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TROUBLE IN PARADISE – PART II

This is the second part of an analysis of the changing, international business structures and how these changes have impacted and will continue to impact on world economies. The first part of this 2-part series was published last Friday, December 1, 2000, in TARGET Intelligence Report, Volume II, Number 229.

The rapid growth of productivity for many *'new'* companies has astounded critics and economists, alike.

This is especially true for those critics and economists who, in the past, had contrary views in respect of the format for the emergence of the world's new economy.

Clouding the issues and making it even more complex to fathom, initially, was that many hi-tech companies fell by the wayside, for one reason or another.

While there have been, over the past few years, a number of corporate duds, that have been dressed up to look as though they were hi-tech or Internet-related companies, nevertheless, there have been quite a number of genuine companies that have hopped aboard the hi-tech bus and are creating ripples in many a corporate boardroom.

America Online Incorporated (AOL) and Microsoft Corporation are, perhaps, 2 amazing examples of forward-thinking businessmen, who saw the future direction, long before many others, and tried to catch the gold ring on the hi-tech merry-go-round.

And succeeded in amazing form.

AOL secured for itself a huge slice of the international Internet market while Microsoft became, in an amazingly short space of time, the largest company in the world.

Dell Computer Corporation, along with archrival, Gateway Incorporated, are 2 more examples of forward-thinking suppliers of hi-tech products that have employed the Internet to boost sales to, what must be, unthinkable levels of 2 decades past.

The high productivity of companies, such as those mentioned above and many hundreds of others, will, inevitably, lead to lower inflation, leading to higher and higher living standards.

The rapid advances in many companies were made possible by the availability of the personal computer (PC) to the man-in-the-street.

As the price of a PC became cheaper, more people could afford to buy them; and, this led to a further expansion of consumer power – on an international scale, never before realised.

The cheaper PC revolutionised many economies of the world, by osmosis rather than by design.

But this phenomenon, also, has spelled the death for companies that were manufacturing typewriters and suchlike, in the same way that the easy availability of the motor car spelled the death for many companies that had been in the business of manufacturing horse-drawn buckboards, surreys, and the like.

After the Model T Ford hit the streets of the United States in 1908, there was no returning to the old ways.

The advances of science rarely permit the backing of the clock.

Henry Ford, just 5 years after launching his Model T, introduced an assembly line in his factories that could employ interchangeable motor-car parts, thus crushing the competition due to its revolutionary concept, which, today, is looked upon as a relatively simple concept.

The dignity of simplicity alludes many – even noble economists of note.

Henry Ford made the motor car available to all by being able to produce cheaper and cheaper models without sacrificing quality.

Where he went wrong was that he did not realise that the buying public demands aestheticism as well as utilitarianism.

There is a parallel to be drawn from Henry Ford's Model T, his rise to being the world's foremost manufacturer of motor cars, and the way in which the personal computer, as we know it, today, has evolved.

As horses were replaced by motor cars as a means of public transport, so the typewriter was replaced by the world processor, leading to the personal computer.

The next step: Aestheticism, coupled with faster and faster processing power and the ability to have numerous bells and whistles.

The personal computer has graduated from being a rich man's toy to being a working man's tool, a school boy's workstation, and a child's window to learning.

And the working man's environment has changed forever, with his ability to work in virtual reality.

He has become more productive, more creative … and this is likely to lead him to become more and more industrious because, after all, *'inventing'* and discovering is fun.

Today, nearly anybody can *'invent'*, using his/her PC – and invent in the comfort of the environment of choice, be it at home or in the office.

The information age has arrived – and with a bang which is being heard in every corner of the world.

It has created wealth unimagined and it has brought the stock market into many a home.

The Key Components

The flexible economy of the world, today, has at least 2 fuel sources.

They are capital, being created on stock markets of the world, The New York Stock Exchange, in particular; and, the flood of new money, flowing into companies that have successfully harnessed the power of the Internet/PC for commercial purposes.

Estimates are that at least $US60 billion (about $HK470 billion) was invested as *'seed capital'* in 1999 in start-up companies in the US, alone.

That was about 30 times more than the amount of money that was invested by USA-based venture capital companies just one decade before.

Initial Public Offerings (IPOs) on US stock markets drew the attention of venture capital to the extent of at least $US75 billion (about $HK590 billion) in 1999.

This was about 7 times more than the amount of money, invested in IPOs just one decade prior.

Price-Earnings Ratios of yesterday are, to a great extent, not applicable as the correct and accurate *'barometer'* for the weighting of a company's value in terms of historic earnings, divided by the market price of the stock, or comparing it with another company in a similar field of endeavour.

Stronger productivity has altered the way in which one has to view, and value, many of the new, hi-tech companies, those privately held and those that are listed on international stock markets, since their profits are, more than likely, growing exponentially.

These companies are able to achieve higher and higher profits because higher and higher productivity leads to achieving economies of scale, which, in turn, leads to higher and higher profit margins.

As the cash is rung up in the virtual cash register, many of these hi-tech companies are finding that it is more advantageous to buy up their own stock, if they are listed on recognised stock markets, because they know a good thing and can guarantee a reasonable rate of return, simply by buying and cancelling their own scrip.

This, naturally, leads to a reduction in the Issued Share Capital, freely floating, which results in higher prices for those shares that are in the hands of third parties, not associated with the operating companies.

The repurchase of publicly held shares by managements has been overlooked of late, and many a US stockbroker, who states to a prospective investor that such-and-such a company's stock is too expensive, may not be tuned into the correct channel.

Competition Makes For Strange Bedfellows

Competition is fierce for the fight for the consumer.

It is more fierce, today, than ever before because the playing field is the world, not a segment of a small community.

This is leading to cutthroat tactics, being engineered and executed by managements of companies, vying with each other in order to try to maintain healthy profit margins.

Today, many companies are finding it impossible to raise prices due to competition; and, so the only alternative is to cut costs.

Many companies are banding together, forming oligopolies for mutual protection and to permit more rapid growth.

Synergistic banding of companies affords the possibility, again, of achieving economies of scale, thus pushing up profit margins and affording the ability of spreading fixed costs over a larger base of sales.

Also, economies of scope afford the ability of offering a one-stop shop for consumers.

Skilled labour looks with more interest and enthusiasm on the company with the perceived, largest potential for growth.

This tends to negate, to a great extent, shortages of skilled labour for the large, successful company, which can offer interesting employment in a variety of locations in addition to offering better benefits for its workers.

Such companies have the ability to buy in bulk from suppliers, be it microchips or cardboard for the making of boxes, and this buying power results in the maintenance of higher productivity and, often, almost absolute control of costs.

As growth is seen in the marketplace, more money is ploughed back into the companies in the form of creating, and/or maintaining, brand awareness.

Consumers are becoming more and more conscious that the high-profile, hi-tech companies – Microsoft, Hewlett-Packard Company, Gateway Incorporated, Dell Computer, Cisco Systems Incorporated, Texas Instruments Incorporated, etc -- are the companies that value customers and customer loyalty.

The managements of such companies are fully cognizant of quality control since reliability is being equated with brand names in the marketplace of today.

This feeling of *'comfort'* on the part of the consumer is being translated into purchases, unseen, through the Internet.

Further, customers, who are used to using a certain system, such as Microsoft's Windows 2000, are unlikely to change horses quickly because the system works -- and works well.

Brand awareness is fast becoming brand loyalty.

The flip side of the coin, however, is that the larger the company often leads to the larger the problems as management starts to lose sight of important objectives and targetted focus.

This corporate myopia has been responsible for many a misstep, some leading to financial failures of companies.

Decisions in large companies must take into account that the importation into one economy of a successful formula in another economy may not result in the desired effect.

When Kentucky Fried Chicken *'died'* in Hongkong in the 1970s, it was due in part, if not in whole, to the fact that the chickens, purchased from the People's Republic of China and used in the preparation of KFC dishes, had been fed fish meal, during the chickens' growing process, and, after frying, the chicken had the taste of fish.

When Thailand first saw a McDonald's Corporation's hamburger in Bangkok, a couple of decades ago, sales were very poor because the hamburgers were considered too dry for the average Thai.

Mixing the beef with chicken fat did the job – and up went sales.

International companies have to think local, not (US or European) headquarters parochial.

Television broadcasters and media magnates, such as the Rupert Murdoch international group of companies, tailor their products to the locale in which they operate.

They know that they may not be able to impose their biases in the countries in which they operate in the same way that the American economist, of some years ago, made the tragic mistake of suggesting that the famines on the Indian Continent could be expunged, simply by teaching the Indians to eat more beef.

Religion may be inflexible, but those indulging in international business must be like the chameleon, crawling over a tartan rug, changing colours as it moves.

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