Going International - The ABBA Strategy for Creating Value

Or

Why ICT Companies should think twice about the U.S. Market

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Emerging technology companies usually do not have the resources to go after all major markets at once. For many of them the choice will come down to making a commitment to going after the U.S. or going after the rest of the world. In this article we will make the case for following the ABBA strategy – Anywhere But Bloody America.

The United States is Different

The U.S. is often seen as being a tempting target because of its size, the fact that it is English-speaking, and it is the largest consumer of just about everything from technology to pop culture. But its very size makes it extremely competitive, and it is not easy for foreign companies to succeed. It is not widely known, but the Swedish pop group ABBA never had a #1 single in the U.S. After emerging in 1974 it conquered virtually every market in the world except America. In 1978 it invested $10 million in a PR and marketing campaign to increase its profile and produce a #1 hit. And it didn't work. The U.S. *is* different.

Consider this: Most American technology companies fail in their own market and go out of business. So a non-U.S. company has to ask itself why they think they are more likely to succeed, and if they do not have a good answer, they should take a serious look at where they should be focusing their attention.

Start with the Exit Strategy

The exit strategy is a term used by investors, and it simply means how they are going to get their money back. They have made an investment in a company, and they expect a significant return. However, even if you are an owner-operator, and have no outside investor, it is still a question you should ask yourself. How does your business become your retirement fund? Your future is invested in your company, and if you do not have a strategy for converting your shares into cash at some point, you will not be in a position to make the best decisions on the direction your company should take.

Traditionally there are three possible outcomes for a company:

1. It can go bankrupt, which is what happens to a majority of technology firms;

2. It can grow quickly, get listed on the stock exchange, and become a sustainable, long term business, but this is a fate reserved for a very few companies;
3. It can be acquired, also called a trade sale, which is usually the most logical outcome.

A trade sale is something you can and should plan for. Done properly it will give you a clear objective to work towards, and you can build your business into something that would be attractive to a buyer. So, what are the elements that could make you a good acquisition target? Why should someone pay you an indecent amount of money for your business?

Creating Value

Companies are acquired for many different reasons. For a technology firm the most spectacular returns are achieved when they have a hot technology that attracts the attention of an industry heavyweight. Cisco, for example, is famous for buying technology and brains. Instead of hiring their own team of PhDs to develop the next cutting edge device, they paid top dollar for smaller companies with a proven technology. This saved Cisco the time and risk involved with doing it themselves. Now, though, times have changed and it is rare to see an emerging firm command an enormous multiple of revenues.

A different acquisition model was pursued by Computer Associates (CA). CA was interested in revenues. They purchased dozens of companies with a mature technology and a large installed base that generated a strong stream of maintenance revenues. Through a process of rationalization they were able to consistently grow their revenues and profits.

Does your company fit either of these profiles? Do you have a hot technology that will help a major player to dominate a new niche or market segment? Do you have a large and stable client base? For many emerging technology firms the answer is going to be “no”. So if you aren’t large enough or growing fast enough to justify a listing, and you don’t have the technology or the revenues to make you an attractive acquisition, how do you build value that can lead to a trade sale?

Creating Value through Distribution

Fortunately, there is a relatively simple way to create value, and that is to build a strong, international distribution channel for your product. And this brings us full circle to the ABBA strategy, because now your choice of markets becomes critical to your success.

The U.S. is home to the overwhelming majority of technology companies, which means that a potential buyer will likely be an American firm. If you are positioning yourself to be purchased, there would be very little value to a potential acquirer if you have an established position in the U.S. – they can handle their own market by themselves, thank you very much. In addition, they will usually have better funding than a South African firm, which will make it that much more difficult for you to compete for clients on their home turf.

There is another dynamic at work which helps create a significant opportunity through international distribution. U.S. companies, usually for the first 2-3 years of their existence, will be focused on their domestic market; after all, it is the biggest market in the world. This is also very often a requirement of their investors, who want to see them get traction at home before going overseas. This means that there is a 2-3 year window of opportunity for non-U.S. companies to get their business established in Europe and Asia. Then, when the major players emerge from the U.S., they will see a competitive product that is already operating in the markets they want to enter. It could be a lot easier for them to write a check, buy out the established competitor, and emerge with a strong presence in multiple markets overnight.

But the U.S. is so big – we can't ignore it!

This argument is based on the "Chinese market share principle". All you need is 1%! The problem is that there are a lot of strong, well-funded companies that are all going after the same 1%, and foreign companies invariably underestimate the cost of marketing in the U.S. It is not uncommon for American VC-funded firms to spend 50-200% of their revenues to build brand recognition, because skeptical IT buyers do not want to look at products they have never heard of.

A variation of the argument above is, "We only have a limited amount of money to spend on international expansion, so we might as well spend it in the largest market, where the potential pay-off is the greatest." This is not unlike betting on a long-shot because the odds are higher, but the risk is significantly higher as well. Going after smaller markets might not be as glamorous, but it is a far better strategy for creating value. I would challenge readers to name five emerging technology companies that have enjoyed meaningful success in the American market.

Does this mean that the American market is never the right choice?

Not at all. If a company truly is part of the exclusive club that has a break-through technology, and where a quick sale to an industry giant is a possibility, being in the U.S. early makes a lot of sense in terms of creating visibility. They can't buy you if they don't know who you are.

We also think that entering the U.S. is a good idea if the company has established a presence in multiple markets and is positioning itself for a sale. From the standpoint of maximising the price, having even a token presence in the U.S. will increase the value of the transaction, because now the price has to include something for the "lost opportunity". By this we mean that you should position your operation in the U.S. as the first step in a serious market entry effort, even if it is only intended to be a beachhead. A buyer would have to factor in something for the revenues and profits that you will be forgoing by selling your company before you have had a chance to succeed in the U.S.

As the largest market in the world, you can demand a premium for selling early, but you can only do this if you are physically present.

Finally, the U.S. can make a lot of sense if a company has been able to build a strong business in other markets, and then enters the U.S. from a position of strength. The lessons learned in Europe and Asia-Pacific can be invaluable, and many of their clients will be subsidiaries of American companies. Having these existing accounts as references will accelerate the sales process in the U.S., as well as providing tremendous credibility that will help overcome the challenge of answering, “What do you mean, you’re from Australia?”

Conclusion

The purpose of being in business is to make money and retire wealthy. Most people are so busy trying to make money and survive that they give little thought to how they are ultimately going to create an exit for their business. Oh, there is usually a fuzzy idea of becoming big and successful and cashing out at some point, but unless there is a clear idea of what the exit strategy should be they will not be in control of their destiny. The ABBA Strategy is a good way to make it happen.

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The York Group is an international organisation with offices in twenty countries. It has been successfully building international sales channels for companies since 1993, first specializing in international business development services for information and communication technology companies, with an initial focus on software. It has followed the evolution of the industry as it moved into Internet and wireless. With a global network of offices and partners, its clients range from familiar names such as Dell, Intuit and WinZip, to small and emerging firms from a range of countries, including Australia, France, the UK, Norway and Italy. For further information, see: http://www.theyorkgroup.com