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# WORLDWIDE CASE COMPETITION

*Sample Case Analysis #1*

Qualification Round submission from the
2016 NIBS Worldwide Case Competition, San Antonio, Texas, USA

**Case:** *Mindray Medical International Limited: Going Global from China*

# MINDRAY MEDICAL INTERNATIONAL LTD.

## *Growing in America*

*Submission prepared for the Qualifying Round of the*
**2016 Network of International Business Schools**
**Worldwide Case Competition**
St. Mary's University

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Word count: 1,486

## Introduction & Situation Synopsis

Mindray Medical International Limited (Mindray) has been successful in growing from a China-focused medical device manufacturer (MDM) into an international player. However, the company currently faces challenges expanding in the United States. To fulfill its long-term goal of becoming a global leader, Mindray must determine the best strategy for growth in the U.S.

## External Analysis

### *The U.S. Market*

As the largest market for healthcare at 42% of global expenditures, the U.S. represents an attractive market for MDMs. However, distribution of medical equipment in this market differs markedly from other areas of the world (i.e., professional technicians procure the products instead of doctors, and the direct sales model is widely employed), which represents a challenge for foreign MDMs. **To operate successfully within the U.S., MDMs must understand this specific market's needs.**

### *Competitive Landscape*

Key success factors in the MDM industry are investment in research & development (R&D), strong distribution channels, and economies of scale to benefit from cost efficiencies (Appendix 1). A trend in the MDM industry is the development of ultrasound products, where competition is becoming increasingly consolidated. **As R&D is an industry norm, competitors must differentiate themselves via an appealing value proposition.**

### *Datascope*

Datascope has seen 4.24% year-over-year revenue growth from 2004-2006. During this time, its stock price has declined by 11.85% and earnings before interest, tax, depreciation and amortization (EBITDA) have shrunk by 1.5% year over year. These declines are attributable to an increase in cost of goods sold (COGS) which has been outpacing revenues, hindering profit growth. **Unless something is done, we believe Datascope's inefficiencies in managing costs will continue to fuel shareholder uncertainty, leading to further decline in share price.**

## Internal Analysis

Mindray has adopted a mid-cut strategy which enables the company to cater to price sensitive clients who seek a superior quality-price ratio, along with functionality and performance. This strategy has also allowed Mindray to differentiate itself from its global competitors using cost efficiencies as a competitive advantage (Appendix 2). As such, Mindray relies on the quality of its employees to drive its technical advances and innovation. **Mindray has a strong company culture, but has difficulty hiring employees outside of China and must consider adapting its human resources (HR) strategies internationally.**

## Analysis of Alternatives & Recommendations

The decision at hand involves identifying a means to strengthen Mindray's presence in the U.S. market. Three alternatives have been identified to satisfy this goal. Each must be weighed against four key decision criteria: time to implementation, fit with long-term objectives, likelihood of success, and opportunities for synergies. In accordance with Mindray's long-term goal to become a global leader, the deal-breaker criteria are the fit with long-term objectives and the likelihood of success (Appendix 3).

### *Alternative 1: Build Own Distribution Network*

If Mindray were to develop a distribution network in the U.S. by itself, it would be able to leverage the lessons learned to improve sales and distribution worldwide. However, establishing an effective distribution network would require at least twice as much time as acquiring one, since distribution channels in the U.S. are currently saturated and Mindray has no experience in distributing to professional technicians. Additionally, Mindray's past efforts to distribute in the U.S. have not yielded the desired results due to a lack of understanding of the market. **Further relying on its own capabilities to grow in the U.S. will likely render Mindray's distribution unsuccessful.**

### *Alternative 2: Acquire Datascope*

Acquiring Datascope would require time to integrate operations and the workforce, but would provide Mindray with a solid market share and strong distribution in the U.S. In addition, Datascope would benefit from Mindray's competency in cost efficiency (making them receptive to an acquisition offer), while Mindray could benefit from Datascope's distribution and sales skills. The high risk of failure among acquisitions poses a threat, but the use of an integrative HR approach will mitigate this risk. **The distribution capabilities gained from this acquisition can be utilized in the long-term to build Mindray's global distribution, helping it to become a global leader.**

### *Alternative 3: Strategic Alliance with SonoSite*

Mindray could also ally itself with SonoSite, a Level II ultrasound U.S. manufacturer, to capitalize on the current trend of ultrasonic product development. SonoSite would give Mindray access to its U.S. distribution network to sell its patient monitoring products, and Mindray would manufacture Sonosite's ultrasound devices in China. Establishing this alliance would involve a time delay; however, the potential synergies would improve the likelihood of success of such an agreement. **Beyond the duration of this alliance, this strategy would not help Mindray achieve its goal of becoming a global leader.**

## Recommendation

Mindray should pursue growth in the United States by acquiring Datascope, thereby gaining access to the latter's distribution capabilities.

## Implementation Plan

The following three-phase implementation plan, named A.I.D (Acquire, Integrate and Develop) will allow Mindray to grow its presence the U.S. by leveraging Datascope's salesforce and expertise in the American market (Appendix 4).

### *Phase 1: Acquire (0 – 6 months)*

Mindray should call a shareholder meeting to discuss the plan to acquire Datascope and hold a vote to solicit shareholder approval. Mindray can then enter into acquisition talks with the investment bank and Datascope. Mindray should offer a premium of 15% to 25% on Datascope's current share price (Appendix 5) in order to acquire a majority stake (51%). Following an initial agreement, Mindray should complete its due diligence process and submit the acquisition for approval by the various U.S. regulatory boards.

### *Phase 2: Integrate (6 months – 2.5 years)*

Once the acquisition has been finalized, Mindray will need to consider the integration of its people, operations, and practices into the existing business.

**Human Resources.** To ensure the successful integration of Datascope and Mindray and mitigate the risks created by cultural differences, Mindray should adopt an integrative HR approach. Mindray will need to adapt some of its Chinese HR practices to the cultural differences of the U.S. market, but should maintain policies that emphasize teamwork, personal responsibility and quality. This will ensure that U.S. employees are able to integrate successfully into Mindray's culture. Cultural training will also be necessary for both Chinese and American employees to increase synergies within the workforce. To further cultivate these synergies, cross-cultural teams composed of both Chinese and American employees should be created both in sales and R&D. This will facilitate the transfer of knowledge and expertise between employees. Language courses in Mandarin and English should be offered to American and Chinese employees to diminish the risk of a potential language barrier (Appendix 6).

**Operations.** Mindray should absorb the operations that Datascope currently outsources to its Chinese facilities in order to increase cost efficiencies. Mindray should also leverage its integrated HR practices to create a cross-cultural R&D team and develop customized products for the U.S.

**Sales.** To gain a better understanding of the U.S. market and to learn from Datascope's salesforce, Mindray should establish a communication channel between the salesforce and Mindray's R&D team. This will enable Mindray to gain knowledge of the current trends within the U.S. medical industry and adapt its product for the U.S. By using Datascope's sales expertise and Mindray's R&D strength, they will be able to capitalize on the newly created synergies to grow Mindray's presence in the U.S.

### *Phase 3: Develop (2.5 years +)*

Following the successful integration of Datascope and Mindray, the company should focus on launching improved products for the U.S. markets. New developments in R&D for modular designs and product integration will be key to selling new Mindray products to current Datascope customers. Mindray should also begin to rebrand Datascope's products and continue developing its current product line, tailored to the U.S. market. Using Datascope's effective sales and distribution channels, Mindray should also be able to improve sales of its ultrasound product segment in the U.S.

Mindray will be able to capitalize on Datascope's worldwide salesforce by further pushing its current and updated product line through Datascope's distribution channels in Europe and Japan. This will support their long-term strategy of becoming a global player.

### *Risks & Mitigation*

The most significant foreseeable risk is that Mindray's offer could be refused by Datascope shareholders. Although the offer has been calculated on the basis of the expected synergies that would materialize from the acquisition, Mindray should be prepared to offer a higher price (up to 30% premium on the current share price), or propose to buy only Datascope's patient monitoring business segment (Appendix 7).

## Financial Analysis

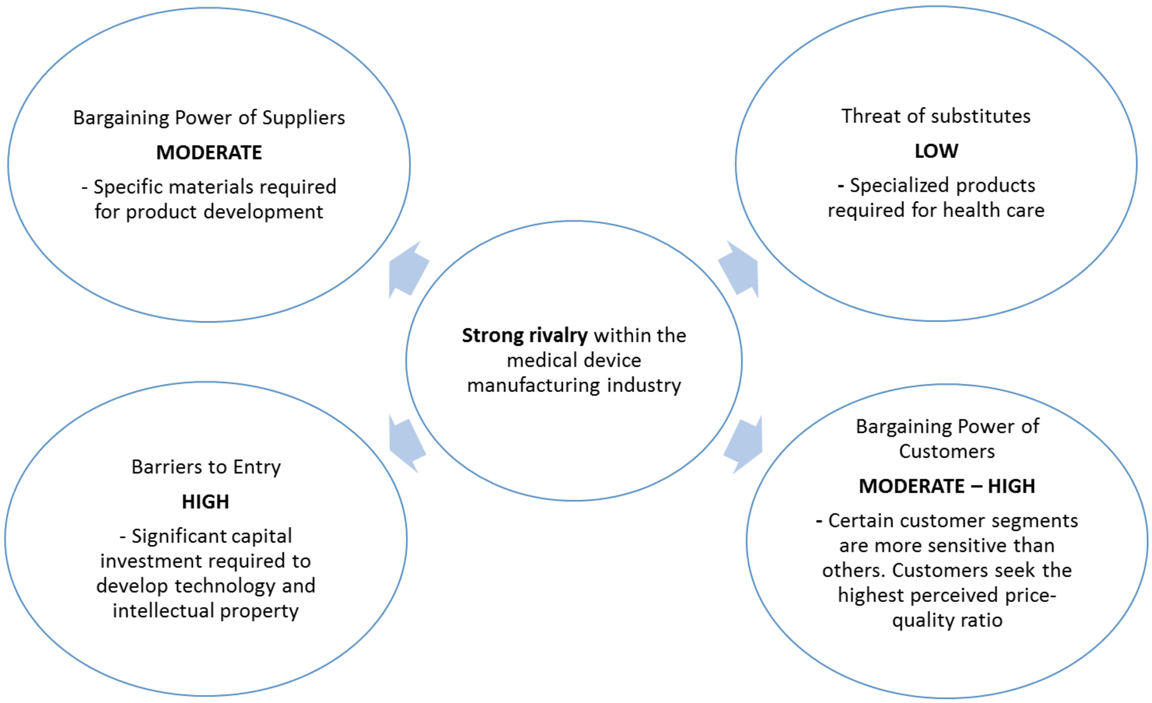
Mindray's cost efficiencies will enable Datascope to achieve a 12.86% profit margin. Datascope was conservatively valued at US$36.76 per share, without accounting for the company's distribution capabilities in the United States. With the synergies from this acquisition, Mindray can expect to increase Datascope's share value to US$39.05 (Appendix 8).

## Conclusion

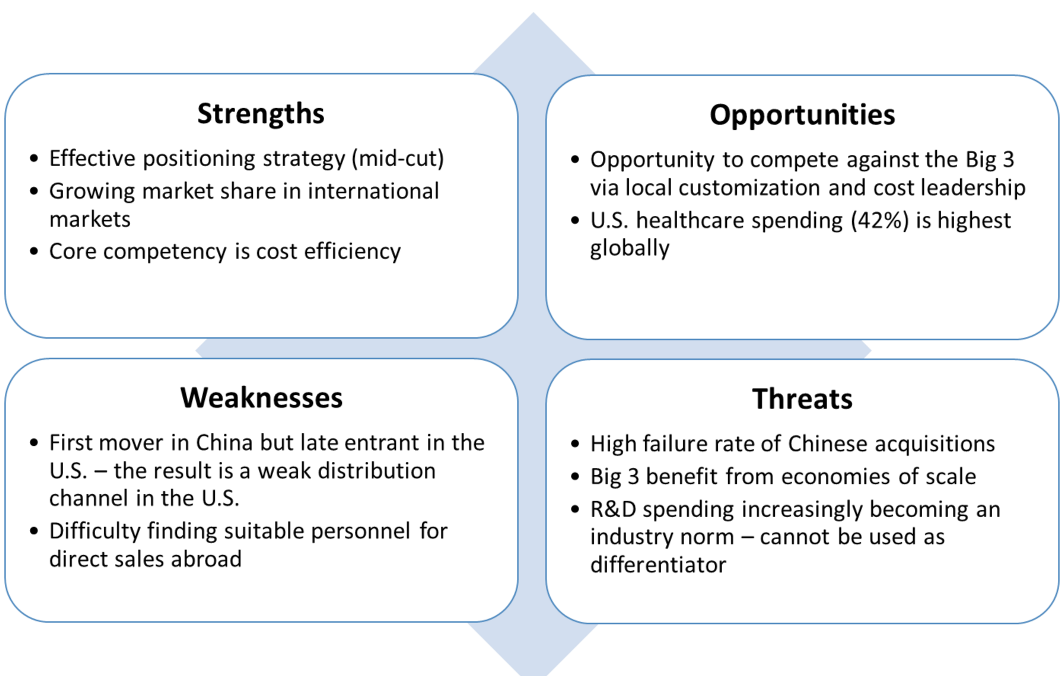
Acquiring Datascope will allow Mindray to gain access to distribution capabilities in the U.S. In the long-term, this strategy will prepare Mindray for product development and growth in markets outside the U.S. to help it become a global leader.

## Appendices

### *Appendix 1: Porter's Five Forces*




### *Appendix 2: SWOT Analysis*



### *Appendix 3: Decision Matrix and Key Decision Criteria Description*

| | Build Own Distribution Network | Acquire Datascope | Strategic alliance with SonoSite |
|---|---|---|---|
| Time to implementation | 1 | 2 | 2 |
| Fit with long-term objectives* | 3 | 3 | 1 |
| Synergy potential | 1 | 3 | 2 |
| Likelihood of success* | 1 | 2 | 3 |
| **TOTAL** | **6** | **10** | **8** |

** Deal-breaker criteria: fit with long-term objectives and likelihood of success*

| Key Decision Criteria | Description |
|---|---|
| Time to implementation | As Mindray has seen little success since its introduction into the U.S., the proposed strategy should provide results in a reasonable amount of time |
| Fit with long-term objectives | Mindray aims to become a global leader, so the proposed strategy should enable the company to achieve those goals beyond the U.S. |
| Synergy potential | Mindray should pursue a strategy that leverages its core strength of cost efficiency and improves its sales of monitors in the U.S. |
| Likelihood of success | Mindray must consider the feasibility of all strategies, taking into consideration internal factors (i.e. past efforts) and external factors (i.e. high failure rate of acquisitions) |

### *Appendix 4: Implementation Timeline*

| Implementation | | Months | | | | Years | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | 3 | 6 | 9 | 12 | 1.5 | 2 | 2.5 | 2.5+ |
| A | Shareholder approval | | | | | | | | |
| A | Negotiations with investment bank | | | | | | | | |
| A | Regulatory board approval | | | | | | | | |
| A | Finalize acquisition | | | | | | | | |
| I | HR integration | | | | | | | | |
| I | Operations transfer | | | | | | | | |
| I | Establish communication channels | | | | | | | | |
| I | Structure cross-cultural R&D team | | | | | | | | |
| D | Modular product redesigns | | | | | | | | |
| D | Datascope product rebranding | | | | | | | | |
| D | Global product development | | | | | | | | |

### *Appendix 5: Datascope Acquisition Share Price*

| Company Acquisition Price Premiums | | | | |
|---|---|---|---|---|
| Premium | 15% | 20% * | 25% | 30% |
| Implied Share Price | $ 35.47 | $ 37.01 | $ 38.55 | $ 40.09 |
| Shares Outstanding | 18,720,000 | 18720000 | 18,720,000 | 18,720,000 |
| Company Value | $ 663,923,520.00 | $ 692,789,760.00 | $ 721,656,000.00 | $ 750,522,240.00 |
| Acquisition Prince(51%) | $ 338,600,995.20 | $ 353,322,777.60 | $ 368,044,560.00 | $ 382,766,342.40 |

* Ideal acquisition price

### *Appendix 6: Human Resource Initiatives*

| Initiative | Goal |
|---|---|
| Cross-cultural teams | To encourage collaboration |
| Language courses in Mandarin and English | To reduce language barriers |
| Expatriate mandates to both U.S. & China | To encourage collaboration and integration |
| Add collaboration criteria to all employees performance evaluations | To ensure that employees actually collaborate |

### *Appendix 7: Risks and Mitigation*

| Risk | Mitigation |
|---|---|
| Conflicts within cross-cultural teams | Implement diversity training and conflict resolution training |
| | Set up collaboration criteria in yearly performance |
| Team integration challenges | Create a transition team composed of HR and managers to pay special attention to team integrations |
| Datascope does not accept Mindray's acquisition offer | Prepare a higher offer (up to 30% premium on the current share price), or propose to buy only Datascope’s patient monitoring business segment |
| Quality control issues from early team integration | Implement additional quality control measures |

## *Appendix 8: Financial Analysis*

| Datascope Consolidated Income Statement | | | | | | |
|---|---|---|---|---|---|---|
| In US Millions (unless indicated) | | | | | | |
| | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
| Cardiac Assists | $ 273.70 | $ 288.60 | $ 319.38 | $ 367.29 | $ 422.38 | $ 485.74 |
| Vascular Products | $ 30.90 | $ 34.60 | $ 51.84 | $ 67.39 | $ 87.61 | $ 113.89 |
| Corporate and other | $ 38.70 | $ 29.50 | $ 1.59 | $ 1.26 | $ 0.99 | $ 0.78 |
| Total Revenue | $ 343.30 | $ 352.70 | $ 372.81 | $ 435.94 | $ 510.98 | $ 600.41 |
| *Growth (YOY %)* | *4.57%* | *2.74%* | *5.76%* | *17%* | *17%* | *18%* |
| COGS | $ 140.48 | $ 147.26 | $ 163.86 | $ 174.37 | $ 194.17 | $ 216.15 |
| *COGS as % of Revenue* | *40.92%* | *41.75%* | *43.95%* | *40.00%* | *38.00%* | *36.00%* |
| Gross Profit | $ 202.82 | $ 205.44 | $ 208.95 | $ 261.56 | $ 316.81 | $ 384.26 |
| *Gross Margin* | *59.08%* | *58.25%* | *56.05%* | *60.00%* | *62.00%* | *64.00%* |
| HR Budget | $ - | $ - | $ - | $ 1.84 | $ 2.11 | $ 2.43 |
| Operating Expenses | $ 152.28 | $ 158.53 | $ 159.88 | $ 189.63 | $ 214.61 | $ 246.17 |
| EBITDA | $ 50.54 | $ 46.91 | $ 49.07 | $ 70.09 | $ 100.08 | $ 135.67 |
| Depreciation | $ 7.17 | $ 7.01 | $ 6.57 | $ 7.06 | $ 8.98 | $ 11.34 |
| Interest | $ 4.30 | $ 11.17 | $ 1.94 | $ 5.80 | $ 6.09 | $ 6.39 |
| Taxes | $ 15.16 | $ 14.07 | $ 14.72 | $ 21.03 | $ 30.03 | $ 40.70 |
| Net Income before XO | $ 23.91 | $ 14.65 | $ 25.84 | $ 36.21 | $ 54.99 | $ 77.24 |
| *Profit margin* | *6.96%* | *4.15%* | *6.93%* | *8.31%* | *10.76%* | *12.86%* |

| Valuation | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Discounted Cash Flow to Firm | | | | | | | | |
| | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | TV | |
| EBITDA | $ 50.54 | $ 46.91 | $ 49.07 | $ 67.54 | $ 83.58 | $ 105.83 | | |
| Depreciation | $ 7.17 | $ 7.01 | $ 6.57 | $ 7.09 | $ 8.78 | $ 11.11 | | |
| EBIT | $ 43.37 | $ 39.90 | $ 42.50 | $ 60.45 | $ 74.80 | $ 94.72 | | |
| Less: Cash Taxes | $ 13.01 | $ 11.97 | $ 12.75 | $ 18.13 | $ 22.44 | $ 28.42 | | |
| **NOPAT** | **$ 30.36** | **$ 27.93** | **$ 29.75** | **$ 42.31** | **$ 52.36** | **$ 66.30** | | |
| Less: Capex | $ 6.83 | $ 6.68 | $ 6.26 | $ 6.75 | $ 8.36 | $ 10.58 | | |
| Plus: Depreciation | $ 7.17 | $ 7.01 | $ 6.57 | $ 7.09 | $ 8.78 | $ 11.11 | | |
| Less: Change in WC | -$ 1.01 | -$ 1.96 | $ 7.31 | $ 8.27 | $ 9.21 | $ 10.32 | | |
| **Free Cash Flow to Firm** | **$ 31.71** | **$ 30.22** | **$ 22.75** | **$ 34.38** | **$ 43.57** | **$ 56.51** | **$ 731.10** | **3.5%** |
| | | | | | Shares outstanding | | 18,720,000 | |
| | | | | | Implied price per share | | $ 39.05 | |

| | WACC | | | | | |
|---|---|---|---|---|---|---|
| Terminal Growth | | 11% | 12% | 12% | 13% | 13% |
| | 2.0% | $ 640.45 | $ 606.74 | $ 576.41 | $ 548.96 | $ 524.01 |
| | 2.5% | $ 681.45 | $ 643.59 | $ 609.72 | $ 579.23 | $ 551.65 |
| | 3.0% | $ 727.57 | $ 684.77 | $ 646.73 | $ 612.69 | $ 582.06 |
| | 3.5% | $ 779.85 | $ 731.10 | $ 688.10 | $ 649.87 | $ 615.67 |
| | 4.0% | $ 839.58 | $ 783.61 | $ 734.64 | $ 691.42 | $ 653.01 |

| Assumptions | | |
|---|---|---|
| **Category** | **Rate** | **Explanation** |
| **Revenue Growth** | | Based on historical growth rates |
| Cardiac Assist/Monitoring | 15% | |
| Vascular Products | 30% | |
| Corporate and other | -21% | |
| **COGS** | 40%-36% | Decreasing by 2% each year as cost-cutting measures are implemented |
| **Operating Expenses** | 43.5%-41% | Beginning at 43.5% of total revenue, decreasing to 41% as cost-cutting measures are implemented |
| **Capital Expenditure** | 10% | Percentage of total revenue based on industry average |
| **WACC** | 11.50% | Based on industry average, sensitivity analysis reflects how sensitive Datascope is to this rate |
| **Terminal Growth Rate** | 3.50% | Based on industry average |
| **Tax Rate** | 30% | Assumed based on regional average |
| **Shares Outstanding** | 18,720,000 | Based on 2006 market capitalization/price per share |