create a cost leadership advantage.

How then is cost leadership created? It is mainly created through a focus on efficiency (Green *et al.*, 1993). This efficiency can be rooted in various economies in the production or distribution process (e.g. economies of scale, scope, marketing, etc.) (Murray, 1988; Wright, 1984). It can also be generated from extra-beneficial access to distribution channels or resources (Murray, 1988). In some cases, the efficiency is the result of proprietary manufacturing technologies or innovations (Porter, 1980; Marques *et al.*, 2000; Murray, 1988). Lastly, efficiency can be the simple result of a managerial focus on cost control, employee productivity and economical asset use (Hambrick, 1983). In all cases, cost leadership is the result of some extra efficiency in the cost structure in comparison to competitors.

Cost leadership has been more prevalent and effective in stable environments. In contrast, discontinuous, unpredictable, and dynamic markets have been found to be better served through a differentiation or focus strategy (Lamont *et al.*, 1993; Lee and Miller, 1996; Miller, 1988). Diversity or heterogeneity is also better served through differentiation or focus (Miller, 1988).

Before continuing to discuss the application of cost leadership to emerging markets, it is important to review the body of literature that has investigated different strategic approaches in emerging or developing markets. Much of this research has been single-country focused (Gopalakrishna and Subramanian, 2001 [India]; Green *et al.*, 1993 [Portugal], Jacome *et al.*, 1993 [Portugal]; Kim and Lim, 1988 [South Korea]; Svatopluk *et al.*, 2001 [Slovakia]) rather than focused on emerging markets as a group.

The results of these studies have been mixed. Some have found that a hybrid of cost leadership and differentiation is most effective (Gopalakrishna and Subramanian, 2001; Svatopluk *et al.*, 2001) while others support the focus on one specific strategy (Green *et al.*, 1993; Kim and Lim, 1988). These articles leave several gaps in the literature. First, it is unclear as to the effectiveness of a cost-leadership strategy in emerging markets. Can this strategy be successfully transferred? Second, articles often fail to discuss emerging markets as a group. Third, articles do not clearly support either the use of one generic strategy globally or the use of different strategies in different markets. This article addresses these gaps in the literature by moving beyond a discussion of a specific country setting and connecting, through an investigation of cost leadership, Porter's (1980) strategies to emerging markets in general.

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Environmental features in emerging markets

The term "emerging market economy" is a difficult concept to define; there is no commonly accepted definition (Arnold and Quelch, 1998). The definition presented by Arnold and Quelch (1998) focuses on three criteria:

(1) low absolute levels of economic development;

(2) a rapid rate of economic development; and

(3) the system of market governance, specifically whether a country's economy is transitioning to a free-market system.

In contrast, Bandoyopahyay (2001, p. 16) defines emerging markets as "developing countries with relatively high GNP growth rates, increasing industrialization, and growing urban buying power,". While both of these definitions have value, they have a level of specificity that is unnecessary and overly exclusive for the purposes of this paper. Instead, a simple definition, taken from Hoskisson *et al.* (2000), is herein used whereby an emerging market is defined "as a country that satisfies two criteria: a rapid pace of economic development, and government policies favoring economic liberalization and the adoption of a free-market system," (p. 249). Examples of countries meeting this definition are China, India, Mexico, Poland, and South Africa.

The group of countries meeting these criteria is heterogeneous and one must be careful to not over-generalize or simplify the discussion (Hoskisson *et al.*, 2000). With that caveat, there are environmental similarities between all or almost all emerging markets that together allow for MNCs to generalize their strategic approach across these markets. These environmental properties are discussed below in general terms.

To begin, emerging markets have institutional and infrastructure deficiencies (Arnold and Quelch, 1998; Hoskisson *et al.*, 2000; Kim *et al.*, 2004; Roth and Kostova, 2003). These include a lack of well-established political and legal institutions (Hoskisson *et al.*, 2000; Meyer and Estrin, 2001; Tateisi, 1996), as well as weak communications (Miller, 1998), and distribution systems, including air, rail, and road (Geib, 1999; Kim *et al.*, 2004). All of these relate to a general lack of technological development that is potentially limiting (Miller, 1998), and a lack of infrastructure that can lead to costly distribution and production problems (Kim *et al.*, 2004; Nakata and Sivakumar, 1997).

Emerging markets also often lack important human, financial, or other resources (Choi *et al.*, 1999; Hooley *et al.*, 1993; Lascu *et al.*, 1993; Peng and Heath, 1996). Usually skilled labor is scarce, if available, whereas unskilled labor is abundant and cheap (Meyer and Estrin, 2001; Peng and Heath, 1996). Additionally, capital is scarce (Choi *et al.*, 1999; Miller, 1998), mainly due to organizational and institutional issues. Resources that are typically available in developed markets may be scarce due a variety of reasons, including cultural differences in consumption (Nakata and Sivakumar, 1997).

In emerging markets, there may be a lack of demand for products, especially for products that appeal to sophisticated or affluent consumers (Bandoyopahyay, 2001; Manrai *et al.*, 2001). Nakata and Sivakumar (1997) compartmentalize emerging market consumers into a large group of "have-nots" and a small but growing group of "haves." MNCs may find themselves in the frustrating position of having access to a huge market of "have-nots" in some cases hundreds of millions of consumers, where demand for their products is lacking and potential-customer resources are insufficient to buy

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their products (Ciu and Liu, 2001). In the end, consumer demand in emerging economies is segmented and rapidly changing, and this presents an additional difficulty for MNCs in these markets (Manrai *et al.*, 2001).

Furthermore, local firms often meet the demand for necessities (Nowak, 1996). While the stereotype of emerging economies is one of markets with low levels of competition, in fact local firms in emerging markets are often highly competitive (Miller, 1998; Walters and Samiee, 2002). They can flood the market with cheap, poor quality products and often their price levels are lower than outsiders can achieve (Nowak, 1996). In some cases, local competitors are subsidized by their government to the point that they can "dump" products in their domestic market (Karande *et al.*, 1999).

The role of governments is important and influential in emerging markets (Karande *et al.*, 1999; Kim *et al.*, 2004). For transition economies, those that are going through the difficult transformation from a planned to a free-market economy, the government's economic role is especially extensive, while in emerging economies as a whole, governmental influence is greater than in developed countries (Geib, 1999; Hoskisson *et al.*, 2000; Roth and Kostova, 2003). Taken as a whole, the importance of government often leads to an extreme dependency on special relationships (Peng and Heath, 1996).

Additionally, governmental influence often fills the gap left by a lack of regulation and legal institutions (Arnold and Quelch, 1998). Frequently the rule of law is replaced by the rule of man. This increases problems with opportunism (Hoskisson *et al.*, 2000), piracy (Arnold and Quelch, 1998), profit repatriation (Geib, 1999), and an overall lack of protection for intellectual property (Nakata and Sivakumar (1997), and likewise increases the risk for firms entering these markets, especially firms highly dependent on intellectual property protections.

On a broad, macroeconomic level, conditions in emerging markets are unfavorable. The main economic problems include frequent and severe financial crises (Mudd *et al.*, 2002) unstable capital flows, and high interest rates (Taylor, 2003). These are often coupled with high inflation and volatile currencies (Geib, 1999; Nakata and Sivakumar, 1997; Svatopluk *et al.*, 2001). These conditions increase the complexity of formulating strategies for emerging markets.

All of these factors together paint a picture of unstable economies with high levels of political and economic risk (Garten, 1996; Kim *et al.*, 2004; Miller, 1998; Peng and Heath, 1996; Svatopluk *et al.*, 2001). However, even with these challenges emerging economies represent large, rapidly growing markets that increasingly are the main drivers of MNC growth (Arnold and Quelch, 1998; Miller, 1998). While emerging market environments present many difficulties, they also offer some positive, unique features that can be leveraged to create advantage. First, available labor is cheap, creating opportunities for MNCs to set up local suppliers to help cut costs, especially for products being exported to developed countries (Cui and Liu, 2001; Dawar and Chattopadhay, 2002). Second, there exists pent-up demand for "American" goods. Global, often western, brands may represent higher quality products and may be purchased to gain increased social status (Arnold and Quelch, 1998; Cui and Liu, 2001). Basic goods in developed markets may be viewed as luxury items in emerging markets (Nowak, 1996). Nakata and Sivakumar (1997) refer to this as a "quality gap" that only can be filled by the experience and capabilities of MNCs from developed markets. Lastly, MNCs may be able to provide products that local companies are as yet unable

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to make, due to structural, technological, or management deficiencies (Meyer and Estrin, 2001).

A cost-leadership strategy in emerging markets

Certain factors common to emerging markets would appear to favor the use of a cost-leadership strategy for both domestic firms and multinationals. For example, input costs for natural and human resources generally are low, and consumer demand is typically elastic. Nonetheless, the preceding discussion of emerging markets presents a picture of notably different environmental conditions than the ones in which cost-leadership MNCs from developed nations first formulated their strategies. How easily, then, does a developed-country, cost-based strategy transfer to emerging market economies? If cost leadership is based on a foundation of advantageous efficiency, how easy is it for MNCs from developed countries to be more efficient than competitors in emerging markets? To answer these questions, the different sources of MNCs' efficiency are considered below in light of the unique environmental features in emerging markets (for a summary of arguments see Table I).

Consumer demand

The cost-leadership strategy is dependent on a large segment of price-sensitive consumers that demand the product(s). This demand frequently does not exist in emerging markets (Bandoyopahyay, 2001; Manrai *et al.*, 2001). Where it does exist, local firms often meet the demand for basic products, and these firms may have prices for locally produced products below the prices achievable for profit-oriented developed-country MNCs (Karande *et al.*, 1999; Nowak, 1996; Walters and Samiee, 2002). In such an environment, slashing prices and cutting product features is not an effective tactic for MNCs from developed countries. For example, both AT&T and General Motors used this method to compete in the Chinese market and failed (Letelier *et al.*, 2003).

Sources of MNC efficiency	Environmental features of emerging markets causing inefficiency
Consumer demand	Lack of large segment of price-sensitive consumers Local producers meet consumers demands for basic products more efficiently than foreign MNCs
Economies of production and/or distribution	Lack large consumer base to fund Infrastructure and institutional weaknesses hinder Lack large pool of resources
Preferential access to distribution of production channels	Local firms have cultural and knowledge advantages when forming local relationships
Proprietary production or innovation	High risk of piracy or counterfeiting.
Managerial focus on cost control and employee productivity	Cultural distance limits managerial effectiveness Lack of knowledge of local business practices and infrastructure limits the transfer of skills
Stable environment	Defining feature is an unstable environment

Table I. Sources of MNC efficiency and conflicting emerging market features

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Consider the case of consumer demand in China, a marquee emerging market. A Gallup poll and a review of the *China Statistical Yearbook* revealed that:

- Only 22 percent of the households plan to buy a television set in the future (82 percent already own one);
- Only 15 percent of the households plan to purchase a washing machine in the future (77 percent already own one);
- Only 9 percent of the households plan to buy a microwave (only 5 percent already own one); and
- Only 22 percent of the households plan to buy an air conditioner (only 10 percent already own one) (Hamer, 1995; Gale, 2003).

In contrast, China already has a growing green foods movement (Gale, 2003). Plainly, consumer demand in China and other emerging markets is considerably different from, and for some products is less intense than, consumer demand in developed markets – even for items that developed-market consumers consider a necessity. This brief example illustrates how unsafe it is to assume that demand is transferable across international borders and consumer groups, and how difficult it may be for MNCs to transfer a cost-leadership strategy to these markets. Frequently, the broad base of demand recognized as a key ingredient to successfully applying a cost strategy is just not present.

Economies of production and/or distribution

Economies of production or distribution require a large consumer base to fund them. To realize such economies in emerging markets, MNCs must either find products that are purchasable by both the "haves" and "have-nots" (Nakata and Sivakumar, 1997) or leverage their resources generated in other markets.

Owing to the myriad of infrastructure and institutional weaknesses noted earlier (Arnold and Quelch, 1998; Hoskisson *et al.*, 2000; Kim *et al.*, 2004), the ability to generate scale economies in emerging markets is restricted. Also, the large pool of resources, especially high quality resources on which scale or scope economies depend, often does not exist in emerging markets (Hooley *et al.*, 1993; Lascu *et al.*, 1993; Peng and Heath, 1999). It is possible that MNCs could realize economies based on their operations in other markets, but the additional costs of transportation plus the ability of local firms to compete on price does not make this a particularly viable solution. In the end, the lack of infrastructure and resources make the transferability of an economy of production or distribution-based cost-leadership strategy doubtful.

The resource difficulties faced by Kentucky Fried Chicken (KFC) when it entered China help to illustrate the problems with transferring economies of production. Upon entering China, KFC found that Chinese agriculture businesses mainly raised pork and did not have the technical skills or experience necessary to produce the quality of poultry the restaurant needed. Thus, KFC suffered from a scarcity of quality chickens, obviously a major problem. To solve this situation, KFC had to undertake an expensive and time-consuming joint venture with the government to create it own hatcheries to produce chickens that met its high quality (by Chinese consumer standards) requirements (Nakata and Sivakumar, 1997). This brief story exemplifies the base-level difficulties facing firms attempting to transfer economies of production or distribution from developed to emerging markets.

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Preferential access to distribution or production channels
In some cases, cost leadership is a result of preferential access due to relationships with governments, suppliers, etc. While relationships have been noted to be especially important in emerging markets (London and Hart, 2004; Peng and Heath, 1996) often it is local firms, not foreign MNCs, which enjoy special relationships and treatment (Geib, 1999; Hoskisson *et al.*, 2000). There are obvious exceptions to this rule (e.g. Pepsi in Russia during the 1970s), but overall, due to cultural and knowledge gaps, local firms are likely to have the advantage for gaining this preferential access.

For example, Wal-Mart is well known for having special relationships with it suppliers due to its size, and for having arguably the world's most efficient distribution system in its home market of the United States. These advantages disappear when it moves into emerging markets. Consider its efforts to penetrate markets in South America. In these markets, the firm has few price advantages, no distribution advantage, and no special relationships to leverage. Instead, the retailer's success is based on an emphasis on high quality customer service. For example, it allows customers to return products if they decide that they do not want or need them. Ultimately, the strategies that Wal-Mart uses in South America "have been invented on the spot, rather than imported from the USA," (Mammarella and Hisey, 1997, p. 27). Instead of being able to leverage special relationships, Wal-Mart abandoned a cost-leadership strategy and instead is focusing on high quality service to create competitive advantage.

Proprietary production or innovation
While intellectual property rights are noted for their importance to firms pursuing differentiation strategies, many cost-leadership positions are also based on proprietary knowledge and innovations. The risk associated with transferring intellectual property to emerging markets may deter MNCs from doing so. This risk is mainly rooted in the vulnerability of developed country MNCs to counterfeiting, piracy and other forms of infringement in emerging markets (Arnold and Quelch, 1998; Nakata and Sivakumar, 1997; Walters and Samiee, 2002). For MNCs with cost advantages derived from innovation or proprietary knowledge, the risk of infringement may be too great to ignore; in many cases, the prudent decision is to not enter the market.

Intellectual property infringement is often too simple and cheap, and the rewards are often too great for individuals in emerging markets to ignore the opportunity. Consider the problems of DVD and CD piracy in emerging markets. It has been estimated that this counterfeiting cost the film industry \$3.5 billion in 2003 (Fowler, 2003). In recent years, piracy operations have evolved into a harder-to-prevent form – small one or two man operations producing thousands of copies a day. A midnight raid of a Hong Kong apartment in early 2003 exposed a prototypical example of these new-age pirates. The one-man commercial thief was caught with a series of CD-R disc burners, copies of many current commercial CDs, and 1,284 blank compact discs. Another raid, this one on the Yongsan Electronics Shopping Town in Seoul Korea in June of 2003, "netted 5,850 DVD-Rs and CD-Rs including copies of Finding Nemo and The Matrix-Reloaded – plus 54 DVD-R burners and 50,000 labels waiting to be attached to recorded discs" (Fowler, 2003, p. 45).

Faced with these challenges, the industry is struggling to compete. It is incapable of contending in terms of cost – the pirates pay only for a burner, blank DVD-Rs and CD-Rs, and some labels (Fowler, 2003); the parent companies pay for artist development,

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sophisticated packaging, shipping, etc. There is no feasible way for legitimate firms to produce more efficiently than the pirates. Any potential cost-leadership strategy is ineffective, therefore, due to counterfeiting. Instead, these companies may consider attempting to differentiate their DVDs or CDs from pirated ones by adding extra features that cannot be copied but add value.

Managerial focus on cost control and employee productivity

Cost control through a managerial focus on employee productivity is another potential route to cost leadership in emerging markets. Consider developed-country MNCs that use their experiences and skill sets to more efficiently produce, market, and distribute products than competitors. On the other hand, due to cultural differences and a lack of intimate knowledge of local business practices, it may be difficult to transfer this knowledge. Human resource skills do not transfer directly to emerging markets (Napier and Vu, 1998). Furthermore, managerial capabilities may be duplicated by competitors, making it difficult to sustain advantage over time.

Unstable environment

The defining feature of emerging markets is volatility. Emerging markets are growing and changing at a rapid rate, and they are generally characterized by moderate to high political and economic risk. This is currently demonstrated in the obvious examples of countries such as Venezuela, Philippines, Russia, Indonesia, and many Middle Eastern states. These uncertain and dynamic markets have consistently been found to be a poor fit with cost leadership (Lamont *et al.*, 1993; Lee and Miller, 1996; Miller, 1988). Instead, research suggests that differentiation is a more appropriate strategy for environments with these features (Miller, 1988), while efficiency strategies are suited to the stable markets that better allow for consistent planning, refining, and improving.

Unique positive features

As discussed above, emerging markets have a pent-up demand for goods from developed countries, and brands from these countries often carry a positive quality connotation. This circumstance does not especially support a cost-leadership strategy, but might support a differentiation or a focus strategy. Consider the case of McDonald's when it first entered China. McDonald's restaurants in the United States and other developed countries emphasize speed of service (economy of distribution) and cost leadership. In China, by contrast, McDonald's found that consumers were attracted to "the clean environment, pleasant ambience, and polite staff," that is, to the high quality service McDonald's offered (Cui and Liu, 2001, p. 103). This encouraged McDonalds to abandon cost leadership as its strategy in China.

Discussion

The factors discussed above and the examples offered provide powerful evidence of the substantial environmental obstacles to the successful implementation by developed-country MNCs of a cost-leadership strategy in emerging markets. In these markets, focus, differentiation, or other strategies, such as those based upon personal or political relationships (Peng and Luo, 2000), may provide a better "fit" with the environment than cost leadership.

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On a broader theoretical level, the discussion above leads us to begin to question the importance of following a single generic global strategy, one consistently applied across all types of economies. Emerging markets are unique environments with unique needs (Arnold and Quelch, 1998). From a strategic contingency theory perspective, strategies that better fit with these distinctive features may be more successful. Using theoretical reasoning and descriptive examples, this paper has shown that developed-country MNCs may find a consistently applied global cost strategy unrewarding. In contrast, MNCs may benefit from switching strategies in some markets, leading to a "stuck-in-the-middle" approach that may in fact be appropriate and effective. These claims – that cost leadership is rarely an effective strategy in emerging markets when applied by MNCs from developed nations, and that different strategies may be necessary for different environments – represent the core contributions of this paper. While contrary to the work of Porter (1980) and others (Green *et al.*, 1993), this argument has important implications for both managers and academics.

Managerial implications

Decisions to enter new markets and the choice of generic strategy to pursue in new markets should not be made or chosen lightly. While emerging markets have many attractive features, their environments are risky and fundamentally different from developed ones (Arnold and Quelch, 1998; Hoskisson *et al.*, 2000). Emerging market environments lack many of the essential resources, infrastructures, demand features, governmental controls, and stability that developed-market MNCs are accustomed to and require to implement their cost leadership strategies (Arnold and Quelch, 1998).

This article highlights the importance for MNCs in developed economies that use a cost-leadership strategy to consider the ease with which their strategy will transfer to emerging markets. MNC managers may wish to pause and consider the source of their cost advantage. In what ways are they more efficient than their competitors? If it is through economies of production or distribution, how easily will they be able to access the resources and infrastructure needed to transfer these economies? If their advantage is through proprietary knowledge, how vulnerable are they to this knowledge being stolen? Are the rewards worth the potential losses? Similar questions and planning should be taken by MNCs whose efficiencies come from different processes.

In the end, managers may wish to consider the costs and benefits of using a differentiation, focus, or other strategy in emerging markets. There are costs associated with switching strategic approach, and there are obviously risks associated with this change, but it is possible that the risks and barriers to a cost-leadership strategy will influence MNCs from developed economies to consider alternative strategies.

Research implications

Before discussing the research implications, it is important to pause and acknowledge the limitations of this paper. This paper did not use empirical data or statistical analysis to support its claims. Instead the arguments made were supported through theoretical discussion and non-systematic observations of MNC actions and consequent outcomes. This limits the strength of the claims made. Additionally, the study assumes a level of homogeneity across emerging markets that may not be true, and many of the emerging markets used for examples were large, possibly atypical, emerging markets. It is possible that the discussion presented above could be further

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focused by looking at different types of emerging markets. Lastly, the study is limited by the theoretical framework used. While Porter's (1980) work is respected, it may take an overly simplistic view by breaking all strategy down into three choices – cost leadership, differentiation, and focus (Figure 1). It is highly likely that firm decisions are more complicated than that. Conversely, it is also true that the simplicity of Porter's (1980) generic competitive strategies facilitates discussion and debate and is a strength of his framework.

Even with these limitations, this paper provides important insights that may motivate future academic research on both emerging markets and the importance of global strategic consistency. First, future research may be based on Miller's (1998) subdivision of emerging markets into four stages: pre-emerging, emerging, accelerated growth, and maturing. It is possible that as emerging markets "emerge" that some of the environmental features blocking cost leadership may be reduced or eliminated. Future study of the issues raised in this paper might use these stages to inspire a more detailed discussion of effective strategies through emerging-market development.

Second, future research should investigate the possible mitigating effect of joint ventures or other strategic alliances. Pepsi, Coca-Cola, and other firms, for example, are known for using such approaches to help enter emerging markets (Miller, 1998). It is possible that these entry-mode options may remove some of the hurdles to cost leadership through what London and Hart (2004) refer to as a global capability for social embeddedness. Moreover, research might also consider possible effects based on industry type.

This paper additionally leaves a question regarding the relative effectiveness of differentiation, focus, or other strategies for developed-country MNCs in emerging markets. This paper in places hints that differentiation may be more appropriate, especially given the high quality associated with developed-country products, but focus or other strategies may also prove effective. More research on these strategies would be informative and have important practical implications.

Lastly, more research is needed exploring Porter's (1980) claim that firms should consistently apply their chosen generic strategy across all of the markets in which they compete. This paper presents some initial evidence, based on a strategic contingency perspective that MNCs may benefit from using different strategies in different markets. Specifically, cost leadership may be a highly effective way to create competitive advantage in developed markets, but its transfer to emerging markets by developed-country MNCs is suspect.

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