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Engaging the Chinese Market

BY PAUL W. BEAMISH

Corporate leaders are being rightly pushed by their boards, investors and the media to develop and maintain a coherent international strategy. Such a strategy is intended to incorporate a dominant role for foreign markets in terms of some combination of these countries as markets, sources and/or loci of competition.

Of particular interest in recent years is the role of emerging markets. The largest and fastest-growing emerging market is China. Hence we use it to illustrate how an emerging market might be engaged. The statistics and evidence offered in support of embracing the China market have been overwhelming: China has the largest potential consumer market in the world, is already the second largest economy on a purchasing power parity basis (see column 1 in Exhibit 1), has a growth rate over the past 20 years averaging nearly 10 percent per annum and sees foreign investment in the range of $50 billion per year.

As a consequence, tens of thousands of companies have established some form of operation in or with China, motivated by one or more textbook reasons for venturing into any foreign market. The emphasis on the first of these reasons—sourcing, or resource-seeking—is on securing key supplies or gaining access to factors of production. With China's seemingly infinite supply of low-cost labor, and the way it has been able to commoditize the manufacturing of many goods and processes, entire industrial sectors now source primarily from China on the grounds that it is the only way for them to remain competitive. Such sectors range from electronics to toys.

A second motivation for the focus on China relates to the market itself. China is perceived as an increasingly important market to sell into, particularly as the pace of development quickens. Such a market-seeking orientation allows the investing firm to exploit some inherent skill or competitive advantage it possesses, permitting it to spread its R&D costs over a larger customer base and to provide scale economies.

The third reason why many firms are being exhorted to go to China is because it is the locus of competition. China is where the action is, where firms can scan first-hand what their existing and future competitors are doing, and learn accordingly.

Yet, despite such compelling arguments, thousands of firms have nonetheless opted not to jump on the China bandwagon. They have little, or no, sourcing from China, are not aggressively pursuing Chinese customers and do not have an ear to the ground with regard to new, emerging competitors there. Why? To answer this question, members of the Ivey cross-enterprise research center focused on engaging emerging markets asked

EXHIBIT 1: Emerging Markets: Major Sources of Economic Output

Purchasing Power Parity GDP (Int'l $ Billion) Economic output measured by looking at the prices of a bundle of goods and services at home in local currencies		**Gross National Income (GNI) (in US$ Billion)** Economic output measured by valuing each country's goods and services in dollars, using three-year average exchange rates		**Population (Million)**	
USA	14, 093	USA	14,574	CHINA	1,325
CHINA	7,909	JAPAN	4,869	INDIA	1,140
JAPAN	4,358	CHINA	3,888	USA	304
INDIA	3,359	GERMANY	3,507	INDONESIA	227
GERMANY	2,905	UNITED KINGDOM	2,827	BRAZIL	192
RUSSIA	2,260	FRANCE	2,696	PAKISTAN	166
UNITED KINGDOM	2,178	ITALY	2,122	BANGLADESH	160
FRANCE	2,122	SPAIN	1,455	NIGERIA	151
BRAZIL	1,978	CANADA	1,454	RUSSIA	142
ITALY	1,872	BRAZIL	1,401	JAPAN	128
MEXICO	1,549	RUSSIA	1,371	MEXICO	106
SPAIN	1,443	INDIA	1,187	PHILIPPINES	90
KOREA	1,344	MEXICO	1,062	VIETNAM	86
CANADA	1,302	KOREA	1,046	GERMANY	82

Source: World Development Indicators database, World Bank, 19 April 2010, for 2008.

Note: Shaded sections signify emerging markets.

dozens of executives working inside and outside China why some companies do not or should not go there. We found that the reasons given by executives for avoiding engagement with the world's largest emerging market were largely chained to an outdated general management paradigm focused on narrow, disaggregated functional disciplines (problems with operations, human resources, marketing and so on). Furthermore, executives tended to invoke narrow rationales for cross-cultural difficulties based on traditional hierarchical command-and-control notions of the firm, rather than viewing their organization and their leadership within it as part of a broader network of value-adding entities with distributed leadership.

Engaging the China market *successfully* requires moving beyond traditional general management approaches to activating a cross-enterprise leadership perspective that is anchored in a deeper strategic commitment to important business issues that permeate functional silos. These business issues include decisions that involve the total enterprise, such as innovation, environmental degradation or health and safety issues. Given the dynamic, complex and uncertain context of emerging markets, traditional general management systems, with their clearly defined functions and organizational boundaries, designed for stable and predictable environments are second-best ways of creating, capturing and distributing value across a network of companies.

Managerial Perceptions of Concerns with the China Market: General Management versus Cross-Enterprise Leadership Approaches

This section details the primary reasons we heard executives give for avoiding engaging with the world's largest emerging market. We demonstrate how, by and large, these reasons reflect a traditional general management perspective to business rather than a cross-enterprise leadership approach, highlighting the missed opportunities along the way. To further illustrate the differences between the two perspectives, we use the research and writing projects undertaken by members of Ivey's Engaging Emerging Markets Centre. We conclude with several recommendations for growing and developing cross-enterprise leaders charged with designing and executing a China strategy.

General Management

Most of the reasons executives provided as to why companies avoid China were anchored in a functional rationale typical of traditional general management models. These arguments can be roughly broken down into problems related to specific departments such as operations, human resources, marketing and legal issues. In what follows, we detail these difficulties as perceived by our panel of executives and described to our research team.

Operations

- **Raw materials and energy shortages** still occur throughout China. It is difficult to maintain manufacturing operations with rotating blackouts or materials shortfalls.
- **Lengthy supply lines** from China are vulnerable to disruption because of port congestion, security-related slowdowns and inadequate infrastructure. As a result, hoped for savings in inventory carrying costs in just-in-time production may be negated by the need to warehouse large quantities of parts due to lengthening supply lines.

Human Resources

- **Employment stability** in China continues to be a significant problem. Workers will literally change jobs for $0.10/hour because even a modest increase of $1.00/day can mean a significant increase in their total annual income. The resultant high employee turnover can have major implications on such areas as quality control, training expense and morale. Some observers have likened it to staffing your factory with a rolling group of summer students. It is hard for North American managers to really appreciate the implications associated with more than 100 million migrant workers in China.
- **The supply of experienced managers** is limited in China. With 127 universities offering MBA and executive MBA programs, China has taken enormous strides to increase the supply of professional managers. This has been supplemented with output from such groups as the National Accounting Institutes, plus Chinese educated abroad who return (known locally as "sea turtles"). Most, however, lack meaningful experience with "best practices" in the west. Those in China with good experience, whether expatriates or locals, are in very high demand. In the absence of an ability to find good quality, affordable management in China, some potential investors prefer to stay home.
- **Employee relations at home** is also an issue that resonates more strongly with some executives than others. The idea of closing down production lines or entire factories, throwing hometown employees into the ranks of the unemployed, is too bitter a pill to swallow for some leaders.

While Japanese-style, life-time employment was never guaranteed, some executives have long felt that they have a moral contract to try to maintain home country employment. To suddenly source product from some real or imagined "sweatshop" in China is not acceptable to them.

Marketing

- **The uneven concentration of target consumers** is a real challenge for many firms marketing in China. The issue is not, of course, one of finding concentrations of people. There are 118 urban districts in China of more than one million people, including 13 with over four million people. The issue is that average wealth levels between these cities vary enormously. Most companies are aware that the citizens of Shanghai have the greatest average income of any city in China, so most companies are marketing in Shanghai. But what about the other provinces and the other urban districts with more than one million people? These districts have per capita annual incomes that are less than half that of Shanghai's. How many widgets or services can you sell if the average citizen is only making $10.00 a day?
- **State-owned enterprises (SOEs) as competitors** in China has given many existing and potential marketers in China real pause. Companies have heard the original horror stories about how China is dominated by SOEs and that some SOEs—which may compete in the same industry—have been allowed to run enormous losses year in and year out. This perception of a lack of normal competitive practices in China, notwithstanding that the central government has been systematically reducing the number of SOEs in

the past decade, has meant that some foreign firms have refused to enter the market.

- **Adapting products/services** to the China market is something that some firms are unwilling to do. Such firms have a take it or leave it attitude to Chinese customers. A lack of willingness to adapt to the unique realities of the market—whether in terms of product size, packaging, language or so on—means that most consumers will not purchase. An unwillingness to adapt products or services thus shuts some firms out of the China opportunity.

- **Country of origin** has always been a major issue for international marketers. While a "Made in China" label will not attract any consumer attention when it is on an inexpensive T-shirt at the local Wal-Mart, what if the same label is on a pharmaceutical product, or critical aircraft part? The importance of the country of origin that consumers attach to products varies by industry. In addition, the overall perception of countries as producers of quality products varies as well. China has started in the low-quality, low-cost quadrant and made some progress. However, the experience of other countries suggests that it takes years to achieve dramatic change with regard to country-of-origin effects.

Legal

- **Intellectual property protection** is inadequate or invisible in much of China. Many foreign firms have found to their great discomfort that the processes they have licensed to a Chinese manufacturer have been stolen outright, with no meaningful legal recourse. Creating a low-cost competitor(s) is never the objective of sourcing from China, but sometimes it's the reality.

- **Corrupt practices** in China cause another group of firms to avoid operating there. In emerging nations, where comprehensive legal and regulatory frameworks either do not exist or are not enforced to curtail fraudulent activity, corruption serves to reduce foreign direct investment. Certainly more corruption exists in China than in any of the industrialized countries of the west, according to Transparency International's Corruption Perceptions Index (CPI). No country, of course, has a monopoly on corruption, nor is any country immune from its citizens participating in corruption. Some potential investors simply prefer to delay entering a particular market until overall corruption falls to an "acceptable" level.

- **Import quotas** are being established by a number of foreign governments to stem the impact of cheap Chinese goods, causing some firms to rethink their China exposure. Chinese exports have been so successful in a variety of sectors that different governments have resorted to protectionist practices to protect domestic employment. It is not that there is widespread "dumping" (the sale of goods below the real cost of production). China is simply producing at a lower cost than is observed in other countries. Ironically, the beneficiaries of this use of quotas are some of the emerging markets, such as Bangladesh, Mexico and Brazil, that lost the same jobs to China over the past decade.

- **Legal recourse** is a concern to a number of investors. Does the rule-of-law apply? Is there a level playing field in the event of legal disputes? Some say no.

Cross-Enterprise Leadership

In comparison, rather than focusing on functional constraints as outlined in the previous section, cross-enterprise leaders are able to anchor strategic business decisions, including the go/no go China decision, in important business issues; in complex, uncertain and dynamic environments, there is no such thing as a *manufacturing* issue or a *marketing* issue, there are just *business* issues. Cross-enterprise leaders can see beyond forced departmental silos and consider how important business issues such as innovation can permeate not only across the various units within their own firm, but also across the entire network of value-adding entities with which they interact. For example, many telecommunications companies such as Motorola and Nokia are focused on delivering on innovation and recognize that they must lead across a network of alliances, joint ventures and strategic partnerships to create and capture value in this regard. Both firms have established—not just outsourced—manufacturing facilities in China and have engaged in developing full-scale R&D centers there, including partnerships with researchers at Chinese universities. These arrangements create complex interdependencies that distinguish an "enterprise" from an "organization"; boundaries are less clear and leadership around the core issue of innovation is more distributed throughout the network, rather than dictated in a hierarchical fashion from within a traditional general management paradigm.

Product safety is another business issue that cannot be the responsibility of just one particular functional department. In 2007, Ivey PhD graduate and Engaging Emerging Markets Centre member Dr. Hari Bapuji began exploring the reasons for the many recalls of toy products from China. His analyses (with colleagues at the University of Manitoba) empirically challenged the received wisdom that most of the problems with recalled toys from China were due to mistakes by the Chinese manufacturers. He was able to demonstrate that most recalls were in fact due to design issues, which were the responsibility of the foreign, not Chinese, companies. In fact, the story that unfolds at Mattel in particular is one of a lack of cross-enterprise vision with regard to leadership on the safety issue.

In mid-2007, Mattel faced two different problems: (1) in some toys, excess lead paint and (2) in other toys small magnets that detached and posed an aspiration hazard to children. While the lead paint problem appears to lie within the supply chain and would therefore be typically defined as a manufacturing problem, the small magnet issue is clearly a design flaw and thus more directly Mattel's responsibility. Mattel, however, tried to pin both issues on its Chinese partners invoking an "us versus them" mentality. The failure here, from a cross-enterprise leadership perspective, was to recognize that product safety cannot be an "us versus them" problem, or even a manufacturing versus design issue—safety is inherently a core business issue at the heart of the Mattel enterprise. Leading cross-enterprise means taking an enterprise-wide perspective on core business issues, such as safety or innovation, and making decisions that create and deliver value to all stakeholders.

Exhibit 2 summarizes some of the key differences between a general management and a cross-enterprise leadership approach.

EXHIBIT 2: Differentiating General Management and Cross-Enterprise Leadership

ELEMENT	GENERAL MANAGEMENT	CROSS-ENTERPRISE LEADERSHIP
Entity	• Within organizations • Boundaries defined	• Enterprise – A network of value-adding entities • Boundaries unclear
Context	• Generally stable and predictable • Longer planning horizons	• Complex and uncertain • Dynamic • Real-time
Leadership	• Hierarchial • Managerial focus	• Distributed • Management & leadership focus
Orientation	• Functional anchor	• Issues anchor
Educational approach	• Knowledge	• Think-Act-Lead

Source: Crossan, Mary and Fernando Olivera, 2006, "Cross-Enterprise Leadership: A New Approach for the 21st Century," *Ivey Business Journal Online*, May/June.

The Four Cross-Enterprise Leadership Capabilities and a China Strategy

Other reasons we heard for not engaging the China market related directly to the lack of knowledge, understanding or skills required by a cross-enterprise leader. Crossan and Olivera, as discussed in chapter 1, have described these four cross-enterprise abilities as strategic, business, people and organizational intelligence. The first of these, strategic intelligence, requires a fundamental understanding of the business context—an ability to see opportunities and threats before they arise as well as an ability to focus beyond the short-term dictates of share price to the longer-term implications of strategic decisions. To illustrate, we found that complacency is at the root of why another group of firms said they have not gone to China. The leaders of these firms are comfortable with the status quo and are either unable or unwilling to embrace change. These executives maintain an attitude that "China" is one more fad of the day that will not affect them, or that its impact will be negligible. Similarly, ethnocentrism still exists in many organizations in industrialized countries. There is a belief in some circles that there is nothing to be learned about best practice as a consequence of doing business in China. Worse, no value is attached to seeing, first-hand, the creation of future China-headquartered competitors. It doesn't matter that China already has 37 of its companies among the Fortune Global 500 largest firms. Despite this fact, some foreigners refuse to believe it could happen. Lastly, some executives focused on the fact that service sector jobs have not migrated in great numbers to China. Unlike India, with its English-speaking, more IT-savvy population, no large-scale, externally focused comparable service sector has emerged in China—yet. However, some service sector executives simply could not see this strategic opportunity, demonstrating a deficit in the type of "strategic intelligence" required for cross-enterprise leadership.

The second type of intelligence is business intelligence, which relates to understanding the fundamental nuts and bolts of the business you're in. Many of the leaders we talked to about going into China may have lacked this business intelligence because of the age of their firm. Acquiring all of the knowledge that one needs (including the portfolio of traditional general management skills like marketing, finance, operations and so on) takes time—and understanding how these connect across departments, units, businesses, alliances, partnerships and networks takes even more time. In international management, this difficulty is known as *the liability of age*—in practice, newly established enterprises simply are unlikely to either source immediately from China or market immediately to China. While there are many examples of so-called "born global" organizations, these nonetheless are more the exception than the rule. While Research In Motion might immediately view "the world" as its target market, a new furniture manufacturer would initially have a much more local or, at best, national orientation. Young organizations initially suffer high failure rates. Young organizations that need to also understand a complex foreign market such as China face an even greater hurdle. Similarly, *the liability of foreignness* suggests that when firms are first expanding abroad, they tend to focus on markets that are geographically close, and where language and cultural differences seem surmountable. For many North American or European leaders, China is indeed "foreign," in fact "too foreign" for some firms to try and source from. These firms may lack leaders with sufficient business intelligence to engage in a China strategy.

Organizational intelligence, the third type of intelligence required for cross-enterprise leadership, requires a solid command of the firm's structures, procedures and compensation systems that drive the culture of the organization. In many respects, the majority of the comments we heard for avoiding China—from operational difficulties to legal barriers—suggest organizational cultures that are resistant to change (complacent, ethnocentric, unwilling to adapt). The *liability of size* is another example of how leaders of small firms in particular might lack the kind of organizational intelligence required to move forward with a China strategy. With all the attendant resource constraints that small organizations face, sourcing directly from China or marketing directly to China might not be among the first steps taken by most small organizations. Since many of the steps required to source from China or market to China are going to be the same for small or large firms, the small firm might not have the sales volume to spread the financial risk of the effort across.

Lastly, cross-enterprise leaders must have people intelligence. In a complex, uncertain and dynamic market such as China, the ability to listen, understand, motivate and inspire organizational members is even more challenging. However, without people intelligence, the effectiveness of certain leaders will be greatly curtailed. In China, this manifests itself specifically as *the liability of relational orientation,* speaking to the heavy use of joint ventures. While it is possible to have a purely contractual sourcing arrangement from China, for example, leaders that take an arms-length approach with suppliers are often met with unpleasant delays and surprises. As a consequence, many investors choose to form joint ventures in China, even though the regulations today do not require it. These investors want a partner who can provide knowledge of the local economy, politics and culture. Yet some potential investors do not like joint ventures and do not like partners. They prefer to do it themselves, or not at all. Those with a do-it-themselves rather than relational orientation may not be willing to invest in developing the social and political connections required—in other words, the people intelligence needed to lead cross-enterprise. This is so very different from China, a country with a long tradition of *guanxi*—a system of personal contacts, networks and relationships.

As we've mentioned, in conjunction with general intellect, these four "intelligences" are the basic ingredients of cross-enterprise leadership capability—a leadership approach that is well suited for engaging emerging markets.

The research on toy recalls from China led to a series of practical recommendations in regard to ways in which a company could reduce its design flaws. These recommendations, essentially, call for building up the stores of strategic, business, organizational and people intelligence required for leading on the product safety issue (see Exhibit 3).

EXHIBIT 3: Steps Companies Can Take to Reduce Design Flaws

First, firms should establish a learning culture in which employees feel safe reporting their concerns about design flaws and in which mistakes are not ignored. Such a culture begins with managers being receptive to employees' ideas and criticisms. Companies should also engage in *reactive* learning: Once a product flaw is discovered, the firm should examine and improve the systems and processes that contributed to it. In addition, companies should engage in the four major types of *proactive* learning:

Study, Listen, Test, Track.

Study competitors' recalls, overall recall trends, issues leading to recalls, regulators' comments, and even medical journals, which sometimes report health problems resulting from product use or misuse.

Listen to design and test engineers, whose concerns are often downplayed or overlooked in the excitement of taking a new product to market.

Test effectively for safety issues. Too many toy companies rely on live humans to test product appeal but not safety features. While dummies are clearly appropriate in crash-testing carseats and the like, many companies can spot potential dangers by having people use products in realistic settings. At the least, such tests would guide companies in providing clearer instructions and warnings.

Track customer feedback to look for patterns that might reveal product flaws.

Doing all this properly requires that companies buck the trend of downsizing design and testing departments. It also requires that teams be set up to monitor the vast amount of useful information out there, from recall data to customer complaints. And it requires that these teams be coordinated at the highest organizational level—by the executives with responsibility for looking, unflinchingly, at the big picture.

Source: Bapuji, Hari and Paul W. Beamish, 2008, "Avoid Hazardous Design Flaws," *Harvard Business Review*, 86(3): 23, 26.

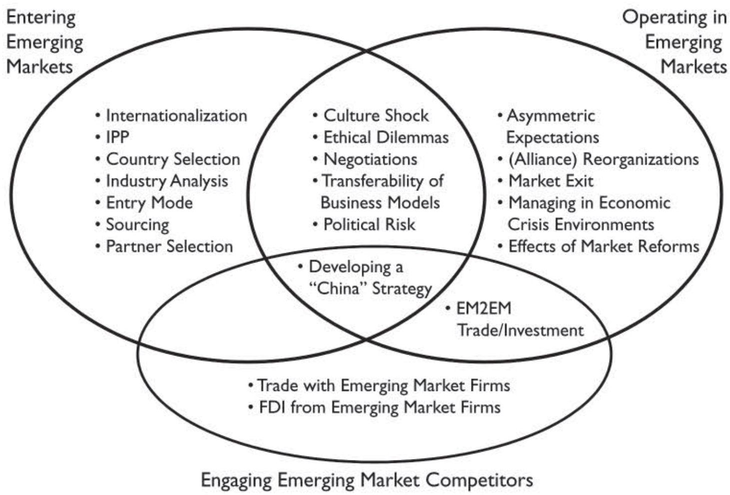
Engaging Emerging Markets—Cross-Enterprise Leadership Centre

The research into toy recalls from China illustrates one of the most important roles for any business school—the generation of intellectual capital or the continuous development of new insights and new models for the discovery of best practices that have direct relevance to managers today. Schools that deliver cutting-edge research not only provide real value to the academic community but also ensure that their programs are consistently renewed with new insights, which have a direct effect on the business community. At Ivey, the Engaging Emerging Markets Cross-Enterprise Leadership Centre is dedicated to research that helps executives overcome some of the perceived barriers listed in this chapter and to pursue the myriad of opportunities that lie within the borders not only of China but other emerging markets as well.

Exhibit 4 provides a more detailed framework for the ongoing research on engaging emerging markets at Ivey. It contains examples of the types of issues and phenomena that Centre members have pursued or are currently investigating. Many other issues undoubtedly will be pursued in the future.

EXHIBIT 4

Examples of Research on Engaging Emerging Markets



Some of the other research initiatives that Centre members have undertaken include tracking the evolving nature of the Chinese market, exploring the emerging market to emerging market (EM2EM) opportunity and partnering with emerging market enterprises to generate teaching cases. Each of these projects is designed to respond to the perceptions of managers about why they might wish to avoid China.

For example, Ivey PhD graduate and Centre member Dr. Andrew Delios (now at National University of Singapore) has been exploring the many transformations underway in China,[1] including developments in the manufacturing sector. Many of the very low-cost manufacturers that originally sprouted among China's coastal cities first moved to less expensive inland cities years ago. However, even these inland locations are now too expensive as manufacturing locales, and, as a result, some of these low-cost manufacturers are now leaving China altogether. One of the realities of the Chinese market is the very rapid speed of change. In the west, economic growth of 2 percent per year would be celebrated, but in China this is typical of quarterly growth. If the market is growing four times as fast (or faster) in China as it is in North America or Western Europe, and as a leader you haven't visited China in a few years, your understanding of current market reality could be the western equivalent of a decade out of date! Good leaders are reassessing very frequently the rules of thumb they have developed about how markets such as China actually work.

Similarly, some business leaders might feel that the business taking place between emerging markets is not relevant to their organization. However, they would be wrong. When, for example, firms from two major emerging markets join forces

1 Delios, A. and X. Ma, 2010, "China Is Undergoing a Transformation…Yet Again," *Ivey Business Journal Online*, January/February; Delios, A., P.W. Beamish and Z. Xuejuan, 2009, "The Evolution of Japanese Investment in China," *Asia-Pacific Business Review*, 15(3): 323–345.

to compete internationally, they can represent a formidable competitor for a North American– or European–based firm. Ivey marketing professor and Centre member Dr. Niraj Dawar has long been interested in the realities of EM2EM trade. Among many observations, Dr. Dawar has recently highlighted the need for multi-national enterprise leaders to define their strategic stance relative to "this EM2EM awakening" and to shed overhead costs in their organizations to gain competitiveness.

Lastly, in addition to the three aforementioned illustrative examples of how research can better inform the perceptions of business leaders, field-based case writing also can play a major role. Exhibit 5, beginning on page 142, provides short abstracts for dozens of available case studies about entering China, doing business in China and engaging Chinese competitors, in which the benefits of a cross-enterprise leadership approach can be found.

Conclusion

The development of a China strategy, let alone a strategy for all emerging markets, is a major challenge for any leader—in fact, the list of challenges may occasionally seem to be insurmountable. However, many of the reasons we heard for avoiding doing business with China were anchored in old-fashioned functional "silo-thinking," rather than focused on how thinking cross-enterprise might help firms successfully tackle core business issues. Business firm leaders are called upon increasingly to deal with the complexity of a rapidly changing and uncertain context. Firm boundaries are becoming less distinct and traditional command and control hierarchical systems simply are not flexible enough to truly leverage the value within complex networks of alliances and partnerships. A genuinely cross-enterprise leadership approach is necessary.

Luckily, strategic, business, organizational and people intelligence can be learned. The first step in developing strategic intelligence with regard to a China strategy is to simply get out from behind the desk and go to China to begin to reduce the uncertainty around the go/no go decision and to fully assess the risk/return trade-offs. This includes seeing beyond traditional barriers to strategic opportunities not just for the immediate short term, but for the longer-term horizon as well. Business intelligence can be honed through further training and development or job rotation programs that stretch leaders out of their comfortable areas of expertise. This cross-exposure can help leaders understand the important links across functional areas and leverage important knowledge regarding key strategic issues throughout the organization and the broader enterprise as well.

Organizational intelligence requires a candid examination of the structures, systems, procedures and policies within the firm that might be contributing to an organizational culture resistant to a China strategy, while developing people intelligence is anchored in a commitment to listen, learn, understand and motivate individuals to achieve extraordinary results. All four intelligences, as well as a certain degree of general intellect, are the basic ingredients of cross-enterprise leadership capability. The leadership challenge for those executives tasked with developing and executing a China strategy is to honestly diagnose their strengths and weaknesses in each area and commit to developing the skills required to lead cross-enterprise.

At the Engaging Emerging Markets Research Centre at Ivey, our objective is to conduct well-executed research in this area. By studying important issues, we hope to be in a position to better inform not only those cross-enterprise leaders charged with developing a China strategy, but also to assist any organization as they engage the world's other emerging markets.

EXHIBIT 5: Case Studies about Entering China, Operating in China, and Engaging Chinese Competitors

Entering China

NES China: Business Ethics (A) [9B01C029]
Joerg Dietz, Xin Zhang

NES is one of Germany's largest industrial manufacturing groups. The company wants to set up a holding company to facilitate its manufacturing activities in China. They have authorized representatives in their Beijing office to draw up the holding company application and to negotiate with the Chinese government for terms of this agreement. In order to maximize their chances of having their application accepted, the NES team in Beijing hires a government affairs coordinator who is a native Chinese and whose professional background has familiarized her with Chinese ways of doing business. NES's government affairs coordinator finds herself in a difficult position when she proposes that gifts should be given to government officials in order to establish a working relationship that will better NES's chance of having its application approved. This method of doing business is quite common in China. The other members of the NES team are shocked at what would be considered bribery and a criminal offence in their country. The coordinator must find a practical way to bridge the gap between working within accepted business practices in China and respecting her employers' code of business ethics. The (B) case (9B01C030) gives a brief summary of the eventual solution to this problem.

Sun Life Financial: Entering China [9B04M066]
Paul W. Beamish, Ken Mark, Jordan Mitchell

Sun Life Financial is a large insurance conglomerate with $14.7 billion in annual revenues. The vice-president for China must formulate an approach for his company's entrance into China. Sun Life has achieved two important milestones: the right to apply for license and the signing of a Memorandum of Understanding for Joint Venture with China Everbright, a local securities company. The financial vice-president must consider strategic options for entry and choose a city in which to focus his efforts in getting a license. In doing so, he needs to consider Sun Life's overall priorities, strategic direction and how he will sell the concept to senior management in Canada. Intended for use in an introduction to international business course, the case includes assessing internal capabilities against an environmental scan, formulating strategy and making operational decisions relating to city selection. It also introduces the idea of joint venture management and government relations.

Palliser Furniture Ltd.: The China Question [9B04M005]
Paul W. Beamish, Jing'an Tang

Palliser is Canada's second largest furniture company. The company has production facilities in Canada, Mexico and Indonesia and experimented with cutting and sewing leather in China. The company is looking at further expanding the relationship with China. Ever since Palliser set up a plant in Mexico, the company has faced increasing competitive pressure from Asia, especially from China. The president of Palliser must decide what form this relationship should follow: Should it be an investment, either wholly or partly owned, or should it be through subcontracting?

Majestica Hotel in Shanghai? [9B05M035]
Paul W. Beamish, Jane Lu

Majestica Hotels Inc., a leading European operator of luxury hotels, was trying to reach an agreement with Commercial Properties of Shanghai regarding the management contract for a new hotel in Shanghai. A series of issues require resolution for the deal to proceed, including length of contract term, name, staffing and many other control issues. Majestica was reluctant to make further concessions for fear that doing so might jeopardize its service culture, arguably the key success factor in this industry. At issue was whether Majestica should adopt a contingency approach and relax its operating philosophy, or stick to its principles, even if it meant not entering a lucrative market.

PepsiCo Changchun Joint Venture: Capital Expenditure Analysis [9B00N016]
Larry Wynant, Claude P. Lanfranconi, Peter Yuan, Geoff Crum

PepsiCo Inc. spanned more than 190 countries and accounted for approximately one-quarter of the world's soft drinks. The vice-president of finance for PepsiCo East Asia had been collecting data on the firm's proposed equity joint venture in Changchun, China. While PepsiCo was already involved in seven joint ventures in China, this proposal would be one of the first two green-field equity joint ventures with PepsiCo control over both the board and day-to-day management. Every investment project at PepsiCo had to go through a systematic evaluation process that involved using capital budgeting tools such as new present value and internal rate of return . The vice-president needed to decide if the proposed Changchun joint venture would meet PepsiCo's required return on investment. He also was concerned what the local partners would think of the project. The final decision would be made after a presentation to the president of PepsiCo Asia-Pacific.

Beijing Toronto International Hospital [9B01A006]
Kenneth G. Hardy, Ken Mark

Beijing Toronto International Hospital was a new private facility being built in Beijing that would offer a full range of general and specialized Western-quality medical services to a very specific market segment: expatriates and wealthy Chinese families. Membership cards were sold that entitled each member to a distinct level of hospital service. The chief executive officer found that as the building neared completion, only a few memberships had been sold, which resulted in a cash shortage. He did not know why sales failed to materialize as expected, but felt that he must redirect and revitalize the marketing campaign. He considered several options and had to determine what would work best in the Chinese market.

Textron Ltd. [9B01M070]
Lawrence Beer

Textron Ltd. is a family-owned manufacturer of cotton- and sponge-fabricated items. The company wants to expand its business with an offshore manufacturing enterprise that will fit with the company's policy of caring for their employees and providing quality products. The company is looking at two options: a guaranteed outsourcing purchase agreement or a joint venture. After several meetings with offshore alliance candidates the vice-president of the company must analyze the cross-cultural differences to established corporate guidelines of global ethics and social responsibility that the company can use in their negotiations with a foreign manufacturing firm.

Scotts Miracle-Gro: The Spreader Sourcing Decision [9B08M078]

John Gray, Michael Leiblein, Shyam Karunakaran

The Scotts Miracle-Gro company is the world's largest marketer of branded consumer lawn and garden products. Headquartered in Marysville, Ohio, the company is a market leader in a number of consumer lawn and garden and professional horticultural products. The case describes a series of decisions regarding the ownership and organization of the assets used to manufacture fertilizer spreaders. This case is intended to illustrate the application of and trade-offs between financial, strategic and operations perspectives in a relatively straightforward manufacturing "make-buy" decision. The case involves a well-known, easily described product that most students would assume is made overseas. Sufficient information is provided to roughly estimate the direct financial cost associated with internal (domestic) production, offshored (non-domestic) production and outsourced production. In addition, information is included that may be used to estimate potential transaction costs as well as costs associated with foreign exchange risk.

Operating in China

Nike Inc.: Developing an Effective Public Relations Strategy [9A99C034]

Kathleen E. Slaughter, Donna Everatt

In the early 1990s, the first article surfaced alleging that factories subcontracted by Nike in China and Indonesia were forcing workers to work long hours for low pay, and for physically and verbally abusive managers. The article was the seed of a media campaign that created a public relations nightmare for the company. A financial crisis in Asia and intense competition in the domestic market contributed to a decline in Nike's revenue and market share after three years of record performance. Though no direct correlation could be proven between the consumer's negative perceptions of Nike and the company's decline in market share and stock, it certainly did not help in their efforts to establish themselves as the global leader in a hotly competitive industry. A linear overview of the adverse publicity that Nike received, and the perspectives of Nike senior management, demonstrates to students the importance and elements of the timely development of an effective media and consumer relations campaign.

Taming the Dragon: Cummins in China (Condensed) [9B05M034]

Charles Dhanaraj, Maria Morgan, Jing Li, Paul W. Beamish

This case documents more than 15 years of U.S.-based Cummins, a global leader in diesel and allied technology, and its investment activities in China. While the macro-level indicators seem to suggest the possibility to hit $1 billion in revenues in China by 2005, there were several pressing problems that put into question Cummins' ability to realize this target. Students are presented with four specific situations and must develop an appropriate action plan. They are related to the respective streamlining and consolidation of several existing joint ventures, distribution and service, and staffing. The case presents the complexity of managing country-level operations and the role of executive leadership of a country manager.

Great Wall Golf & Country Club [9B00M003]
Paul W. Beamish, Donna Everatt

The newly hired director of human resources for a large golf and country club near Beijing, China, has just presented her human resources plan to the company's founder. At issue is whether this plan—in terms of recruiting, training and development, rewards and benefits—was directionally correct and implementable.

Bax Global Limited: Staff Turnover in Mainland China [9B05C035]
Jean-Louis Schaan, Nigel Goodwin

The human resources manager for logistics and supply chain management at BAX China must consider her company's high rate of staff turnover: 12 percent in the first eight months of the year. She must evaluate the company's current methods of dealing with turnover and consider what additional action should be taken. The case offers a uniquely Chinese perspective on workforce recruitment, management and retention. Logistics was a complex and rapidly growing industry in mainland China. Many multinational and domestic service providers were entering the market and expanding their operations; however, these companies had to respond to complex operational challenges and escalating customer demands. The resulting demand for skilled workers led to high turnover rates across the industry and at all organizational levels, and created margin pressure and other management challenges. The industry and the broader economy were growing rapidly. Skilled workers were in short supply because logistics was a new and developing discipline. Also, in the human resources manager's opinion, cultural attitudes resulted in low loyalty among the workers.

Mattel and the Toy Recalls (A) [9B08M010]
Hari Bapuji, Paul W. Beamish

On July 30, 2007, the senior executive team of Mattel, under the leadership of Chief Executive Officer Bob Eckert, received reports that the surface paint on Sarge Cars, made in China, contained lead in excess of U.S. federal regulations. It was certainly not good news for Mattel, which was about to recall 967,000 other Chinese-made children's character toys because of excess lead in the paint. The decision ahead was not only about whether to recall the Sarge Cars and other toys that might be unsafe, but also how to deal with the recall situation. The case details the events leading up to the recall and highlights the difficulties a multinational enterprise faces in managing global operations.

Mattel and the Toy Recalls (B) [9B08M011]
Hari Bapuji, Paul W. Beamish

On August 14, 2007, the U.S. Consumer Product Safety Commission, in cooperation with Mattel, announced five different recalls of Mattel's toys. On September 4, Mattel announced three more recalls. Some were due to the use of lead paint, while others were due to small magnets coming loose. The case outlines the handling of the recalls and their consequences, such as consumer outrage, media scrutiny, government intervention and the effect on China. Further, it discusses the design flaws for which large toy companies are responsible. The case raises issues such as who Mattel's stakeholders are, what values Mattel followed and whether Mattel needs to revisit its China strategy.

Spin Master Toys (A): Finding a Manufacturer for E-Chargers [9B01D001]

John S. Haywood-Farmer, Ken Mark

Spin Master Toys was a Canadian manufacturer of toys ready to produce its latest product, E-Charger, an electrically powered model airplane. The operations manager had to decide which supplier should design and manufacture this new product. The time frame from design to delivery was very short, requiring an accelerated development schedule. The company had a short-list of two potential companies, both located in the major toy manufacturing district of southern China, near Hong Kong. The operations manager had to develop the appropriate criteria for this decision and evaluate the two suppliers. With relatively little information and already behind schedule, the company must make its decision in the face of considerable uncertainty. The supplemental (B) & (C) cases follow the progress and the challenges of the production of the E-Charger.

Worldwide Equipment (China) Ltd.: A Sales Performance Dilemma [9B02A028]

June Cotte, Alan (Wenchu) Yang

Worldwide Equipment Ltd. is one of the world's largest manufacturers of heating, ventilating and air conditioning equipment. The Beijing regional sales manager has just heard that the sales performance of his office ranked the lowest among the sales offices in China. The Beijing sales force will not receive their year-end bonus unless the situation can be turned around quickly. He must determine whether the sales management process or a recent new hire on the sales force, whose hiring was strongly suggested by the manager's boss, are to blame for the poor sales performance, and how to keep the situation from recurring.

Wuhan Erie Polymers Joint Venture [9B03C002]
Thomas Begley, Cynthia Lee, Kenneth Law

The Erie Performance Polymers division manager in China and general manager of Wuhan Erie Polymers joint venture has just received approval for his requested transfer to divisional headquarters in the United States. In preparation, a key decision concerns his successor. He has received information on six candidates under consideration and knows that his recommendation will carry heavy weight in the final decision. The general manager has attempted to inculcate in his mainly Chinese workforce an appreciation for Western business practices and an ability to enact them. At the same time, acknowledging their substantial differences, he has tried to mix elements of both Chinese and Western values in creating a culture for the joint venture. He believes strongly that his successor must be responsive to the tensions between the relevant cultures. As he compares them, he wonders which candidate has the best set of qualities to succeed him as general manager.

Carrefour China, Building a Greener Store [9B08M048]
Andreas Schotter, Paul W. Beamish, Robert Klassen

Carrefour, the second largest retailer in the world, had just announced that it would open its first "Green Store" in Beijing, before the 2008 Olympic Games. David Monaco, asset and construction director of Carrefour China, had little experience with green building and was struggling with how to translate that announcement into specifications for store design and operations. Monaco had to evaluate the situation carefully both from ecological and economic perspectives. In addition, he had to take the regulatory and infrastructure situation in China into account, where no official green building standard exists and only a few suppliers of energy-saving equipment operate. He already had collected energy and cost data from several suppliers and wondered how this could be used to decide among environmental technology options. Given that at least 150 additional company stores were scheduled for opening or renovation during the next three years in China, the project would have long-term implications for Carrefour.

Engaging Chinese Competitors

Yunnan Baiyao: Traditional Medicine Meets Product/ Market Diversification [9B06M088]

Paul W. Beamish, George Peng

In 2003, 3M initiated contact with Yunnan Baiyao Group Co., Ltd. to discuss potential cooperation opportunities in the area of transdermal pharmaceutical products. Yunnan Baiyao (YB) was a household brand in China for its unique traditional herbal medicines. In recent years, the company had been engaged in a series of corporate reforms and product/market diversification strategies to respond to the change in the Chinese pharmaceutical industry and competition at a global level. By 2003, YB was already a vertically integrated, product-diversified group company with an ambition to become an international player. The proposed cooperation with 3M was attractive to YB, not only as an opportunity for domestic product diversification, but also for international diversification. YB had been attempting to internationalize its products and an overseas department had been established in 2002 specifically for this purpose. On the other hand, YB also had been considering another option, namely whether to extend its brand to toothpaste and other healthcare products. YB had to make decisions about which of the two options to pursue and whether it was feasible to pursue both.

Cola Wars in China: The Future Is Here [9B03A006]
Niraj Dawar, Nancy Dai

The Wahaha Hangzhou Group Co. Ltd. is one of China's largest soft-drink producers. One of the company's products, Future Cola, was launched a few years ago to compete with Coca-Cola and PepsiCo and has made significant progress in the soft-drink markets that were developed by these cola giants. The issue now is to maintain the momentum of growth in the face of major competition from the giant multinationals and to achieve its goal of dominant market share.

Midea: Globalization Challenge for a Leading Chinese Home Appliance Manufacturer [9B00A031]
Niraj Dawar, Peter Yuan

The managing director and director of overseas marketing of Midea Group, China's largest air conditioner manufacturer, had concerns about the company's domestic and global competitive position. They felt the company needed to develop a strategy to defend its home market in the wake of more liberalized imports and simultaneously develop the resources and skills required to play in a global market where its cost advantages had been nullified because international players also were exporting from China. To do so, they needed to review the company's current international strategy and examine both branding and private label options.

China Kelon Group (A): Diversify or Not? [9B03M004]
Paul W. Beamish, Justin Tan

In 1998 the soon-to-retire founder of China Kelon Group, a major home electrical appliance manufacturer, was confronting issues of market diversification (urban to rural), product diversification (refrigerator manufacturer now also producing air conditioners), and the evolution of his senior management team (from an entrepreneurial firm to one managed by professional managers). Besides offering a context to address the above issues, this case illustrates to a non-Chinese audience just how rapidly local Chinese manufacturing has developed and that such firms are future competitors for foreign companies. It also helps students explore the broader question about the ability of founder/entrepreneurs to effectively manage the transition to becoming a larger, more diversified company. Supplement to this case is China Kelon Group (B): Integration After Merger, product number 9B03M005.

Gome—King of China's Electrical Appliance Retail Chain [9B06M098]

Shigefumi Makino, Anthony Fong

The chairman of Gome Ltd., a well-known appliance retail chain, congratulated his management team for their excellent performance over the past year. For three consecutive years, Gome had been ranked the largest electrical appliance retail chain in China, and the second largest overall retail chain. Claiming to be the only true national player, Gome achieved total sales of RMB23.9 billion in 2004 and in 2005 doubled its number of stores to 426. The company's four-year plan is to capture 10 to 15 percent of the market share nationally. Gome would need to double the number of stores in the coming three years, and more importantly, it would need to work out a strategy to fend off its local and global competitors.

China Minmetals Corporation and Noranda Inc. [9B06M013]

Isaiah A. Litvak

The proposed takeover of Noranda Inc. (one of the biggest mineral players in the world) by the Chinese state-owned enterprise China Minmetals Corporation was cause for Canadian government concern as it required some understanding about the workings and objectives of state-owned enterprises. There was particular concern around the labor issues and human rights violations in China, and the possible impact of these on the proposed takeover. Equally important, Canada ran the substantial risk of sending the wrong message to China if it was to block such a takeover, and in some respects, to be seen as shutting its doors to one of the world's largest and most powerful emerging economies.