The Internationalization of SMART FIT:

Challenges to the Sustainability of an Innovative Model in the Fitness Industry

Track: Strategies for Global Competitiveness

(Teaching Case)

After failing in the sophisticated gym market and then joining a family business, Edgar Corona launched Smart Fit – a low cost / low price model in the fitness industry, which has reached unbelievable growth in a short period of time. The firm was established in Brazil in 2009 and, as of mid-2016, had already expanded to several Latin American markets and is the absolute industry leader in the continent. However, the model seems easy to copy – so Smart Fit management has to develop a package of benefits and expand rapidly. The question is: Can Smart Fit sustain its high-growth path?

Keywords: fitness industry, gym industry, competitive positioning, internationalization, teaching case

1. Introduction

Sao Paulo, Monday, 8:00am. Edgard Corona begins his day visiting recently opened Smart Fit locations in various Sao Paulo neighborhoods. Edgard Corona used to be a top athlete, who ended up pursuing a career as a chemical engineer. After a ski accident, he decided to revive his hobby in the form of an entrepreneurial venture – and then he entered the fitness business. However, he advices: “If you have a hobby, be careful about turning it into a business – you might come to hate your hobby”.

Before establishing Smart Fit, Edgard almost went out of business several times and overcame many obstacles. Edgard’s first job was in a material analysis laboratory. For him, what was important about being a chemical engineer was dealing with transformations. “People picked elements and transformed them into other elements. I took petroleum and transformed its derivatives into plastic. I took sugarcane and produced sugar and ethanol”. However, that job wasn’t able to engage him enough to follow it as a career. “I wasn’t very content in that line of work, so I decided to sell my car (so I didn’t need to depend on my father) and to enter the clothing business with two friends”.

The three partners opened two clothes stores in Sao Paulo, one each in the Iguatemi and Ibirapuera shopping malls. This was Edgard’s first experience leading a business focused on customer service. In the 1980’s, he left the stores to manage his family’s sugar mill. He proudly states,

> That was the first journey of my life, where I left my associates and the stores and went to run my family’s sugar mill, in the Sao Paulo countryside. I learned to plant, harvest, transport, and mill sugar. I learned to produce steam and electric

> energy, sugar, ethanol, and to sell these products on the market. I stayed there for 16 years, and the business grew. I learned much during that experience!

By 1995, the mill had achieved the third position in the sugar and ethanol sector in Brazil. However, due to conflicts that occurred from a third generation of the family entering into the business, exacerbated by the exchange and financial crises Brazil was suffering, Edgard decided to leave the company. He took advantage of a period of change to take vacation and recover from the preceding years' stresses.

He then resolved to resume one of his prior projects, intensifying his participation in managing a gym where he was already a partner, restructuring it with the support of consultants. While conducting business, he was able to observe that the location chosen was more important than efforts at structural or service improvements. Choice of location made a significant difference in the success or failure of that kind of venture. This led Edgard to envision the possibility of opening a gym location on Avenida Paulista, in the financial district of Sao Paulo – the Bio Ritmo (Bio Rhythm). It was a more open floor plan and high-end concept, focused on ambiance and a diverse portfolio of activities. This was a parting of the waters in company history and led the Bio Rhythm chain to become a success, with a strategic positioning targeting high-income clients.

Attention to the client was focused as much on attraction as well as retention, as Edgard explains:

> Before, you would do a physical evaluation that was a masterpiece on how to mistreat the client at first contact. You would take a woman, who was overweight, ask her to take off her shirt, and she would only have on her bra and shorts…it was terrorism, no…a torture, to pinch, pinch a woman 25 times. That wasn't enough; you would ask her to flex her arm, and her stomach, and then tell her she was fat and out of shape.

It was necessary to change the client perception from the first day. Bio Rhythm gym counted on a broad and varied offering of group classes, specialized training and the most modern equipment in the fitness industry. The business would expand and, as of mid-2016, it had 29 locations spread out across Brazil.

2. FROM LUXRY TO POPULAR GYMS

However, in 2009, Edgar noticed that the Sao Paulo market had become saturated with luxury gyms and identified a business opportunity inspired by the innovative "low cost, low price" model from the United States and parts of Europe.

He thus decided to invest in the market of popular gyms, which in general have lower fixed costs and practice lower unit margins in order to attract a larger number of clients and guarantee profitability. It is worth stressing that during this period, the market for popular gyms in Brazil had been little explored and possible competitors were only neighborhood gyms with limited resources and simplistic ambiance and equipment.

That same year, Edgard inaugurated the first four locations of Smart Fit in Sao Paulo, emphasizing the advantages of its unique experience and building a better price-benefit relationship for clients. The purpose of Smart Fit is to democratize physical activity, reaching the most diverse public and making exercise as easy a habit as possible in order to develop a more active and healthy lifestyle. All of this was offered in an intelligent model with state of the art equipment, extended hours, daily operations and accessible prices.

Corona had noticed that 70% of its students were only interested in "pumping iron" and cardiac exercises to burn calories, by using such equipment as bikes and treadmills – and did not want to pay for other activities and equipment that they did not use. "In the US, the classes were separated from the academies. You have yoga and Pilates studios in the city, but not within the academy, so they are cheaper," he says (Carvalho, 2014).

In fact, the combination of quality equipment (of the same level as those used in the sophisticated Bio Ritmo gyms) and a modern ambience (see Figures 1 thru 5) coupled with lower prices attracted a large number of clients. The lower fixed costs derived from the need of fewer employees, and the use of automated processes (e.g., registration of new clients carried out over the Web), and no extra activities (e.g., yoga classes or martial arts classes).

In 2010 the company opened 10 gyms and had seven new locations under construction, but the company's financial resources were then exhausted. Edgard sold almost all of his possessions so as to continue with the expansion, but it wasn't enough: "I sold real estate, I sold everything, but I was without credit and it was impossible to keep opening locations".

That was when investment fund Patria entered with the fuel the business needed and ended up forming a partnership that was capable of overcoming obstacles. Patria injected financial resources and technology, becoming a 50% partner of the Grupo Bio Ritmo (Carvalho, 2014), in particular for the expansion of the Smart Fit business. This infusion of capital accelerated the expansion process and enabled the establishment of a victorious marketing strategy.

After enjoying success for some time, Edgar finally reached a point where he couldn't stand the heavy work routine anymore. That was when Edgard experienced a "metanoia" (which means a change of thought and direction) – a process that seeks to create "more humane" leaders and companies with "purpose". Edgar then found that his company, which today is the largest gym chain in Latin America, could only continue successful growth if he managed to stimulate a chemistry between people. For Edgard, "[…] one of the company's skills is its adaptability: to be able to make a mistake and quickly correct and implement [a solution], because the world revolves 24 hours a day".

3. THE SMART FIT MODEL

Smart Fit is the largest gym chain in Latin America, operating in six countries with its slogan “Smart Fit is the intelligent gym”. In Brazil, there are over 220 locations and more than 660,000 clients. The gyms offer bodybuilding exercises and weight training to clients over 14-years old, with experienced teachers who are capable of guiding and training in a safe, autonomous and comfortable manner. Clients share the large number of bicycles and treadmills on a first-come-first-served basis, without fixed schedules. There are no personal trainers, but rather a small number of “shared” trainers. Business hours vary slightly between locations, but the gyms are usually open from Monday to Friday, between 6:00 AM and 11:00 PM, as well as on weekends and holidays with reduced hours.

4. CONSUMER BEHAVIOR IN THE FITNESS INDUSTRY

The modern lifestyle contributes to people being pressed for time, stressed out and sedentary. The need for overall well-being leads to physical exercise. Even though people have access to information and are aware of the dangers of an unhealthy lifestyle, a large portion of the population doesn’t practice physical activity, even in developed countries (Saba, 2001). It is common for individuals to prioritize work, study and family to the detriment of health, but feel the need for being in good shape and eating healthy when they are sick or need to engage in some kind of aerobic activity, like climbing stairs or walking for a long period of time.

According to estimates by the Brazilian Institute of Geography and Statistics (IBGE), in August 2016, Brazil had approximately 206.1 million residents, of which only around eight million are gym members (IHRSA, 2016), which is equivalent to about 3.9% of the population. According to Carvalho (2014), in the USA the penetration rate is 14%, while in New York it reaches 33% of the population.

The reasons that lead an individual to attend a gym can be his/her search for better quality of life, longevity, satisfaction, pleasure or physical beauty (Liz et al., 2010). “Vanity has always been a characteristic associated with Brazilians, and not without reason. The country is one of the largest beauty markets in the world – it is first in plastic surgery and perfumes, second in hair care, and third in cosmetics. Body worship doesn’t stop there. In the last few years, Brazil has also started attracting attention for the growth in businesses focused on weight lifting” (Luders, 2016).

The average time a person stays in a gym is between 60-90 minutes, with an average of three times per week, and consumers generally choose a gym based upon its location (Saba, 2001). Another important aspect to consider is the influence of peer groups and people close to a consumer. Several people prefer to exercise together with co-workers during lunch or to work out with family.

Fitness consumers move the globalized market by acquiring clothes, shoes, health food, nutritional supplements, vital sign monitoring gadgets, etc. The offer of products and services to meet this demand is also extensive, varying from orthomolecular substances to aesthetic treatments, as much for men as for women.

The *Worldwide Survey of Fitness Trends*, from the American College of Sports Medicine (ACSM) reports that the primary fitness tendencies are: the use of technology linked with the body; training with the weight of the body; trained and experienced professionals; personal trainers; functional training; and fitness programs for elderly (Thompson, 2015).

Being a member of the fitness world in many cases becomes a lifestyle – of routine habits involving sports, socialization, participation in events outside of the gyms (such as marathons, tours, tournaments, festivals, parties, and trips), information exchange, and participation in social networks, among others.

5. THE BRAZILIAN FITNESS MARKET

The International Health, Racquet & Sportsclub Association (IHRSA) – an international association which gathers representatives from gyms, spas, sports centers and equipment manufacturers – asserts that, in 2015, there were 187 thousand gyms in the world with 151 million clients. In Latin America, there are more than 16 million clients in over 55 thousand gyms, considering a market of 16 countries (IHRSA, 2016).

Brazil has 31,000 gyms and 8 million members. According to IHRSA's Global Report 2016, Brazil is the country with the second highest number of gyms per capita and 10th in terms of revenues, which corresponds to $2.4 billion (IHRSA, 2016). The report also highlights that the ten countries with the highest revenues account for 71% of all industry revenues. The USA is the ranking leader.

According to Fitness Brasil (a firm specialized in training and networking related to the fitness industry), the total revenue of the fitness industry in Brazil grew from US$ 1.1 billion in 2009 to US$ 2.4 billion in 2015, which represented 44% of the total industry revenue in Latin America; the number of gym centers jumped from 14 thousand to almost 32 thousand in the same period, which meant 66% of the total gyms in Latin America; and the number of gym clients went from 4.4 million to 8.0 million, which is 59% of the total number of clients in the continent (Fitness Brasil, 2016).

It is apparent that "in Brazil today there are different gym management models depending upon the location and purchasing power of clients. In any case, one can observe greater professionalization and location of gyms in any part of the national territory, in rich or poor areas, constituting one of the institutions having the greatest presence in the country and an important means of generating employment and economic activity" (Bertevello, 2005: 176).

Gyms can range, for example, from high to low cost, unisex or single-sex, family-oriented, for youths, and others. This diversity seeks to cater to different target-publics, which vary according to their beliefs and customs, values, culture and social groups, social class, lifestyle, gender, age, and needs and desires. Most gym members are from lower-middle classes and working classes, who have turned to paid physical exercising after recent economic and social gains. This has led to significant changes in the diversity of sports: soccer, wrestling, swimming, water aerobics, dance, martial arts, spinning, and indoor rowing (Arruda, 2015).

Given this scenario, competitors are companies that offer weightlifting and aerobic exercising at competitive prices and at locations in various cities and neighborhoods. These include the smaller, traditional gym chains Curves and Contours, which offer 30-minute exercise programs specifically for women. Leonardo Cirino, CMO of Grupo Bio Ritmo in Brazil, declared that less than 3% of the population practice physical activities in a gym, which means it is a market with potential. This perspective is also shared by the IHRSA (2016), which affirms that the opportunities are more attractive in emerging markets of Asia and Latin America.

6. SMART FIT POSITIONING AND OPERATIONAL MODEL

The business model adopted by Smart Fit is based on the low cost/low price concept, which offers consumers leaner, practical and less-complex services. Prices are also lower than market average, resulting in a service that is more accessible to a greater number of consumers. Smart Fit manages to distinguish itself from its competitors by offering a superior quality structure, as opposed to the simple gym models usually used in the USA for this category.

The biggest operational difference is management aimed at an organic model which is inserted into corporate culture, including qualities and characteristics of a human being that is able to respond with agility and flexibility to the demands of the external world. In this way, the adoption of a simplified and horizontal management model that gives meaning and empowerment to teams, with decision-making coming from the base (Corona, 2014), represents a key competitive advantage.

The idea of making the experience in each new Smart Fit location more surprising than the last one seems, at first glance, to be an easy model to copy. However, it requires engagement with teams as well as a considerable amount of financial resources to compete with the same expansion speed and capillarity (i.e., presence in several neighborhoods and cities). It is worth emphasizing that capillarity itself may not be perceived as a benefit for every client. On the other hand, for the company, it works as an entry barrier for new players and offers explicit scale gains in the purchase and maintenance of equipment. Furthermore, it performs an important role in reinforcing brand success and protecting against copycats since it is a pioneer in this market.

In summary, the lean cost-structure allows Smart Fit to offer lower prices than competitors, which attracts a group of consumers that are more price-sensitive and who demand less-complex services.

7. THE SMART FIT EXPERIENCE

Consumers normally seek a gym close to home or work. Smart Fit developed a life style ecosystem, where exercise is pleasurable and benefits from a differentiated infrastructure – equipment, architecture, lighting, sound, air conditioning, customer service, among others.

Focusing on people that are only interested in individual physical activities, and who don’t want to pay for a complete gym structure, Smart Fit only offers stair machines, ergonometric bicycles, and weight machines. The company offers two kinds of fitness plans: Smart and Black. A Smart plan member has access to only one location and its equipment. With the Black plan, members can use any location in Latin America and have the right to bring a visitor five times per month and have access to massage chairs.

The registration process is very simple and can be done at a gym or over the internet. All that is required is filling out a form with basic information and choosing a payment method – either checking debit or credit card – and payment date – the 5th, 10th, or 20th of each month. There is no cancellation fee, only an annual account maintenance fee.

On the first day at the gym, the member should find an instructor, always wearing a yellow shirt, to establish a plan according to desired objectives: weight loss, improved cardio, muscular definition, among others. The workout plan is designed according to the member’s ability to go to the gym (number of days per week and length of time). The instructor guides each exercise in terms of how to use the machines, posture, repetitions, etc. All machines also have a button to call an instructor if necessary. Equipment at every Smart Fit is state of the art and members have comfortable locker rooms. They are expected to bring their own padlock to use while at the gym.

8. THE EXPANSION OF SMART FIT

The operational model adopted by Smart Fit, associated with volume of resources supplied by the Patria Fund, allowed a rapid expansion in Brazil and other countries. After starting with fours gym centers in 2009, the company opened 12 locations in 2010, and 18 more the next year. The internationalization process began in 2012, when four locations were opened in Mexico, and 25 more in Brazil. In 2013, 35 new locations were opened in Brazil and nine in Mexico. Smart Fit penetrated Chile in 2014 by opening four locations, as well as 62 more in Brazil and 20 more in Mexico. Another 94 gyms were opened in 2015, with 70 in Brazil, 18 in Mexico, five in Chile and one in the Dominican Republic. In 2016, Smart Fit arrived in Peru and Colombia and the plans are to have 385 gyms total by the end of the year. See Table 1.

There are currently around 300 Smart Fit locations in Brazil, with only 10% begin franchises. There are close to 1 million members. One Smart Fit gym in Rio de Janeiro has over 12,000 members. Smart Fit also won a title of most-loved brand by Rio de Janeiro residents in 2015.

9. THE INTERNATIONALIZATION OF SMART FIT

With the entrance of the Patria Fund into the partnership, the Grupo Bio Ritmo began to build a success story. The Smart Fit model has become known and elicited interest from potential partners in other world regions. In 2010, at an event in Mexico, Edgard began contemplating the internationalization of the chain. To the entrepreneur, the challenge would be to combine three fundamental aspects: identification of an ideal partner, a favorable economic environment, and a growing market.

The company wanted to always work with a local partner, who had local market and culture knowledge to help accelerate the penetration process. Edgar believed that the formation of a joint venture protected the company and offered competitive advantages in the local market. Partner choice involved exposure to some risks, including, but not limited to, poorly designed strategies, tactics or procedures, brand infringement, and poor business performance.

The first foreign experience started casually, via contact from a Mexican investor in the fitness market interested in introducing the Smart Fit model into Mexico. The entry model for other countries (Colombia, Peru and Chile) was similar. Entry mode was only different for the Dominican Republic, where a franchise model was adopted. See Table 2.

The expressive international expansion transformed Smart Fit into one of the five largest buyers of fitness equipment in the world. For Leonardo, the CMO, one of the benefits of internationalization was to "not remain dependent on one country, the oscillations of its economy and all of the other socio-political questions involved. The company's product and service are highly adaptable to any country in the world".

Nevertheless, there were specifics for each culture. For example, in Brazil, a Black program member has the right to use a massage chair, while a member of the same plan in Mexico has at their disposal a tanning bed, which is appreciated more by Mexicans than the massage chairs. In each country, the business model experienced adaptation to an extent, prioritizing what aggregates value in each country, and taking into consideration socio-economic and cultural aspects. Still, the CMO emphasizes that the essence of the product and service doesn't change.

Each country's work team is chosen from local collaborators, especially the management. The company understands that a strong exchange of cultural experiences is a relevant factor for valuing the brand purpose. One exchange program was realized between Brazilian and Mexican managers, which involved even hosting the foreigner in a local home for a specific period of time.

Regarding return on the investment abroad, Smart Fit management was surprised to see that it was much greater and faster than in Brazil. This is because costs associated with the importation of equipment are lower, as well as construction and labor costs. In all, the costs of opening a gym abroad can be 35% lower than in Brazil.

Smart Fit is the largest chain of gyms in Latin America, and the absolute leader in Brazil and Mexico. The company objective is to become the market leader in its other markets.

For Leonardo, in times of crisis, Smart Fit is an incredible option for consumers in cost-benefit terms. Member retention is a reflection of the gym experience and also of the aggregated products that benefit the client. These products are in expansion and include isotonic exercise, member's advantage club, and other new ideas are coming every year.

9.1. Mexico

Mexico was the company's first venture into international markets. Entry into the country was in the form of a partnership with the local chain Sport City. This was a company owned by Grupo Marti, the leader in the sports sector with premium gyms. Each company holds 50% of the joint venture. Marti became aware of Smart Fit and sought out the company to propose a partnership. The first gyms were inaugurated at the beginning of 2012 and rapid expansion enabled Smart Fit to become the largest chain in Mexico, with over 60 locations as of mid-2016.

This process counted on the efforts of the local partner who had already decided to launch a low cost gym, in order to exploit the potential of the Mexican middle class. The complementary nature of the two partners' interests led to the Mexican structure being responsible for expansion of business into Colombia and Guatemala.

9.2. Chile, Dominican Republic, Peru and Colombia

Smart Fit started to operate in Chile in 2014 through a partnership between Grupo Bio Ritmo and the Chilean Grupo O2 Fit. As of mid-2016 there were nine locations open.

In the Dominican Republic, Grupo Bravo became the exclusive representative. Under a franchise structure, 10 locations were opened there in 2015.

A partnership in Peru in 2016 included plans for opening four locations by the end of the year. Another partnership in 2016 has enabled Smart Fit to penetrate Colombia, where it already opened four locations as of mid-2016.

10. THE MANAGERIAL DILEMNA

Smart Fit's internationalization process started from the outside-inwards, in that potential partners from other parts of the world were aware of the work the company was doing in Brazil and made the initial contact. Entry into a new market means multiplication of brand penetration, that is, one country gives the company visibility, and then another, and so on. In addition, it reduces dependence on the domestic market and its fluctuations, and also benefits the whole firm in terms of economies of scale (especially in purchase of equipment).

The gym business demands little need for adaptation from one country to another, which makes it easier to replicate a model. Even though it is apparently an easily copied business model, it requires a large amount of resources, and especially the creation of an environment or ambiance that provides a differentiated experience for clients.

Smart Fit has gained extensive experience in Latin American markets, and is always aware of the size of the local economy, market potential, cultural diversity, and the formation of solid partnerships. In order to continue its aggressive expansion process, the company finds itself in the position of needing to choose new target countries.

The first question is how to sustain its successful business model and proctect if from copycats; the second question involves whether or not to extend its presence in Latin America, which it knows well, or to pursue other potential markets in Asia, the USA and Europe.

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FIGURES AND TABLES

Figure 1 – Facade Design

Source: www.smartfit.com.br

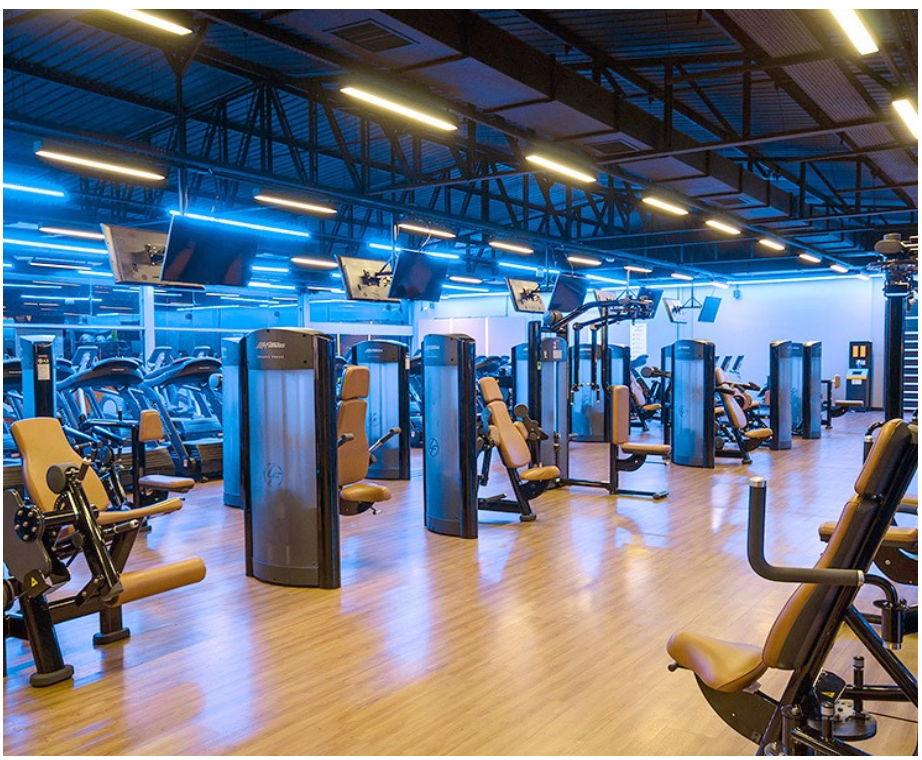
Figure 2 – Gym reception

Source: www.smartfit.com.br

Figure 3 – Ambiance/Environment

Source: www.smartfit.com.br

Figure 4 – Equipment and ambiance



Source: www.smartfit.com.br

Figure 5 – Equipment and ambiance

Source: www.smartfit.com.br

Table 1 – Smart Fit Expansion (new locations)

Country	2009	2010	2011	2012	2013	2014	2015	2016*	Total
Brazil	4	12	18	25	35	62	70	65	**291**
Mexico	0	0	0	4	9	20	18	9	**60**
Chile	0	0	0	0	0	4	5	7	**16**
Dominican Republic	0	0	0	0	0	0	1	9	**10**
Peru	0	0	0	0	0	0	0	4	**4**
Columbia	0	0	0	0	0	0	0	4	**4**
Total	**4**	**12**	**18**	**29**	**44**	**86**	**94**	**98**	**385**

* Estimated existing and planned locations

Source: Smart Fit

Table 2 –Smart Fit Internationalization Process

Country	Entry Year	Entry Mode
Brazil	2009	Direct Investment and Franchise
Mexico	2012	Joint Venture
Chile	2014	Joint Venture
Dominican Republic	2015	Franchise
Peru	2016	Joint Venture
Colombia	2016	Joint Venture

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TEACHING NOTES

These teaching notes – in particular, the analyses to the suggested questions – reflect the views of the authors of this teaching case and may not necessarily represent the opinions of Smart Fit's management.

Abstract

After failing in the sophisticated gym market and then joining a family business, Edgar Corona launched Smart Fit – a low cost / low price model in the fitness industry, which has reached unbelievable growth in a short period of time. The firm was established in Brazil in 2009 and, as of mid-2016, had already expanded to several Latin American markets and is the absolute industry leader in the continent. However, the model seems easy to copy – so Smart Fit management has to develop a package of benefits and expand rapidly. The question is: Can Smart Fit sustain its high-growth path?

Keywords: fitness industry, gym industry, competitive positioning, internationalization

Teaching objectives

This case illustrates the development of a new business model in a relatively mature industry – the fitness business – and the challenges (and payoffs) associated with it. Specifically, the case of Smart Fit's expansion in Brazil and Latin American countries is explored.

This teaching case can be used in Strategy classes as a way to discuss industry analysis (e.g., the Five Forces Model, *cf*. Porter, 1980), macro-environment analysis (Piercy & Giles, 1989), competitive positioning (Porter, 1985, Mintzberg, 1988) and the VRIO framework (in particular, the "I"mitability issues) (Barney & Hesterly, 2011). The case also serves International Business classes, in particular to discuss issues related to: motivations to go abroad, country selection, and international operation mode.

Sources of information

One of the authors of this case has a business relationship with Smart Fit's owner and has had several talks with him, which are reflected in the text. In addition, this author interviewed the Chief Marketing Officer (CMO) of the Grupo Bio Ritmo (Bio Rhythm Group), Leonardo Cirino.

Data also came from secondary sources, in particular a presentation by Smart fit's founder, Edgar Corona, published on the Web (https://endeavor.org.br/day1-formula-empreendedorismo-de-sucesso-edgard-corona-bioritmo/) and publicly available reports published in the business media, including web reports, about the fitness industry and the company itself.

We also used previous analysis of the company and its strategy, conducted with undergraduate students by one of the authors.

Suggested questions for in-class discussion

What follows are mere suggestions of potential questions that can help the instructor lead the discussion in class. The first two questions fit better a Strategy class, while the last three questions fit better an International Business class.

1. What aspects of the macro-environment and of the service offered by Smart Fit have favored the quick growth of the company?
2. What are the main challenges for Smart Fit to keep up its growth and profits in the domestic market?
3. Should Smart Fit expand abroad before it has exhausted its potential for (quick) growth in the domestic market?
4. Which criteria should Smart Fit employ in order to select future countries for expansion?
5. Which operation modes should Smart Fit adopt in foreign markets? Should the firm go alone or should it find local partners? If partnering is advisable, should Smart Fit participate in the operation of the fitness facilities or should the firm franchise the operations?

Suggested analysis

1. What aspects of the macro-environment and of the service offered by Smart Fit have favored the quick growth of the company?

The economic, demographic and socio-cultural aspects of the macro-environment have been favoring the search for fitness- and health-related services in Brazil.

Brazilian middle class (in terms of income per family) has grown considerably since President Cardoso's Real Plan (1994) and especially during President Lula's government (2003-2010) (Neri, 2011). Given that the average number of children per family has been decreasing and that young adults tend to leave their parent's home later (often after they are 30), more discretionary income lies in the hands of adolescents and young adults – the main targets of Smart Fit.

From a socio-cultural perspective, the pressure for a "perfect" body – both for men and for women – has lured more youngsters into fitness activities.

However, many youngsters may not be willing to pay dearly for fitness activities – that is where Smart Fit model "fits". As the firms manages to keep cost low (or at least lower than competitors) by hiring fewer instructors (in an almost "self-service" manner for customers), it is able to charge an attractive price. Besides, Smart Fit's equipment is new and of good quality – a feature valued by youngsters, although it also increases the costs of the business. The growth has led to scale economies in the purchase of equipment, helping to keep costs lower.

The quick expansion of the fitness rooms to several neighborhoods in the same city(ies), which allows customers to exercise in any room of the firm, is an additional appeal for young people who are always "on the move" – to their girl(boy)friend's, to their friends', to the workplace and even to other cities for professional purposes.

The instructor can introduce the concept of macro-environment analysis and conduct an opportunities and threats analysis (as presented in several textbooks). The instructor may complement the opportunities and threats analysis with a strengths and weaknesses analysis (in order to fill in the SWOT analysis).

2. *What are the main challenges for Smart Fit to keep up its growth and profits in the domestic market?*

Smart Fit's competitive model – based on simple service (fewer trainers and no additional activities), good equipment and low price – is imitable. The instructor can take the chance to discuss the VRIO Framework (Barney & Hesterly, 2011), in particular the non-**I**mitability issue.

Therefore, preemption (Porter, 2008) over potential followers is key. Smart Fit has to arrive at new places earlier than competitors in order to create an "isolated" micro-geographic zone. Such quick expansion, however, demands monetary resources and managerial time. Partnering and franchise may be a solution.

As the firms expands quickly and occupies spaces, it brings an additional benefit to clients, which is more difficult to imitate: the possibility of exercising in multiple fitness rooms. In fact, the free time of these youngsters is paradoxically scarce, since they engage in several activates; therefore, they tend to value this flexibility of exercising wherever is closer to where they are. Moreover, the presence of their gyms in several places reinforces the brand and reduces the need for advertising efforts.

As the firm grows, it reaps economies of scale in terms of procurement (of equipment), marketing and the architectural project of facilities – which provides the firm with a cost advantage that is difficult to match.

The instructor may wish to address industry analysis, in particular, the Five Forces model (Porter, 1980). The discussion of barriers to entry and of rivalry among competitors may be very illuminating. Also, a discussion of potential substitutes – including the "do it yourself" solution, that is, exercising on one's own, by jogging on the beach or on the streets.

3. *Should Smart Fit expand abroad before it has exhausted its potential for (quick) growth in the domestic market?*

Given the fact that the operational and commercial model of Smart Fit is imitable, the firm runs the risk of being copied in other countries. Hence, it should expand to international markets even before it has exhausted its potential in the home country.

Again, some kind of partnership seems inevitable, in order to gain speed and save own resources. Dealing with a partner, though, entails some difficulties. See response to question #5.

Here, the instructor can introduce the literature on motives to go abroad (e.g., Benito, 2015; Cuervo-Cazurra et al., 2015; Dunning, 1988; and van Tulder, 2015) in order for students to understand that Smart Fit's international expansion meets market-seeking and efficiency-seeking objectives.

4. *Which criteria should Smart Fit employ in order to select future countries for expansion?*

Any firm that plans to expand abroad should employ country assessment criteria that cover:

- Demand characteristics (customers preferences, profile, size and future prospects)
- Configuration of the offer (competitors and substitutes)
- Configuration of related industries (e.g., suppliers, channels, complementors)
- Macro-environment (institutional environment) issues

Since the competition for clients for fitness rooms is more of a local (city, and, in fact, neighborhood) nature rather than of a national nature, the proper focus of analysis – as far as demand prospects are concerned – is the city, not really the country. However, the country is relevant inasmuch as legislation and socio-cultural aspects affect the business.

Local demand may already be served by entrenched competitors. Therefore, Smart Fit will have to "drive the market" instead of behaving in a "market-driven" way (Jaworski et al., 2000), that is, it will have to convince potential clients that it offers a better price-benefit package than incumbents.

The company should check about the regulations related to the service it offers, including laws and taxes. Besides, psychic distance issues (Johanson & Vahlne, 1977; Pirme et al., 2009) should be considered – for example, differences in business practices, types of contracts, marketing and promotion practices, degree of expected personalization of the service, verbal interaction and physical contact between service provider and customer, owner-employees relationships (e.g., work pace and business social tempo), not to mention the meaning itself of exercising and of fitness (beauty? health? happiness?).

The legal environment is also relevant – for example, enforcement of contracts, conflict resolution, and profit remittance rules among other issues. Also, the economic environment – for example, exchange rate volatility (although the costs and revenues will be denominated in the same (local) currency, part of the investment will be denominated in the firm's home country currency and the firm's owners will expect profits to be translated to their home currency also), local prices of competitors and substitute services, costs of equipment and of supplies.

It is clear that the motivations for Smart Fit to go abroad are the quest for markets and efficiency (Dunning, 1988). Country selection wasn't focused only on identifying ideal partners, but also on selection of markets that minimize psychic distance (Anderson & Buvik, 2002) as shown through the choice of expansion into other Latin American countries.

While farther-away countries (such as the USA and countries in Europe or Asia) may offer good market potential, and the operational model demands little adaptation, there are psychic distance concerns that may affect the decision. On the other hand, if Smart Fit does not expand fast in order to preempt competitors in other countries, it risks being copied and missing the opportunity of establishing a pioneering advantage.

5. *Which operation modes should Smart Fit adopt in foreign markets? Should the firm go alone or should it find local partners? If partnering is advisable, should Smart Fit participate in the operation of the fitness facilities or should the firm franchise the operations?*

Finding partners in foreign markets seems essential for Smart Fit to be able to (i) expand quickly in the country and (ii) better understand and deal with psychic distance issues.

Here, the instructor can discuss the advantages and disadvantages of going alone vs. partnering. Also, there are advantages and disadvantages of sharing the operational control with a partner (e.g., by means of hiring managers locally or by expatriating managers, while the partner may contribute with financial resources, but also with some managerial responsibility) versus franchising.

Partnering has the advantage of sparing Smart Fit from too much financial and managerial resources. Sharing the control of the operations with partners demands more financial and managerial resources from Smart Fit than franchising. However, franchising provides less control over the activities abroad and conveys the risk of opportunistic behavior of foreign partner (with potential loss of intangible assets) and even the "preparation" of a future competitor; there is also the risk of not enough commitment on the part of the franchisee. On the other hand, franchising would spare Smart Fit from investment and managerial involvement.

Smart Fit has shown a preference for joint ventures over franchising, as a way to maintain the essence of their business. Be it as it may, the firm needs partners or franchisees to come up with financial (and managerial) resources to fuel rapid expansion and preempt competitors.

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