

Organization Structure and Control Systems

8 CHAPTER



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OBJECTIVES

1. To understand the importance of appropriate organizational structures to effective strategy implementation.
2. To become familiar with the types of organizational designs suitable for the level and scope of internationalization of the firm.
3. To be able to recognize why and when organizational restructuring is needed.
4. To understand the role of technology in the evolution of the networked structure; and to appreciate the role of “human networks” in achieving business goals.
5. To realize how organizational design affects the manager's job; for example, on the level and location of decision making.
6. To emphasize the role of control and monitoring systems suitable for specific situations and locations in the firm's international operations.

OPENING PROFILE: KRAFT'S POST-MERGER INTEGRATION AND REORGANIZATION

Organizational structures are major pillars on which firms build their foundations. Also important are interorganizational alliances, and control and monitoring systems that help to maintain efficient operations. Firms normally seek short-term/long-term changes when dealing with new markets, corporate expansion, and competition. This has been the case with Kraft Foods Inc. (hereafter “Kraft”), which is the largest food and beverage firm from the U.S. In 2012, the company’s high-profile and billion-dollar brands included Oreo cookies, Milka and Cadbury chocolates, Trident gum, Tang (powdered beverage), etc. Kraft also sold other brands such as Nabisco, LU, Jacobs and Maxwell House coffees, Philadelphia cream cheeses, and Oscar Mayer meats.¹

In 2011, the company’s sales stood at \$55.30 billion versus 2010’s \$49.20 billion, and its net profit surpassed \$4 billion. To capitalize on the BRICs (Brazil, Russia, India, and China) and other emerging markets, Kraft sought two major acquisitions. In 2007, the company bought LU, a biscuit firm that was owned by Groupe Danone of France for \$7.6 billion. In 2009, Kraft acquired the UK’s Cadbury Plc for \$19 billion that turned into a hostile takeover on the part of Kraft. Both acquisitions were the results of cost pressures, global consolidation, and long-term brand building.² Interestingly, in December 2011, Kraft announced its plan of splitting the whole company into two corporate entities: “snack business” (\$32 billion) and “grocery business” (\$16 billion).³ This high-profile reorganization and these corporate spinoffs were the result of Kraft’s post-merger integration that aimed at creating business efficiencies and productivity. Of course, Kraft’s post-merger spinoffs and cost-cutting plans attracted analysts’ criticism and media attention. Scott Moeller in the *Financial Times* observed: “Little did Cadbury’s management know that Kraft’s plan was to split in two to eliminate its conglomerate nature and become two more focused businesses, thereby creating more value for its shareholders.”⁴ In the business world, this was a normal process to cut cost and make changes in the post-merger period. Of course, investors and stakeholders were equally involved behind the scene when dealing with “trophy assets” and future plans of the company.⁵ The British Parliament’s Commons Select Committee also commented on the post-takeover developments in May 2011 and stated:

*“Our overall conclusion, therefore, is that, while there remain some significant concerns about Kraft’s takeover of Cadbury, a number of positive signs may be beginning to emerge. Those positive messages would have been considerably more convincing if conveyed directly to bodies such as ourselves from the top of the organization.”*⁶

Source: Syed Tariq Anwar, West Texas A&M University. Written exclusively for this book. Copyright © 2012 by Syed Tariq Anwar; used with permission.

Strategic plans are abstract sets of decisions that cannot affect a company’s competitive position or bottom line until they are implemented. Having decided on the strategic direction for the company, international managers must then consider two of the key variables for implementing strategy: the organizational structure and the control and coordinating mechanisms. The necessity of adapting organizational structures to facilitate changes in strategy, competitive moves, and changes in the environment is illustrated in the opening profile describing Kraft Food Inc.’s reorganization to accommodate new strategic directions. The failure to adapt to changing market conditions both strategically and structurally is evidenced by the short life-span of even large companies. As one example of studies highlighting corporate mortality, only 160 out of 1008 large corporations studied by Foster and Kaplan survived between 1962 and 1998.⁷ This is particularly apparent in times of radical change such as new technologies and the economic relapse that started in 2008 and resulted in many firms, such as Eastman Kodak Inc. and Borders Bookstores, going out of business or filing for Chapter 11 bankruptcy. Even General Motors, one of the largest global companies, was tipped over the edge into bankruptcy after decades of poor management, surviving only with radical downsizing and government aid. Comparatively, IBM has adapted in various ways. After realizing that the company had missed opportunities for growth initiatives, the company developed its EBO (emerging business opportunities) model into three horizons—current core businesses, growth businesses, and future growth businesses.⁸

ORGANIZATIONAL STRUCTURE

There is no permanent organization chart for the world. . . . It is of supreme importance to be ready at all times to take advantage of new opportunities.

ROBERT C. GOIZUETA,
(FORMER) CHAIRMAN AND CEO, COCA-COLA COMPANY⁹

Organizational structures must change to accommodate a firm's evolving internationalization in response to worldwide competition. Considerable research has shown that a firm's structure must be conducive to the implementation of its strategy.¹⁰ In other words, the structure must "fit" the strategy, or it will not work. Managers are faced with how best to attain that fit in organizing the company's systems and tasks.

The design of an organization, as with any other management function, should be contingency based, taking into account the variables of that particular system at that specific point in time. Major variables include the firm's strategy, size, and appropriate technology, as well as the environment in those parts of the world in which the firm operates. Given the increased complexity of the variables involved in the international context, it is no easy task to design the most suitable organizational structure and subsystems. In fact, research shows that most international managers find it easier to determine what to do to compete globally (strategy) than to decide how to develop the organizational capability (structure) to do it.¹¹ Additional variables affecting structural choices—geographic dispersion as well as differences in time, language, cultural attitudes, and business practices—introduce further layers of complication. We will show how organizational structures need to, and typically do, change to accommodate strategies of increasing internationalization.

EVOLUTION AND CHANGE IN MNC ORGANIZATIONAL STRUCTURES

Historically, a firm reorganizes as it internationalizes to accommodate new strategies. The structure typically continues to change over time with growth and with increasing levels of investment or diversity and as a result of the types of entry strategy chosen. Internationalization is the process by which a firm gradually changes in response to international competition, domestic market saturation, and the desire for expansion, new markets, and diversification. As discussed in Chapter 6, a firm's managers weigh alternatives and decide on appropriate entry strategies. Perhaps the firm starts by exporting or by acting as a licensor or licensee, and then over time continues to internationalize by engaging in joint ventures or by establishing service, production, or assembly facilities or alliances abroad, moving into a global strategy. At each stage, the firm's managers redesign the organizational structure to optimize the strategy's chances to work, making changes in the firm's tasks and relationships and designating authority, responsibility, lines of communication, geographic dispersal of units, and so forth. This model of **structural evolution** has become known as the **stages model**, resulting from Stopford's research on 187 U.S. multinational corporations (MNCs).¹² Of course, many firms do not follow the stages model because they may start their internationalization at a higher level of involvement—perhaps a full-blown global joint venture without ever having exported, for example, or a "born global" e-company.

Even a mature MNC must make structural changes from time to time to facilitate changes in strategy—perhaps a change in strategy from globalization to regionalization (see Chapter 6), or an effort to improve efficiency or effectiveness. The reorganization of Aluminum Company of America (Alcoa), for example, split the company into smaller, more autonomous units, thereby giving more focus to growing businesses, such as automotive products, where the market for aluminum is strong. It also enabled Alcoa to link businesses with similar functions that are geographically divided—that is, to improve previously insufficient communication between Alcoa's aluminum operations in Brazil and its Australian counterparts. Alcoa, as with most MNCs, has found the need to continuously adapt its structure to accommodate global expansion and new ventures. As of February 2012, Alcoa had a presence in 31 countries, employing 61,000 people worldwide. In other situations, firms find the need to consolidate and restructure to respond to negative environmental conditions; such was the case for Samsung Electronics, as described in the nearby Under the Lens feature.



UNDER THE LENS

*Samsung Electronics Reorganizes to Fight Downturn*¹³

Companies change their structures not only to align with new strategic directions and competition, but also to respond to developments in their operating environment. Such was the case early in 2009 when Samsung Electronics of Seoul, South Korea, implemented a radical reorganization in order to become more efficient to deal with worsening economic conditions.

Samsung Electronics is the world's leading manufacturer of memory chips, liquid crystal displays, and flat screen televisions, and is second in mobile phones after Finland's Nokia Corp. (Samsung Electronics is part of the Samsung Group, which includes dozens of companies, with interests in shipbuilding, construction, life insurance and leisure. Samsung, which began as a small noodle business in 1938, was, in 2012, a network of 83 companies that account for a staggering 13% of South Korea's exports.¹⁴) But Samsung had been badly hit by the global economic downturn that resulted in falling prices for semiconductors and flat screens, and such a radically declining profitability could "threaten its existence," according to a Samsung spokeswoman Hwang Eun-ju. She stated that the changes were needed to "effectively respond to the current global recession."¹⁵

As a result, Samsung Electronics Co. announced a major restructuring, consolidating business operations into two operating divisions: one focused on consumer products such as televisions and cell-phones, and the other on components such as memory chips and displays. Thus the company integrated four business units—semiconductors, LCDs, mobile phones, and consumer electronics—into two divisions, regarded as "parts" and "sets." This necessitated reassigning two-thirds of its executives and relocating 1,200 staff members, cutting executives' pay by 20 percent, and reducing other benefits. The company also replaced the heads of five of its eight overseas operations—North America, Europe, the CIS (Commonwealth of International States), and the Middle East and Africa.

Clearly, the company strategy has had to change from high-tech competition to controlling cash flow and profitability. The reorganization was expected to eliminate bureaucracy and speed decision making. Another goal of the restructuring was to help resolve conflicts in that Samsung's components businesses serve customers who are competitive with its own consumer-products businesses. Samsung's CEO Lee Yoon-woo was selected to directly oversee the components division, and Mr. Choi Gee-sung was to head the consumer products division.

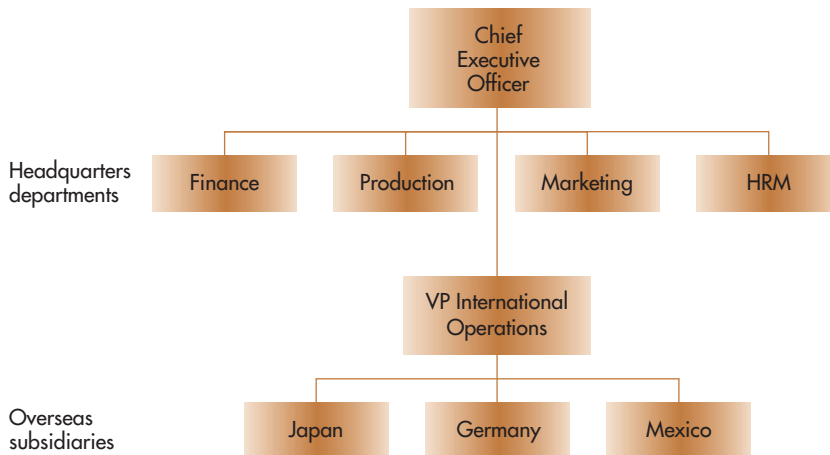
The typical ways in which firms organize their international activities are shown in the following list. (Larger companies often use several of these structures in different regions or parts of their organization.) After the presentation of some of these structural forms, the focus will turn to transitional organizational arrangements.

- Domestic structure plus export department
- Domestic structure plus foreign subsidiary
- International division
- Global functional structure
- Global product structure
- Matrix structure

As previously stated, many firms—especially smaller ones—start their international involvement by exporting. They may simply use the services of an export management company for this, or they may reorganize into a simple *domestic structure plus export department*.

To facilitate access to and development of specific foreign markets, the firm can take a further step toward worldwide operations by reorganizing into a *domestic structure plus foreign subsidiary* in one or more countries (see Exhibit 8-1). To be effective, subsidiary managers should have a great deal of autonomy and be able to adapt and respond quickly to serve local markets. This structure works well for companies with one or a few subsidiaries located relatively close to headquarters.

With further market expansion, the firm may then decide to specialize by creating an *international division* organized along functional, product, or geographic lines. With this structure, the various foreign subsidiaries are organized under the international division, and the subsidiary managers report to its head, who is typically given the title "Vice President, International

EXHIBIT 8-1 Domestic Structure Plus Foreign Subsidiary

Division.” This vice president, in turn, reports directly to the CEO of the corporation. The creation of an international division facilitates the beginning of a global strategy. It permits managers to allocate and coordinate resources for foreign activities under one roof, and thus enhances the firm’s ability to respond, both reactively and proactively, to market opportunities. Some conflicts may arise among the divisions of the firm because more resources and management attention tend to get channeled toward the international division than toward the domestic divisions and because of the different orientations of various division managers. Companies such as IBM and PepsiCo have international divisions called, respectively, IBM World Trade and Pepsi-Cola International.

Integrated Global Structures

To respond to increased product diversification and to maximize benefits from both domestic and foreign operations, a firm may choose to replace its international division with an integrated global structure. This structure can be organized along functional, product, geographic, or matrix lines.

The **global functional structure** is designed on the basis of the company’s functions—production, marketing, finance, and so forth. Foreign operations are integrated into the activities and responsibilities of each department to gain functional specialization and economies of scale. This form of organization is primarily used by small firms with highly centralized systems. It is particularly appropriate for product lines using similar technology and for businesses with a narrow spectrum of customers. This structure results in plants that are highly integrated across products and that serve single or similar markets.

Much of the advantage resulting from economies of scale and functional specialization may be lost if the managers and the work systems become too narrowly defined to have the necessary flexibility to respond to local environments. An alternative structure can be based on product lines.

For firms with diversified product lines (or services) that have different technological bases and that are aimed at dissimilar or dispersed markets, a **global product (divisional) structure** may be more strategically advantageous than a functional structure. In this structure, a single product (or product line) is represented by a separate division. Each division is headed by its own general manager, and each is responsible for its own production and sales functions. Usually, each division is a **strategic business unit (SBU)**—a self-contained business with its own functional departments and accounting systems. The advantages of this organizational form are market concentration, innovation, and responsiveness to new opportunities in a particular environment. It also facilitates diversification and rapid growth, sometimes at the expense of scale economies and functional specialization. H. J. Heinz Company CEO William R. Johnson came on board in April 1998 and decided that the company should restructure to implement a global strategy. He changed the focus of the company from a multidomestic international strategy using the global geographic area structure to a global strategy using the global product divisional structure. His goal was further growth overseas by building international operations; this structure also readily incorporated Heinz’s Specialty Pet Food Division for marketing those products around the world.¹⁶ As of 2012, Heinz was a \$10.7 billion global company with 35,000 employees around the world.

Particularly appropriate in a dynamic and diverse environment, the global product structure is illustrated in Exhibit 8-2.

With the global product (divisional) grouping, however, ongoing difficulties in the coordination of widely dispersed operations may result. One answer to this problem, particularly for large MNCs, is to reorganize into a global geographic structure.

In the **global geographic (area) structure**—the most common form of organizing foreign operations—divisions are created to cover geographic regions (see Exhibit 8-3). Each regional manager is responsible for the operations and performance of the countries within a given region. In this way, country and regional needs and relative market knowledge take precedence

EXHIBIT 8-2 Global Product (Divisional) Structure

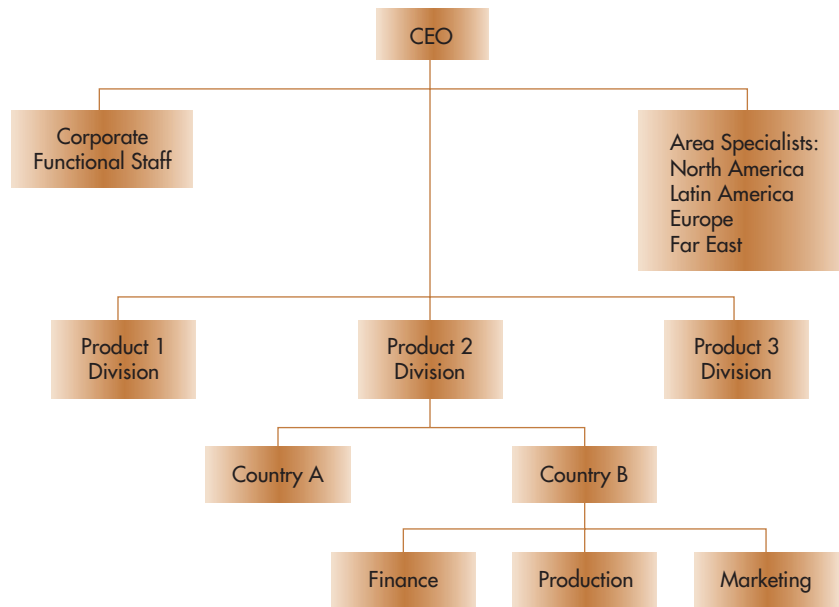
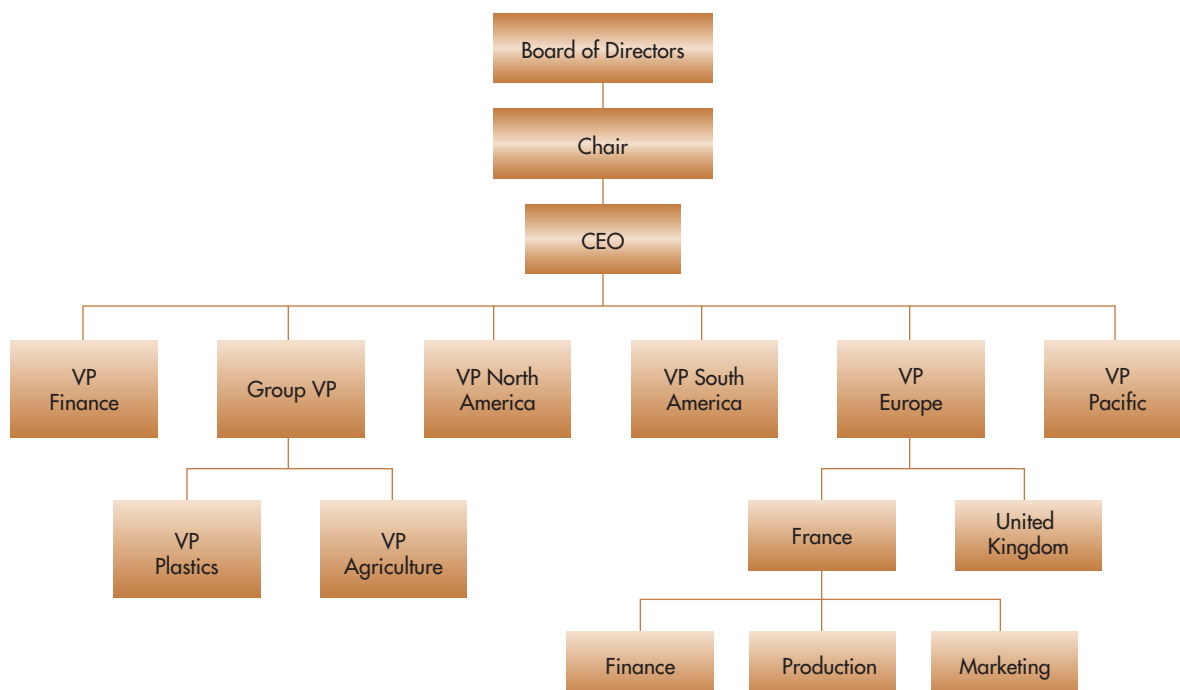


EXHIBIT 8-3 Global Geographic Structure



over product expertise. Local managers are familiar with the cultural environment, government regulations, and business transactions. In addition, their language skills and local contacts facilitate daily transactions and responsiveness to the market and the customer. While this is a good structure for consolidating regional expertise, problems of coordination across regions may arise.

With the geographic structure, the focus is on marketing, since products can be adapted to local requirements. Therefore, marketing-oriented companies, such as Nestlé and Unilever, which produce a range of products that can be marketed through similar (or common) channels of distribution to similar customers, will usually opt for this structure. Nestlé SA, for example, uses this decentralized structure, which is more typical of European companies, because it is Nestlé's policy to generate most of its sales outside of Switzerland. The company strives to be an insider in every country in which it operates.¹⁷ In 2005, Nestlé reinforced its global business strategy of emphasizing its brands by making its head of marketing responsible for Nestlé's seven strategic business units (SBUs)—dairy, confectionery, beverages, ice cream, food, pet care, and food services. Those SBUs help determine the company's regional business strategy, which then shapes the local market business strategies.¹⁸ Still Peter Brabeck-Letmathe, who was Nestlé's marketing manager, and in 2012 is the Chairman, insisted that . . .

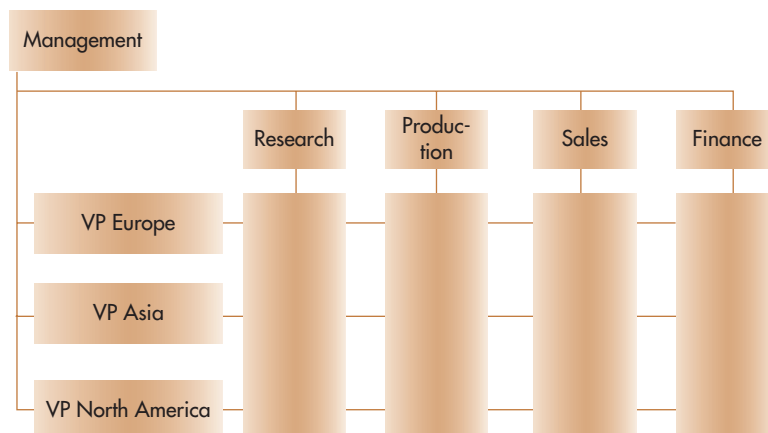
*There is no such thing as a global consumer, especially in a sector as psychologically and culturally loaded as food. . . . This means having a local character.*¹⁹

As of 2012, Nestle had a presence in almost every country in the world, including emerging markets; and it had various partnerships around the world—most recently with the Chinese confectionery company Hsu Fu Chi. The Nestlé company website describes the organization of the food and beverage business, with some product exceptions, as being managed by geographies in three zones—Europe, the Americas, and Asia/Oceania/Africa. The other products, such as Nestlé Purina Petcare, Nestlé Nutrition, and Nestlé Waters, are managed on a global basis; the company calls this group the Globally Managed Businesses.²⁰

A **matrix structure** is a hybrid organization of overlapping responsibilities. The structure is developed to combine geographic support for both global integration and local responsiveness; also it can be used to take advantage of personnel skills and experience shared across both functional and divisional structures. In the matrix structure the lines of responsibility are drawn both vertically and horizontally as illustrated in Exhibit 8-4. While this method of management and organization maximizes the focus of skills and experience in the company brought to bear on a particular product as well as a particular region, it often brings confusion, communication problems, and conflict over having more than one boss to whom to report as well as stress over prioritizing time among overlapping and conflicting responsibilities. Indeed, in their research of 36 Dutch organizations, including subsidiaries of global firms, Strikwerda and Stoelhorst concluded from the majority of interviewees that:

*executives associate the matrix organization with unclear responsibilities, a lack of accountability, and political battles over resources, resulting in risk-averse behavior and loss of market share.*²¹

EXHIBIT 8-4 Matrix Geographic Structure



ORGANIZING FOR GLOBALIZATION

No matter what the stage of internationalization, a firm's structural choices always involve two opposing forces: the need for **differentiation** (focusing on and specializing in specific markets) and the need for **integration** (coordinating those same markets). The way the firm is organized along the differentiation–integration continuum determines how well strategies—along a localization–globalization continuum—are implemented. This is why the structural imperatives of various strategies such as globalization must be understood to organize appropriate worldwide systems and connections.

As previously presented, global trends and competitive forces have put increasing pressure on multinational corporations to adopt a strategy of **globalization**, a specific strategy that treats the world as one market by using a standardized approach to products and markets. The following are two examples of companies reorganizing to achieve globalization:

- **IBM.** Big Blue decided to move away from its traditional geographic structure to a global structure based on its 14 worldwide industry groups, such as banking, retail, and insurance, shifting power from country managers to centralized industry expert teams.
- **Asea-Brown Boveri (ABB).** A global leader in the power and the oil and gas industries, ABB is legendary in its record of changing its organizational structure to fit its new strategic directions and its competitive environment, such as the losses it incurred resulting from the East Asian currency crisis. Exhibit 8-5 illustrates two phases of the company's strategic direction and organization structure.

Organizing to facilitate a globalization strategy typically involves rationalization and the development of strategic alliances. To achieve rationalization, managers choose the manufacturing location for each product based on where the best combination of cost, quality, and technology can be attained. It often involves producing different products or component parts in different countries. Typically, it also means that the product design and marketing programs are essentially the same for all end markets around the world—to achieve optimal economies of scale. The downside of this strategy is a lack of differentiation and specialization for local markets.

Organizing for global product standardization necessitates close coordination among the various countries involved. It also requires centralized global product responsibility (one manager at headquarters responsible for a specific product around the world), an especially difficult task for multiproduct companies. Henzler and Rall suggest that structural solutions to this problem can be found if companies rethink the roles of their headquarters and their national subsidiaries. Managers should center the overall control of the business at headquarters, while treating national subsidiaries as partners in managing the business—perhaps as holding companies responsible for the administration and coordination of cross-divisional activities.²²

Governments as well as firms may structure their holdings in order to attract and integrate strategic allies. Such was the case for Brazil's federal energy company Petrobras (NYSE: PBR) when it announced in February 2009 that it had created six wholly owned companies, along product lines, for the Rio de Janeiro Comperj petrochemical complex, commenting that:

*Petrobras will hold a 100% stake in the companies and voting capital at the initial stage while it integrates and defines the relationship between Comperj's component parts. By establishing these companies Petrobras is laying the foundations for the potential involvement of partners. Planned investments in Comperj are expected to total US\$8.4bn and operations are scheduled to begin in 2012.*²³

A problem many companies face in the future is that their structurally sophisticated global networks, built to secure cost advantages, leave them exposed to the risk of environmental volatility from all corners of the world. Such companies must restructure their global operations to reduce the environmental risk that results from multicountry sourcing and supply networks.²⁴ In other words, the more links in the chain, the more chances for things to go wrong.

Organizing to “Be Global, Act Local”

In their rush to get on the globalization bandwagon, too many firms have sacrificed the ability to respond to local market structures and consumer preferences. Managers are now realizing

EXHIBIT 8-5 ABB's Old Versus New Corporate Strategy and Organizational Models During the Tenures of CEOs Percy Barnevik and Jürgen Dormann (1988–2004) and Fred Kindle (2005–2008) (Joseph Hogan took over in 2008)

Old Corporate Strategy/Organizational Model

(Percy Barnevik, 1988–2001)

- Create a powerful global corporation
- Seek aggressive global expansion
- Design and implant matrix management structure
- Encourage entrepreneurship, decentralization, and multiculturalism in overseas subsidiaries
- Seek internal benchmarking and corporate parenting
- Keep local corporate identities while seeking globalization
- Seek cosmopolitan conglomerates
- Seek pan-European and global strategies
- Concentrate on Asian markets

Net Output

- Global corporation
- Matrix structure
- Networking
- Horizontal structure

New Corporate Strategy/Organizational Model

(Jürgen Dormann, 2002–2004) and Fred Kindle to 2008

- Revise core competencies
- Sell off non-core businesses
- Seek corporate restructuring
- Improve financial health of company
- Seek more regional strategies
- Resolve old disputes such as asbestos liabilities
- Simplify ABB's global structure; create two divisions (power technology and automation)
- Seek cost cutting; seek downsizing
- Unload unproductive units
- Improve credit rating

Net Output

- Rationalization
- Simplicity
- Avoid non-core businesses
- Downsizing
- Save money
- Redesign the company

Sources: Based on *BusinessWeek*, *The Economist*, the *Financial Times*, and the *Wall Street Journal*. Updated by Helen Deresky, originally compiled by Syed Tariq Anwar, case study “ABB, Sweden: What Went Wrong?” in the 6th edition of this book.

that—depending on the type of products, markets, and so forth—a compromise must be made along the globalization–regionalization continuum, and they are experimenting with various structural configurations to “be global and act local.”

Levi Strauss is another example of a company attempting to maximize the advantages of different structural configurations. The company employs a staff of approximately 10,000 people worldwide, including approximately 1,010 people at its San Francisco, California, headquarters. Approximately half of the company's revenues comes from outside the United States. The company is organized into three geographic divisions:

Levi Strauss Americas (LSA), based in the San Francisco headquarters.

Levi Strauss Europe, Middle East, and North Africa (LSEMA), based in Brussels.

Asia Pacific Division (APD), based in Singapore.

In the LSEMA division there is a network of nine sales offices, six distribution centers, and three production facilities, employing a total of approximately 4,600 people. The headquarters are located in Brussels, Belgium. The company's European franchise partners bring the products to consumers throughout the region.²⁵

Levi Strauss & Co.'s Asia Pacific Division is comprised of subsidiary businesses, licensees, and distributors throughout the Asia Pacific region, the Middle East, and Africa.

Thus, through these various structural global–local formats, the company has ensured its ability to respond to local needs by allowing its managers to act independently: Levi's success turns on

its ability to fashion a global strategy that doesn't snuff out local initiative. It's a delicate balancing act, one that often means giving foreign managers the freedom needed to adjust their tactics to meet the changing tastes of their home markets. The company's website in 2012 states that "our goal is to expand the Levi Strauss & Co. brands in India, China, Russia, Brazil and other emerging markets."²⁶

One well-known global consumer products company, Procter & Gamble, is succeeding with its global-local "Four Pillars" structure, as described in the accompanying Management in Action feature.



MANAGEMENT IN ACTION

Procter & Gamble's "Think Globally-Act Locally" Structure— 10 Years of Success

In 2012, Procter & Gamble (P&G) attributes much of its success to its global/local "Four Pillars" organization structure. The well-known \$83 billion company melds its global scale efficiencies with a local focus in the 180 countries in which it operates. The company lauds its growth and competitive advantage in adopting new business models and in more than doubling of its capacity to innovate.

P&G touches the lives of people around the world three billion times a day with its broad portfolio of leading brands, including Pampers®, Tide®, Charmin®, Downy®, Crest®, Gillette®, and Braun®.²⁷

P&G's organizational structure is broadly divided into three heads: GBU (Global Business Unit), MDO (Market Development Organization), and GBS (Global Business Services). Upon the acquisition of Gillette, it was decided that the structure would change from business units based on geographic regions to GBUs based on product lines. "MDOs will develop market strategies to build business based on local knowledge and GBS will bring together business activities such as accounting, human resource systems, order management, and information technology, thus making it cost-effective."²⁸

Since 2001, P&G has acquired three leading companies with leading brands in Clairol, Wella, and Gillette. The acquisition of Gillette in 2006 added five brands with annual sales in excess of \$1 billion. CEO A. G. Lafley had expressed confidence that the company could deliver on a full decade of growth because of P&G's strategies and strengths, and the company's unique organizational structure. P&G's structure makes it the only consumer-products company with global business unit profit centers, global market development organizations, and global shared services, all supported by innovative corporate functions. P&G's organization structure as of 2012 is described below, as provided in the company's corporate information description on their Web site.²⁹

P&G'S GLOBAL/LOCAL STRUCTURE—2012

Four pillars—Global Business Units, Market Development Organizations, Global Business Services, and Corporate Functions—form the heart of P&G's organizational structure.

- Global Business Units (GBUs) build major global brands with robust business strategies.
- Market Development Organizations (MDOs) build local understanding as a foundation for marketing campaigns.
- Global Business Services (GBS) provide business technology and services that drive business success.
- Corporate Functions (CFs) work to maintain our place as a leader of our industries.

P&G approaches business knowing that we need to Think Globally (GBUs) and Act Locally (MDOs). This approach is supported by our commitment to operate efficiently (GBS) and our constant striving to be the best at what we do (CFs). This streamlined structure allows us to get to market faster.

Global Business Units

Philosophy: Think Globally

General Role: Create strong brand equities, robust strategies, and ongoing innovation in products and marketing to build major global brands.

GBUs:

- Baby Care/Family Care
- Beauty Care/Feminine Care

- Fabric & Home Care
- Snacks & Beverage
- Health Care

Market Development Organizations (MDO)

Philosophy: Act Locally

General Role: Interface with customers to ensure marketing plans fully capitalize on local understanding, to seek synergy across programs to leverage corporate scale, and to develop strong programs that change the game in our favor at point of purchase.

MDO Regions:

- North America
- Asia/India/Australia
- Northeast Asia
- Greater China
- Central-Eastern Europe/Middle East/Africa
- Western Europe
- Latin America

Global Business Services (GBS)

Philosophy: Enabling P&G to win with customers and consumers

General Role: Provide services and solutions that enable the Company to operate efficiently around the world, collaborate effectively with business partners, and help employees become more productive.

GBS Centers:

- GBS Americas located in Costa Rica
- GBS Asia located in Manila
- GBS Europe, Middle East, & Africa located in Newcastle

Corporate Functions (CF)

Philosophy: Be the Smartest/Best

General Role: Ensure that the functional capability integrated into the rest of the company remains on the cutting edge of the industry. We want to be the thought leader within each CF.

Corporate Functions:

- Customer Business Development
- External Relations
- Finance & Accounting
- Human Resources
- Information Technology
- Legal
- Marketing
- Consumer & Market Knowledge
- Product Supply
- Research & Development
- Workplace Services

Although strategy may be the primary means to a company's competitive advantage, the burden of realizing that advantage rests on the organizational structure and design; that structure, in turn, establishes the responsibilities and guides the decisions, actions, and communications of its employees. Because of the difficulties experienced by companies trying to be "glocal" companies (global and local), researchers are suggesting new, more flexible organizational designs involving interorganizational networks and transnational design.

EMERGENT STRUCTURAL FORMS

Companies are increasingly abandoning rigid structures in an attempt to be more flexible and responsive to the dynamic global environment. Some of the ways they are adapting are by transitioning to formats known as interorganizational networks, global e-corporation network structures, and transnational corporation network structures, described below. An increasing number of companies, like Cisco Systems and IBM, create customized structures according to the client needs. By selectively moving their skilled employees into cross-company teams they are able to move rapidly and flexibly to take advantage of their portfolios of opportunities. To do this,

They assemble and disassemble teams of hundreds of people from across the company who move from opportunity to opportunity. Their reconfigurable organizations consist of a stable part and a variable part. The stable structure is usually the functional and/or geographical home for nurturing talent.

J. R. GALBRAITH,
2010.³⁰

Other new structural formats are evolving as emerging market companies make their rapid entrée onto the global scene, as discussed in the following Comparative Management in Focus section.



COMPARATIVE MANAGEMENT IN FOCUS

Changing Organizational Structures of Emerging Market Companies

Rapidly changing competition and global business activities demand that companies run their worldwide operations efficiently and effectively, based on the right business models and organizational structures. Stable organizational structures and control systems are necessary to seek timely internationalization. The major variables involved in choosing the right organizational structure depend on a company's global involvement and degree of localization. Fast-growing companies from emerging markets (EMs), BRIC countries (Brazil, Russia, India, and China), and rapidly developing economies (RDEs) continue to internationalize their operations. Examples are: CNOOC (China), Dr. Reddy's Laboratories (India), Embraer (Brazil), Gazprom (Russia), Haier Company (China), Infosys Technologies (India), Koc Holdings (Turkey), Lenovo Group (China), Tata Motors (India), and Wipro (India).³¹ These emerging market companies are the first wave of highly successful firms benefiting from the globalization phenomenon.³²

Interestingly, the expansion models sought by these new emerging-market companies from Asia, Latin America, and Eastern Europe are unique and may not fit with today's mainstream multinational corporation (MNC) model because of the following three reasons: First, many emerging market companies are avoiding the traditional roadmap to internationalization and are instead capitalizing on the "born-global phenomenon," which means running their operations and opening subsidiaries worldwide from the beginning. Second, they are finding niche businesses where competition is limited. Third, they are thriving in those old-economy industries that have been abandoned by established MNCs from developed countries.

A new breed of companies is emerging in those geographic areas that have excelled in global business because of their unique organizational structures and design. Like Korean chaebols (industrial conglomerates), most emerging market companies were started as family businesses and entrepreneurial entities where ownership and control of the firms resided with the families. Therefore, the control mechanism is somewhat bureaucratic and headquarters-centered. Currently, a multitude of changes are in the pipeline that will force emerging market companies to redefine their family-based governance structures and rigid control systems.

Major structural changes include simplifying hierarchies, reducing family ownerships, providing more powers to subsidiaries, and seeking organizational structures based on either the traditional MNC model or company-specific hybrid structures. Interestingly, many emerging market companies have been following the model of "be global, act local" in becoming responsible citizens and also adapting their products and services. Embraer, Haier Group, Lenovo, Mittal Steel, Orsacom, and others fit in this category. In addition, overseas Chinese business networks (OCBNs) are also changing to become part of the globalization phenomenon. Increasingly, emerging market companies from Asia, Latin America, and Eastern Europe will seek internationalization in their own unique ways, leading to hybrid structures and fast-growth entities. Of course, these newly emerging MNCs will become globally integrated, utilizing multidomestic synergies, and international/global/transnational strategies. Their future goals and scope of operations will determine organizational structures and global initiatives.

Source: Written exclusively for this text by Syed Tariq Anwar, Professor, West Texas A&M University.

Interorganizational Networks

Whether the ever-expanding transnational linkages of an MNC consist of different companies, subsidiaries, suppliers, or individuals, they result in relational networks. These networks may adopt very different structures of their own because they operate in different local contexts within their own national environments. Similarly, the “I-form” is described by Miles et al. as a collaborative, multi-firm network along with community-based structures, used by innovative firms such as Taiwan’s Acer.³³ By regarding the MNC’s overall structure as a network of interconnected relations, we can more realistically consider its organizational design imperatives at both global and local levels. Royal Philips Electronics of the Netherlands, one of the world’s biggest electronics companies, has operating units in 100 countries as of 2012, using a network structure. These units range from large subsidiaries, which might be among the largest companies in a country, to very small single-function operations, such as research and development or marketing divisions for one of Philips’s businesses. Some have centralized control at Philips’s headquarters; others are quite autonomous. For some time, Philips had fallen far behind its Japanese competitors in productivity because of missteps and seemingly endless restructurings. However, when Philips’ then chief executive Gerard J. Kleisterlee—a 30-year Philips veteran—took over in 2001, he again reorganized the company. He divested \$850 million in less important or unprofitable businesses and shuttered a dozen factories, and outsourced manufacturing for much of the electronics and appliance manufacturing as well as chip production.³⁴

In yet another structural variation, Intel, in adapting to changes in the semiconductor industry, announced in early 2005 a wholesale reorganization of its businesses. Intel’s executives decided that they wanted the company to focus more on what was going on outside the business, and developed a structural focus they call “Platformisation”—that is, customizing a range of chips in a combination suitable for a particular target market, as a response for the increasing need for speedy adaptation to the market.³⁵ As the world’s biggest semiconductor maker, with 82,500 employees worldwide, the company’s general description of its approach to organizing, in response to an inquiry by this author, is as follows:

Intel is not a very hierarchical company so a formalized organizational structure is not a particularly good representation of how the company works. At the highest level, Intel is organized into largely autonomous divisions. Intel uses matrix management and cross-functional teams including IT, knowledge management, human resources, finance, legal, change control, data warehousing, common directory information management, and cost reduction teams (to name a few) to rapidly adapt to changing conditions.

www.intel.com.³⁶

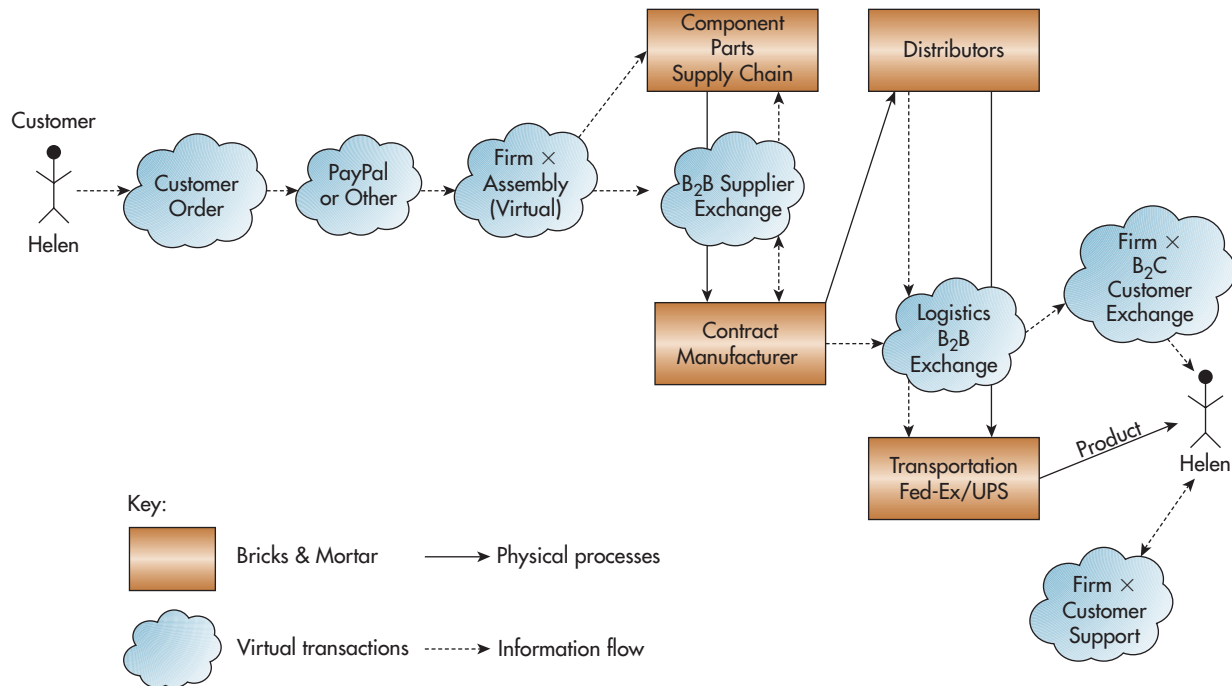
The network framework makes clear that the company’s operating units link vastly different environmental and operational contexts based on varied economic, social, and cultural milieus. This complex linkage highlights the intricate task of a giant MNC to rationalize and coordinate its activities globally to achieve an advantageous cost position while simultaneously tailoring itself to local market conditions (to achieve benefits from differentiation).³⁷

The Global E-Corporation Network Structure

The organizational structure for global e-businesses, in particular for physical products, typically involves a network of virtual e-exchanges and “bricks and mortar” services, whether those services are in-house or outsourced. This structure of functions and alliances makes up a combination of electronic and physical stages of the supply chain network, as illustrated in Exhibit 8-6.

As such, the network comprises some global and some local functions. The centralized e-exchanges for logistics, supplies, and customers could be housed anywhere; suppliers, manufacturers, and distributors may be in various countries, separately or together, wherever efficiencies of scale and cost may be realized. The final distribution system and the customer interaction must be tailored to the customer-location physical infrastructure and payment infrastructure, as well as local regulations and languages.³⁸

The result is a global e-network of suppliers, subcontractors, manufacturers, distributors, buyers, and sellers, communicating in real time through cyberspace. This spreads efficiency throughout the chain, providing cost-effectiveness for all parties.³⁹ Dell Computer is an example of a company that uses the Internet to streamline its global supply systems. It has a number of factories around the world that supply custom-built PCs to customers in that region. Customers’

EXHIBIT 8-6 A Global E-Corporation Network Structure

orders are received through call centers or Dell's own Web site. The order for components then goes to its suppliers, which have to be within a 15-minute drive of its factory. The component parts are delivered to the factory, and the completed customers' orders are collected within a few hours. Dell maintains Internet connections with its suppliers and connects them with its customer database so that they have direct and real-time information about orders. Customers also can use Dell's Internet system to track their orders as they go through the chain.⁴⁰

Dell's organizational structure to implement its business model has evolved to what is known as a virtual company, or value web. Dell's strategy is to conduct critical activities in-house, while outsourcing non-strategic activities.

The Transnational Corporation (TNC) Network Structure

To address the globalization–localization dilemma, firms that have evolved through the multinational form and the global company seek the advantages of horizontal organization in the pursuit of transnational capability—that is, the ability to manage across national boundaries, retaining local flexibility while achieving global integration.⁴¹ This capability involves linking foreign operations to each other and to headquarters in a flexible way, thereby leveraging local and central capabilities. ABB (discussed earlier) is an example of such a decentralized horizontal organization. In 2012, ABB operates in 100 countries with 145,000 employees and eight geographic region managers, with only one management level separating the business units from top management. ABB prides itself on being a truly global company, with 11 board members representing seven nationalities. Thus, this structure is less a matter of boxes on an organizational chart and more a matter of a network of the company's units and their system of horizontal communication. This involves lateral communication across networks of units and alliances rather than in a hierarchy. The system requires the dispersal of responsibility and decision making to local subsidiaries and alliances. The effectiveness of that localized decision-making depends a great deal on the ability and willingness to share current and new learning and technology across the network of units. The matrix structure typical of the transnational company creates a complex coordination and control system as it attempts to combine:

- The capabilities and resources of a multinational corporation
- The economies of scale of a global corporation
- The local responsiveness of a domestic company
- The ability to transfer technology efficiently typical of the international structure⁴²

Whatever the names given to the organizational forms emerging to deal with global competition and logistics, the MNC organizational structure as we know it, with its hierarchical pyramid, subsidiaries, and world headquarters, is gradually evolving into a more fluid form to adapt to strategic and competitive imperatives. As is now well known, these more flexible forms are facilitated by the ever-developing technologies that enable various forms of electronic instant communication to connect elaborate networks of people and information around the world, regardless of their locations. In this new global web, the location of a firm's headquarters is unimportant. Various alliances tie together units and subunits in the web. Corning Glass, for instance, changed from its national pyramid-like organization to a global web, giving it the capability of making optical cable through its European partner, Siemens AG, and medical equipment with Ciba-Geigy.

CHOICE OF ORGANIZATIONAL FORM

Two major variables in choosing the structure and design of an organization are the opportunities and need for (1) globalization and (2) localization. Exhibit 8-7 depicts alternative structural forms appropriate to each of these variables and to the strategic choices regarding the level and type of international involvement desired by the firm.

This figure thereby updates the evolutionary stages model to reflect alternative organizational responses to more recent environments and to the anticipated competitive environments ahead. The updated model shows that, as the firm progresses from a domestic to an international company—and perhaps later to a multinational and then a global company—its managers adapt the organizational structure to accommodate their relative strategic focus on globalization versus localization, choosing a global product structure, a geographic area structure, or perhaps a matrix form. The model proposes that, as the company becomes larger, more complex, and more sophisticated in its approach to world markets (no matter which structural route it has taken), it may evolve into a transnational corporation (TNC). The TNC strategy is to maximize opportunities for both efficiency and local responsiveness by adopting a transnational structure that uses alliances, networks, and horizontal design formats. The relationships between choice of global strategy and the appropriate structural variations necessary to implement each strategic choice are further illustrated in Exhibit 8-8.

Organizational Change and Design Variables

When a company makes drastic changes in its goals, strategy, or scope of operations, it will usually also need a change in organizational structure. However, other, less obvious indications of organizational inefficiency also signal a need for structural changes: conflicts among divisions and subsidiaries over territories or customers, conflicts between overseas units and headquarters staff,

EXHIBIT 8-7 Organizational Alternatives and Development for Global Companies

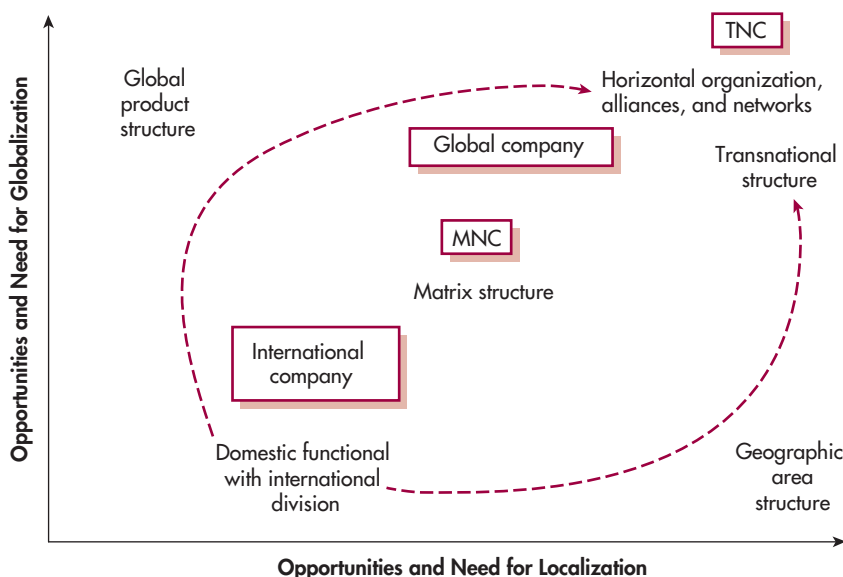


EXHIBIT 8-8 Structural Variables to Implement Global Strategies

Strategy	Organizational Structure	Delegation	Need to Coordinate	Organizational Culture
Multidomestic	Global area	To national unit	Low	Low impact
International	Intl. Division	Centralize core; rest to units	Medium	Medium
Global	Product Group	Locate where globally optimum	High	Important
Transnational	Global Matrix	Centralized and decentralized	Very High	Crucial

Source: Based on C. W. L. Hill and E. R. Jones, *Strategic Management: An Integrated Approach*, 3rd ed., 390. 1995, Houghton Mifflin Company.

EXHIBIT 8-9 Changes That May Necessitate New Structural Designs⁴³

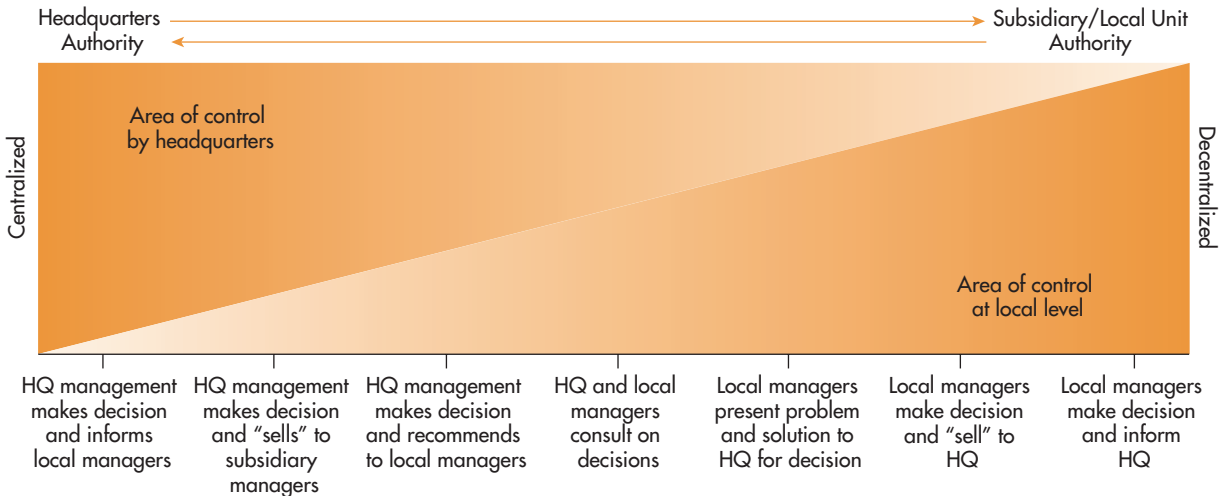
- New management with different goals and strategies
- Downturn in profitability or finances
- Lack of competitiveness; failure to meet goals or capitalize on opportunities
- Poor management, leadership, communication, delegation, or morale
- New strategic directions: growth, alliances, retrenchment; expanding globally from directing export activities to controlling overseas manufacturing and marketing units; a change in the size of operations on a country, regional, or worldwide basis; or failure of foreign operations to grow in accordance with plans and expectations
- Clashes among divisions, subsidiaries, or individuals over territories or customers in the field
- Divisive conflicts between overseas units and domestic division staff or corporate staff
- Underutilization of overseas manufacturing or distribution facilities
- Duplication of sales offices or geographic operational units within an area
- An increase in overseas customer service complaints
- Breakdowns in communications within and among organizations
- Bottlenecks, too many reporting layers, and ill-defined executive responsibilities
- Lack of innovation

complaints regarding overseas customer service, and overlapping responsibilities are some of these warning signals. Exhibit 8-9 lists some indications of the need for change in organizational design.

At persistent signs of ineffective work, a company should analyze its organizational design, systems, and work flow for the possible causes of those problems. The nature and extent of any design changes must reflect the magnitude of the problem. In choosing a new organizational design or modifying an existing structure, managers must establish a system of communication and control that will provide for effective decision making. At such times, managers need to localize decision making and integrate widely dispersed and disparate global operations.

Besides determining the behavior of the organization on a macro level (in terms of what the different divisions, subsidiaries, departments, and units are responsible for), the organizational design must determine behavior on a micro level. For example, the organizational design affects the level at which certain types of decisions will be made. Determining how many and what types of decisions can be made and by whom can have drastic consequences; both the locus and the scope of authority must be carefully considered. This centralization–decentralization variable actually represents a continuum. In the real world, companies are neither totally centralized nor totally decentralized: The level of centralization imposed is a matter of degree. Exhibit 8-10 illustrates this centralization–decentralization continuum and the different ways that decision making can be shared between headquarters and local units or subsidiaries. In general, centralized decision making is common for some functions (finance, research and development) that are organized for the entire corporation, whereas other functions (production, marketing, sales) are more appropriately decentralized. Two key issues are the speed with which the decisions have to be made and whether they primarily affect only a certain subsidiary or other parts of the company as well.

As noted, culture is another factor that complicates decisions on how much to decentralize and how to organize the work flow and the various relationships of authority and responsibility.

EXHIBIT 8-10 Locus of Decision Making in an International Organization

Part 4 of this book more fully presents how cultural variables affect people's attitudes about working relationships and about who should have authority over whom. At this point, it is important merely to note that cultural variables must be taken into account when designing an organization. Delegating a high level of authority to employees in a country where workers usually regard "the boss" as the rightful person to make all the decisions is not likely to work well. Clearly, managers must think through the interactions of organizational, staffing, and cultural issues before making final decisions.

In summary, no one way to organize is best. Contingency theory applies to organizational design as much as to any other aspect of management. The best organizational structure is the one that facilitates the firm's goals and is appropriate to its industry, size, technology, and competitive environment. Structure should be fluid and dynamic, and highly adaptable to the changing needs of the company. The structure should not be allowed to get bogged down in the administrative heritage of the organization (that is, "the way we do things around here" or "what we've always done") to the point that it undermines the very processes that will enable the firm to take advantage of new opportunities.

Most likely, however, the future for the MNC structure, as well as for small businesses and "born globals," lies in a global web of networked companies. Ideally, a company tries to organize in a way that will allow it to carry out its strategic goals; the staffing is then done to mesh with those strategic goals and the way the organizational structure has been set up. In reality, however, the existing structural factors often affect strategic decisions, so the end result may be a trade-off of desired strategy with existing constraints. So, too, with staffing: "ideal" staffing plans have to be adjusted to reflect the realities of assigning managers from various sources and the local regulations or cultural variables that make some organizing and staffing decisions more workable than others.

What may at first seem a linear management process of deciding on strategy, then on structure, and finally on staffing is actually an interdependent set of factors that must be taken into consideration and worked out as a set of decisions. Chapter 9 explores how staffing decisions are—or should be—intricately intertwined with other decisions regarding strategy, structure, and so forth. A unique set of management cadre and skills in a particular location can be a competitive advantage in itself, and so it may be a smart move to build strategic and organizational decisions around that resource rather than risk losing that advantage. The following sections present some other processes that are involved in implementing strategy and are interconnected with coordinating functions through organizational structure.

CONTROL SYSTEMS FOR GLOBAL OPERATIONS

To complement the organizational structure, the international manager must design efficient coordinating and reporting systems to ensure that actual performance conforms to expected organizational standards and goals. The challenge is to coordinate far-flung operations in vastly

different environments with various work processes; rules; and economic, political, legal, and cultural norms. The feedback from the control process and the information systems should signal any necessary change in strategy, structure, or operations in a timely manner. Often the strategy, the coordinating processes, or both, need to be changed to reflect conditions in other countries. Organizations may also restructure and set up reporting systems in order to preemptively avoid problems which will negatively impact its processes and image. Such was the case when FIFA decided to set up a structure to provide decision oversight and transparency to its worldwide activities, as explained in the nearby Under the Lens feature.



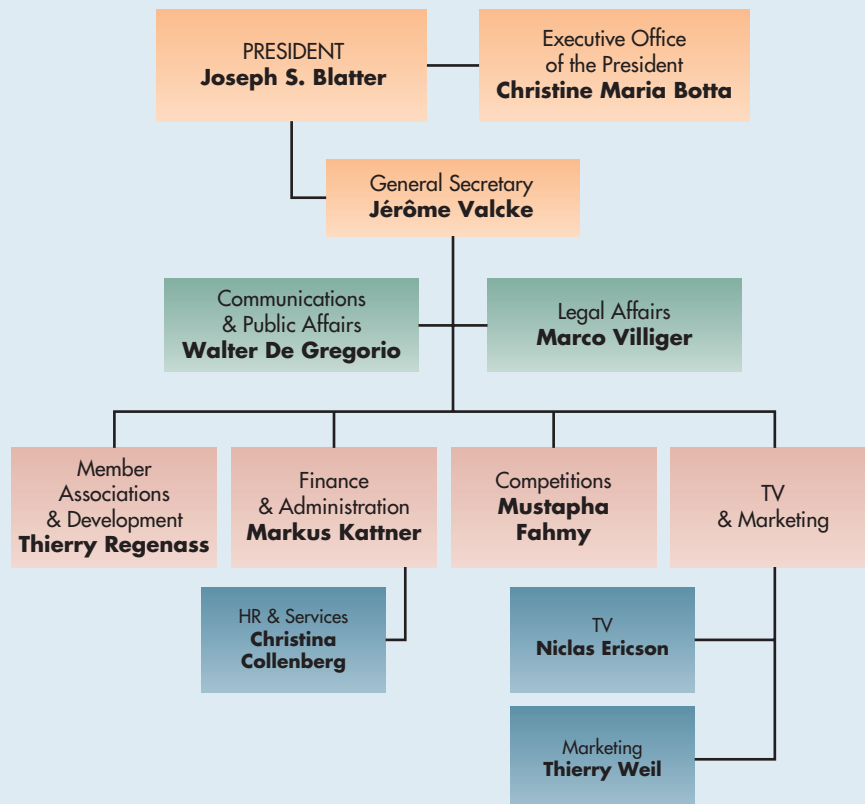
UNDER THE LENS

FIFA—Restructuring for Governance Oversight of Ethics⁴⁴

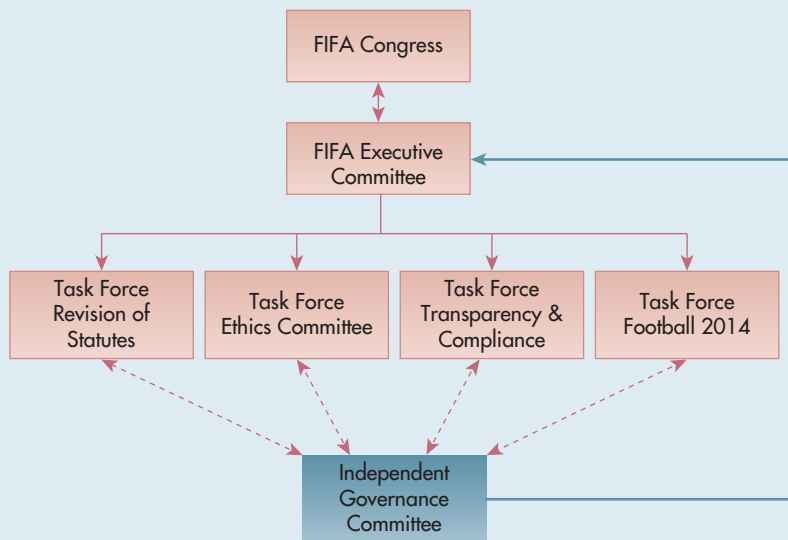
Most sports organizations developed on a small scale but have now grown in size and complexity to organizations similar to multinational corporations. As such, those sports organizations should have a structure and a set of policies in place to oversee anti-corruption and conflict-of-interest compliance; this awareness has grown in particular in the wake of the scandal surrounding the International Olympic Committee (IOC) and the Salt Lake City Olympics. However, the governance structure of FIFA for example, had not previously encompassed the responsibility for ethical behavior in the organization. In October 2011, however, FIFA restructured and took the steps as outlined below and as described in www.FIFA.com.

The Fédération Internationale de Football Association (FIFA), located in Zurich, Switzerland, is the international governing body of association football. The association, which has 208 national associations within six regional areas, oversees the governance and organization of the FIFA World Cup; the next one will be held in Brazil in 2014. The administrative organization chart is shown in Exhibit 8-11.

EXHIBIT 8-11 FIFA Administrative Organization Chart



Source: Administrative Organization Chart, www.FIFA.com, accessed February 1, 2012.

EXHIBIT 8-12 Independent Governance Committee

Source: www.FIFA.com, accessed February 1, 2012, used with permission.

Following the proposals made by the FIFA President, Joseph S. Blatter, at the FIFA Congress on June 1, 2011 in terms of good governance, transparency, and zero tolerance toward wrongdoing on and also off the pitch (during games or at any time), the FIFA Executive Committee, meeting on October 20–21, 2011 at the home offices of FIFA in Zurich, agreed on the following measures:

- The creation of four task forces, mandated to propose reforms: *Task Force Revision of Statutes*, chaired by Dr. Theo Zwanziger (Germany); *Task Force FIFA Ethics Committee*, chaired by the Chairman of the Ethics Committee, Claudio Sulser (Switzerland); *Task Force Transparency and Compliance*, chaired by Juan Ángel Napout (President of the Paraguayan FA) and Frank Van Hattum (President of the New Zealand FA); and *Task Force Football 2014* (operating since May 2011), chaired by Franz Beckenbauer (Germany).
- The creation of an Independent Governance Committee (see Exhibit 8-12) which, among other tasks, will oversee reforms undertaken by FIFA. It comprises of representatives not only from the international football family but also from other spheres.
- The establishment of a “FIFA Good Governance” road map between October 2011 and the 2013 FIFA Congress.

The design and application of coordinating and reporting systems for foreign subsidiaries and activities can take any form that management wishes. MNCs usually employ a variety of direct and indirect coordinating and control mechanisms suitable for their organization structure. For example, in the transnational network structure, decision-making control is centralized to key network nodes, greatly reducing emphasis on bureaucratic control. Other specific mechanisms are summarized in the next sections.⁴⁵

Direct Coordinating Mechanisms

Direct mechanisms that provide the basis for the overall guidance and management of foreign operations include the design of appropriate structures (discussed previously in this chapter) and the use of effective staffing practices (discussed in Chapters 9 and 10). Such decisions proactively set the stage for operations to meet goals, rather than troubleshooting deviations or problems after they have occurred.

*Staffing is not only a means of control, but also a venue through which groups and individuals bring their cultural properties into a system.*⁴⁶

Expatriates from “headquarters” exert control over the foreign affiliate through the expectations of the national and corporate culture of the parent company; whereas, if the staffing assignment is through third country nationals, it is likely that somewhat less of the corporate culture might be brought to bear locally, and certainly less of the national culture of the parent.⁴⁷ In situations where parent control might be considered less important, local managers would be considered, thus delegating the control to the local level.

When McDonald’s first opened its doors in Moscow in 1990, the biggest control problem was that of quality control for its food products. McDonald’s anticipated that challenge and adopted a strategy of vertical integration for its sourcing of raw materials.⁴⁸ To control the quality, distribution, and reliability of its ingredients, McDonald’s built a \$40 million, 110,000-square-foot plant in a Moscow suburb to process the required beef, milk, buns, vegetables, sauces, and potatoes. In addition, the company brought the managers to Toronto, Canada, for five months of training.⁴⁹ Top management at McDonald’s anticipated difficulties with the setup and daily operations of this IJV and, indeed, had been working toward the opening day for 13 years. Through careful planning for the control of crucial operational factors, they solved the sourcing, distribution, and employment problems inherent in the former Soviet Union.⁵⁰

Other direct mechanisms are visits by head-office personnel and regular meetings to allow employees around the world to consult and troubleshoot. Increasingly, those meetings comprise videoconferences to allow face-to-face, if not physical, interaction among managers around the world to enable faster and less-expensive frequent meetings. Top executives from headquarters may use periodic visits to subsidiaries to check performance and help to anticipate future problems. The meetings allow each general manager to keep in touch with her or his associates, with the overall mission and strategy of the organization, and with comparative performance data and new problem-solving techniques. Increasingly, the tools of technology are being applied as direct mechanisms to ensure up front that operations will be carried out as planned, in particular in countries where processes such as efficient infrastructure and goods forwarding cannot be taken for granted. An example of this is the logistics monitoring system set up by Air Express International in Latin America to minimize its many problems there.⁵¹

Indirect Coordinating Mechanisms

Indirect coordinating mechanisms typically include sales quotas, budgets, and other financial tools, as well as feedback reports, which give information about the sales and financial performance of the subsidiary for the last quarter or year.

Domestic companies invariably rely on budgets and financial statement analyses, but for foreign subsidiaries, financial statements and performance evaluations are complicated by *financial variables in MNC reports*, such as exchange rates, inflation levels, transfer prices, and accounting standards.

To reconcile accounting statements, MNCs usually require three different sets of financial statements from subsidiaries. One set must meet the national accounting standards and procedures prescribed by law in the host country. This set also aids management in comparing subsidiaries in the same country. A second set must be prepared according to the accounting principles and standards required by the home country. This set allows some comparison with other MNC subsidiaries. The third set of statements translates the second set of statements (with certain adjustments) into the currency of the home country for consolidation purposes, in accordance with FASB Ruling Number 52 of 1982. A foreign subsidiary’s financial statements must be consolidated line by line with those of the parent company, according to International Accounting Standard Number 3, adopted in the United States.

Researchers have noted comparative differences between the use of direct versus **indirect controls** among companies headquartered in different countries. One study by Egelhoff examined the practices of 50 U.S., U.K., and European MNCs over their foreign subsidiaries. It compared the use of two mechanisms—the assignment of parent-company managers to foreign subsidiaries and the use of performance reporting systems (that is, comparing behavior mechanisms with output reporting systems).⁵² The results of this study show that considerable differences exist in practices across MNC nationalities. For example, U.S. MNCs monitor subsidiary outputs and rely more on frequently reported performance data than do European MNCs. The latter tend to assign more parent-company nationals to key positions in foreign subsidiaries and can count on a higher level of behavior control than their U.S. counterparts.⁵³

These findings imply that the U.S. system, which measures more quantifiable aspects of a foreign subsidiary, provides the means to compare performance among subsidiaries. The European system, on the other hand, measures more qualitative aspects of a subsidiary and its environment, which vary among subsidiaries—allowing a focus on the unique situation of the subsidiary but making it difficult to compare its performance to other subsidiaries.⁵⁴

MANAGING EFFECTIVE MONITORING SYSTEMS

Management practices, local constraints, and expectations regarding authority, time, and communication are but a few of the variables likely to affect the **appropriateness of monitoring (or control) systems**. The degree to which headquarters' practices and goals are transferable probably depends on whether top managers are from the head office, the host country, or a third country. In addition, information systems and evaluation variables must all be considered when deciding on appropriate systems.

The Appropriateness of Monitoring and Reporting Systems

One example of differences in the expectations regarding monitoring practices, and therefore in the need for coordination systems, is indicated by a study of Japanese and U.S. firms. Ueno and Sekaran state that their research shows that “the U.S. companies, compared to the Japanese companies, tend to use communication and coordination more extensively, build budget slack to a greater extent, and use long-term performance evaluations to a lesser extent.”⁵⁵ Furthermore, Ueno and Sekaran conclude that those differences in reporting systems are attributable to the cultural variable of individualism in U.S. society, compared to collectivism in Japanese society. For example, U.S. managers are more likely to use formal communication and coordination processes, whereas Japanese managers use informal and implicit processes. In addition, U.S. managers, who are evaluated on individual performance, are more likely to build slack into budget calculations for a safety net than their Japanese counterparts, who are evaluated on group performance. The implications of this study are that managers around the world who understand the cultural bases for differences in control practices will be more flexible in working with those systems in other countries.

The Role of Information Systems

Reporting systems, such as those described in this chapter, require sophisticated information systems to enable them to work properly—not only for competitive purposes but also for purposes of performance evaluation. Top management must receive accurate and timely information regarding sales, production, and financial results to be able to compare actual performance with goals and to take corrective action where necessary. Most international reporting systems require information feedback at one level or another for financial, personnel, production, and marketing variables.

The specific types of functional reports, their frequency, and the amount of detail required from subsidiaries by headquarters will vary. Neghandi and Welge surveyed the types of functional reports submitted by 117 MNCs in Germany, Japan, and the United States.⁵⁶ They found that U.S. MNCs typically submit about double the number of reports than do German and Japanese MNCs, with the exception of performance reviews. German MNCs submit a few more reports than do Japanese MNCs. Thus U.S. MNCs seem to monitor much more via specific functional reports than do German and Japanese MNCs. The Japanese MNCs put far less emphasis on personnel performance reviews than do the U.S. and German MNCs—a finding consistent with the Japanese culture of group decision making, consensus, and responsibility.

Unfortunately, the accuracy and timeliness of information systems are often less than perfect, especially in less-developed countries, where managers typically operate under conditions of extreme uncertainty. Government information, for example, is often filtered or fabricated; other sources of data for decision making are usually limited. Employees are not used to the kinds of sophisticated information generation, analysis, and reporting systems common in developed countries. Their work norms and sense of necessity and urgency may also confound the problem. In addition, their available technology, and the ability to manipulate and transmit data are usually limited. The **MIS adequacy** in foreign affiliates is a sticky problem for headquarters managers in their attempt to maintain efficient coordination of activities and consolidation of

results. Another problem is the **noncomparability of performance data across countries**—the control problem caused by the difficulty of comparing performance data across various countries because of the variables that make that information appear different—which hinders the evaluation process.

The Internet has, of course, made the availability and use of information attainable instantaneously. Many companies are starting to supply Internet MIS systems for supply-chain management. European partners Nestlé S.A. and the Danone Group, world leaders in the food industry, set up Europe's first Internet marketplace for e-procurement in the consumer goods sector, called CPGmarket.com:

*CPGmarket.com will enhance the efficiency of logistics while at the same time reducing procurement costs for businesses producing, distributing and selling consumer goods. CPG (based on mySAP.com e-business platform) allows companies not only to buy and sell, but also to access industry information.*⁵⁷

Evaluation Variables Across Countries

A major problem that arises when evaluating the performance of foreign affiliates is the tendency by headquarters managers to judge subsidiary managers as if all of the evaluation data were comparable across countries. Unfortunately, many variables can make the evaluation information from one country look very different from that of another country, owing to circumstances beyond the control of a subsidiary manager. For example, one country may experience considerable inflation, significant fluctuations in the price of raw materials, political uprisings, or governmental actions. These factors are beyond the manager's control and are likely to have a downward effect on profitability—and yet, that manager may, in fact, have maximized the opportunity for long-term stability and profitability compared with a manager of another subsidiary who was not faced with such adverse conditions. Other variables influencing profitability patterns include transfer pricing, currency devaluation, exchange-rate fluctuations, taxes, and expectations of contributions to local economies.

One way to ensure more meaningful performance measures is to adjust the financial statements to reflect the uncontrollable variables peculiar to each country where a subsidiary is located. This provides a basis for the true evaluation of the comparative return on investment (ROI), which is an overall control measure. Another way to provide meaningful, long-term performance standards is to take into account other nonfinancial measures. These measures include market share, productivity, sales, relations with the host-country government, public image, employee morale, union relations, and community involvement.⁵⁸

CONCLUSION

The structure, control, and coordination *processes* are the same whether they take place in a domestic company, a multinational company with a network of foreign affiliates, or a specific IJV. It is the extent, the focus, and the mechanisms used to organize those activities that differ. More coordination is needed in global companies because of uncertain working environments and information systems and because of the variable loci of decision making. Headquarters managers must design appropriate systems to take into account those variables and to evaluate performance.

Summary of Key Points

1. An organization must be designed to facilitate the implementation of strategic goals. Other variables to consider when designing an organization's structure include environmental conditions, the size of the organization, and the appropriate technology. The geographic dispersion of operations as well as differences in time, language, and culture affect structure in the international context.
2. The design of a firm's structure reflects its international entry strategy and tends to change over time with growth and increasing levels of investment, diversity, or both.
3. Global trends are exerting increasing pressure on MNCs to achieve economies of scale through globalization. This involves rationalization and the coordination of strategic alliances.

4. MNCs can be regarded as interorganizational networks of their own dispersed operations and other strategic alliances. Such relational networks may adopt unique structures for their particular environment, while also requiring centralized coordination.
5. The transnational structure allows a company to “be global and act local” by using networks of decentralized units with horizontal communication. This permits local flexibility while achieving global integration.
6. Indications of the need for structural changes include inefficiency, conflicts among units, poor communication, and overlapping responsibilities.
7. Coordinating and monitoring systems are necessary to regulate organizational activities so that actual performance conforms to expected organizational standards and goals. MNCs use a variety of direct and indirect controls.
8. Financial monitoring and evaluation of foreign affiliates are complicated by variables such as exchange rates, levels of inflation, transfer prices, and accounting standards.
9. The design of appropriate monitoring systems must take into account local constraints, management practices and expectations, uncertain information systems, and variables in the evaluation process.
10. Two major problems in reporting for subsidiaries must be considered: (1) inadequate management information systems and (2) the noncomparability across countries of the performance data needed for evaluation purposes.

Discussion Questions

1. What variables have to be considered in designing the organizational structure for international operations? How do these variables interact, and which do you think are most important?
2. Explain the need for an MNC to “be global and act local.” How can a firm design its organization to enable this?
3. What is a transnational organization? Since many large MNCs are moving toward this format, it is likely that you could at some point be working within this structure. How do you feel about that?
4. Discuss the implications of the relative centralization of authority and decision making at headquarters versus local units or subsidiaries. How would you feel about this variable if you were a subsidiary manager?
5. As an international manager, what would make you suggest restructuring your firm? What other means of direct and indirect monitoring systems do you suggest?
6. What is the role of information systems in the reporting process? Discuss the statement “Inadequate MIS systems in some foreign affiliates are a control problem for MNCs.”

Application Exercises

1. If you have personal access to a company with international operations, try to conduct some interviews and find out about the personal interactions involved in working with the organization’s counterparts abroad. In particular, ask questions about the nature and level of authority and decision making in overseas units compared with headquarters. What kinds of conflicts are experienced? What changes would your interviewees recommend?
2. Do some research on monitoring and reporting issues facing an MNC with subsidiaries in (1) a country in Asia, and (2) a country in South America. Discuss problem areas and your recommendations to the MNC management as to how to control potential problems.
3. Find out about a foreign company with an IJV in the United States. Google some articles, email the company for information, and if possible visit the company and ask questions. Present your findings on the company’s major control issues to the class—both at the beginning of the venture and now. What is the company doing differently in its control process compared to a typical domestic operation? Are the control procedures having the desired results? What recommendations do you have?

Experiential Exercise

- In groups of four, consider a fast-food chain going into Russia. Decide on your initial level of desired involvement in Russia and your entry strategy. Draw up an appropriate organizational design, taking into account strategic goals, relevant

variables in Russia, technology used, size of the firm, and so on. At the next class, present power points of your organization chart and describe the operations and rationale. What are some of the major control issues to be considered?

Internet Resources

Visit the Deresky Companion Website at www.pearsonhighered.com/deresky for this chapter’s Internet resources.

CASE STUDY

HSBC's Global Reorganization and Corporate Performance in 2012

HSBC Holdings owns subsidiaries throughout Europe, Hong Kong and the rest of the Asia/Pacific region, the Middle East and Africa, and the Americas.”¹

The above statements truly reflect HSBC Holdings' (hereafter HSBC) massive and distinct operations in 2012 that maintained 89 million customers worldwide. Originally known as Hong Kong Shanghai Banking Corp., the bank was founded in Hong Kong and Shanghai in 1865. Currently based in London, UK, HSBC is a well-known global entity (with two nationalities), has 7,200 offices in 80 countries, and employs 295,000 workers worldwide. In emerging markets, HSBC continues to be a visible player and has expanded because of tangible consumer demand and growth opportunities.

In 2011, HSBC had revenues of \$105.80 billion and made a pretax profit of \$21.95 billion. The bank's total assets stood at \$2.55 trillion. As of 2012, HSBC's operations are in most major parts of the world.² The bank's main revenues come from commercial banking, global banking, retail banking and wealth management, and private banking. HSBC did lose money during the 2008 global financial crisis. At the same time, the bank did not seek any bailout in Europe and Asia and continues to be a visible brand in the global banking industry. No wonder HSBC's distinct slogan (“*The world's local bank*”) reflects its strong corporate identity and global networks.

The global banking industry is a major strategic industry in world business, impacting countries, industries, and firms alike. Historically the industry's growth has been based on region- and country-specific strategies because of national developmental agendas and ideologies. Banks may be global in their operations but mostly thrive because of national identities, networks, and financial resources.

In July 2011, HSBC was rated the third largest bank in its tier one capital (\$163 billion).³ Other top banks in the list included Bank of America, JPMorgan, CitiGroup, Mitsubishi UFJ Financial Group, Industrial Commercial Bank (China), and Wells Fargo. The top 25 banks originated from the U.S., the UK, Japan, China, Japan, France, Italy, and the Netherlands. The pace of change and competition in the global banking industry is highly dynamic and fierce. The 2008 global financial crisis created havoc in the banking industry. During the crisis, banks' and financial institutions' “*systematic distress*” and “*spillover effects*” created major problems for the industry.⁴ HSBC was also impacted by the crisis and ended up losing money and customers. Unlike American banks, HSBC's operations were somewhat spared but growth remained stagnant during this period. The bank closed its money-losing operations and sold a few assets. This was a major disruption in HSBC's history and weakened the bank's well established business model.

To deal with the 2008 financial crisis, HSBC embarked on a major reorganization that changed its strategy and growth patterns. In 2011, HSBC trimmed its North American operations because of losses in the area of subprime lending.⁵ At the same time, HSBC started expanding in emerging markets of Asia. China was selected to be the bank's major market for future growth. Other reorganization took place that aimed at mostly downsizing and trimming operations. These changes did impact the bank's massive operations in global markets.

In February 2012, HSBC announced its financial results where the bank increased its net by 27 percent. This was clearly the result of HSBC's 2010 restructuring plan, which was designed in the post-financial crisis period. While HSBC trimmed its operations in North America, the bank's Asian markets witnessed a good increase in revenues because of growth in emerging markets.⁶ *Financial Times* called HSBC “*the world's Asian bank*.”⁷ No wonder HSBC plans on having a major presence in China and has announced increasing its share in China's Bank of Communications. HSBC also plans on expanding its branches in China from 110 locations to 800.⁸ This is a major part of the bank's reorganization that was initiated by Stuart Gulliver (CEO) and his team in 2009–2010.⁹

Although competition in emerging markets has been heightened because of the arrival of local and multinational banks,¹⁰ markets are available to those financial institutions that carry efficient business models and operations. HSBC has major plans in the Asia markets. Because of its long history and brand identity, the bank's future plans and restructuring initiatives can bear fruit if implemented accurately. In a special research report (“*The World in 2050: Quantifying*

the shift in the global economy”), Karen Ward, HSBC’s chief economist, observed with convincing data and logical arguments:

*“19 of the 30 largest economies will be emerging economies; the emerging economies will collectively be bigger than the developed economies; global growth will accelerate thanks to the contribution from the emerging economies. . . . Asia will continue demonstrating extremely strong growth rates and those with large population will overtake Western powerhouses.”*¹¹

This clearly shows HSBC’s long-term ambitions in the emerging markets of Asia, where growth is significantly available to those banks that carry prudent policies and networks. At the same time, the areas of technology and financial services have become more efficient because of the availability of online banking, the accessibility of large-scale and real time data, useful analytics, and other technologies on hand. This has helped multinational and local banks to be more competitive, efficient, and effective in their markets.

In conclusion, firms’ organizational structures, interorganizational networks and alliances, and control and monitoring systems are important when seeking expansion in the global banking industry, which thrives on strategic locations, networks, and customer service. The same areas apply to other industries and firms as well. Above all, firms must change on a continuous basis when dealing with growth opportunities, corporate expansion, and unexpected events in global markets.

Case Questions

1. How do you evaluate HSBC’s global reorganization and expansion in the post-financial crisis period?
2. Compare and contrast HSBC’s global operations with its main competitors.
3. What did you learn from the HSBC’s case when applying concepts and theories from Chapter 8?

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