



# Global Strategy & Organization

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Class 6 & 7

# Haier

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## *Haier USA*

<http://www.youtube.com/watch?v=5F2ISPEZPbA>

Haier first entered Europe through Germany. The first imported technology used by the company came from Germany and in 1990 Haier exported 20,000 refrigerators to that country marking Haier's introduction into the European market. In addition to the The Haier Group's own trading companies, Haier also has research, design, and development centers in Italy, Holland Germany, and Denmark, as well as manufacturing facilities in Italy and OEM Factories in Romania and Ukraine. More than 96% of the staff at Haier's European operations are local employees.

## *Haier Europe*

Haier's global branding strategy aims at positioning the company as a local brand in different world markets in conjunction with enhanced product competitiveness and strong corporate operations. Haier's international business framework encompasses a global network of design, procurement, production, distribution and after-sale services. Today, Haier has established 15 industrial complexes, 30 overseas production factories and bases, 8 design centers and over 58,000 sales agents worldwide.

## *Haier Global*

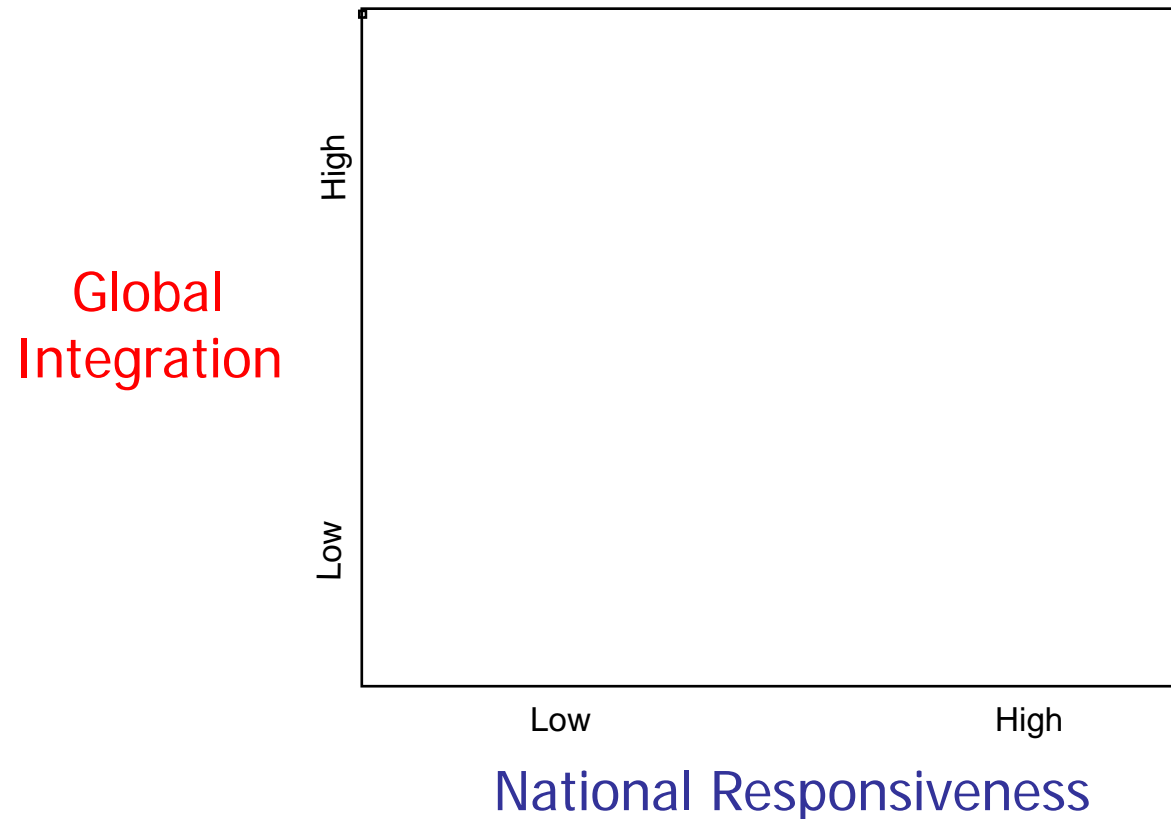
Haier. "Company Profile." October 26, 2011.

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(Source: Haier corp. websites)

## The Strategy of the MNC *as Multinational*

- 1) The multinational company (MNC) is particular because its *organization* spans different countries, not because it does business in different countries. The MNC is a multi-unit hierarchy with units in two or more countries. Managing in a MNC is particular in that one manages *with*, and *for* different peoples in their respective national contexts.
- 2) The strategy of a MNC *as a* MNC has to include an organizational value proposition. Any description of a MNC strategy without such organizational element is incomplete. This MNC-specific strategy element has for long been established as “global integration.”
- 3) “National responsiveness” and “global integration” constitute the two fundamental factors of the economic (value created) and financial (value captured) performance of the MNC.
- 4) “National responsiveness” refers to how the MNC responds to the economic, political, and organisational forces that arise from the differences and similarities across nations. National responsiveness choices are content choices embodied in two kinds of specialization. One is “local specialization” (or “local adaptation” or “localization”): the extent to which the product and the activities of the MNC in each country are specific to the national context there (i.e. dependent on the local “pitch” *and* applied only there). Local specialization optimizes local performance (say, the country unit P. & L.). The other is “international specialization”: the extent to which locally specific product features and activities in a particular country apply to the world or to a set of countries. International specialization optimizes local and global performance. For example, if a MNC decides to have a “center of excellence” of design *in* Milano, Italy for Europe, that is “international specialization” there; if the same MNC decides that its products *for* Italy will be branded with Italian names, that is “local specialization.”
- 5) “Global integration” determines the overall (global) organization of the MNC. The global integration of a MNC reflects the value of the union of the country units that constitute the MNC. Global integration is not – at all – the extent (let alone the increase) of similarity or standardization across country units in the MNC. Choices of similarities and differences are “national responsiveness” choices.
- 6) Note that the local organizational choices in each country unit of a MNC depend also on its global integration. Only if global integration is zero (the MNC is a pure portfolio of country-business units) would the local organization in each country be a consequence of the business strategy there (i.e. the local unit of the MNC would be equivalent to a local indigenous company).



The two dimensions above define the strategy of a multinational company *as multinational*. IKEA, for example, has a *business strategy*: it is furniture retailer, with a particular offering and a unique business model. But IKEA has a *multinational strategy* too: high in “global integration” and low in “national responsiveness” (or “local adaptation” or “localization”).

(Source: Prahalad & Doz, 1987; Bratlett & Ghoshal, 1989)

# IBM

**IBM: Helping Canada and the World Work Better**

*(Source: IBM Canada website)*

# Global Integration

- 1) As the world becomes globally integrated, so does the production and delivery of many goods and services. The “global supply chain” is now a common feature in many industries. “Made in the World” is becoming the norm. Printed on the back of an iPhone, you will read: “Designed by Apple in California. Assembled in China”. Implicit is the statement that the various components are made in many countries. The iPhone is a good instance of national specialization along the value chain.
- 2) In the case of apparel, Li & Fung is one remarkable instance of an innovative global business model that relies on the global integration of production activities by local companies. Li & Fung’s part is to locally differentiate and globally coordinate and control the whole process (what the company calls “orchestration”). This model can be replicated in many other businesses. Apparel was a good candidate to begin with, for it is a very mature business with international trade involved for over one century. Note that the business of Li & Fung is not “international trade” (nothing new there) but rather “international management.” This is the novelty. A relatively small multinational company “manages” the business of thousands of local companies around the world. In the past, such activity would have very high transaction costs and, if it had existed, it would be inside a large multinational company, not in a global world. The more global the world, the less important multinational companies will be in terms of numbers of employees and value of fixed assets. In a global world, even local companies will have a global strategy within a global network of partnerships. This still has a long way to go, but is one way.
- 3) The Renault-Nissan alliance provides yet another model of global integration, in this case through a strategic alliance between two large MNCs from distinct countries.
- 4) However, just a couple of decades ago, the norm for multinational companies (MNCs) was not “global integration” but “local autonomy” in the the so-called “multinational” or “multidomestic” model, in which country subsidiaries were rather self-sufficient and geared towards the optimization of local performance (e.g., country P&L). The high autonomy of many local units made them known as “fiefdoms” and the respective country managers were “barons.” Several MNCs spoke of their worldwide “federation” of national units with pride. They saw the world as a portfolio of country markets.
- 5) The global integration “of production and delivery” started early for some companies. Some GIEs (“globally integrated enterprises”, as IBM’s CEO Sam Palmisano called them) were already visible in the 80s. As one might predict, the “GIE” movement began in industries with high economies of scale in R&D and manufacturing: cars, consumer electronics, and semiconductors, just to name a few.

## “Global Integration”: option or imperative?

- “The multinational corporation ... is taking on a new form, one that is promising for business and society.”
- “The emerging *globally integrated enterprise* is a company that fashions its strategy, its management, and its operations in pursuit of a new goal: *the integration of production and value delivery worldwide.*”
- “Moving toward the globally integrated enterprise will **require long term vision and continuous investment** ... [and] also call for **patience and understanding from the part of stockholders**”.
- “The alternative to global integration is not appealing. Left unaddressed, discontent with globalisation will only grow.”

(Source: Sam Palmisano (CEO, IBM), “The Globally Integrated Enterprise”, FA, 2006)

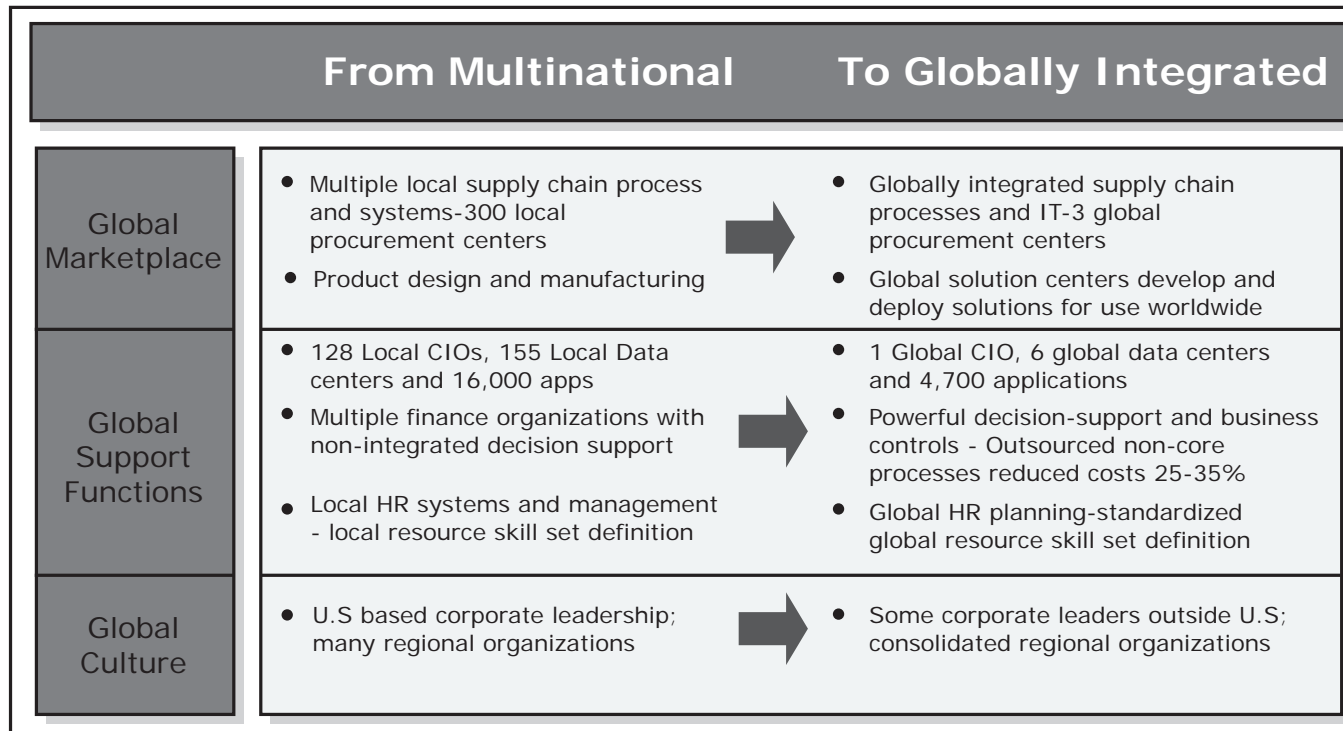
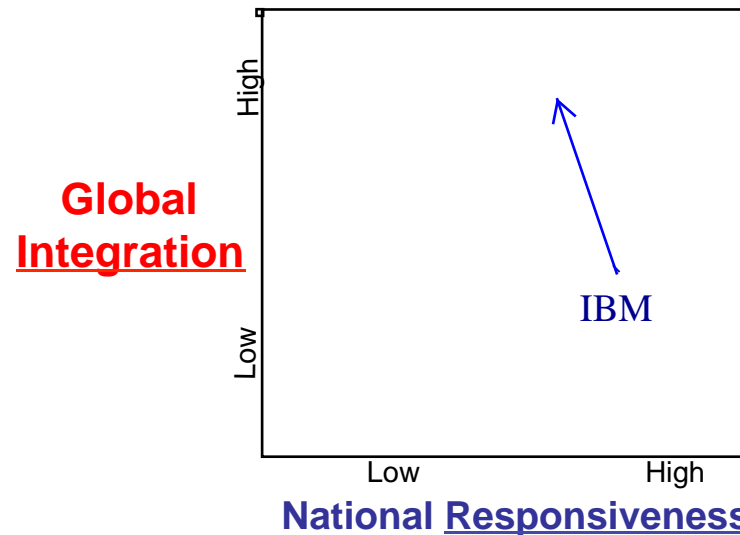


Image by MIT OpenCourseWare.

(Source: IBM presentation, 2008)








## IBM's Integration of Production and Value Delivery Worldwide

<b>Global Supply Management</b>	<b>Global Production Optimization</b>	<b>Global Demand Management</b>
Efficiently locates and secures the best global talent and production resources available in the world, inside or outsourced	Creates global scale and efficiency through modular global service centers integrated via common platforms, values and governance	Aggressively pursues high growth global markets, e.g., emerging markets, global niche markets, and global solution requirements

Image by MIT OpenCourseWare.

# The value of *Global Integration*

- ✓ Specialization  
(market knowledge, ...)
  - ✓ Proximity to customers  
(international lead customers, distant customer sites, ...)
  - ✓ Integrity  
(consistency of image, international reputation, ...)
  - ✓ Serving global customers  
(namely, customers *becoming* global!)
-  Higher global  $v^3$
- 
- ✓ Specialization  
(technologies, skills, operational capabilities. ...)
  - ✓ Scale  
(R&D, manufacturing, operations, procurement, ...)
  - ✓ Scope (across countries)  
(management teams, plants, offices, distribution channels, ...)
  - ✓ Flexibility  
(redundancy in the supply chain, arbitrage of factor costs,...)
-  Lower global  $c^3$
- 
- ✓ Competing globally  
(coping with multipoint competition and “grey trade”)
-  Higher overall  $p$

# Global Integration: The value propositions

- 1) Global integration is not equally advantageous to all companies in all businesses. One needs to assess the economic and financial value of global integration, for the cost of global integration is granted and noticeable (namely for the multi-domestic MNC). There is no benchmark here. However, if the extra value of global integration is not substantial (say, 15% or more of your top line), it may be wiser to reconsider it. However, failure to globally integrate may simply mean going out of business, in which case it becomes an imperative, not an option. When estimating the value propositions of global integration, the base case is the same MNC with autonomous country subsidiaries.
- 2) High global integration brings added *value to customers or users* (and higher “willingness to pay”) because of one or more of the following factors: market specialisation; proximity to customers; integrity; and serving global customers.
- 3) The active *proximity to local customers* is particularly valuable during customer acquisition, business negotiation, and delivery, more noticeably in the provision of services and solutions. Behaving like a drone will not satisfy a local customer that values a supplier that is “easy to work with”, flexible and able to perform real time adjustments. If the MNC supplier is seen as distant or slow, this will easily generate a perception of unreliability and turn into loss of business. However, this is valid for all MNCs as suppliers, globally integrated or not. What the globally integrated MNC can achieve by being proximate to its local customers is to access the knowledge of users in the product’s lead country market, even tacit and locally-specific knowledge, as well as to learn how to respond to the most demanding customers in the world and convey such knowledge internally to its other units around the world. In both cases this will potentially turn into differentiated offerings and superior value proposition to local customers everywhere. For example, an integrated MNC can augment their offering to a local customer by throwing in the role of international knowledge broker. Accenture, for example, can benefit a local ERP implementation by adding the knowledge it gained from its experience of similar implementations in more advanced contrives in the client’s industry with due respect for third-party IP. This will most likely increase the performance of the client, or be perceived as such. Local suppliers or local units of non-integrated MNCs can’t easily offer that.

## Global Integration: The value propositions (cont.)

- 4) Local units should be specialists of local demand and be intimate with local lead users, local demanding customers and local non-customers. Such *local market knowledge* (for example, what product attributes local customers value more and value less, now and tomorrow) is then brought into the product design and development processes *together* with that from colleagues from other country markets. It is this *comparative* and *parallel* process of product design and development that will optimize the value for the various local customers while aggregating those features that are commonly shared across borders (the "*global product platform*", as is called in some industries). A product is no longer the ad-hoc adaptation of a home-based design to each local market (a sequential process, regularly sub-optimal), but a globally integrated design.
- 5) *Integrity* and reputation are valuable in all businesses and paramount in some, be it goods such as pharmaceuticals, food and beverages, or cars, or services such as healthcare, auditing, or corporate banking. This is not new in a global world. What is new is that an incident anywhere, even in a small and remote location of the planet, will quickly be turned into worldwide news. Customer trust and investor goodwill everywhere can be lost in a blink of an eye. Just recall that Arthur Andersen, an old, large and highly respected auditing firm by all over the world, disappeared in a fortnight after the Enron imbroglio, which was traced to a failure by a relatively small office in Texas – of which most partners around the world had never heard of before. The recent BP disaster in the Gulf of Mexico is another case in point – and the BP chief executive had never heard of that platform either. This has a direct bearing on global integration, for both local failures and ineffective responses are indicators of a non-globally integrated organisation, particularly one where local performance optimization is managed irrespective of global risk, and where global compliance and global oversight are lacking. Arthur Andersen and BP are exemplary in these respects too; in the instances above, and given the high status and businesses of the two institutions, what the world did not forgive was the obvious lack of compliance with professional and safety norms. "One for all" is even more effective in the negative.
- 6) A *global customer* finds value in a MNC supplier that is equally integrated or more so. The particular needs of a globally integrated customer include the coordination of procurement and delivery across borders, joint worldwide capacity, logistics planning and review meetings, flexibility in delivery locations, worldwide quality assurance, global service levels, and, not least, global pricing agreements. A non-integrated MNC supplier is disruptive to a MNC customer in the process of integrating as the supplier local units will act as centrifugal forces to the customer local units.

## Global Integration: The value propositions (cont.)

- 7) High global integration brings *lower costs* because of the following factors: specialization; scale; scope (across countries); and flexibility.
- 8) The international *specialization* of operations brings lower costs through two direct efficiency effects. Focusing a plant or a service center on a particular product for a set of countries, even the whole world, brings *faster* accumulated experience, a “learning curve” effect. But it also allows for a unit’s location choice that will optimize the local availability of *world-class* technicians and workers, suppliers, and knowledge spillovers from similar local units, a “cluster” effect. Furthermore, the MNC can learn first-hand experientially where in the world are the more technically savvy, capable and efficient suppliers, R&D institutes, banks, consultants, and so on. Such deep access to superior technologies and other inputs will not only provide for the continuous improvement of the MNC’s operations and product offering everywhere, but even bring about new breakthrough products.
- 9) Global integration allows for the geographical concentration of operations. This will bring about larger *economies of scale* than even the largest country market affords (technology permitting). Historically, the Japanese MNCs in cars and consumer electronics that grew to prominence in the 80s (such as Toyota, Sony, or Matsushita/Panasonic) took great cost advantage from their “export-model”, often based on a single plant in Japan producing for the whole world. Their Western competitors, established MNCs, had a large number of plants around the world, sometimes producing for one country only – the legacy of a non-global world. Such impact of economies of scale and lower prices in the growth of Japanese MNCs in such industries (at the expense of famous local and international brands such as Volvo, Rover, RCA, Philips, and many more) prompted scale to become the most obvious and popular effect of globalization. Bargaining power with suppliers is steeply increased by buying at a multi-country level. Economies of scale in R&D are also very relevant in industries such as chemicals, semiconductors, or pharmaceuticals, where product differentiation across countries is minimal – and which were among the first industries to become “global.” (“R&D intensity,” the ratio of R&D expenditures over sales, is one of the accepted measures of an industry’s propensity to globally integrate.)

## Global Integration: The value propositions (cont.)

- 10) However, the more specific efficiency effect of global integration lies in *economies of scope* across countries. Such international scope in the MNC can easily be confused with scale. Economies of scope derive from the use of the same asset to produce two (or more) different products or activities. Economies of scale come from it producing twice or more of the amount of one product or activity. The confusion between scope and scale in the MNC comes from the fact that “global markets” are rare, and therefore most goods and services are somewhat locally adapted. Such localization in a non-global world meant one factory per country with local scale. In a global world, it means one factory capable of producing several *country variations* of the product. There will be economies of scale in the production of the common parts or “global platform” of the product, and economies in scope in the rest of the product. However, if one considers the economics of the whole product, then what we should account for are economies of scope across countries, for that is the source of variation. If one repeatedly focuses on economies of scale, there may be the usual and uncalled for confusion between aggregation and integration, the belief that globalization requires standardization of the product across borders. The potential for economies of scope is yet very large in all functions and tasks, including management. Many MNCs have now dispensed of country head offices, and one regional office manages selected activities in a number of countries. Again, note that overseeing sales in Spain and Portugal are *not* the same activity (local languages differ, labour and commercial law are different, buying patterns are different, and so on). One should not state that a central office in Madrid for the whole of the Iberian Peninsula provides an economy of scale across the two countries – what it constitutes are economies of international scope. For what has happened in some cases is that the Madrid office starts to treat sales in Spain and Portugal *as if* the two were the same. The corollary is poorer top line performance, usually superior to the realized economies of scale (literally, in such case...).
- 11) *Flexibility* across borders is a particular source of lower costs or higher returns in the integrated MNC. There are two sources of advantage here. One is the flexibility of diverting operations to another country unit in the presence of local surges in demand, local shortages of inputs, or local disasters. The other is the arbitrage of factor costs, namely on the price of inputs that are immobile or non-tradable across borders, such as energy prices, labour rates, tax rates, licensing rights, or exchange rates. The ability to draw on flexibility in the MNC calls for redundant capacity by design; worldwide information on current capacity utilization, short term requirements, and factor prices; as well as suppleness in capacity planning and procurement routines across countries. Flexibility in the MNC also reduces the bargaining power of local unions as the threat of activities being sent abroad is credible. Unions have responded by coordinating their actions across countries (globalization is for all...).

## Global Integration: The value propositions (cont.)

- 12) High global integration also brings a higher value captured through *higher price* because of higher willingness-to-pay and superior ability to compete globally.
- 13) Industrial economists were among the first to look into how competition would change in an open world. Take the popular “five forces” model by economist Michael Porter. If the forces that matter in one industry are all by local agents (suppliers, buyers, rival incumbents, new entrants, and substitutes), then the industry will behave as a domestic industry in different countries (hence, multi-domestic), even in a global world. The global integration impact on product prices and on factor prices will be zero or very small. However, if one or more forces have international reach, then the industry is “global.” The case of multipoint competition is illustrative. Company A competes with company B in country X and in country Y. If A lowers the price in X and forces B to lose an important deal there, then B can lower its prices in Y to cause even greater damage to A. The country manager of A in Y won't know what hit him, and may not even suspect that the cause of such loss was an act by his colleague managing A in X. In an industry where incumbents reach internationally, global integration keeps the average price higher by coordinating pricing within the company across countries and by stopping or minimizing local competitive races to the bottom. Another instance: facing up to a powerful international buyer or supplier will imply coordinated sales or purchasing negotiations across countries. A non-integrated MNC supplier will have lower bargaining power when facing a more integrated MNC customer, who can better gather and put to use information about the procured product market conditions, pricing and terms around the world.
- 14) Higher average price will also result from a higher willingness-to-pay by local and global customers that will value the global positioning of the MNC as we saw above with the customer value proposition of global integration.
- 15) The coordination and control of sales and prices across borders inside the MNC can also keep the world average price higher by eliminating or minimizing the viability of grey-trade (when a local customer buys from a MNC and is able to re-sell the same goods in another country in competition with the same MNC or its official distributor there). These practices usually fall under local and international competition laws.

## Global Integration: The value propositions (cont.)

- 16) A note on the transfer of “best-practices”: The international transfer of best-practices is not a trademark of the globally integrated MNC. Any local unit of any MNC or even any local company can benefit from sourcing knowledge abroad. Such transfer is difficult and costly anyway because of the messy and sticky nature of knowledge (for example, technical know-how and operational skills are markedly tacit and context-specific). However, global integration creates the conditions for superior transfer of best-practices in two ways. Even before the transfer begins, the receiving unit must be aware of the very existence of the different practice abroad and whether it constitutes a best-practice. And then it must be able to source it, which may simply be impossible or very costly if the IP is owned by a competitor. The globally integrated MNC addresses these access difficulties by institutionalizing internal contests and exhibitions of best-practices, technical steering committees, cross-country functional teams, centers of excellence, and through the mutual visits of local managers around the world or via the information exchange at the eGLT. We also know that the transfer of best-practices depends on the absorptive capacity and motivation (the “skill and will”) of the receiving unit, and on the quality of relations between the sending and receiving units. Again, the global integrated MNC fosters a corporate context in which such factors can be addressed with team spirit across countries, complemented with training in-context and special performance appraisal metrics and incentives. So, the *transfer of best practices* is not specific to global integration, but a globally integrated MNC can benefit from a more effective and efficient transfer of best-practices across its units around the world. Therefore, global integration causes a *better performing transfer* of best-practices.
- 17) And what about *risk*? Global integration may sharply increase economic performance and financial returns, but it will also increase risk. The multi-local MNC diversifies country risk, the globally integrated company amplifies enterprise risk. That is the hallmark of interdependence. What happens anywhere can affect everywhere. Note that the root cause of such added risk is the “global world” we live in. Even a multi-local company can suffer from the domino-effect of a failure across countries. What is special about the global integrated MNCs is that structural choices *made by the company* render its units in each country dependent on units in other countries, irrespective of what happens in the world. An operational failure in one country may turn into higher costs in many countries. A global customer poorly served in one country may react everywhere. The internal and external global risk amplification may produce very nasty effects, as the recent Toyota’s “sudden acceleration” case shows.



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