This case presents the experience of six Chilean manufacturing companies that opted for joining forces to conquer international markets. Each specializes in a different line of hardware or construction-related items, and taken together, they offer a wide range of products. The case describes the reasons for the formation of the consortium, including a severe economic recession that drastically affects the construction industry and reduces the sales of the hardware manufacturers. One option is to export, but entry in international markets requires a broad line of products, physical presence, advertising and promotion, and brand recognition, which none of the companies acting independently can attain, and even less so if they compete with one another. Therefore, the companies decide to join in a consortium, consisting of two interrelated companies: Ferrex Trading Company, with offices and warehouses in Miami, which acted as a U.S. importer and distributor, and Ferrex Chile S.A., which received orders from its U.S. counterpart and distributed them among the six member companies. It also prepared shipments and complied with export procedures, maintaining close contact with government entities that supported the initiative such as the Central Bank of Chile, the export promotion agency PROCHILE, and customs. The case describes how Ferrex negotiated with the government for favorable conditions such as free zone status that allowed the consortium to reduce operating costs and provide better service both to member companies and to final consumers. This case is an excellent vehicle for exploring ways that small companies have been successful in their domestic market but that lack the resources to penetrate international markets as independent companies can join forces in combining product lines, pooling marketing efforts, enforcing quality standards, advertising, and developing a single brand name that comes to be respected among consumers. The case documents the consortium’s success in obtaining brand recognition for quality and a reputation for excellent service. Moreover, it now has an opportunity to reduce operating costs by signing contracts with nationwide distributors. The problem facing the consortium at the time of the case was that the domestic market for hardware products in Chile had recovered, demand was strong, and four of the six members had lost interest in export marketing, which is less profitable and more difficult. Mr. Patricio Lioi, president of the consortium and owner of one of its most active member companies, had to decide between pressuring the consortium members to honor their original commitments or looking for new companies to join. Among Mr. Lioi’s options were to buy out the shares of the less active members in the consortium and to continue ahead with the project.

Consorcio Ferrex

In August 1988, at his office in Estación Central, Santiago, businessman Patricio Lioi was recalling the events that had occurred since the start-up of the first Chilean export consortium specializing in hardware products, of which he had become President.

Many factors had led this group of businesses to get together for the purpose of opening up new markets. It started in 1985 when the Chilean economy was undergoing a recessionary adjustment after the 1984 boom. The new economic policy, based on maintaining a high real exchange rate to stimulate exports, had not yet brought in concrete results. For the first time, Chilean business people were receiving clear signals indicating that the country’s long-term growth would be driven by expansion in the marketable goods sectors.

Lioi had been analyzing the evolution of sales in the businesses associated with the Consortium (Table 1) and realized that year after year, their exports had been concentrated in two of the six companies, Inchalam S.A. and Patricio Lioi and Cia., Ltda. The first of these was a large company that had been handling commercial activities abroad for many years but only within Latin America.

Overall increase in economic activity at the domestic level and growth in the building sector in particular had caused some of the Consortium companies to become less interested in exports. The domestic market offered greater feasibility and security for continuing to expand their operations, since
current conditions were very different than those of 1985. At that time, the domestic market had been in a true depression.

Lioi was concerned about this situation since he was interested in the continuing growth of Consortium activity and taking advantage of the prestige it had already earned. Opening the U.S. market had been an uphill task since access was generally very difficult for exporters of manufactured products originating anywhere south of the Rio Grande. There had been relatively significant financial and administrative outlays, and Lioi felt that continued effort would result in an important expansion of the volume of business that had been handled to date.

Lioi was ready to continue the adventure that had been initiated, although this required some thought about how to keep control of the Consortium. He was turning over in his mind whether or not to purchase the shares of his associates and continue alone. Would this be feasible? Did he have the experience necessary for taking on this kind of initiative...? These doubts would have to be cleared up in the next few days, as there was no time to lose in making the decision—at the end of the month representatives of each Consortium partner would be meeting to evaluate the 1987–1988 results. This would be the right moment for any change in strategy.

**Formation of an Export Consortium**

Chilean businessmen had always encountered many obstacles to their efforts in opening markets for new manufactured products. Some of the problems that kept many businessmen away from foreign markets included, for example, the regulations governing foreign trade of various items and markets. Limited resources was another factor hindering export initiatives. Economic circumstances in Chile during 1985 had required seeking out new areas to place national production, which could not be absorbed completely by depressed domestic demand, and this was particularly true for construction.

“Union makes for strength...” This expression was the rallying cry when ASEXMA, or the Association of Exporters of Manufactured Products, was formed several earlier. The purpose of this organization was to provide assistance, information, advice, and even resources for Chilean manufacturers interested in expanding into foreign markets.

In January 1985, ASEXMA and Pro-Chile, an export promotion agency under the aegis of the Ministry of Foreign Affairs, collaborated to form a hardware committee which later became the consortium for the export of hardware, Ferrex Chile, S.A.

Committee activities were divided into four stages. The first stage the Committee conducted was an exhaustive international investigation to analyze markets feasible for export. Legal consultants were hired to learn about existing legislation in each of the countries researched. Participation in Feria Expocomer ’85, in Panama, and visits to New York and Tampa, in the United States, made it possible to identify possible markets in those places and decide where to set up a base of operations later on. The most promising markets seemed to be the United States and the Caribbean, through Panama.

In the second stage, an agreement for technical assistance was established with CESMEC, a company specializing in quality (measurement and certification) and the Consortium participated in the Hardware Wholesalers Indianapolis Trade Show, a fair for hardware products, the largest of this kind in the world (importers/exporters). The fair provided an excellent opportunity for beginning to identify more closely which markets to penetrate.

This experience made it possible for the Consortium to decide where it would finally set up its base of operations for international activities; the Consortium decided on Miami. The decision led to a third stage, in which Consortium products would be adapted and certified in order to meet U.S. requirements.

In the fourth stage, the first shipment was manufactured and sent out, accompanied by an elaborate set of promotional and sales catalogues.

**Associated Companies**

In the first stage, companies associated with the Hardware Committee (Table 2) saw an excellent opportunity in the United States and Caribbean markets, but any project of this

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**Table 1. Annual Sales**

<table>
<thead>
<tr>
<th>Empresas</th>
<th>1986</th>
<th>1987</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deva Ltda</td>
<td>24,960</td>
<td>53,975</td>
</tr>
<tr>
<td>Fund. Pacífico</td>
<td>3,900</td>
<td>0</td>
</tr>
<tr>
<td>Imabro Ltda</td>
<td>1,255</td>
<td>0</td>
</tr>
<tr>
<td>Inchalam S.A.</td>
<td>772,660</td>
<td>2,771,098</td>
</tr>
<tr>
<td>Lioi &amp; Cía</td>
<td>180,462</td>
<td>803,665</td>
</tr>
<tr>
<td>Nibsa S.A.</td>
<td>2,336</td>
<td>0</td>
</tr>
<tr>
<td>Venta Total</td>
<td>985,573</td>
<td>3,628,738</td>
</tr>
</tbody>
</table>

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4 Fiscal year ending August 31.  
5 In thousands of US$.  

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Table 3. Description of the Consortium Companies

<table>
<thead>
<tr>
<th>Company</th>
<th>Products</th>
<th>Export Offer in US$</th>
<th>Export Offer in Units</th>
</tr>
</thead>
<tbody>
<tr>
<td>Broncería NIBSA S.A.</td>
<td>Valves and fittings in bronze</td>
<td>US$ 110,000</td>
<td>860,000 connections 60,000 faucets</td>
</tr>
<tr>
<td>Manufactura de Bronce Ltda. IMABRO⁶</td>
<td>Valves and fittings in bronze</td>
<td>US$ 60,000</td>
<td></td>
</tr>
<tr>
<td>Industria Cerrajera DEVA Ltda.</td>
<td>Locks</td>
<td>US$ 100,000</td>
<td></td>
</tr>
<tr>
<td>Industria Chilena de Alambre (INCHALAM)⁵</td>
<td>Wire, fencing, nails</td>
<td>US$ 800,000</td>
<td></td>
</tr>
<tr>
<td>Patricio Lioi y Cía. Ltda.</td>
<td>Locks and wheelbarrows</td>
<td>US$ 100,000</td>
<td>800,000 pieces</td>
</tr>
<tr>
<td>Soc. Fundición del Pacifico Ltda.</td>
<td>Hardware²</td>
<td>US$ 50,000</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>US$ 1,150,000</strong></td>
<td></td>
</tr>
</tbody>
</table>

¹ Fittings: for bathrooms.
² Had already exported previously.
³ Already exporting when the Consortium was formed.
⁴ Hardware: sundry metallic products, handles and knobs for furniture, latches, etc.
⁵ NIBSA: 1920.

nature implies a great administrative effort and long gestation period before there is any glimpse of results. This discouraged some of the first companies from beginning the project. The businesses that ultimately began Ferrex Chile S.A. activities were the associates listed in Table 2.

Each of these companies committed a certain line of product and an export offering (expressed in dollars and numbers of units.) This information appears in Table 3. As can be observed, the size of the offerings is similar, but in practice there was a great deal of variation among the companies.

**Consortium Operations**

As mentioned earlier, the United States, Miami specifically, was selected as the center of Consortium operations. Reasons included the growth indices for Florida's economy, the rise in construction, the flow of maritime traffic facilitating transport from Chile, and the high percentage of Latinos in the area.

In January 1985, the direction of Ferrex Chile S.A. operations was assumed by Patricio Lioi, who was also the owner of one of the companies in the Consortium.

The Miami organization functioned independently from Chile and was called FERREX TRADING CO.¹ It had its own offices and warehouses and operated as an importer, distributor, or U.S. wholesaler. Personnel included two executives and a secretary. Initially U.S. personnel were hired and trained, but the difference in business styles between Chile and the U.S. market ultimately made it necessary to contract Chileans.

One very important factor contributing in large part to the Consortium’s successful start-up was that the Chilean Central Bank’s consent to prolonging the period for negotiating foreign currency earnings, in that the 90-day expiration period would begin from the time merchandise left the warehouse, not when it left the country.

Ferrex Trading Co. operated like a U.S. importer, receiving merchandise, dealing with the procedures for clearing customs, warehousing products, maintaining inventories, promoting sales through wholesalers and retailers, shipping out orders to customers, and finally returning earnings to Chile.

In Chile, Ferrex Chile S.A. was considered a service company. It coordinated all the tasks related to exporting, received orders from Miami and remitted them to the partners for processing, and prepared consolidated shipments from the members of the Consortium. It was also in charge of negotiating shipping rates, contracting space in the ships transporting merchandise to the port of destination, performing quality control with CESMEC, and making containers and graphics.

Ferrex Chile S.A. was also responsible for ensuring effective communication between the Miami office and partners in Chile and dealt with all the organizations that affected Chilean foreign trade in one way or another, such as PROCHILE, for the preparation of catalogues, the Central Bank, for negotiating foreign exchange earnings, and Customs, for declarations.

Each of the two companies was financed separately. Ferrex Chile S.A. depended on quotas from Consortium members, while Ferrex Trading Co. Inc. charged a 2.5% commission on the FOB value of each shipment of merchandise.

**U.S. Marketing**

**Product Changes**

Products exported by Ferrex Chile S.A. had low unit value and were difficult to differentiate. In general these were basic hardware items, from nails to hinges, and from metal screening to miscellaneous small hardware items. These types of prod-
The Brand

At the beginning of 1985, Chilean brands were still unknown in 99% of foreign markets. Nevertheless, when Consortium operations began, the companies associated were either exporting or had exported in the past (Table 3).

A decision was made to market all Consortium products under the umbrella brand of “Ferrex,” taking advantage of a uniform presentation for the entire line of products in order to create an image of quality. It was thought that this would result in greater sales in the future.

With this decision, marketing efforts concentrated on one brand. The idea was for the Consortium associates to maintain excellent relations and not be fighting among themselves to get a better position for their own brand name. Executives at Ferrex Trading Co. would be able to work without worrying about how much time they were spending on each of the associated companies. Having just one brand would avoid creating confusion in the mind of the U.S. consumer and hasten brand familiarity.

A difficulty arose as operations were being developed. American farmers, who represented an important percentage of the market, were systematically refusing to buy imported products. Ferrex solved the problem by acquiring the Ranger brand then available on the market. Barbed wire and other lines of fencing were marketed under this name, which was accepted by the farmers.

The Market

The market for Ferrex products included Miami, Atlanta, Savannah, Colombia, Boston, Los Angeles (home of the principal hardware company in the United States), and Puerto Rico.

The American market has separate and distinct characteristics from the Chilean market, and this made it difficult to penetrate. Quality and confidence were linked in this market. Any noncompliance with the conditions of a contract generated the same mistrust as a defective product.

Ferrex members had to meet technical and administrative demands imposed by the American business environment, and this required them to double their efforts.

An important factor in earning the confidence of the American consumer was the installation of a complete infrastructure with offices and warehouses. This helped win the necessary reputation and recognition for acquiring a better position in the market.

Performance of executives in Miami was essential in getting the large U.S. distribution chains interested in the Chilean products. Arnel and Prudential became two important Consortium customers, but obtaining their confidence always depended on strict compliance with agreements.

Lioi thought that all the work that had been done represented a valuable asset and would make it possible to win a few concessions in case he were to continue operations alone.

The Situation in August 1988

At the end of August, Mr. Lioi ran into a dilemma, one of the biggest he had faced since the Consortium was set up. His associates had been satisfied with the results of the Consortium and had not shown any interest in expanding operations. In addition, national profit margins were larger than those earned in the U.S. market, and Lioi had noticed that his associates did not seem very concerned with what was going on with the Consortium.

In Lioi’s opinion, there was untapped capacity in Ferrex operations, and he was optimistic in thinking that with a little more effort the Consortium could move more volume. On the other hand, he was aware of the prestige they were earning in the American market, which led him to think about the possibility of offering new products, although still within the metal-mechanical line.

This presented a problem, since these types of new products would mean bringing in articles from companies outside the Consortium, which would not be very well received by his associates.

Lioi felt that the distributors Arnel and Prudential represented an opportunity to eliminate the storage facilities in Miami and consequently free up resources needed for financing the new stage of expansion that he visualized. That way the partners would not need to make any more contributions. It had been made clear to Lioi that they were unwilling to continue investing in the Consortium and in fact were expecting higher profits.

Selling off the warehouse would turn Ferrex Trading Co. into a straight wholesaler and would thus demand higher

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2 Two large wholesalers that together cover entire country.
levels of production from each of the members in order to comply with orders for full containers.

Lioi had a lot of projects in mind for Ferrex, but they all depended on what his partners thought. He had established very good relations with them and did not forget that this had been a determining factor in the Consortium’s success.

One fact was clear to Lioi and in some ways made him understand his associates’ reluctance to expand U.S. sales: since Chile’s departure from GSP their margins in the U.S. market had fallen, making domestic sales more attractive.

With the passing of time, operating conditions for the U.S. administration were changing, and this was what concerned Lioi most. The Miami company had become simply an office that handled part of the associated companies’ international sales. The size of the companies, which was too varied, kept Inchalam, for example, from carrying out its exports through Ferrex and it reserved the privilege of direct sale in some areas of the U.S.

The changes Lioi wanted to make included transforming the nature of the company and making it into a real, profit-making trading company that would have a life of its own. Instead of being limited to the products of Consortium associates, this would mean that Ferrex Trading would be able to widen its range of products and the countries providing these products.

The problem for Lioi was how to communicate his ideas to the rest of the partners and get the support he needed. A meeting had already been called for the next day, but he still wasn’t clear what he would say to them. He thought he would begin by presenting the projects for Ferrex’s future and watch their reactions: if they were positive, he would put his ideas into action. The difficulty would be if these were rejected, since he had already come to the decision that he would resign from the Consortium if this occurred.

Another possibility was to arrive at this meeting and announce with a tone of decision that, given the large concentration of sales, he was no longer willing to continue financing operations for the others. If the partners were unable to understand the situation, he had thought of the possibility of taking control of the company and buying the others out. This implied a great deal of risk, however, and Lioi knew that such a course could destroy his good relations with them and he would lose the dynamism that comes from union and pursuing common interests together.

### Teaching Note

#### Case Purpose and Teaching Objectives

The purpose of this case is to explore the export consortium as an option for the increased competitiveness of Latin American products in world markets. The teaching objectives are:

1. To understand the difficulties faced by some Latin American manufacturers upon deciding to penetrate international markets.
2. To analyze and discuss different options for penetrating international markets, including various types of alliances.

#### Suggested Questions for Discussion

1. Why did the six Chilean hardware manufacturers decide to form a consortium?
2. What is your evaluation of the organization and operation of the consortium?
3. What problems does Mr. Patricio Lioi face in 1988? What actions should he take?
4. What lessons might we learn from this consortium experience as a means of penetrating international markets?

### Case Analysis

**WHY DID THE SIX CHILEAN HARDWARE MANUFACTURERS DECIDE TO FORM A CONSORTIUM?**

In January 1985 the Chilean economy was in deep recession, and the construction industry particularly was hard hit. These hardware companies had exported in the past and formed part of an exporters’ association. Faced with declining domestic sales, the option of further penetrating international markets was attractive. However, the individual companies (with the exception of one) did not have the resources to market their own brands or to obtain significant participation. Moreover, these companies had complementary product lines, so that each would benefit from a consortium that offered a broad line and that could achieve significant economies in promotion and distribution, as well as advertising with an umbrella brand, Ferrex. However, the companies were heterogeneous in size and in previous export experience.

**WHAT IS YOUR EVALUATION OF THE ORGANIZATION AND OPERATION OF THE CONSORTIUM?**

The consortium was organized after a careful planning process, something that was relatively rare for private business associations in Chile. This process included four discrete stages in which market and legal studies were carried out, there was widespread participation in trade fairs to get to know the markets firsthand, technical assistance in international quality standards was sought, and eventually an organizational structure was decided upon. Throughout this process the consortium members enlisted the support of government agencies including a public export promotion agency, PROCHILE; and the Central Bank of Chile.

The organization that was set up eventually included a company in Chile that adapted products and ensured quality standards and an importer in Miami that was responsible for marketing. The setting up of offices and a warehouse in the United States was a key factor in reducing working capital needs, providing rapid service to customers, and in bolstering buyer confidence. Initial problems were encountered with the
hiring of employees in the U.S. who were culturally incompatible with parent organization, so that personnel changes had to be made and Chileans were hired. Such cultural differences should be considered when the decision to internationalize is made.

**WHAT PROBLEMS DID MR. PATRICIO LIOI FACE IN 1988? WHAT ACTIONS SHOULD HE HAVE TAKEN?** The consortium was successful in market penetration but most products sold were manufactured by two of the six companies. The other four companies had not complied with their export commitments, apparently because the Chilean economy had recovered, and they preferred to sell in the domestic market at higher margins. Mr. Lioi believed that this was shortsightedness. Much effort had been made to build a brand in the U.S. market with considerable growth potential. He then had to decide how to deal with the reluctant consortium members.

Some options that arose are the following:

1. Persuade the reluctant members to comply with their export commitments.
2. Replace the reluctant members with new consortium partners.
3. Offer to buy the shares of the reluctant members.
4. Consider an alternate distribution system in the U.S.

Mr. Lioi could not allow the achievements of the consortium to be lost because of the shortsightedness of some of its members who were currently enjoying higher margins in the domestic market. He needed to make decisions that ensured the continuity of consortium operations in the United States.

The advantage of persuading the reluctant members is that they have complementary product lines, and it may be difficult to find new members to replace them. Though margins in the United States are lower, the growth potential is enormous. Moreover, the members simply provide products to Ferrex Chile without having to worry about marketing. A simulated classroom negotiation can be used to bring out the advantages and disadvantages of remaining in the consortium.

If Mr. Lioi had been unable to persuade the reluctant members, he could have offered to buy their shares. However, he could have decided to let them keep the shares, in the hope that they would eventually see the benefit of exporting. This would have made it easier for them to rejoin the consortium, say, in the event of another economic downturn.

Finally, Mr. Lioi had to decide whether to cut fixed costs by eliminating the warehouse and signing contracts with two nationwide distributors. Such contracts would enable the consortium to increase sales volume. However, the benefits must be weighed against the risk that he may not have been able to comply with the orders in terms of volume or variety.

**WHAT LESSONS MIGHT WE LEARN FROM THIS CONSORTIUM EXPERIENCE AS A MEANS OF PENETRATING INTERNATIONAL MARKETS?** This case provides a number of ideas to Latin American businessmen who do not see any possibility of penetrating international markets alone. A consortium may do a number of things that an individual company may not be able to, including detailed market research, negotiating technical services agreements, setting up an office or warehouse overseas, undertaking advertising campaigns, and building brand recognition. Uniting forces in the consortium has enabled the member companies to do all of these things.