Death Goes Global:
An Examination of Foreign Direct Investment in the Death Care Industry

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ABSTRACT

We present a case study—the U.S. death care industry—that largely violates the assumptions of foreign direction investment (FDI) theory. Based on this anomaly, we develop several questions to help us understand whether this is a unique case, whether other anomalies may also exist, and what this might mean for FDI theory. We hope to generate discussion to help us answer these questions.
The decision to undertake (no pun intended) foreign direct investment (FDI) is a complicated firm-level process. To operate in a foreign market, a firm must obtain a certain minimum stock of economic, social, legal, and cultural knowledge, such as is essentially inbred in indigenous competition, but may be quite costly for foreigner firms to obtain (Caves, 1971). Said differently, entering firms must overcome a liability of foreignness that, all other things being equal, places incoming firms at a disadvantage relative to domestic firms.

To overcome this barrier to entry, a foreign firm contemplating FDI must possess some sort of unique advantage that its domestic rivals do not (Hymer, 1960). This unique advantage often takes the form of an intangible asset with a public good characteristic; i.e., high fixed startup costs and nominal or zero marginal costs (Caves, 1971). The rents accruing to this intangible asset may offset the costs associated with the liability of foreignness. Caves (1971) also points out that the firm must find FDI preferable to exporting or licensing, lest these options be used, since it is considered preferable, all else equal, to utilize the lowest level of ownership.¹

These traits point to product differentiation as a characteristic of the type of market in which a firm prone to FDI would exist. The successful differentiated producer has special knowledge about serving a market that allows it to earn excess profit, and this knowledge can be transferred to another market with little or no marginal cost (Caves, 1971). These traits are also indicative of oligopoly as a market characteristic of FDI-likely firms (Caves, 1971). FDI entails a large fixed setup cost, so larger firms are more easily able to spread this cost, and thus more likely to employ FDI than a small firm. In addition, scale economies in production or sales in the home market for a differentiated product suggest that a firm would not move abroad until all

¹ The rationale is the same as used by Coase (1937) to explain the theory of the firm. That is, without a market imperfection, it is preferable (less costly) to use the market mechanism rather than internalize.
profitable domestic opportunities have been exhausted, and thus the firm is likely to be relatively large with few competitors in the home market when it decides to go abroad.

However, the $12 billion\(^2\) domestic death care industry\(^3\) is not characterized by differentiation or oligopoly, yet firms within it are expanding internationally via FDI at a rapid pace. The largest international death care firm, Service Corporation International (SCI), has expanded from its home in Houston, Texas, to gain holdings all across North America, Europe, and the Pacific Rim. In 1995, SCI purchased Pompes Funebres Generals SA, Europe’s largest death care company, which also had holdings in the Pacific Rim, as well as Gibraltar Mausoleum Corporation, which was then North America’s fourth-largest death care company (M&A Report, 1996). Throughout the year, SCI acquired 1,204 funeral homes, 99 cemeteries, and 29 crematoria, greatly increasing its total holdings to 2,795 funeral homes, 324 cemeteries, and 138 crematoria (Breyer, 1996). SCI continued its acquisition frenzy unabated into 1997, expecting it to be its biggest year yet (IPO Reporter, 1997). Loewen\(^4\), the second largest international death care chain, spent nearly a billion dollars on acquisitions of funeral homes and cemeteries in 1996, almost double its $600 million in annual revenues (Larson, 1996).

The domestic death care industry is a highly fragmented industry dominated by independent operators, with family-owned funeral homes often passing from one generation to the next. The four largest death care firms in the US as of 1996--SCI, Loewen, Stewart

\(^2\) As stated by Breyer (1996). Other figures: $25 billion (Horn, 1998), $15 billion (Economist, 1996), $10 billion (McLean, 1997), and $7 billion (Newman, 1997).

\(^3\) The death care industry is typically said to comprise funeral services, cemeteries, crematoria, urns, caskets, and memorials (IPO Reporter, 1997).

\(^4\) Technically not a US firm (based in Vancouver, Canada), but Loewen competes in most of the same US markets
Enterprises Inc., and Equity Corp. International--together comprised just 8 percent of the overall domestic market\(^5\) (M&A Report, 1996). Death care chains are the exception, not the rule, and form a small portion of an otherwise highly fragmented industry.

Because of its peculiar features, differentiation is somewhat hard to characterize in the death care industry. The death care industry has three characteristics that make consumer comparison shopping unlikely\(^6\): ignorance, sentiment, and taboo (Economist, 1997). Ignorance, as well as inexperience, often leaves many buyers at the mercy of the undertaker, who is blindly trusted as if he were a doctor, not a salesman. The good fortune of inexperience at arranging funerals for loved ones is a double-edged sword when it comes to knowledge of the reasonableness of prices and the necessity of add-ons like embalming and sealed coffins. Further, given that this is normally a distress purchase, requests for second opinions are rare. Sentiment puts more upward pressure on spending. Who wants to seem like a cheapskate when arranging a loved one’s funeral? In addition, the costs may be coming out of the estate or from an insurance policy, so the buyer does not feel as if she’s spending out of her own pocket. Finally, taboo creates a void between necessity and tradition. Many of the trappings of a funeral are simply not needed, but the buyer feels uncomfortable bringing up questions of religious interpretation.

Due to these features, it seems highly unlikely that most funeral homes could

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\(^5\) Another estimate places the total at “less than 9%” (McLean, 1997), while a third states, “close to 13%” (Breyer, 1996). Regardless, the industry has low concentration.

\(^6\) Trends are changing with the advent of pre-planned funerals and FTC-mandated and increasingly enforced public pricing lists (Cavanaugh, 1996).
distinguish themselves on anything other than proximity to the deceased’s home. Most funeral homes meet a threshold level of “poshness” and provide all the other features that someone, especially when making a distress purchase, would find acceptable enough to at least not have incentive to search further. Granted, there are certain funeral homes in many larger cities that cater to “high profile” clientele, but this is a niche market.

By and large, the domestic death care industry is not a differentiated market, nor is it an oligopoly. Yet firms within it are expanding internationally through FDI. In the remainder of this paper, we point out how the case of the death care industry deviates from the tenets of long-standing FDI theory. We culminate with several questions for discussion that explore whether the case of the death care industry is unique, whether such anomalies exist in other industries, and whether there is need to reexamine FDI theory.

**Explaining Domestic Expansion**

The US death care industry is highly fragmented, but some chains have made massive inroads toward oligopolization of parts of the domestic market. Several states’ funeral markets were more than more than 20 percent owned by the top two chains, SCI and Loewen Group: Hawaii (31%), Nevada (24%), Florida (23%), and Texas (21%) (Market Share Reporter, 1997). The Austin-American Statesman, in its June 7, 1996 edition, touts the prediction of an unnamed Texas funeral director in its headline: “Four companies predicted to own about 60% of US funeral [sic] within 15 yrs” (Breyer, 1996). This prediction may be overly optimistic due to antitrust concerns addressed later in this paper, but clearly, consolidation is alive and well.

Building a death care empire entails significant costs. Funeral homes are, by their very nature, a sort of monopoly based on location. Families normally select a funeral home based not on cost considerations, but proximity (Newman, 1997). Said less tactfully by the CEO of a coffin dealership, consumers will select “whoever can get Mama out of the living room fastest”

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7 Six other states were in the range of 14 to 20 percent owned by these two chains.
(Newman, 1997). Jeff Spillane, SCI’s managing director of operations analysis, acknowledges that SCI takes account of this need “to be close to people’s homes,” and estimates this area to be, in general, about a 5- to 10-mile radius. However, “In West Texas, New Mexico, or rural Pennsylvania, the market area might extend as far as 30 miles away, because people will drive that far. But in New York City, it’s more like a four- or five-block radius” (Spiegler, 1995).

It is possible that a market, as defined by the radius, is underserved, but in all likelihood, unless a tremendous change in demographics occurs, existing funeral homes can meet market demand. This makes the prospects for new entry grim. Other factors make the prospects even grimmer:

- Starting a new funeral home is difficult and costly. Land costs, zoning regulations, and not-in-my-back-yard protests are deterrents to establishing new cemeteries and crematoria and, to a lesser extent, funeral homes (M&A Report, 1996).

Because of the difficulties of building new facilities, the death care industry has turned to acquisition. Due to the barriers to entry and the battle between chains for new markets, existing facilities command a significant premium when acquired. Chains often attempt to take over other chains to “get more bang for the buck” (IPO Report, 1997) instead of buying independent homes one at a time. SCI and Loewen often compete head-to-head for the same acquisitions, creating such animosity that when SCI attempted a hostile takeover of Loewen, SCI offered a 39 percent premium, yet was still unsuccessful (Economist, 1996). What makes expansion through acquisition so desirable?

Economies of scale and scope are the driving forces behind acquisitions in the death care industry. Robert Waltrip, CEO of SCI, took note of the high fixed cost, low volume nature of the industry and implemented the concept of the “cluster” to minimize costs. According to Waltrip, “There were always peak periods when there weren’t enough facilities and people, and then times when everyone was sitting around playing cards. So it stood to reason that you could spread out some expenses and centralize others,” (Galarzo, 1995). To do this, you must own several facilities within a region, forming a cluster. Funeral homes within this cluster act as
independents, often maintaining the original name and management. However, they centralize to share costly resources such as hearses, embalming facilities, crematoriums, and even coffin manufacturing. For SCI, this drops operating expenses from the industry average of 65 percent to just 54 percent (Galarzo, 1995), adding considerably to the bottom line of a firm in an industry said to be up to 80 percent fixed costs (Jacob, 1992).

The following description of SCI’s Houston operations illustrates how a cluster maximizes the use of expensive resources:

In Houston, for instance, a single transport location with 13 gleaming hearses and 12 limousines serves 14 funeral homes in the area. Night calls to the 14 homes get forwarded to the limousine center, where a single employee is on duty. Instead of employing an embalmer at every site, SCI consolidates the function at one. Houston headquarters handles accounting, and administration runs through six regional centers (Jacob, 1992).

It is easy to see how the addition of a fifteenth funeral home to the Houston cluster would boost income without substantially increasing operating costs, and thus why SCI would be willing to pay a premium for the additional home.

Size also equates to buyer power in the market for funeral goods, the most expensive of which is the casket. It is estimated that the average funeral home buys only 60 caskets per year, while the larger chains may buy in excess of 100,000 (McLean, 1997). Through bulk purchases, SCI cuts its cost of goods to just 15 percent, which is well below the 23 percent industry average (Galarza, 1995).

Another way to take advantage of size is to vertically integrate into other high-margin funeral products, then bundle the goods into a single funeral package (Economist, 1997). Traditionally coffins and grave markers were not purchased through funeral homes. Instead, firms who offered these goods had to market them separately, and marketing of such goods was not always easy. By vertically integrating, these goods can be bundled, saving marketing costs, and allowing the funeral home to grab the high markup (Economist, 1997).

For Service Corp., the real gravy is in the so-called add-on merchandise: Caskets,
generously marked up by 200% to 400%, run as high as $99,000. Then there are memorial busts ($7,500 and up) and grave site monuments ($295 to $40,000). “We give them the choices and they’re willing to pay for them,” says Waltrip [CEO of SCI] (Galarza, 1995).

Though such practices would surely violate antitrust laws, another possible source of income from consolidation is through vertical foreclosure:

[A] funeral provider owning its local crematorium is like an airline that owns a hub airport. Even if prices are nominally the same for all, he can easily favour the in-house customer--for example, by keeping competitors out of the prime-time weekend and mid-day slots. SCI insists it never does this (Economist, 1997).

Again, such practices could never become overt, and even when covert become susceptible to lawsuit, so it is unlikely that any significant gains are made through vertical foreclosure. Nonetheless, it is very likely (given human nature) that favoritism does exist toward the owner, and thus some advantage may be had.

Provided the costs of acquisition were not excessive, it is easy to see why the benefits of large-scale operation would push the domestic death care industry toward consolidation. Clustered operations lead to tremendous savings, most (if not all) of which is retained by the company. In fact, prices at chain homes often rise following acquisition, despite the lowered operating costs:

“Chains have bought mortuaries and doubled the price the next day,” said Rev. Henry Wasielewski, a Catholic priest who is a member of the Interfaith Funeral Information Committee, which does price surveys of mortuaries. Wasielewski’s committee recently surveyed Houston funeral homes to find out the cost of their least expensive traditional funeral service and lowest priced metal casket. The lowest price available, offered by the Community Chapel Funeral Home--an independent funeral home--was $1,495. The lowest price offered by SCI’s George H. Lewis Funeral Home was $6,890 (Breyer, 1996).

Though it is possible that the funeral offered by the Lewis Funeral Home was more lavish, it is
not likely to be 461 percent better, as the price differential reflects. Instead, as described earlier, SCI and other chains are able to take full advantage of price insensitivity in the death care market. As a result, earnings are astounding and investors are giddy. In 1995, SCI reported record earnings of $183.6 million on revenues of $1.7 billion, and the stock price jumped 150 percent in the first six months of 1996 (Breyer, 1996). Loewen’s 1995 gross profit margin was a staggering 41.5 percent (Larson, 1996), and in October 1997, its stock price was 426 percent higher than its 1991 initial public offering price (Horn, 1998). The industry is doing so well, in fact, that a death care industry mutual fund, Pauze Tombstone Fund, was created in 1997 (Newman, 1997).

The cluster concept is working extremely well domestically. Cost savings achieved through clustering are contributing to astounding profitability in the industry. The basic principles underlying the cluster concept—economies of scale, buyer power, bundling of goods—are fairly universal ideas, and should work well in most any economically advanced nation. Indeed, foreign firms are well aware of the benefits of clustering and have established their own. Non-US chains form a large part of many foreign death care markets. But SCI, Loewen, and the other major US players are acquiring many of these foreign chains. As detailed in the following section, given the barriers that exist, it is unclear at this point why US firms would bear the costs of owning and operating foreign chains.

**Barriers to International Expansion**

Caves (1971) lists the factors that create the liability of foreignness as differences in “economic, social, legal, and cultural conditions” (1971: 5). International death care providers have confined their expansion to advanced industrialized nations thus far. According to Todd Matherne, director of investor relations for SCI, SCI will only make acquisitions in countries with strong demographics, stable governments and currencies, and high per capita incomes (M&A Report, 1996). Such nations are similar in many economic respects, but certainly are not completely homogenous with respect to all the factors creating the liability of foreignness.
Even when the analysis is confined to a single city within the borders of the United States, economic differences from neighborhood to neighborhood can lead to differing marketing strategies. The “Nike mentality” is a label used to describe the tendency of poor inner-city residents to spend a disproportionate amount of income on funerals, thereby “providing in death what you couldn’t provide in life” (Newman, 1997). High juvenile death rates among blacks spurn amazingly tacky innovations such as the casket that can be drawn on with magic markers, a product expected to be a big hit in the inner city (Horn, 1998).

Social and cultural differences can also be profound. For example, funeral directors distinguish between Catholics, Hispanics, African-Americans, and Asians, who tend to prefer more elaborate funerals, and white Protestants, who increasingly opt for cheap “bake and shake” cremation (Horn, 1998), a method once seen as “sacrilege, a cruel way to treat the body” (Newman, 1997). As you move beyond US borders, the differences can become even more exaggerated. Application of cosmetics to the deceased to present a peaceful and attractive last image is seen as “grotesque” in much of the world (Farrell, 1997), but is common practice in the United States. Islam and Orthodox Christianity prohibit cremation, while this is the preferred option in northern Europe and eastern Asia (Economist, 1997).

Caves (1971) fourth consideration, legal concerns, also adds several bricks to the high wall that must be scaled by internationally-expanding death care firms. In the United States, the Federal Trade Commission watches funeral homes closely and imposes stiff fines for failure to meet stringent laws, or at least has stepped up its enforcement actions recently (FTC Statement, 1996). Jumping into other countries requires getting up to speed on their complex laws as well. For example, Britain requires funeral homes to make their ownership more visible so as to avoid the untrue appearance of a family-owned business, while French law makes it illegal for funeral homes to sell coffins, memorials, and many of the other profitable add-ons, and forces crematorium owners to make their facilities available to competitors at a reasonable charge (Economist, 1997). The myriad laws covering many minute aspects of such an emotionally charged industry likely help to keep many lawyers in business.
The economic, social, legal, and cultural barriers that must be overcome present a formidable challenge to internationally-expanding firms in the death care industry, and are especially noteworthy in light of the existence of additional domestic opportunities for expansion. Firms expanding internationally must envision a huge pot of gold at the end of the rainbow to move beyond the familiar confines of the United States, given that all the domestic opportunities have not yet been exploited. Caves (1971) points out that “a firm would not invest abroad while profitable opportunities remained for the exploitation of scale economies in production or sales in the home market” (1971: 12). However, according to Metherne, an abundance of opportunities for continued consolidation still exist within the North American market (M&A Report, 1996). Despite this, SCI and the other major international players have made huge international acquisitions, often paying a hefty premium (Economist, 1996).

A further barrier to international acquisition is the minimum efficient scale. It is just not feasible to share a US embalming facility or crematorium with a French subsidiary. Shipping costs and time lags lessen the benefits from centralized purchasing of coffins. And hearses generally have a hard time crossing the Atlantic Ocean. In other words, resources cannot be shared across great geographic distances. Instead, clusters must be established in each market entered. Thus, to gain a foothold in another country, multiple funeral homes, as well as crematoria, cemeteries, etc., must be purchased.

Barriers to internationalization in this industry appear very real and very strong. How do US firms overcome these barriers?

**Explanation of International Expansion**

Prevailing logic of why a firm would take on the burden of foreign control of another firm, given that less involved options exist, centers on the existence of intangible assets that cannot be profitably exploited through arm’s length contracts, and thus must be internalized to allow the owning firm to capitalize on their true worth (e.g. Coase, 1937; Hymer, 1960; Caves, 1971; Dunning, 1973). These intangible assets are said to include: (1) technological know-how;
(2) marketing ability and related consumer goodwill; and (3) effective and dedicated management (Morck & Yeung, 1992).

Technological know-how is the reason for a good deal of FDI. Firms in possession of a specialized asset or technique have likely invested a considerable sum of money in research and development, which now becomes a sunk cost. The costs of production of additional units likely pales in comparison to the fixed costs incurred, and thus it is extremely profitable to sell to a large market, much of which may lie beyond domestic borders. This high fixed cost, nominal variable cost characteristic (quasi public good) can make free riding very profitable. If the specialized know-how is not closely guarded, others may profit without incurring the high development costs.

In the death care industry, there does not appear to be any such technological know-how that might spawn FDI. No one firm has a specialized technology, such as a better grave digger or super-fast hearse, through which it might gain advantage over others. Technology seems to be a dead issue (again, no pun intended) within the death care industry, as methods are essentially the same as many decades past. It is this love of tradition that the death care industry relies upon. Without it, consumers might turn to more cost-conscious alternatives, such as “virtual heaven”, in which mourners may grieve via a dedicated web site, or do-it-yourself funerals, possibly including back-yard burial (Economist, 1997). Technology can make a funeral home seem less personal, and thus is frequently viewed as a liability, not a valuable asset:

[This is] a dilemma that funeral directors have faced for nearly a decade: how do you introduce technology into the business while maintaining the warm, caring human presence that customers expect? The tools that other companies use to streamline operations and improve service can backfire in the “death care” industry, where a strategically placed box of tissues can mean more than a state-of-the-art ordering system (Schafer, 1997).

Marketing ability and consumer goodwill seem much more fertile areas in which to dig for an explanation of death care industry FDI. First, let’s examine consumer goodwill. Is it possible that certain chains have established a brand name that can be profitably exploited in
other countries? Actually it is just the opposite, and the death care chains are well aware of this situation. They know that individualized service is important to consumers, so they work hard to avoid the image of becoming “Funerals R Us” (Harris, 1997) or “McDeath” (Horn, 1998):

In a corporate replay of Invasion of the Body Snatchers, Loewen seeks to create the illusion that local funeral homes are still run exactly as they always have been, by native sons and daughters with a vested interest in the community. Although Loewen boasts its acquisitions to shareholders, it otherwise keeps its ownership quiet (Larson, 1996)

This careful strategy of maintaining the image of independent ownership so as to capitalize on local goodwill seems to work, according to the outspoken funeral industry reform activist, Jessica Mitford:

You think of dear old Mr. Johnson, an honest old chap that your family has dealt with over the years, and so you go to Johnson’s, and it turns out to be this highly predatory different outfit where nothing’s the same. I don’t think people know anything about it. I think they’re absolutely ignorant (Larson, 1996).

There is no goodwill associated with chain ownership that can be leveraged through FDI. Chain ownership is instead a great disadvantage, an Achille’s heel to be carefully guarded. As the owner of an independent funeral home said, “I believe there are some things you can’t streamline into a factory, and death is one of them” (Hagstrom, 1995). Though we have argued that this industry is not differentiated by anything much more than location, it is possible that the negative connotation of ownership by an impersonal chain could differentiate funeral homes were this to be flaunted. Family members fear, sometimes justly, logistical nightmares:

This centralization can increase the risk of administrative errors like the one that occurred recently in Arizona when an SCI cluster facility mistakenly cremated a body that was supposed to be shipped intact to Utah (Larson, 1996).

Turning to marketing savvy, claiming that the death care industry is very adept at selling its wares is much like saying a tornado is breezy. Funeral associations and chain headquarters hold seminars to teach funeral directors the fine art of “Third Unit Target Merchandizing” or
“remerchandizing” in which low price caskets are not shown to customers so as to up the anchor price and cash in on the tendency to choose the product two levels above the lowest price option offered (Larson, 1996). Other seminars include advice on how to tack $1,400 on to the bill by requiring unnecessary extras.

Any mortician can perform these tricks, whether part of a chain or not. However, chains have certain other marketing advantages over independents: “The bigger funeral chains can also command higher prices by selling harder: the typical family funeral director may be reluctant to fleece his poorer neighbours when they are most vulnerable” (Economist, 1996). Thus, there is yet more reason to hide a chain identity. On the positive side, according to SCI’s executive vice president for corporate development, marketing also involves “making [SCI] come across as caring and empathetic” through such means as conducting seminars for doctors, nurses, clergy, and the public on dealing with sorrow, as well as giving away videocassettes and books on how to handle grief (Jacob, 1992).

Marketing is indeed a great skill in this industry, but none of this appears to be proprietary tacit knowledge. No single firm, be it the large and impersonal SCI, or the small and warm mom and pop independent funeral home down the street, holds much guarded knowledge on how to best squeeze money from a bereaved family once they enter the door. It is a matter not of possession of a quasi-public good, but rather willingness to use the tactics. As far as getting customers in the door, we have already seen that selection is based not on slick marketing campaigns, but on proximity (Newman, 1997).

The third and final intangible asset that a firm wanting to make a foreign direct investment would likely possess is effective and dedicated management. As noted by Penrose (1959), firms will want to expand if they have excess management capacity, since they will be able to manipulate additional resources for a profit. Her thoughts applied to domestic firms, but may also explain multinational growth. Is it the case that domestic death care chains possess superior management capability that can be exploited in international markets?

As discussed in a previous section, the cluster concept is the basis for domestic
expansion. Savings from shared resources and bulk purchases are considerable. But this sharing of resources cannot cut across oceans. Clusters must be recreated in foreign locations to realize these advantages. Perhaps then the idea to create clusters and the managerial capability to implement the concept is the intangible good that is being exploited by domestic firms through FDI. Expansion into countries not employing this approach might then be profitable.

Though SCI is believed to be the original consolidator, and the first to conceive of the cluster concept, funeral homes in other countries, including those in which SCI has expanded, are well aware of the idea. Waltrip, CEO of SCI, began his “merger mania” in the 1950s, but Howard Hodgson, a British funeral home chain owner, was just a few decades behind. In a story that sounds amazingly similar to that of Waltrip’s, Hodgson began with his father’s funeral home in 1975, then expanded out through use of the cluster concept, cutting costs, yet keeping the independent home family name to maintain community goodwill (Cope, 1992). By 1992, Hodgson’s company, Co-op, owned 25 percent of the British market. Hodgson wasn’t the only chain in the British market either--the top three chains owned 40 percent of the British funeral industry (Cope, 1992).

The cluster concept was certainly not foreign to the British industry but SCI still expanded into Great Britain, buying out the second and third largest players, and gaining a 15 percent share of the market, though at a hefty price (Galarzo, 1995). This is typical of the way US chains expand internationally--through large-scale acquisition. When Stewart went into Canada, it bought out Urgel Bougie Ltee (Montreal), which had 77 funeral homes (Globe & Mail, 1997). SCI made a splash in the Australian market by buying its largest death care provider, and didn’t hold back in Europe when buying its largest, Pompes Funebres Generals SA (M&A Report, 1996). Given the size of the chains purchased, it can be inferred that the cluster concept was employed to some degree. Thus, it does not look like the domestic death care providers were uniquely innovative in employing the cluster concept. Are they more effective at managing the clusters after acquisition?

The death care industry is an extremely profitable industry. Demand is very inelastic,
and there are many ways to add charges to a bill that seldom are questioned by a grieving buyer. This is regarded as one of the great things about the business:

The Loewen Group and the other big consolidators know full well that family members make funeral arrangements in a daze . . . Out of grief or a desire not to seem cheap at such a weighty juncture, survivors jettison the consumer instincts . . . As a result, funeral homes traditionally haven’t had to worry much about price competition. In its annual 10K report to the Securities and Exchange Commission, the Loewen Group describes this lack of price sensitivity as one of the “attractive industry fundamentals” of the funeral business (Larson, 1996).

Taking advantage of this price insensitivity may seem a bit “insensitive” to many, but some of those inside the industry have no shame about profiting from these “attractive industry fundamentals”. On the contrary, SCI’s chief operating officer views low-priced funerals as a disservice to the consumer: “If I tried to sell a $1,400 funeral at one of our good properties . . . nobody would come. Spending $10,000 makes some people feel better” (Horn, 1998).

Lowering prices could lower consumer satisfaction.

US-based firms may be more adept at taking advantage of this situation through increased marketing of add-on merchandise. If they have more centralized control of the acquired homes, they may better align the marketing practices of operators at each home. With tighter control, they may also be able to reign in costs. Though homes are outwardly seen as independent, and often sold to the chains under the presumption of “bottoms-up management”, in which local funeral directors are allowed to retain great authority, much control remains with corporate headquarters:

In practice, new members of the Loewen family are likely to find they do not have quite as much leeway as bottoms-up management might suggest. The company immediately begins a process that Ray Loewen calls “normalization,” or bringing newly acquired homes up to financial expectations. All the comfy perks of a family business--extra cars and dry cleaning--suddenly disappear. And prices rise (Larson, 1996).

Cost-cutting is not a unique ability, but it is possible that domestic chains are more
willing to slice unnecessary costs, and thus can operate even more cheaply than already consolidated foreign chains. This willingness to “cut the fat” out of operations may separate US chains from others, and cause them to value acquisitions higher. Similarly, confidence in their ability to sell add-on merchandise through centralized marketing systems may also explain US firms’ willingness to pay a premium for foreign chains.

Large acquisitions require large amounts of cash. The big chains have spent hundreds of millions of dollars per year over the last several years in acquisitions. Firms must be careful not to get crushed under heavy debt burdens. Ability to manage debt burdens may set US chains apart. For example, the French firm, Pompes Funebres Generales, with some 950 funeral homes in France, Switzerland, Belgium, Italy, Czech Republic, and Singapore, found itself in trouble when interest rates rose and recession set in while it was attempting to offload assets to pay a high debt service (Cope, 1992). SCI was able to take over the financially strapped firm (Buchan, 1995). Loewen, after an expensive lawsuit settlement and a nearly billion-dollar acquisition binge put it $1.3 billion in debt, was so strapped for cash that it was nearly taken over by SCI (Larson, 1996).

Part of SCI’s skills at controlling capital includes its ability to scout out good acquisitions, ones that generate ample cash flows. Expansion into unprofitable terrain can eat up critical cash reserves, which was at the root of Pompes Funebres Generales’ troubles. SCI created a demographics department around 1990 to guard against this (Spiegler, 1995). They have created maps showing death rate projections by zip code, and place themselves accordingly (Jacob, 1992). With such data (though it could be obtained by other chains fairly easily), SCI may make better assessments of the value of acquisition targets.

To summarize, technological know-how and consumer goodwill can be ruled out as explanations for FDI in this industry. Marketing ability may provide some explanation. But the biggest piece of the puzzle is effective management. Though the cluster concept is not unique to domestic chains, the ability to effectively run clusters may be. On the surface, it appears that US firms, and especially SCI, are very skilled at centralizing control, cutting costs, scouting out the
best acquisition targets, and controlling capital. These management intangibles may be the assets US chains rely on to overcome the liability of foreignness, as well as to offset the purchase premiums, when undertaking FDI.

**Discussion**

Extant theory predicts that FDI occurs in differentiated and oligopolistic markets, wherein firms exploit intangible assets to overcome the liability of foreignness. The death care industry appears to largely violate these tenets of FDI theory. The U.S. market provides evidence of consolidation through acquisition and leveraging economies of scale and scope through clustering and bundling strategies. However, it is not evident that these are the strategies that are guiding FDI expansion. Why is FDI expansion on the rise in the death care industry? What are the peculiar characteristics of this industry that support FDI spending? Are there other markets or industries with similar traits that are also experiencing FDI growth? Are there other markets or industries with different traits that also violate FDI theory?

For the EAM 2003 Conference, we propose conducting a session that would generate dialogue on the challenges to FDI theory. First, we would present our paper as a case discussion of what we view as largely an anomaly to FDI theory. To stimulate useful feedback, we would proceed through inquiry of the dialog framework illustrated in Figure 1. Based upon feedback, our goal is to enrich existing FDI theory. As our discussion above indicates, extant theory can only explain FDI in the death care industry in terms of the rather broad, ill defined, and perhaps tautological concept of “effective and dedicated management.” If other industries also violate all but this concept of FDI, perhaps the literature should move toward more thorough examination and explication of this vague concept, or perhaps FDI should be augmented.
Is the death care industry incompatible with long-standing FDI theories?

YES

Discuss the characteristics that are not compatible with FDI theory

Identify other industries that also appear to be anomalies to FDI theory

Examples of Market Types

Regional client base (i.e., auto repair, used car sales)

Highly fragmented markets (several competitors)

Determine the factors of commonality in anomaly cases, and determine whether they are sustainable

Discuss ways of modifying FDI theory to account for anomalies, or building a new approach to FDI

NO

Why not?

How does it fit into existing FDI theory?

What are the unique dimensions of this market relative to more typical FDI markets?
References


Prepared statement of the Federal Trade Commission for the Special Committee on Aging, United States Senate. September 27, 1996. From the FTC internet page.
