McKinsey&Company

Perspectives on global organizations

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Welcome to the inaugural edition of McKinsey & Company's "Perspectives on global organizations." In 1959, our former colleague, Gil Clee, wrote "Creating a world enterprise" for the Harvard Business Review. He described the "different and infinitely more complex problems of managing large-scale international enterprises." In that article, he described the major shift that companies were making from having their international operations separately organized from the rest of the business to structuring a company around major regions and the challenges they experienced.

Over the last 50 years, economic and corporate globalization has accelerated. Leading corporations are no longer large companies with international operations. They are truly global institutions. Many companies' CEOs have described to us the increasing challenges of managing a large global company with an ever-growing geographic footprint. In our dialogues with senior executives, we realized that these challenges are likely to increase even further over the coming years as global companies shift more activity to emerging markets and as new competitors from those markets go global.

Over the last two years, we have talked to hundreds of executives and colleagues and asked them what it takes to manage a global organization well. They told us that their global footprint creates unmatched opportunities but there are challenges to manage a global organization to capture those benefits. Many corporations are beginning to address those challenges, and exciting examples of new organizational approaches are now appearing—often enabled by new technologies.

In 1959, Gil Clee wrote, "The new international scope of many US corporations today calls for creating a world enterprise." Fifty years later, we are seeing the start of a new era of global companies of enormous scope and scale. Senior executives leading them say that determining how best to manage a truly global organization is a critical topic on their agendas.

We are very grateful to all of the companies who have participated in this work to date and who have been so generous in sharing their own experiences with us and with each other. Many of those companies are at the forefront of defining the shape of the next generation of global organizations, and the leaders we have spoken with are actively innovating approaches to management inside their organizations today.

We hope that you find these perspectives on managing global organizations of help as you chart your own course.

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"Perspectives on global organizations" is written by experts and practitioners in McKinsey & Company's Organization Practice.
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Next-generation global organizations

To capture the opportunities of emerging markets and to counter the penalties of operating globally, the next generation of global organizations is beginning to be defined

Martin Dewhurst
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Global organizations have a very long history—arguably dating as far back as the Venetian trading empire in the 10th century. In recent years, the importance of being global has increased, driven in part by the rise of emerging markets, which are expected to contribute more than half of global growth over the next decade.

The rebalancing toward these markets is happening quickly, partly the result of ever-improving communications technologies: it took the early Asian corporate globalizers such as Sony or Honda 15 or more years to become global, but only 5 or so years for Tata and Lenovo to do so. Indeed, some of the companies in the most recent waves of globalizers might be said to have been "born global."

To better understand the changes, we surveyed and interviewed more than 300 executives at 20 of the world's leading global organizations[1]. More than half expect radical change to their business models in the next decade. And with external change picking up pace, these executives also expect that their organizations will have to accelerate their "metabolic rate"—the pace at which they change themselves. Many global leaders believe, as do we, that we may now be entering a new phase of globalization, in which companies will need to explore radically new models and practices.

To win in this new era, companies must understand the value of being global in four domains: strategy, people, cost, and risk. With that understanding, they can then start capturing the opportunities that are opening up to the next generation of global organizations.

1 See "Surveys" sidebar on page 5 for details of key surveys underpinning this work.

The benefits and challenges of being global

We define global companies as those that have a significant proportion of their sales, assets, or employees outside their home market (if indeed they still have a home market). That said, global companies are not homogenous; Citibank has little in common with Boeing, or Tata with Sinopec, other than size and reach. Our ongoing research has identified five broad archetypes, based on the primary way in which each creates value in the global business (see "Five archetypes" on page 3):

- Resource seekers, such as mining and oil and gas companies
- Researchers, such as pharmaceutical and some high-tech companies
- Global offerers, such as luxury goods manufacturers that offer the same product worldwide
- Customizers, such as consumer goods companies that tailor their offerings for local markets
- Networkers, such as airlines, third-party logistics companies, and professional services firms, which derive much of their value from their network.

Despite their differences, companies in all archetypes broadly agree that there is value in being global. In our survey of more than 300 executives, 88 percent said that their global footprint created value for their shareholders, employees, and other stakeholders. Still, even financially successful global companies often find it difficult to maintain their organizational health and agility in local markets, especially in comparison with strong local companies. Our analysis of McKinsey's Organizational Health Index, a database of nearly 600,000 employee surveys from more than 500 organizations, showed that high-performing global companies

Five archetypes

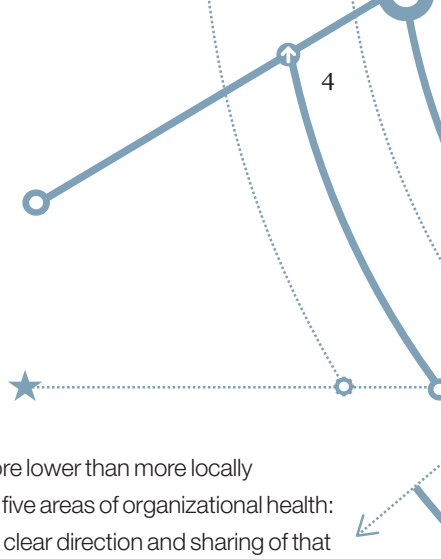
The *resource seeker* archetype includes companies such as Rio Tinto and China National Offshore Oil Corporation that globalize to gain access to raw materials or natural resources. In a world where resources are becoming scarcer, this entails operating in disparate and remote environments and running large operations that are concentrated around those resource assets. For these companies, the strategic benefits of being global are considerable. However, so too are the challenges, including engaging and staying connected with employees in those remote locations, grappling with local talent shortfalls, and managing substantial operations in countries that may be unfamiliar, entailing different risks and involving complex relationships with local stakeholders and regulators.

Companies that fall into the *researcher* archetype make significant investments in R&D to create products that address customer needs that are broadly similar across geographies. Pharmaceutical companies, certain engineering and automotive companies, and some high-tech companies are in this group. For example, the fundamental design and engineering of Airbus's A380 are standard for all customers; only minor adaptations, such as changes to the interior layout to meet individual airline needs, are necessary. Typically, these companies have a small number of R&D sites, and each site focuses on a few highly specialized skills. Historically, companies would have located these sites in their home region, but they are now establishing them in the markets with the most abundant talent. AstraZeneca, for example, has a center of excellence in Bangalore focused on developing medicines such as tuberculosis medication for the developing world. Likewise, the Novartis Institutes for BioMedical Research in Shanghai taps a strong and growing pool of local researchers. Once the product is developed and readily available, companies maximize value by achieving the widest possible geographic reach.

The *global offerer* archetype, like the researcher archetype, includes companies that provide broadly distributed products, but this group does so with lower levels of capital expenditure or R&D investment. It includes luxury goods companies (such as Burberry and the fashion and leather goods businesses of LVMH). The global offerer does not face the same challenges as other archetypes; for companies in this group, core operations are often concentrated in their home market but still linked to a global presence. And insofar as their global offering is a "volume play," the marginal costs of taking an identical product to a new marketplace are, of course, minimal.

A fourth archetype is the *customizer* or local deliverer. The difference between these companies and the researchers and global offerers is that these companies customize their offer in multiple markets. In some cases, only a part of the product or service is customized, but this tailoring is at the core of the global strategy and requires more substantial in-market operations. McDonald's, for example, offers beer in its French restaurants and a beef-free menu in India. Tailoring is supported by strong, consistent global processes such as standard operating procedures. These companies face the challenges of balancing those global strengths with a local focus, of maintaining much more substantial and often more distributed global operations than researchers or global offerers, and of attracting, training, and retaining local executives and other workers. They can often learn from local innovation, but they also face considerable obstacles in engaging a distributed workforce.

Finally, we have the *networker* archetype. Companies in this group base their business on the network benefits of their global reach. This group includes information providers such as Thomson Reuters, logistics companies such as DHL and UPS, certain financial services firms, professional services firms such as McKinsey, and major airlines. The network can create benefits at different points along the value chain. For example, investment banks can draw on local knowledge in Kuala Lumpur



and Johannesburg and provide clients in London with the ability to access and trade in those markets. DHL and UPS attract customers who want the reliability of a global delivery network owned by one carrier. Like customizers, these companies have local operations (albeit smaller ones) in many locations to maintain and operate the network; they therefore face challenges in engaging widely distributed employees.

Beyond archetypes, we have also found that a company's heritage—that is, whether it grew organically or through M&A—strongly affects its experience of being global. Companies that have grown organically often find it easier to operate consistently across all countries; however, they may find it harder to adjust their products and services to local market needs because they have a strong core. M&A makes local adaptation easier, because local expertise has often been brought in, but it can make it more difficult to achieve the benefits of scale and scope and to create alignment.

It is also worth noting that although we have described these archetypes and sources of growth as separate, some global organizations may contain businesses that match different archetypes or which have grown in different ways, particularly offerer and customizer, are on a continuum.

consistently score lower than more locally focused ones in five areas of organizational health: the creation of a clear direction and sharing of that direction; coordination and control; capabilities; innovation and learning; and external orientation (engagement with external stakeholders such as customers, suppliers, partners, and local governments).[2] And companies headquartered in developed markets seem to face even bigger challenges in emerging markets than their peers headquartered in those markets. When we looked at the growth rates of companies in emerging markets, we found that those headquartered in another emerging market had a compound annual growth rate of 31 percent, far higher than for those headquartered in a developed market, where the rate was 13 percent.[3]

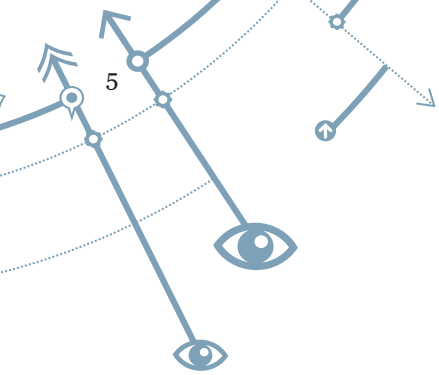
But what is the true value of being global? And what are the challenges that frustrate firms pursuing the benefits of globalization? We group the benefits and challenges on four axes: strategy, people, cost, and risk. On each axis, there are both benefits and challenges that can come into conflict if they are not handled carefully. For example, taking advantage of the strategic benefits of being global by entering new markets can also make it harder to find the right balance between global standardization and local optimization. Companies should seek a point on each axis that best positions them for sustained success.

Striking a balance can be difficult. In almost all cases, we find that companies are not capturing the full range of potential benefits of being global.[4] Sometimes they do not appreciate the value that could be captured (for example, most global companies do not realize the full extent of the knowledge and expertise held within the organization); at other times, the challenges and complexities of capturing that value can seem insurmountable.

2 Martin Dewhurst, Jonathan Harris, and Suzanne Heywood, "Understanding your 'globalization penalty,'" *McKinsey Quarterly*, July 2011 (mckinseyquarterly.com).

3 Sumit Dora, Sven Smit, and Patrick Viguerie, "Drawing a new road map for growth," *McKinsey Quarterly*, April 2011 (mckinseyquarterly.com).

4 Some of these benefits—in particular, cost benefits—can also be captured by a large company that is not global. In reality, however, many large companies need to go global to achieve the scale necessary to capture such benefits fully unless they have an extremely large home market (such as China, India, or the US).



Surveys

Our initial research which identified the global penalties (see Exhibit 1 opposite) included an analysis of McKinsey's Organizational Health Index database of 600,000 employee surveys from more than 500 organizations.

As a further part of our research, we administered 3 separate but related surveys in a 3-month period to gather data on the benefits and challenges facing global executives.

- The primary survey referenced to most frequently throughout this document is the McKinsey Globalization Survey; it is accompanied by structured interviews of more than 300 executives at 20 of the world's leading global organizations as of November 2011.

- The McKinsey Talent and Organization Imperatives Survey of 120 executives at 17 Indian country organizations within multinationals as of February 2012 was based on the Globalization Survey, however, with a particular focus on talent in emerging markets.

- The McKinsey Quarterly also surveyed more than 4,000 executives worldwide in September 2011, using questions from the Globalization Survey. However, these surveys were not complemented by structured interviews. This data set provides a broader corroboration of our in-depth findings from the Globalization Survey and interviews. See "McKinsey Global Survey results: Managing at global scale," McKinsey Quarterly, at mckinseyquarterly.com.

These surveys are footnoted throughout the document.

Axis 1: Strategy. Benefiting from greater access, opportunities, and reach while remaining agile and relevant

Most companies go global initially to gain strategic benefits from accessing new markets. Once they have become global, however, greater balance sheet depth and a larger geographic footprint can afford them new opportunities. For example, Unilever had a commercial presence in China for many years, then went on to establish a global research center in Shanghai. Networker companies in particular exploit this effect; their strategic returns from geographic expansion increase as they enhance their network and thus provide greater reach and coverage for their customers.

However, there are also strategic challenges to being global. Many companies find it difficult to be locally flexible and adaptable while increasing their global footprint. In particular, strategy development and resource allocation processes may have difficulty coping with the growing diversity of markets, customers, and channels.

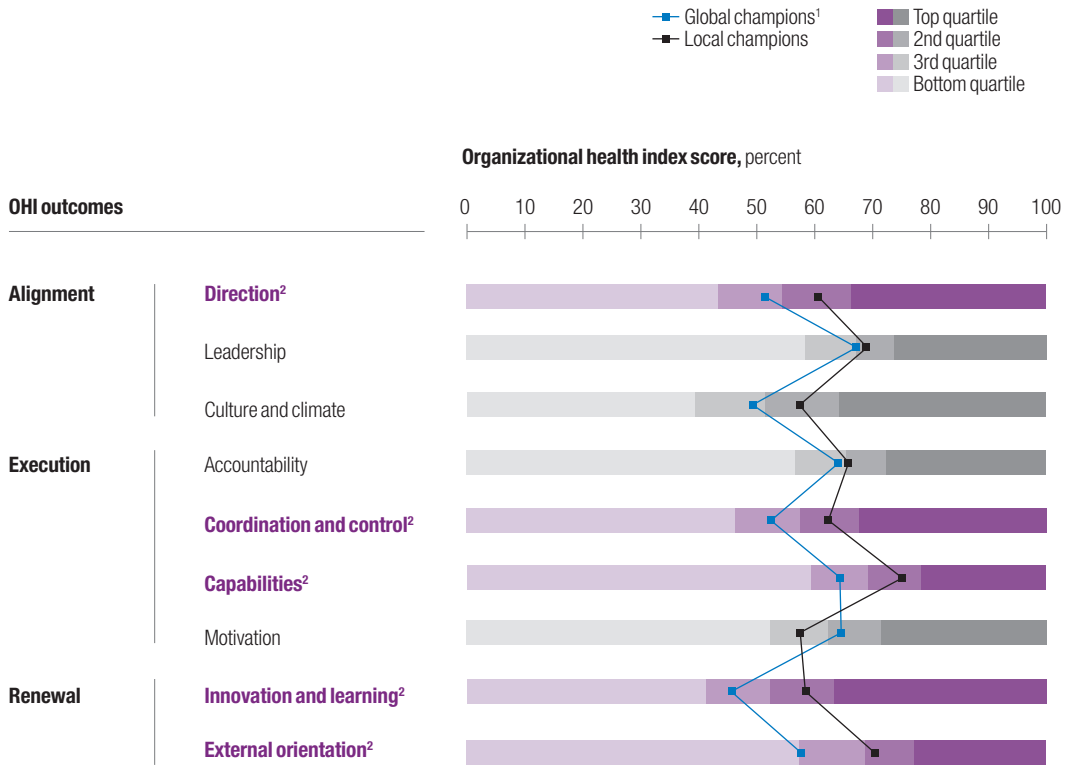
These issues were clear in our recent research; only 38 percent of executives thought they were better than their local competitors at understanding the operating environment and customers' needs, and only 39 percent felt that their priority global processes met most business unit- or country-specific needs.

Axis 2: People. Capturing value from diverse experiences and skills while creating engagement and alignment

The second axis focuses on people. There is a huge, frequently untapped benefit in the diversity of ideas, knowledge, and skills within a global company. Of the four axes, the benefits derived from people are perhaps the least appreciated,

Exhibit 1

There is an organizational "penalty" from being global, particularly in 5 areas



[1] Companies were defined as global based on proportion of sales outside of home geography, proportion of employees outside of home region, geographic diversity of top management team, and proportion of shareholders that are outside of home region.
[2] Elements with a statistically significant difference.

Source: Organizational health index database; McKinsey analysis

but their value is increasing as many global companies shift emphasis to emerging markets. These markets, which represented only 5 to 10 percent of their business a few years ago, may represent 50 percent or more within a decade. To succeed in these markets, global companies must make sure their employees represent the diversity of their global footprint. They can then make full use of the breadth of insight and knowledge contained in this diversity to allow them to innovate quickly.

A major challenge with the people axis in addition to the challenge of people engaging with staff who are distributed globally[5] is how to win the war for talent in emerging markets. For example, in China, attracting and retaining talent is exceptionally difficult. In interview after interview, multinational executives said that they simply cannot find enough people in the country with the managerial skills and ability to work in an Anglophone environment. Another aspect of the problem is the league table of preferred employers. In 2006, the list of the top 10 preferred employers in China contained only 2 local companies (China Mobile and Bank of China); the others were well-known global names. By 2010, the tide had turned;

5 This engagement challenge was highlighted in our article in the globalization survey, *McKinsey Quarterly*, July 2011.

7 of the top 10 were Chinese companies. As one executive told us, "Local competitors' brands are now stronger than they were, and they can offer more senior roles within their home market, which is very attractive to local talent." The difficulty of retention compounds the problem: annual staff turnover rates of 20 to 30 percent are not unknown for global companies in emerging markets.

For customizers who need to tailor their product or service in each market, this talent challenge creates particular difficulties, as emerging markets often require greater product and service differentiation than established markets do—and this, in turn, necessitates different business models. As an executive at one successful global company told us, "Historically, we only changed either our product or our geography, but to be successful in emerging markets, we need to do both together. This is fundamentally challenging the way we operate. We need to get better at understanding local markets and better at capturing local innovations, and then exporting that knowledge globally."

Global companies are acutely aware of this challenge. Indeed, only 52 percent of the more than 300 executives we studied in depth thought their company was effective at tailoring its recruiting, retention, training, and development processes for different geographies—and the more geographies a company spanned, the more complicated and pressing the problem was. An emerging-market leader within one global company told us, "Our current process favors candidates who have been to a US school, understand the US culture, and can conduct themselves effectively on a call with the head office in the middle of the night. The process is not designed to select people who understand our local market."

Axis 3: Cost. Exploiting economies of scale while managing complexity and ensuring flexibility

Global companies gain value from scale-related cost efficiencies. Some of these benefits—those that derive from transactional scale (such as economies of scale in shared services)—are now also available to local companies through outsourcing, access to cloud resources, and so on. However, large global companies can still use their balance sheet strength and business reach to create more sophisticated efficiencies, for example, by building infrastructure that can be used by multiple business units (such as R&D centers and global training facilities).

As with the other dimensions, being global brings cost challenges as well as benefits. In particular, we know that the bigger and more diverse a corporation is, the greater the risk of excessive complexity that creates cost without creating value. The good news is that this value-destroying complexity can be substantially reduced by simplifying processes, clarifying accountabilities, and reducing organizational duplication.

However, some of the other cost challenges of being global can be more difficult to manage. These include allocations of corporate functional costs whose value is opaque at best for far-flung markets, the cost to local businesses of complying with global standards, the higher operating costs that result from global processes that are too rigid, and the costs of management coordination. These cost penalties have been raised frequently in our work with global organizations and are, of course, a consequence of the increased formality of structures and processes that global organizations often require to capture the cost benefits of globalization. One hundred pages of budget guidelines might be acceptable for major

markets, but the same document could be a significant hurdle for a nascent organization in, say, Peru, Romania, or Vietnam.

Axis 4: Risk. Locking in process quality and portfolio benefits while retaining a transparent view of risk

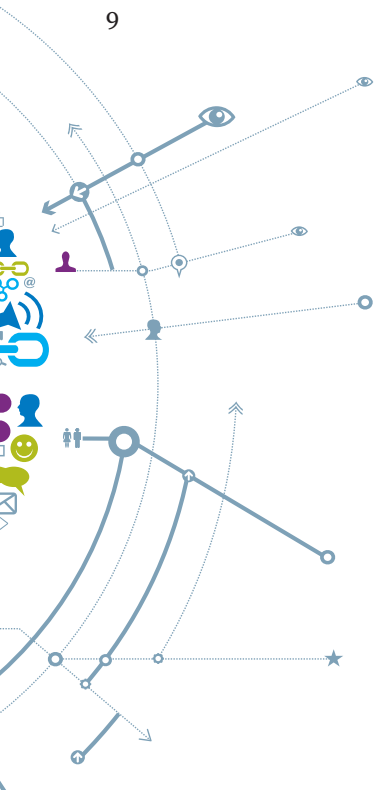
The risk mitigation benefits available to global companies are increasingly valuable as volatility in the global economy continues. A diverse portfolio gives companies the opportunity to gain profits from high-performing or very mature economies—where assets may be expensive—and reinvest them in other countries where assets are cheaper or growth prospects are better. For example, many aircraft manufacturers are looking to insulate themselves from the volatility of demand in developed markets by investing in emerging markets, as Bombardier is doing in Asia. A geographically diverse portfolio also provides a natural hedge against country and currency risk; even as national economies become more interconnected, growth rates and cost of capital (among other factors) still vary enough to make a difference.

Once again, although global companies benefit on this axis, they also confront a set of risk challenges that stem from increased geographic reach. In more geographically focused companies, the set of risks is usually narrower, and senior leaders are more familiar with them. Our Organizational Health Index analysis[6] shows that global champions find it harder than local champions to measure and manage their risk consistently and to address problems when they arise. Many global companies respond by making their risk processes more rigorous and standardized. This, however, can create further tension when a standardized global process overestimates less familiar local risks and undervalues local opportunities. For example, one executive said, "A mindset that 'this is the way that we do things around here' is very strongly embedded in our risk process. When combined with the fact that the organization does not fully understand emerging markets, it means that our risk process rejects opportunities that our CEO would approve."

Approaches to reorganize for global success

Leading global companies have the opportunity to reshape their business fundamentally to address the opportunities and challenges on these four axes. As a result, over the next few years, very different approaches to global organization will

6 Martin Dewhurst, Jonathan Harris, and Suzanne Heywood, "Understanding your 'globalization penalty,'" *McKinsey Quarterly*, July 2011 (mckinseyquarterly.com). For more on the Organizational Health Index database, see solutions.mckinsey.com.



emerge. There will be no one solution—what will win will reflect a company's archetype and its unique context. Furthermore, even the most sophisticated companies will discover that reorganizing for global success is an ongoing process; they will have to evolve as the landscape changes, and so the "solution" may actually feel like a work in progress. However, we believe that five emerging approaches will play an important part in shaping the next generation of global organizations.

Approach 1: Making growth markets a center of gravity

Many global companies continue to expand their global footprint across the value chain, from research to operations to sales and marketing. And they are immersing themselves in emerging markets such as Brazil, China, and Nigeria, all of which have different consumer and stakeholder requirements. As companies shift their geographic focus, it will be critical to ensure that the financial resources and talent dedicated to these regions fully reflect the potential value at stake. This is not the case in most companies today. Recent McKinsey research showed significant strategic inertia in the ways that companies allocate capital to new opportunities; it also demonstrated that the companies that reallocated their capital most dynamically earned, on average, 30 percent higher total return to shareholders than their more sluggish peers.[7] We believe this provides a powerful lesson—not only for capital allocation but also for talent allocation.

Equally critical will be the reshaping of key processes, such as resource allocation, innovation, and risk management, to accommodate the realities of emerging markets. All too frequently, processes are still geared to the developed-market priorities of the past decade instead of the imperatives of the next. In addition, some companies are exploring structural changes such as managing high-growth regions separately from lower-growth regions rather than clustering regions based solely on proximity. Other approaches we have seen include having key markets report directly to the CEO or appointing a CEO or country president to drive integration across business units in a key geography and thus raise the company's profile with governments, potential partners, and talent.

More fundamentally, many companies are rethinking the role of the corporate center—even challenging the extent to which that concept is still helpful. Increasingly, companies are "unbundling" their structure and establishing corporate functions in the location that best fits their market, cost, and talent needs. IBM's global emerging market business, for example, is headquartered in Shanghai; a conscious decision was made to separate it from the company's central functions in its suburban New York location.

For further details, see "How Western multinationals can organize to win in emerging markets" on page 13 and "Reinventing the global corporate center" on page 41.

Approach 2: Reshaping the global/local operating model to increase the "metabolic rate"

A broader geographic footprint, including more diverse employees, customers, and other stakeholders, naturally increases complexity. The traditional approach to reducing complexity—standardization—may be of only limited use for the next wave of global organizations because it reduces local-market agility. For example, an executive we interviewed described how his company's risk process frequently flagged a new partnership in an emerging market as a risk when, in reality, the partnership was critical to success.

7 Stephen Hall, Dan Lovallo, and Reinier Musters, "How to put your money where your strategy is," *McKinsey Quarterly*, March 2012 (mckinseyquarterly.com).

To address this, global companies must become far more adept at defining the processes that need to be globally standardized because they are core to value creation. For a resource seeker, these might include major contract or investment decisions. By the same token, global organizations must also excel at recognizing those processes that can create more value through local variation. For a customizer, this might mean greater latitude in forging local partnerships. A conscious redesign of these processes with an eye toward improving quality and accelerating their pace will be essential. Companies will also benefit from specifying clear accountabilities at each level in the organization, reducing duplicated accountabilities, and building an ecosystem to foster collaboration and networking. These are not new problems, but they may need to be addressed in new ways—for example, by focusing on customer- or market-back designs rather than on top-down programs.

For further details, see "Structuring your organization to meet global aspirations" on page 29, and "Getting ruthless with your processes" on page 51.

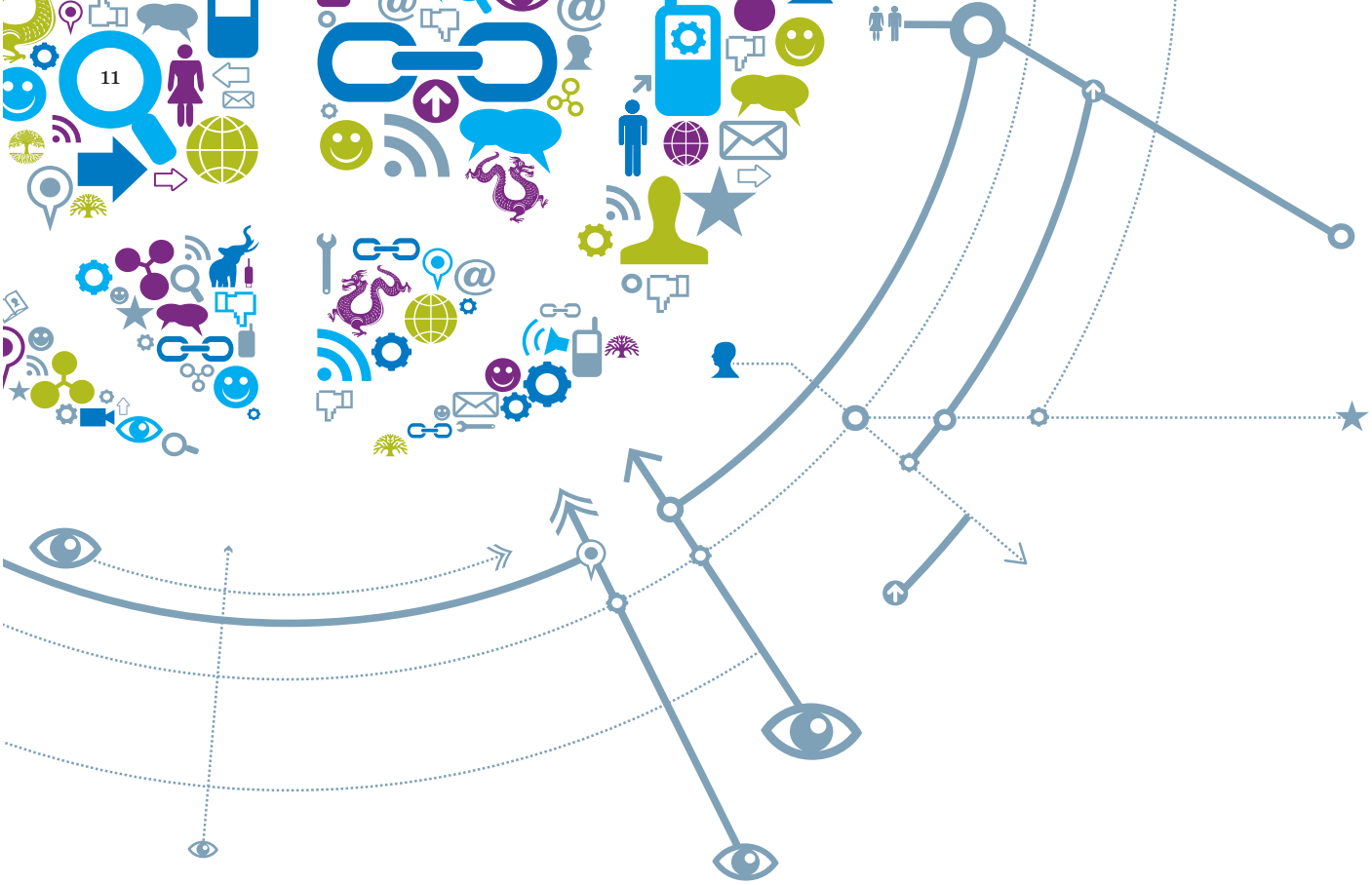
Approach 3: Developing more diverse and dynamic approaches to engage partners, networks, and external stakeholders

To increase strategic agility and reduce risks, global organizations need to explore new forms of external partnerships and collaborations—for example, by working more closely with suppliers, customers, and (particularly in emerging markets) governments and their agencies.

This challenge is important for most types of companies. For resource seekers, the ability to create consortia and win local contracts in increasingly remote locations is critical. For networkers, the ability to navigate local regulators and governments is essential. Local partnerships may often be the solution, although our analysis suggests that only 50 percent of partnerships meet expectations, with joint ventures proving particularly challenging to balance over time. Customizers also need to mobilize a broad range of partners to tailor products for local customers' needs. For example, several Japanese and Korean automakers have demonstrated the value of making significant local commitments, building greenfield plants in the US with state support, and becoming so established that they can now promote their products as "made in the US." Researchers such as pharmaceutical companies can also benefit from partnerships that provide access to the accelerating academic activity in emerging markets.

But an external focus does not come easily to global organizations: their need to standardize processes and manage risk can lead to an internally focused and conservative approach. At a local division of a global company that we interviewed recently, the local staff was overwhelmed by the task of completing 120 different strategy templates, that had been designed for more developed markets.

Setting clear aspirations can help: for example, A. G. Lafley, the former chairman and CEO of Procter & Gamble, set a goal that 50 percent of innovation at the company be externally sourced. Other important transformations include revamping investment management and portfolio management processes, such as Cisco's "proudly sourced externally" projects, as well as redefining relationships with partners and suppliers to increase transparency and align aims (as BMW has been doing with BASF to create a "cost per painted car"). Technology can also help, as shown by the increasing number of company



Web sites, like those of Nike and the LEGO Group, that allow customers to tailor their own products.

For further details, see "Getting more value from your global footprint" on page 59.

Approach 4: Building the next-generation cohort of global leaders and local teams

Global companies need a cadre of leaders to reflect the diversity of their businesses. This challenge has never been more pressing than it is now, as businesses rebalance toward new markets and customers. Organizations need to accomplish this in the face of intense competition for talent (increasingly from local players), high turnover rates, and relatively small pools of talent with the right cultural and linguistic fit. In this context, strong, committed local leadership is essential.

There are many talent issues for this leadership to address to achieve this diversity. For example we have found that some senior executives in the emerging-market operations of global companies do not have the skills to move up. In other cases, they do not have the opportunity; one executive described this as a nationality-based "glass ceiling." Another familiar problem is that companies find it hard to hire senior leaders locally because they are looking for employees just like the ones they have at home, based on traditional skill sets and educational achievements.

To meet these challenges, a few companies are revamping their training at all levels. One example of these efforts is a program at Goldman Sachs designed to help Asian executives overcome cultural barriers that have hindered their promotion. Organizations are also fundamentally altering their recruiting programs so that they are not hiring for familiarity with home office norms but are instead hiring for local-market skills and connections. Additionally, companies are innovating to improve retention, for instance, by offering more attractive career paths and greater access to world-class executive training. And leading companies are rethinking their expatriate programs, seeking to reverse traditional flows and create a new culture of long-term assignments so that these are no longer viewed as "here today, gone tomorrow" stays.

For further details, see "Winning the talent war in local markets by staying global" on page 67.

Approach 5: Capturing the power of knowledge, networks, and skills across the enterprise

Finally, ensuring that companies benefit from the knowledge and skills they already have is a crucial challenge. In our experience, even successful global companies struggle to deploy just a small fraction of their collective expertise. A salesperson in Korea could likely benefit from the experience of a colleague in Brazil in negotiating with a client—but how can the Korean learn what the Brazilian knows? A company intranet or an employee handbook is not by itself enough to make that exchange take place.

Companies must find new ways to capture expertise and spread best practices. There is no one solution. Many look first to technology, which is certainly a key enabler. But technology-based approaches will not flourish without people seeing the value of sharing and exchanging insights. More promising are approaches to retool processes and forums such as strategy meetings that ensure that growth markets are represented adequately. As is too often the case today, the decision maker on a project team is from North America or Europe. Another option is to reshape incentives. One company asked its local leaders to "search and spin." Each is challenged to identify ideas from their peers and to discuss the insights and best practices they have shared, or "spun," with their colleagues.

Beyond individual structures or processes, many global companies have started to find new ways to establish linkages across locations, enabling local knowledge and innovation to be captured and then deployed globally. Often, this is done by creating formal and informal communities of interest. Technology can facilitate these communities. IBM's internal Beehive Web site, for example, allows more than 100,000 employees to engage in communities of interest on multiple topics. Other companies have chosen more formal approaches, like creating global "functional families" to share knowledge and expertise.

For further details, see "Getting more value from your global footprint" on page 59.

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The next decade will see fundamental changes in the organization of global companies. Although each will chart its own path, we believe a map leading toward the next-generation global corporation is emerging; the rewards for experimentation and boldness, particularly increased agility and a higher metabolic rate, will be considerable.

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The authors would like to acknowledge the contributions of Kate Aquila and Roni Katz to the development of this article.

How Western multinationals can organize to win in emerging markets

As organizations from the developed world shift their focus to emerging markets, they must adjust their structures, processes, and decision making speed to compete successfully

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Many leading Western multinational corporations expect that their future success will depend on their ability to win in emerging markets. They project that the share of their business based in emerging markets will increase from some 20 percent to 50 percent or more over the next decade. While their intentions are clear, results thus far have been mixed, even for those Western multinationals that have operated in emerging markets for several decades.

Our experience and research suggests that companies are still learning how to organize for success in these markets. They are looking for better ways to allocate financial and human resources to match their aspirations. They are trying to attract and retain senior talent with the skills to align stakeholders in a global network and the entrepreneurialism to drive initiatives on the ground. They are working to innovate so they can be relevant in a local market at the prevailing price point, all while maintaining global quality standards. They are exploring how to improve risk management to accelerate the "metabolic rate" of decision making in a complex matrix organized by products, segments, countries, and functions. And they are working out when they should get into emerging markets and how they will sustain long-term commitments once they do so.

Some leading globalizers are coming up with solutions that work in emerging market; in the face of new challenges, a few are even throwing out the playbooks that worked so well at home. Companies are finding ways to entice local talent, customize their innovation processes, and develop new kinds of partnerships. Those moves allow them to follow through on bold and public commitments to emerging markets, entrusting more power to their local organizations and simultaneously unifying the global organization with a set of core values.

The challenges

Our research indicates that Western multinationals routinely confront five main challenges in emerging markets.

Challenge 1: Mismatched resources

Leaders often do not allocate the right resources to emerging markets—for example, one analysis showed that while leaders of large global companies saw a potential for 34 percent of their sales to come from emerging markets in Asia, they currently have only 2 percent of their top 200 employees in those countries, just 3 percent of their R&D budget is spent there, and 5 percent of assets are located there.[1]

Leaders may need some convincing to change this resource allocation; the emerging-markets business heads we have talked with say that global headquarters sometimes see more risk than reward in many emerging markets, where returns can be volatile or uncertain. One business leader said, "Emerging markets will soon be 50 percent of our revenue, but all our developed-market executives want to talk about is the risk." And plenty of global executives, he added, are reluctant to change their own responsibilities to place more organizational emphasis on emerging markets. Even when leaders agree with the need to rebalance in principle, making it happen has been difficult for both business reasons (for instance, it is difficult to find enough local talent) and psychological ones (for example, headquarters staff may be reluctant to change the way they work).

Challenge 2: Talent

Western multinationals face a number of challenges getting the right people in the right places: a shortage of senior global leaders with

1 "Multinationals in Asia: All mouth no trousers," *The Economist*, March 29, 2007.

sufficient breadth of experience and mindsets, a huge shortfall of local leaders with the skills (including English language skills) needed to work both locally and globally, and strong competition for talent at all levels from local as well as global competitors. Most executive talent pools in emerging markets are small. There are simply not enough people who know the local market thoroughly, understand what it takes to execute strategies, and are credible with the country's senior stakeholders.

Although finding such people is a challenge, a bigger one is retaining them: good executives in emerging markets no longer want to work for a "branch" of a global company, and today they have plenty of other options as local companies become increasingly global themselves. Whether people leave because of what an executive at one global bank referred to as a "local glass ceiling," meaning they see no chance to move up in the global organization or do not want to move overseas in order to do so, or because they are poached by local competitors offering more money and greater responsibilities, the result for a global company is the same: a shortage at the top. A further challenge is that many local executives can be daunted by the matrix structures that global firms commonly use; they do not have the usual networks of mentors and advisers needed to navigate a complex global organization.

Challenge 3: Innovation

International products and prices do not always translate into profits in emerging markets, particularly for consumer industries. Significant differences in income, language, literacy, social diversity, and urbanization can make it difficult for companies to offer a standard global (or even regional) product. And yet expectations are high; emerging-market customers frequently demand products with most of the same features as their developed-market counterparts, but at a fraction of the price. A one-minute mobilen phone call in the US can cost 10 to 50 cents. In India, that same call can be made for less than a penny, due in large part to innovations like Airtel's "minutes factory" approach, in which much of the capital-intensive business of network deployment is outsourced to other companies, allowing the operator to adjust its costs to match demand. Most global companies are simply not organized to support this degree of innovation; when they do try, they are often slower than local competitors. To be fully effective, however, will require radical innovation.

There is a second dimension of the innovation challenge for many global companies as, when innovations succeed in one local market, it may be highly valuable to export the concept to other markets. Although some organizations are becoming proficient at leveraging this so-called "reverse innovation," most do not believe they are capturing the full global potential of innovations originating from emerging markets.

Challenge 4: Risk and stakeholder management

No matter how successful a global organization is at managing risk at home, the task is larger for emerging markets: companies must manage multiple regulatory regimes, which may be less stable than in developed markets, as well as a diverse range of business practices. And operating in an ever-expanding number of regions and countries exposes the organization, naturally, to more varied risks. These could include political complexities (which can, for example, delay decision making between the national and state or local levels), geopolitical

risks (such as nationalization of assets), a high level of government influence on the market (for example, in China, the government can influence more than 50 percent of the relevant market for some global organizations), governance issues such as corruption, and social tensions.

Some emerging-market risks can be difficult to assess—and easy to overestimate—given a lack of local knowledge, distance from corporate expertise, or poor connections with local stakeholders. This challenge is compounded by technology, as social media, blogs, and other new formats require increased attention and rapid responses. Indeed, the chairman of a global organization in India said, "Anywhere between 25 and 50 percent of our CEO's time is spent on regulatory management."

Challenge 5: Early and long-term commitment

Western companies' operations in emerging markets can become stuck in what we have come to call a "midway profitability trap": these businesses see some success but suffer from a lack of commitment to increase investments and build operations or management systems specific to a given market. Executives have told us that some senior leaders are gun-shy from previous crises, which accounts for the half-hearted commitment. Yet emerging-market policy makers and entrepreneurs have long memories, and "state visits" by the global CEO or chairman are not sufficient to maintain good relationships if a company's commercial dedication is seen to have faltered.

How to win

Some multinational companies in emerging markets have already seen incredible success; for example, Telefónica transformed itself from a state-owned Spanish telecommunications company to a broad-based player with a deep footprint across Latin America. Throughout those emerging markets, it has close to 30 percent market share and is either the number one or number two player. Many global companies—such as GE, Citigroup, Unilever, and P&G—also have rich histories in emerging markets with decades of experience in building large businesses and global talent pools. From our research, including conversations with executives at these companies and many others, we have begun to identify some cross-cutting organizational solutions to overcome the challenges described above. Even the most advanced of these players would not claim to have solved all the issues. However, for companies that possess a strong emerging-market footprint as well as for those who aspire to, the following approaches are worth considering.

Approach 1: Manage talent with a local eye

Companies need to ensure that there are multiple paths to success for local leaders, even if they start their careers in low-profit or "less core" markets. One approach involves shifting regional or global responsibilities to emerging markets. Similarly, companies can place functional or geographical hubs in emerging markets, as GE, Honeywell, Dell, and Cisco have done. For example, Cisco's Globalization Center East in Bangalore was established to develop local leaders in functional areas who will, in short order, account for 20 percent of the company's senior leadership team.

Efforts such as these can also help local executives develop deeper functional expertise, thus opening another path to success.

In addition, companies must make sure their core value proposition to talent is appropriate to emerging markets. At one company, emerging-market businesses grew by double digits in one year and also had strong operating margins, while the global business unit grew by only 2 percent. If the company had adhered to its policy of aligning incentives to global performance, the emerging markets would have received low payouts, undermining their accomplishment and demotivating their future performance. The company therefore reallocated its global bonus pool to raise payouts in the emerging markets. Unsurprisingly, questions of equity arose as the company debated the relative contributions of global support and local execution. One tactic to manage those concerns is to establish a separate bonus pool for high performers in emerging markets.

It is also important to recognize cultural differences in the kinds of incentives people value. Many young Russians who are starting their careers in sales, for example, value higher salaries, prestigious titles, and other visible signs of success more than long-term compensation such as stock options or pensions. ("Winning the talent war in local markets by staying global" on page 67 addresses additional issues related to expatriate executives and attracting local talent.)

Skill development at all levels is crucial. McDonald's, for example, dealt with a lack of local skills by opening a Hamburger University in China in 2010. By 2014, it will train more than 4,000 employees, from operators to restaurant managers. At a more senior level, such investments can become a source of supply for

global executive talent pools: in 2010, Unilever's India unit relocated more than 200 managers to the global organization to run operations in other markets. The company has also brought quite a few of these leaders back to India after their global rotations, finding that the combination of global expertise and local knowledge provides the best platform for success.

Approach 2: Bring new approaches to innovation

Though some products like airplanes or pharmaceuticals do not require significant customization to succeed in emerging markets, most others do. The challenge is to balance the best of the "global" assets (the brand, opportunities to develop capabilities, and others) with the need to tailor locally—particularly given the rapid pace at which companies want to develop progressive and distinctive value propositions in their product portfolio. For example, well-intentioned innovation systems can be counter-productive if too much emphasis is placed on global standardization. Instead it is critical to ensure that innovation captures local insights and responds to them at pace and scale—a challenge that frequently involves radically altering the company's historical innovation process. Leading brewer SABMiller faced this issue in Africa. The company determined that through product innovation it could reach additional consumers at the "bottom of the pyramid." In a couple of African markets, it changed from cereal crop inputs such as barley and maize to cassava, a local root crop that is taxed at a lower rate but which yields a beverage that consumers like. The early results are promising; the company expects with this low-priced beer it can attract additional consumers who until now have not been able to afford aspirational, but expensive, "conventional" malt-based beer.

Another African brewer was equally creative. In Kenya, Diageo realized that it had to compete with the local homebrews popular with many consumers. The company wanted to ensure consumers had access to safe and affordable beer, and so it had to change the way it typically brought new products to market. In this case, that meant involving an external stakeholder early in the process. The company successfully sought a temporary tax waiver (for itself and other brewers) from the government, which was also interested in reducing consumption of the sometimes contaminated and unhealthy homebrews.[2] In four years, Diageo has earned revenue of $250 million from its new Kenyan beers.

It is not just brewers who are innovative. In Colombia, Telefónica partnered with Banco de Bogotá and the National Federation of Coffee Growers to develop the Intelligent Coffee Identification Card, a card that identifies the 300,000 member growers. The card gives them secure access to mobile-banking services, a new business model developed by this pioneering three-way partnership. Within a month of the service's launch in 4 municipalities, more than 1,300 transactions were recorded.

Some companies are now also recognizing the huge potential for revenue innovation that brings insight from emerging markets to the rest of the global business, particularly for accessing new pools of consumers. John Deere, for example, developed a no-frills tractor at its R&D center in Pune, India, at a fraction of its normal cost. With some minor tweaks, the company now also sells these tractors to hobbyist farmers in the US who do not require advanced features. This in turn opened a new market for John Deere, which now exports half the tractors built in India.

2 "Easier said than done," *The Economist*, April 15, 2010.

Approach 3: Build broad and deep partnerships and collaborations

Success in emerging markets requires companies to focus externally as they need to establish extensive networks and look beyond traditional types of partnerships. Given the extensive influence of the state and its agencies in emerging markets, there may be far more opportunities for public-private partnerships like Diageo's.

Another model is the joint venture, which has a mixed track record. Certainly those joint ventures based on well-defined roles, a long-term commitment, a shared vision of the goals, and strong and open communication to ensure all parties are aligned have greater chances of success. For example, joint ventures such as Tata Cummins and Bajaj Allianz in India have flourished because each partner brought complementary skills and assets (like deep distribution networks, customer insights, and high brand recognition) as well as long-term commitment.

Approach 4: Create "glue" with values

Working across cultures can be difficult. But executives we have talked with agree that values can be meaningfully translated across cultures and that creating a system of shared values does help hold a global company together—improving employee attraction and retention and, often, allowing for faster decision making, even on tough issues like risk management.

Johnson & Johnson applies this idea with its annual "Credo" survey, which asks the same core questions of all employees globally, with only minor adjustments for cultural differences. The survey, which every Johnson & Johnson employee is required to participate in, consists of 130 questions (90 common questions and approximately 40 country-specific questions, as in the case of Japan). An executive at another company described its approach as asking expatriate managers to "carry the strategy and values" while "creating space to understand the local environment." One well-publicized approach was IBM's "values jam," which recently allowed over 319,000 IBM employees across the globe to contribute to the process of defining their company's values.

Approach 5: Empower local organizations

Creating the appropriate "freedom to operate" so that multinationals can compete at the same pace and with the same flexibility as their local peers is a critical element of success. As one senior Indian executive at a global company put it, "We need empowerment—we can then utilize the global pool of contacts, knowledge, and resources we have." Another global conglomerate recently consolidated all its business units in one important emerging market under a single country head, who now has direct profit-and-loss responsibilities. He makes all major decisions, including those related to headcount, pricing, and customization, and all business unit heads in the country report to him rather than to global business unit leaders. This has helped concentrate resources and decision making to better serve local customer needs and ultimately achieve faster growth. An empowered country head can also help build strong relationships with the government and regulators.

Empowerment also means ensuring local leaders have a clearer line of sight to global leaders. In some cases, India and China CEOs now report directly to the global CEO. Other companies are grouping their businesses by growth opportunity rather than geography, putting typically high-growth emerging-market businesses together into one or more units so that their different economics,

innovation needs, and risk management requirements can be recognized. For example GE and IBM have recently created very senior roles to oversee their "growth markets." Structure, of course, is not the only approach. It is equally critical that governance and processes create the right level of involvement and empowerment. In one instance, a leading global telecommunications company established a Latin America operating committee with strong decision making authority on the issues that affect that region's business.

Approach 6: Make your commitment visible and senior

Companies need to maintain their focus in emerging markets: investments, especially strategic investments, should not fall victim to short-term financial concerns. This involves the CEO and top management making a commitment to emerging markets and maintaining it, investing in local leadership and R&D, and building sustainable and healthy communities through corporate social responsibility. Novartis, for example, announced a $500 million investment in Russia in manufacturing and local R&D to demonstrate its commitment toward the market. Similarly, Wal-Mart Stores recently announced a training and education program in collaboration with nongovernmental organizations aimed at teaching critical life skills that will benefit about 60,000 women working in its suppliers' factories in India, Bangladesh, and China. Listing shares on local exchanges, especially in bigger markets, where allowed (as Unilever and Diageo have done), can attract local investors and provide the additional benefit of demonstrating strong commitment. Companies like AstraZeneca stage "analyst days" that focus on emerging markets

to highlight their operations and signal their commitment to those countries.

Local managers must also ensure that global leaders really understand the opportunities—and challenges—of each local market. Cisco's Globalization Center East in Bangalore, which is primarily a leadership development center, also acts as a closely connected extension of corporate headquarters. Holding board meetings in important emerging markets is another tactic some companies are starting to use. Leaders at Starwood Hotels have committed to spending time in the company's most significant markets: they spend a month in China one year and in India the next. Companies can also benefit from appointing directors and creating senior advisory boards with deep, insider knowledge of these markets, which can act as a source of key intelligence and guidance.

Many companies are starting to establish big R&D centers in emerging markets to tap talent and cost advantages and to increase their ability to tailor products for local markets. Indeed, there are now 1,200 multinational R&D centers in China representing a $12.8 billion investment; 4 of IBM's 11 research centers are in emerging markets. One heavy-manufacturing conglomerate tends to establish its global training centers in emerging markets (it recently added one in Thailand). That helps the company to both develop skills among local workers and signal a long-term commitment.

It is also important to contribute to the local community by fulfilling corporate social responsibility commitments. In China, for example, Siemens has worked closely with regional governments on energy efficiency, donated to healthcare programs, and provided advanced medical equipment to rural areas.

Finally, Western multinationals can also learn from Asian companies like LG, which is now a top three player in most consumer durables categories in India. The company's initial entry was not particularly smooth, and it included some failed joint ventures. But it remained committed, maintained its investment, supported the local organization, and over time attained great success.

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There are many exciting opportunities for Western multinationals as they mobilize their global capabilities, people, and technology to expand in emerging markets. Many of these companies have already made important progress. But it will not be a rising tide for all; the leaders will be the ones to make significant changes to their ambitions, capabilities, and talent management—and sustain them—to capture the full potential.

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An interview with Nick Blazquez, President, Africa, Diageo

Diageo, the international drinks company, first shipped Guinness to Sierra Leone in 1827. It built its first brewery outside the British Isles in Nigeria in 1963. And in the latest fiscal year, 14 percent of Diageo's global business—and 40 percent of its total growth—came from Africa. In this interview, McKinsey's Martin Dewhurst talked with Nick Blazquez about the company's growth strategies, the role of partnerships in its success, and how it attracts and develops people through a reliance on core values.

Martin Dewhurst

McKinsey: *Tell us a little about the scope of your business in Africa and how you make decisions about growth.*

Nick Blazquez: Within Africa we operate in 40 different countries. We tend to prioritize the largest profit pools; the top 10 markets account for about 80 percent of the profit pool. If you split those into beer and into spirits you've got 20 beverage alcohol categories. Five years ago, we were in 6 of those beer or spirits profit pools; now we're in 16. We've expanded our participation within the beverage alcohol category by building beer and spirits, and we've expanded geographically through acquisition, greenfield, or joint ventures. We plan to double our business in the next four years, and I suspect that most of our growth will be organic.

We are, however, open to all routes forward. In emerging markets, I think finding the right partners and flexing your go-to-market model is important. For example, we had a very well-established and scaled spirits business in South Africa, but no direct access to their beer market, which accounts for about 40 percent of the beer profit pool across Africa. We could have built one of our own brands. But it's quite difficult to go in against an incumbent like SAB in their home market without scale. So it made sense for us to form a joint venture with Heineken and Namibia Breweries to drive scale benefits of beer and spirits together. It was different in Ethiopia. People knew we were bidding for the Meta Abo Brewery there, and a number of them asked whether they could partner with us. We couldn't see what added value a partner would bring at that stage, so it made sense from a value creation perspective that Diageo acquire that asset 100 percent.

McKinsey: *"Africa" can be a scary word to many investors. How do you think about the relative risk of Africa versus other emerging markets?*

Nick Blazquez: I think "brand Africa" is somewhat tarnished. By and large, if you talk about Africa, people immediately think about disease, poverty, corruption, war, and famine. That stuff does exist, by the way, but it exists all over the world. However, elsewhere in the world, people also talk about the opportunities as well. There are plenty of opportunities in Africa that are not talked about as much. We encourage people inside and outside of Diageo to take a look at the complete picture. This is why, eight years ago, Diageo launched the Africa Business Reporting Awards, which sought to celebrate journalism that paints a more accurate picture of the business environment in Africa. The continent is transforming—you need only look at the GDP growth rates, where Africa has 7 of the top 10 fastest-growing countries.

Five or six years ago, Africa was managed somewhat separate from the rest of Diageo. As the African business has grown, people have been able to rely on it more and have seen the consistency of growth from Africa. There has been greater interest in our marketing programs, our innovative corporate social responsibility (CSR) programs, our agricultural programs,

"Our success as 21st century company is dependent on the health and prosperity of the communities in which we operate. In Africa, we see firsthand how socioeconomic development through inclusive business models and innovative partnerships can enhance reputation, attract talent and mitigate risk. We also see how it can help create an environment in which entrepreneurialism flourishes."
– Nick Blazquez

and our sales development programs. We implemented SAP in a number of markets; it was recognized as the best implementation anywhere in Diageo. Many people in Diageo today come to Africa and get promoted out of it. That sends a really good message internally to the organization. It's really come of age.

When we look at Africa, we look at it from a point of view of having a long history in the continent, having seen the ups and downs; we're prepared to take a longer-term view and ride the turbulence. We know how to navigate this volatility. We know that we can do this while operating to the highest standards of international corporate governance. Sometimes things might take a little bit longer, and it might be a bit more costly in terms of the infrastructure, but with patience and perseverance you can navigate your way through and the returns are good. In fact, the margins we earn in Africa compare very favorably with those in the rest of the world.

Another risk is foreign exchange volatility. One of the ways of mitigating this is to source more locally. We buy a lot of grain with which to brew beer, so as our business grows, the more we source locally, the better. We source about 65 percent of all our grain locally and buy from more than 100,000 farmers now. Some people think we do this just because it's a good thing to do for the local society. Of course it does have those benefits, but we also do it because it makes sound good business sense. It is a natural hedge to fluctuating foreign exchange rates.

And something that's particularly important in all emerging markets is having a really good local network, so we are well connected into the community in which we operate, having insights and a broad network of people we can use to understand immediately what's going on and take actions quickly.

McKinsey: *These relationships can also offer new ways to think about innovation.*

Nick Blazquez: Yes. In Kenya, for example, we were asking how we could accelerate growth. We had built a strong business in what is known as the formal sector. With a large informal sector in Kenya, we realized that we needed to redefine the pond that we were in. And if you redefine the pond you're in, you pick up all sorts of opportunities.

In Kenya it was estimated that about 50 percent of all alcohol consumed was in the illicit sector. This has a huge impact on health, as illicit drinks are often manufactured using substances that are seriously damaging. We decided that we could engineer a product at a lower cost using local grains. In turn, the government waived duty so we were able to sell a 30-centiliter mug of this new beer for 20 shillings—about the same amount as people were paying for the illicit brews. So now, the consumer could go to a dedicated bar which we have invested in to make a pleasant consumer environment, trade up by drinking a mug with a brand name on it, and drink something that is not injurious to health for the same price as illicit alcohol. The government saw returns because we were employing more people, including more farmers to grow barley, and we were paying more corporation tax. We grew our business—it's our biggest brand by volume and it has generated $250 million of revenue over four years. So it's good for the consumer, good for the government, and good business for us.

McKinsey: *You've mentioned good corporate governance. How does Diageo think about values more broadly in Africa?*

Nick Blazquez

Vital statistics

51 years old

Married, three children

Education

PhD,
University of Bristol

Bachelor of Science,
University of Aberdeen

Career highlights

Diageo Plc
(1989–present)

President, Africa
(2004–present)

Managing director, Asia Key Markets (2001–04)

Various managerial positions (United Distillers)

Chairman of Seychelles Breweries Ltd.

Member of the boards of Guinness Nigeria Plc, East African Breweries Ltd.

Fast facts

Former chairman and current board member of Private Investors for Africa (pan-regional business coalition) and board member of Mercy Corps (global non-governmental organization that aims to assist transitional societies)

Nick Blazquez: The question is not whether you can make a fast buck, but rather whether what you're doing will create value in the long term. Playing a positive part in the communities in which we operate has a number of benefits. Part of this is consistently sticking to our processes and not compromising on any standards. I think that's why we've been around the continent for so long. Sometimes it's difficult to get our products through the ports, for example. We will not pay facilitation payments; but we've now built a reputation in many of the countries where people know us for not paying these, so they don't bother coming to us anymore. One's reputation therefore becomes important.

Let's take Ethiopia as an example. The government was aware of the agricultural work we had done in Uganda, Kenya, Ghana, and Cameroon. The Ethiopian prime minister was keen to transform the agricultural sector, stimulate local production, and rely less on imports. The brewery we were looking to buy imported all of its grain. So the prime minister brought forward the idea of a big, well-run corporate providing regular demand for local grain; that benefits us, it benefits the government, and it benefits the local economy. In Cameroon, we created the Coalition Against Corruption to act as a catalyst in promoting corporate integrity. We got a number of businesses, the police authorities, and the government to commit to it. That idea has been used elsewhere, and it makes us the kind of company people want to have around.

It helps with talent too. People hear about Diageo and want to be associated with a

company that has a good reputation and high standards—it is a reflection of the way they want to conduct their lives. When I ask graduates why they joined Diageo instead of another company, half of them spontaneously mention our CSR initiatives and say they wanted to join a company they could connect with, that had a motivating purpose. There's a real spirit of community in Africa and a desire to give back amongst many employees. Employees are increasingly seeking companies they can relate to. And that is not just in Africa but around the world too.

McKinsey: Retaining talent is a major challenge for companies in most emerging markets. How does Diageo address it?

Nick Blazquez: Africa is no different from anywhere else, other than that there are loads of opportunities for employees to get experiences in many places. You've got to help people develop their careers and get reward and retention mechanisms in place. If you look at our projected growth, we'll need a lot of people in Africa. Three years ago, we started our own pan-Africa graduate recruitment program, through which we recruit 100 African graduates a year. We develop them in Africa, the UK, and elsewhere around the world. In addition, we have our "growing leaders scheme," a mid-career program to take people with potential and accelerate their progress. As a result of those conscious actions, we've become far less dependent on expatriates. Something like 60 percent of our general managers are now Africans, as opposed to about 20 percent a few years ago.

McKinsey: *And what about the skills that senior leaders need?*

Nick Blazquez: A general manager leading a business in an emerging market needs a different skill set from a general manager in a developed market. You have fewer data points, there's less transparency, and they need to engage with a broader set of stakeholders. You're also dealing with taxation issues. Another difference is that Diageo has a huge production footprint in Africa, with one or two or three breweries per market. Compare that with our spirits business, where we have two or three manufacturing sites that serve 180 markets. I fully expect a general manager in an African country to be engaging with finance ministers and prime ministers. When I was a general manager in the UK 20 years ago, I needed to be a good commercial guy who could lead people. I engaged occasionally with government, but it was really not very much.

Looking ahead to the leaders we'll need, I used to think that to optimize the impact, a general manager should work in a developed market for a period of time, because that's where you see well-developed competencies. I'm just not seeing that now. If I think about marketing competencies, for example, some of Diageo's most innovative marketing solutions are in Africa—we are way ahead of where we are elsewhere. So I just don't think that there's a need anymore for somebody to have worked in a developed market to be a really good manager.

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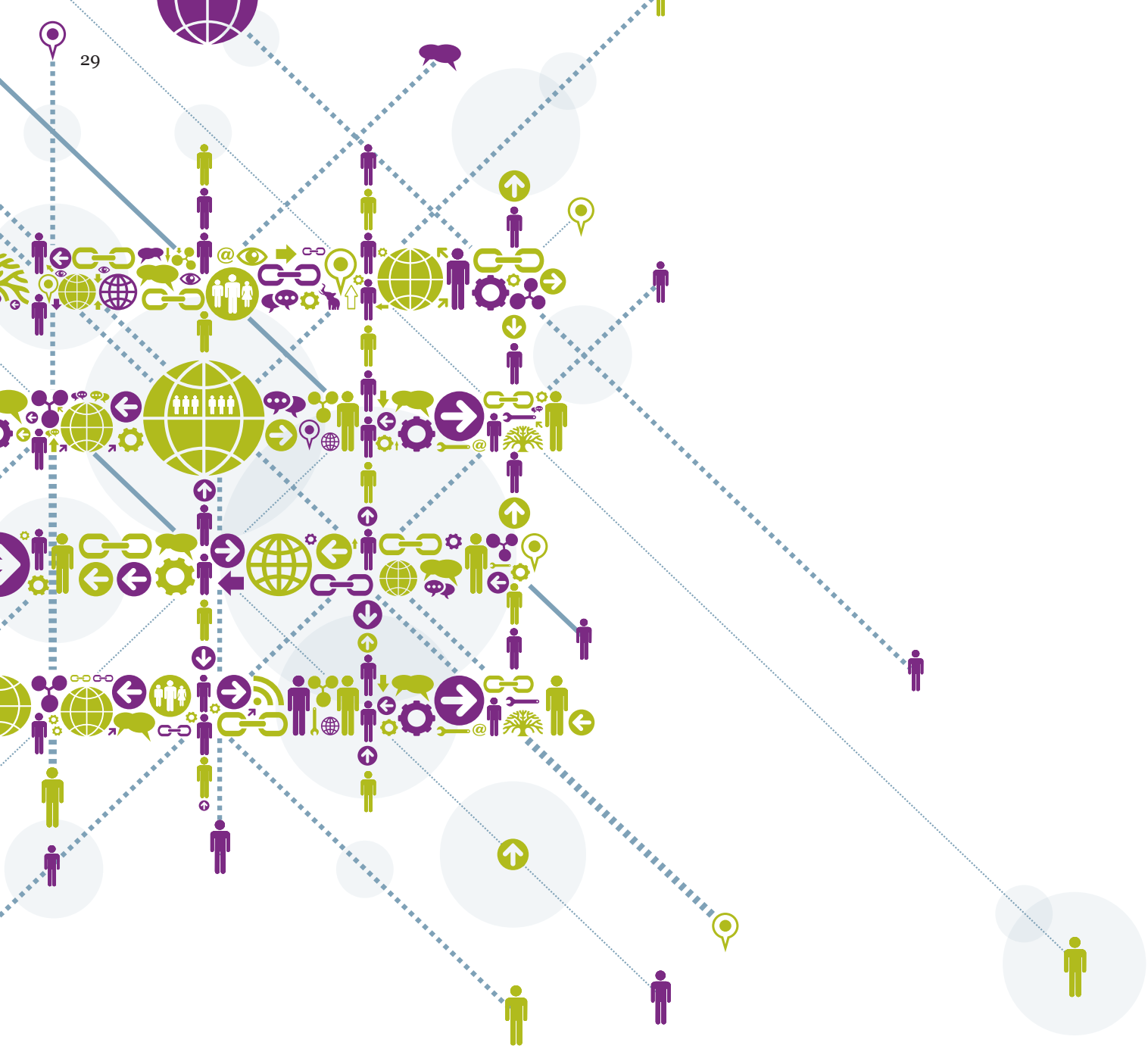


Structuring your organization to meet global aspirations

The matrix structure is here to stay, but its complexity can be minimized, and companies can get more value from it

Suzanne Heywood
Roni Katz

The way a company organizes itself—how it allocates responsibilities, how it organizes support services, and how it groups products, brands, or services—can have a substantial impact on its effectiveness. Global companies, however, find structure difficult: in our recent survey of over 300 senior executives,[1] only 44 percent agreed that their organizational structure created clear accountabilities.

Global companies find structure difficult because there are no simple solutions—most global structural options create challenges as well as benefits. For example, many companies have focused for years on standardizing structures; easily understood and navigated structures simplify costs and make sharing of risk and information easier and therefore support many of the benefits of being global. However, global companies are now often finding that they are reaching the limits of this benefit—their standardization has become so thorough that they find it hard to achieve the flexibility needed to respond to local market requirements. Many are therefore starting to revisit the trade-off between standardization and local flexibility.

Another structural challenge faced by global companies is creating the right balance between minimizing complexity (making it easy to get things done and get decisions made) and capturing knowledge and innovation. It is often hard to get things done in a global organization due to its size and the multiple time zones that it encompasses. In addition, the inevitable duplication of some activities across businesses, regions, and functions creates uncertainty about where to go to get a task completed or a question answered. One way to solve this is to create self-contained, vertically integrated, global businesses within which decisions can be made quickly and complexity is minimized. However, such silos make it much harder to find, share, and benefit from knowledge across businesses. In our survey, for example, only 46 percent of senior executives felt that ideas and knowledge were freely shared across divisions, functions, and geographies within their companies.

For most global organizations, these trade-offs are greatly influenced by their archetype. (See "Next-generation global organizations" on page 1 for a description of these.) For example, the right answer to the trade-off between complexity and knowledge sharing for a *customizer* company, which tailors its products and services to each market and which therefore needs to create a lot of local innovation wherever it operates, is likely to be very different than it is for a *global offerer*, which offers standardized products.

Other issues may also affect these trade-offs. For example, the correct answer to the trade-off between standardization and local flexibility may vary across markets even for the same business; there may be a need for greater delegation in dynamic high-growth markets, where decisions need to be taken more quickly, than in established developed markets. Likewise, the way in which a company has grown can also be important. If, for example, a company has grown organically, it may have a high degree of structural standardization; its biggest challenge may be deciding how to flex the model to allow more local tailoring. If a company has grown inorganically, it may have the opposite problem: country or business silos may operate relatively independently and be difficult to standardize globally.

Given the complexity of these issues, it is not surprising that many global companies end up creating highly complex structures that incorporate multiple businesses within a matrix of business, functional, and geographic structures. As one executive told us, "The overall matrix between

1 McKinsey Globalization Survey of more than 300 executives, November 2011

geography, service line, and global function in our company is, at best, cumbersome: this is no way to out perform local competition in fast-moving markets."

Emerging thinking on new structures

Each company will, of course, face a somewhat different mix of the challenges described above, depending on their archetype, their strategy, and their history. Nevertheless, we see a number of approaches emerging that may in time help global companies find the right structure for their situation.

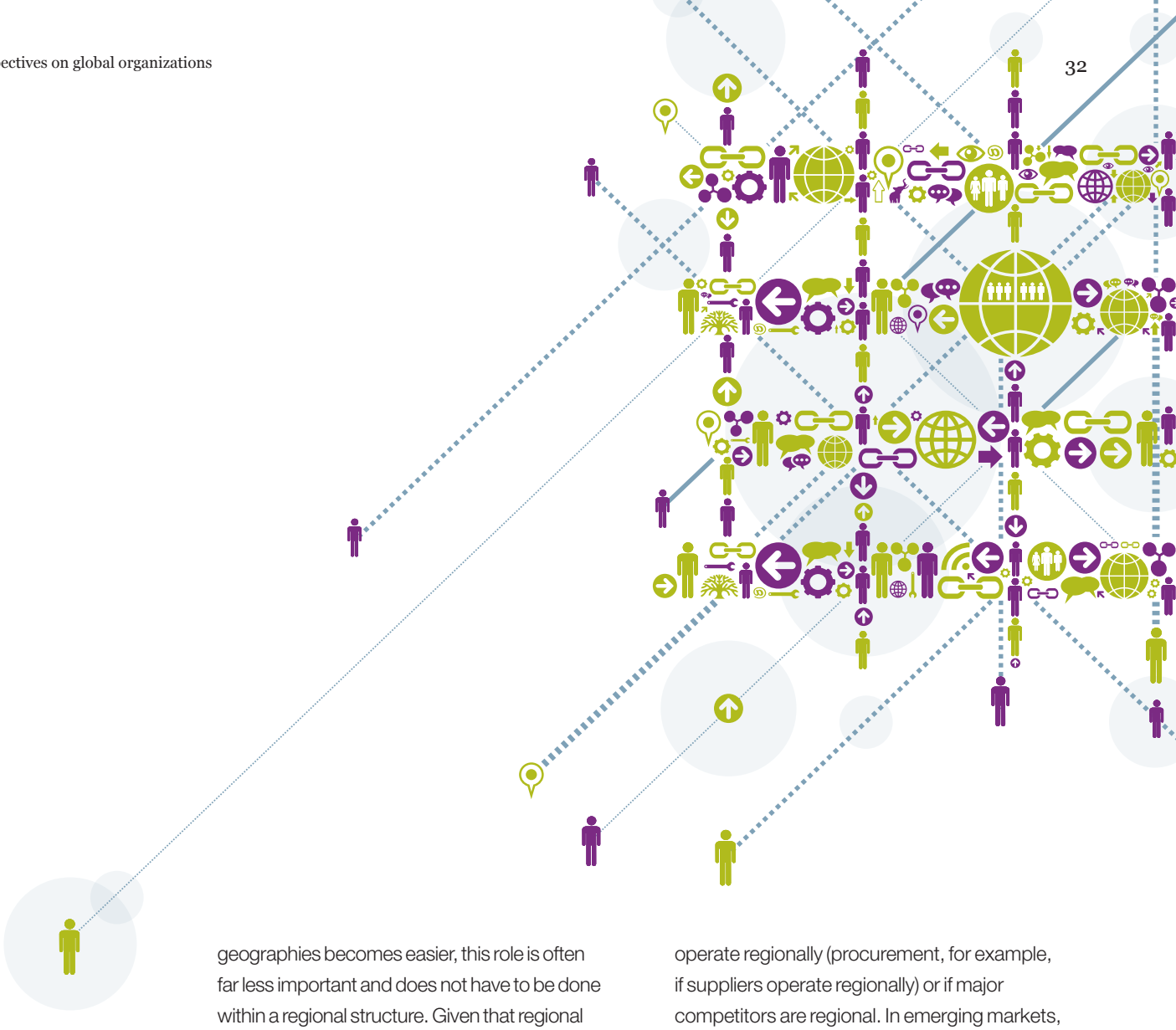
Be clear about what needs to be global. Globalizing businesses, products, or functions can make it easier to capture strategic and cost benefits, and to share knowledge and skills to drive innovation. This could mean moving from a geographic structure—say, three regional product development centers—to a single global structure that groups all related activities together. For example, a global publishing company recently created "global verticals" of people who work on similar publications in every country. This made it easier to exchange ideas on those types of publications and increased innovation. And that added more value than the previous geographic structure, which had only made it easy for people working on different kinds of publications in the same country to share information.

Focus country organizations on what needs to be local. Even as they determine what needs to be global, companies need to be just as deliberate in deciding what should be local. Globalization can destroy value if the activities globalized in fact need to be locally tailored. The publishing company reorganized with that awareness. Although many activities were globalized, country managers were retained to manage sales and marketing operations, which require much more local customization; some back-office services (such as local finance and HR support) were also left under local management and they managed the interface with global shared services.

The right answer here will be affected by the organization's archetype. But this is not the only consideration; other issues can be just as important. In industries where local risks can threaten an entire organization—such as oil and gas, metals and mining, and even audit—global transparency on risk is critical and therefore risk processes need to be more globalized.

The expected growth rate of a market can also be important. Markets that are growing rapidly often require more local decision making on issues needed to compete, such as product innovation, marketing, and partnering. More activities will likely need to be localized when a company first enters a market and is less familiar with it (this may particularly be the case in emerging markets, where building relationships with local stakeholders such as regulators and governments is often critical). As the local business grows, some of this decision making may be taken back above the country level to the business division or corporate center. Companies need to think through all these issues systematically in deciding what should be local, and be aware of both the benefits and constraints of localizing decision making as well as the possibility that the right answer may vary by business as well as by country.

Be clear on the logic for regional structures. A traditional rationale for regional structures was the need for a "span breaker" within a global organization, to gather information from local organizations and pass it to the corporate center. As communication and travel across



geographies becomes easier, this role is often far less important and does not have to be done within a regional structure. Given that regional structures are often expensive—they quickly start to duplicate corporate functions such as finance, HR, and marketing which also exist at both local and global levels—we are starting to see a trend toward either removing or radically reducing the size of regional offices. In some cases, companies have reduced these offices to small teams of 10 or fewer, which focus on people (rather than business) performance management, coaching, and business intelligence activities such as spotting regional and country risks, competitive risks, and opportunities. These new regional structures typically do not spend time aggregating financial or other data at a regional level and then reaggregating it at a global level.

There are, of course, exceptions to this trend; in organizations where the logic for regional structures is clear, the personnel should be retained. For example, some companies are retaining them if a corporate function tends to operate regionally (procurement, for example, if suppliers operate regionally) or if major competitors are regional. In emerging markets, regional structures can be important if the company seeks to build capabilities that are specific to operating in faster-moving markets (e.g., new innovation approaches). But even in these cases, companies will benefit from making sure that these structures are not duplicating other activities that add more value by being done globally or locally.

Companies should also consider whether the underlying premise of many regional structures—the traditional logic of managing countries in groups based on their proximity—is still valid. As barriers to travel and communication fall, it may make more sense to group companies according to their strategic needs and rate of growth if these are more important in determining the support needed from a regional office. However, when doing this, it is important to assess whether the new structures that are being created contain roles that are sustainable over time.

Create small physical corporate centers that focus on external reporting, serving the board, and holding the brand and values of the organization. Other elements traditionally housed in the corporate center (such as strategy, HR, procurement, and supply chain) can be retained in the corporate center (or global shared services), but in some cases, they can be relocated to the physical region where they add the most value. (See "Reinventing the global corporate center" on page 41 for a more detailed discussion.)

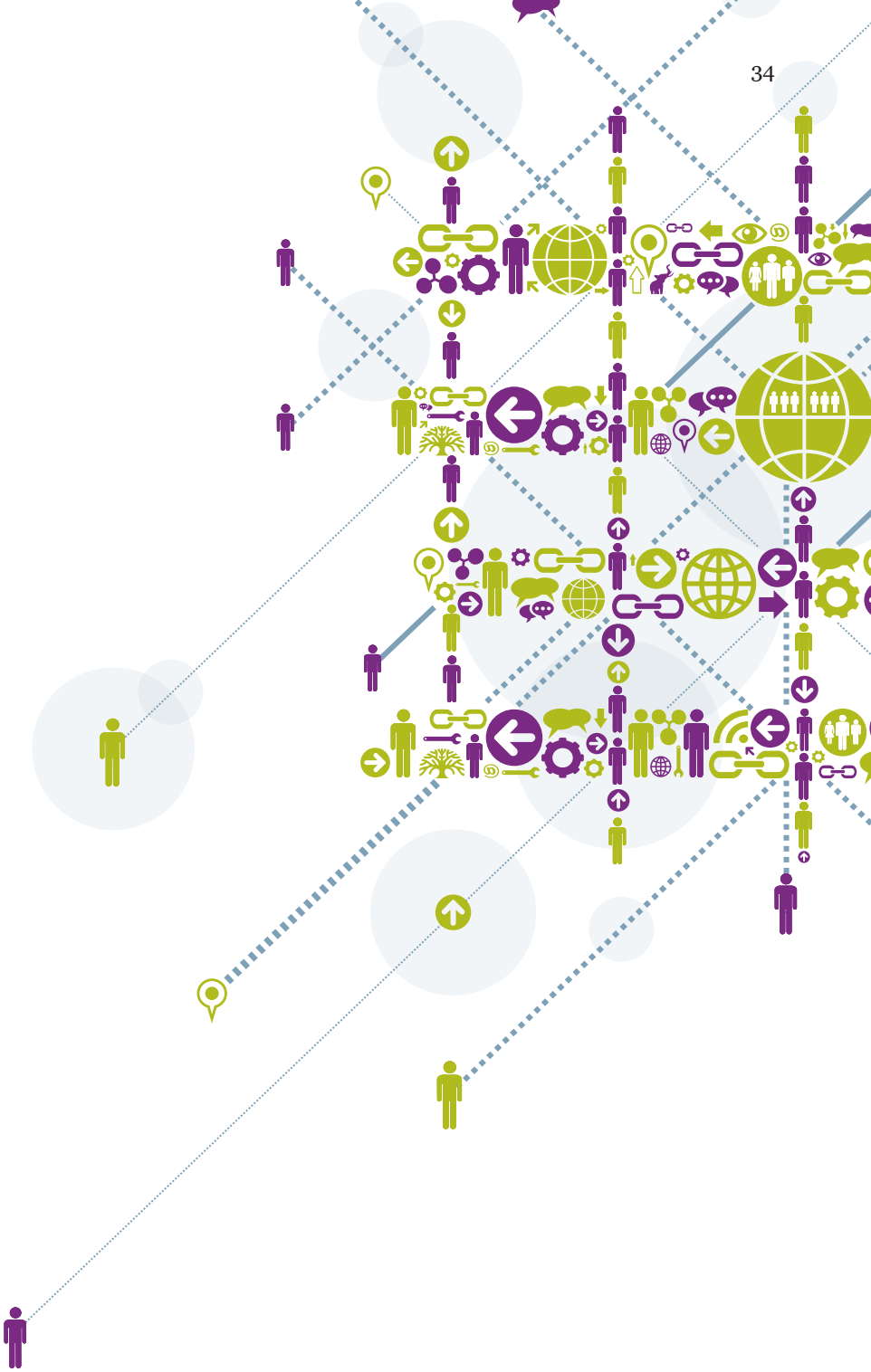
New ways to manage complexity. Inevitably, organizing a global company will require a matrix, but the complexity this creates can be minimized. We know from our research on organizational complexity[2] that getting accountabilities right—making it clear who is responsible for what and removing duplications in responsibility—is one of the major ways in which companies can make it easier to get things done. So, for example, a company could create a network of marketing experts to share knowledge and skills across the enterprise on issues such as new communications approaches, while leaving the responsibility for decision making on these issues to the local management. With minimal duplication, and managers who are trained and given incentives to be highly collaborative, this approach will add value from shared knowledge without reducing local flexibility. Standardizing structures—for example, in this case, making marketing roles relatively similar across businesses—makes it easier to create these links. Companies are also now reducing complexity by decreasing the number of cells within the matrix structure rather than assuming that every intersection within the matrix requires separate management: Unilever recently reported that it had reduced the number of its managed organizational units from more than 200 to 32.

Create end-to-end global business services with clear customer interfaces. Most global companies have long since brought widely used services—IT, HR, purchasing, financial reporting, and the like—together across their businesses and regions. We are now starting to see the next step in the evolution of these services, one that can increase business effectiveness and reduce cost. A few companies, such as P&G, DHL, and Unilever, are integrating back-office services from several functions so that a comprehensive package of services is provided for discrete processes—for example, integrating HR and financial data to support a single reporting process. This approach can remove some hard-to-spot duplication between functional tasks and create services that are better suited for users' needs. It also means that a senior manager can have a single point of contact for global business services, rather than separate links into each shared service function. And providing all the services needed for a given process can also help firms capture greater economies of scale and create more attractive roles for services leaders.

• • •

We believe that the rebalancing of many global companies toward emerging markets combined with the accelerating pace of communication technologies opens up a whole new set of structural options. By being thoughtful about the global-local balance within their companies, the role of regions, the corporate center and business services, companies can create organizations that capture global benefits while remaining locally agile.

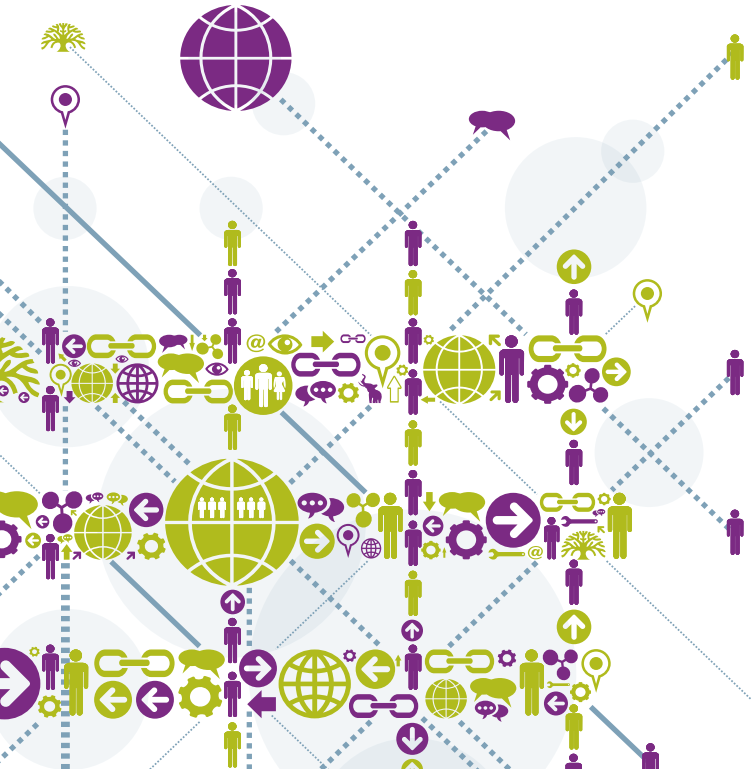
2 Suzanne Heywood, Jessica Spungin, and David Turnbull, "Cracking the complexity code," *McKinsey Quarterly*, May 2007.



Suzanne Heywood is a principal in McKinsey's London office, where **Roni Katz** is an associate principal.

An interview with Michael Cannon-Brookes, Vice President, Business Development, China and India, IBM Corporation

In 2009, emerging markets made up 17 percent of IBM's revenues, rising to 22 percent in 2011. Currently the company is poised to achieve 30 percent by 2015. McKiney's Martin Dewhurst talked with Michael Cannon-Brookes, IBM's vice president of global strategy for growth markets. The conversation focused on the cultural changes that are critical to successful growth in emerging markets.



Martin Dewhurst

McKinsey: *IBM has moved from aggregating business units as part of a global strategy to possessing a fully global strategic perspective. What kicked off that change?*

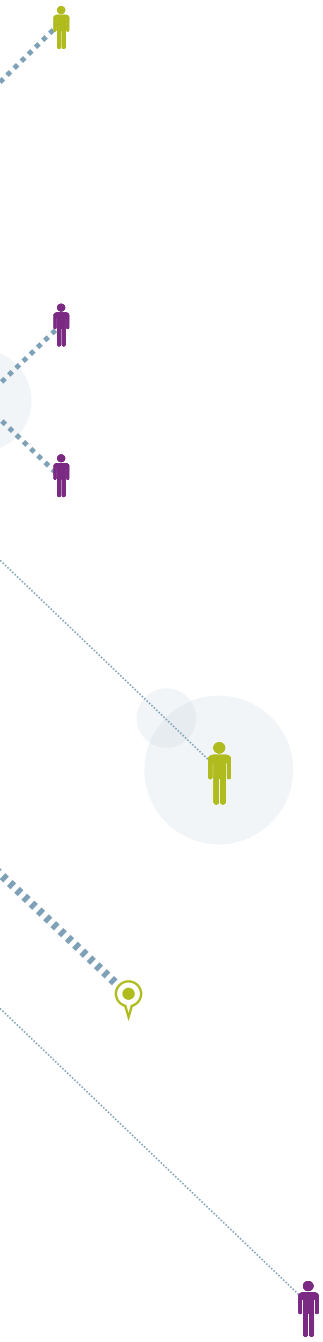
Michael Cannon-Brookes: Just after the millennium, we started thinking about IBM's global evolution, based on the assumption that it was no longer viable to have every function of the company in every major country. This had been our model until that point, and one that still is for many multinationals. We first identified 11 shared services with commonalities including supply chain, legal, communications, marketing, sales management, HR, and finance. These had been scattered across all of the product brands, and we appointed one global owner to run each consolidated function across all the businesses. We took a disciplined approach, assessing for each function where we could bring greater value to the business. Assessments were then made about which activities could be optimized, eliminated, and, based on skills and cost models, which functions possessed the viability to deliver the service. This provided the basis for IBM's globally integrated enterprise model.

In its simplest form, a globally integrated enterprise (GIE) is a 180-degree change from the traditional multinational. Instead of taking people to where the work is, you take work to where the people are. This means moving from the traditional vertical organization, where command and control are the driving forces, to a horizontal model, where the driving forces are coordination and communication. The structure of the work becomes more flat and less hierarchical. We began looking at the world very differently, seeking out pools of high value, competitively priced, talent and skills that could be used globally to serve both our internal and client needs. A great internal example comes from Japan, where corporate culture is often considered very insular. Yet under our GIE model, we now have the HR for IBM Japan done in Manila, accounts receivable done in Shanghai, the accounting done in Kuala Lumpur, procurement in Shenzhen, and the customer service help desk is in Brisbane. *That* is true global integration, and it is also optimal for our Japan business.

When we started down the GIE path, we knew that this would be a 10- to 15-year journey as, fundamentally, this is a cultural change. Changing organization charts can take a few mouse clicks. Changing business processes can take months. However, changing a culture and the way employees adapt to new ways of working takes years. Laying these foundations has recalibrated the company for success and growth in these emerging markets.

McKinsey: *How did this change your approach in emerging markets?*

Michael Cannon-Brookes: Over the past few years, massive investments have been made by emerging market economies to build out their national infrastructure. Millions of citizens are entering the middle class, increasing their purchasing power, doing banking transactions, using mobile phones, consuming energy, taking mass transportation, and demanding access to healthcare services. The market opportunities and the IT solutions required to address them are staggering. It was in this context, not long after we had embarked on our globally integrated journey, that it became clear that emerging markets were very different from mature markets. The reality of doing business in emerging markets requires a deep understanding of the business and industry drivers. To succeed, we needed to adopt a radically different way of thinking, which was very hard to do from Westchester County, New York, where IBM is headquartered.



Traditionally, the multinational business model began with colonial roots. Today for practical reasons of proximity or skills transfer, multinationals tend to link developing markets to developed ones. This is why Latin America often reports to the US, South Africa reports to the UK, Eastern Europe reports to Western Europe, and so on. However, this model actually limits growth because the mature markets snap up the best resources and highest management attention. Developing markets get short shrift because they represent a small percentage of the overall business of the region. And because they receive neither resources nor attention, they fail to live up to expectations.

Building closer relationships with our clients in these markets is key to understanding local market industry drivers and business challenges so that we can create solutions that address their business needs. In 2008, IBM made the decision to establish a growth markets unit to run our emerging-market business globally out of Shanghai. We now have a leader and senior vice president for the emerging-market group who are based there with global responsibilities. This has fundamentally changed the way we do business across many time zones.

McKinsey: *IBM's Values Jam is a well-known technology story. From an emerging-market perspective, how did you see it help build shared values?*

Michael Cannon-Brookes: In 2003, we launched IBM's Values Jam, which, at that time was an unprecedented 72-hour company-wide conversation with employees from all over the world. The premise was simple. In an effort to stay true to IBM's core beliefs, we asked for global feedback to refresh the IBM set of values that would reflect the company's position to employees, clients, and the world.

The key themes that emerged were then shared online with IBMers around the world, prompting feedback and comments as well as pride of ownership. Every employee had the opportunity to participate utilizing IBM technologies as part of this global exercise.

Three core IBM values emerged as a result:

1. Dedication to every client's success
2. Innovation that matters—for our company and for the world
3. Trust and personal responsibility in all relationships.

McKinsey: *How did IBM manage this global cultural transformation?*

Michael Cannon-Brookes: There is no one silver bullet that addresses a complex multi-level transformation of a global corporation—essentially it's an exercise in planning, time, and patience. Cultural transformation begins at the top. It requires a CEO who is passionate and drives through to achieving the target. As the saying goes, it's not what you say, but what you do, and every large transformation needs milestones as proof of this change.

Part of the cultural change comes from our awareness as individuals that we are now part of a larger global business environment, which has implications on the working life of an employee. Even small things, like time zone consideration, count. For example, many people in New York like to have global calls on a Friday morning so they can get it all clear before the weekend. However, that's Friday evening in Asia and therefore impacts colleagues' lives on the other side of the world.

Moving people around the world to gain a global perspective and experience is a key part of the process. This includes career development

Michael Cannon-Brookes

Vital statistics

64 years old

Australian and UK citizenship

Lives with his wife in Shanghai, plus three children and seven grandchildren in Sydney

Education

Graduated with Honors in Law, University of Cambridge

Career highlights

IBM
(1997–present)

Vice President, Global Strategy, IBM Growth Markets (2008–present)

Vice President, Strategy & Business Development, IBM China and India (2005–07)

Vice President, Global Strategy, Marketing, and Operations, IBM Business Consulting Services (2002–05)

General Manager, IBM Industry Value Project (2001–02)

General Manager, IBM Global Banking Industry (2000–01)

Vice President, Financial Services, IBM Asia-Pacific (1997–99)

Freehills
(1992–94)

Managing Director of leading Australian law firm

Citibank
(1969–1991)

Leadership roles across Asia, Australia, the US, and Europe

Fast facts

27 years of growth markets experience

assignments from mature to emerging markets, from emerging to mature markets, and increasingly between emerging markets. In this way, we try to develop global IBMers. Teams from across the world often work together on projects, senior leaders address their teams via webcasts, global programs are delivered via intranet portals, and teams network via mobile smartphones and tablets.

Another part of this cultural shift is the willingness to develop products and solutions designed specifically *for* emerging markets *in* emerging markets, and then "re-innovate" them back into major markets to add vitality there. The emerging markets provide large pools of skills, talent, and innovation. That's why our largest research, hardware, and software development labs are outside the US in locations like India, China, Latin America, and Eastern Europe.

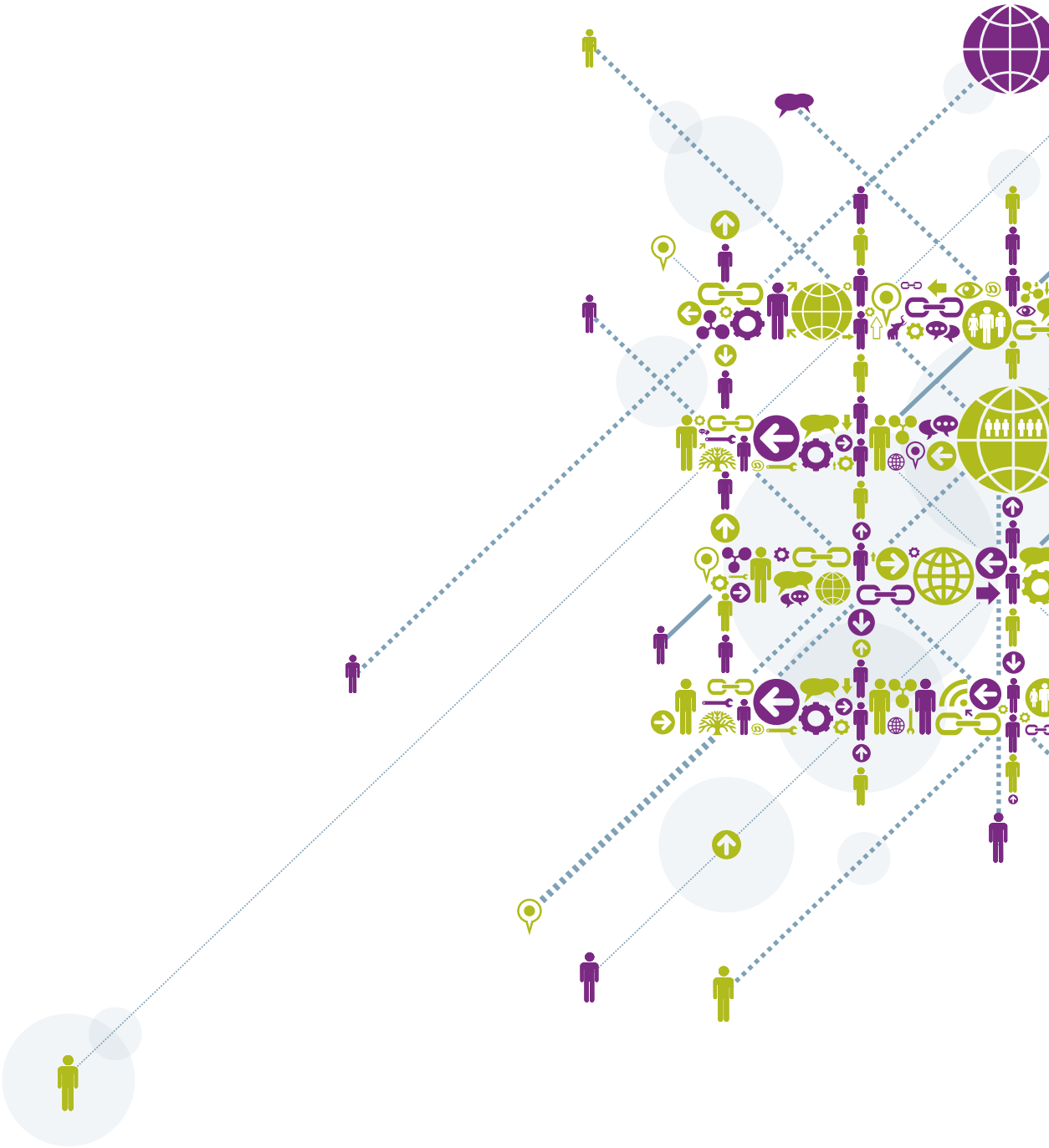
McKinsey: *How do you think about managing people in this new culture?*

Michael Cannon-Brookes: One fundamental lesson I've observed is that people underestimate the cultural change that an executive has to go through when they move from a mature market to an emerging market. They usually come from an

environment where the business opportunities are constrained and productivity and cost cutting are a constant focus. Suddenly they find themselves in a climate and culture of growth in Shanghai or São Paulo or Dubai, in an environment where there are more business opportunities than there are resources to match. Adapting to this can take time. These executives need to have a certain passion for such markets, with unpredictable working hours across multiple time zones.

The most important challenge in these markets is the recruitment, development, and retention of local talent, which differs significantly from country to country. At a foundational level, a well-designed campus recruitment program, an employer value proposition that resonates and differentiates you in the market concerned, and a well-recognized and respected brand name in the marketplace are essential. In many of these markets where there is a rapidly growing organization, you are faced with the situation where recent recruits suddenly become first-line managers and then second-line managers. This requires sophisticated training programs to develop management, sales, and technical skills. As a result, leadership training and career development assignments in other markets are a vital ingredient in developing leadership and skills for the 21st century.

Martin Dewhurst is a director in McKinsey's London office.



Reinventing the global corporate center

Headquarters still have a key role to play but must focus more tightly on the right activities

Pascal Baumgarten
Suzanne Heywood

A recent McKinsey Quarterly survey[1] of thousands of international executives gave what amounted to a vote of no confidence in the corporate center of many of today's global organizations. Only half of the executives surveyed said they thought their company's corporate center added value. And only 42 percent thought the corporate center was appropriately sized and staffed to perform its mandate; many local managers, in particular, perceived central functions as grossly overstaffed.

The corporate centers of today's global companies often "grew up" simply by expanding the functions needed for operations in a single country to an international scope. But in a world where the economic center of gravity is shifting and the pace of change is ever faster, this kind of corporate center is now getting in the way.

We have identified three main issues facing corporate centers. First, many of the center's tasks and duties replicate what the business units do; only 45 percent of respondents to our survey said their organizations clearly differentiated responsibilities between the two levels. Second, many executives were not convinced that centralized activities really created value because economies of scale tend to be erased by additional interface costs and reduced flexibility. Finally, executives do not think the center is adept at encouraging communication and collaboration among different parts of the organization. The center's inability to make connections among businesses that are often managed in silos means that decision making stays slow, the organization's global scope is not fully exploited, and people do not consistently have access to the right knowledge and skills.

Our work suggests that leaders seeking to reinvent their corporate center should take three steps: redefine the mandates of headquarters, centers of excellence, and shared services; reassess where headquarters ought to be; and radically redefine the staffing of headquarters, shrinking the numbers and improving the skills.

Step 1: Redefine the mandates of headquarters, centers of excellence, and shared services

Corporate centers often become unwieldy because they combine three very different types of activities: headquarters functions, centers of excellence, and shared services. Each creates value differently and should be managed differently.

Headquarters is responsible for upholding the organization's values, developing a corporate strategy, managing the portfolio of businesses in line with those values and the corporate strategy, and managing the performance and health of the company via continuous dialogue with business units on one side and the board on the other.

Centers of excellence hold expertise centrally for the use of all of the businesses; they also form links and encourage collaboration across business units in areas where the company must be distinctive such as product innovation, operational efficiency, or brand management.

Shared services groups supply world-class low-cost "backbone" processes and functions like HR and finance—and increasingly supply chain, legal, communications, marketing, and sales management services—to internal customers.

Over the past decade, leading global companies have started to experiment with separating centers of excellence and shared services from headquarters. However, few senior executives can answer questions such as: Do the business units recognize the value of the centers of excellence? Are the shared services centers

1 McKinsey Quarterly Global Survey, September 2011; garnered responses from more than 4,000 executives representing the full range of regions, industries, company sizes, tenures, and functional specialties.

really demonstrating better value for money than external suppliers? Are their relationships with the business units transparent client-supplier relationships? Without rigorous answers to these kinds of questions, activities located in centers of excellence or shared services may be little more than traditional, mandatory central functions in a new guise.

In core headquarters functions, despite the impression of control given by new information technologies, many global companies have difficulty grasping the diversity of their markets, leading to ineffective communication and inflexibility. A company based in the US, for example, accepted 2 percent growth targets from some of its local managers in India, given that the US market was only growing by 1 percent annually, only to find out later that it was losing share in the rapidly growing Indian market. Similarly a large industrial group suffered because it implemented "one size fits all" processes for planning discussions despite having acquired companies with very different geographic portfolios.

Another issue global headquarters must address is the duplication of tasks performed at global, regional, and country levels, often the result of uncoordinated development of functions in each layer of the organization as the company expanded. Neither bold centralization nor decentralization will address the problem. Fully centralizing HR or finance will not give local operations needed flexibility or be acceptable to region heads. Full decentralization will make the company too unwieldy for the CEO to steer. A better approach is to identify key business decisions, define clear accountability for each, and adjust the organization accordingly. For example, a large global insurer combined the transformation of its global headquarters with a mirroring redesign of its regional headquarters, ensuring clear interfaces and escalation rules in each function (for more thinking on regional structures, see "Structuring your organization to meet global aspirations" on page 29).

Step 2: Rethink where headquarters is

Having clarified the mandates of the corporate center's activities, the second step is to consider the location of these activities.

Two of the activities—shared services and centers of excellence—are relatively simple to relocate wherever they are most effective, taking into account availability of local talent, the relevance of these activities for corporate center local businesses and unit costs. Headquarters functions are tougher: they often remain where they have always been for reasons of history, convenience, or legal constraints. But senior executives should be aware that, whether by choice or default, the location of headquarters sends a signal about company priorities internally and externally. As companies' growth markets move, typically to emerging economies, headquarters could too. Such a shift would bring global leaders closer to future customers and to future managerial talent (see also "How Western multinationals can organize to win in emerging markets" on page 13 for more on why signaling a long-term commitment is important to success).

One option that more and more companies are considering is creating a "virtual headquarters," in which vision setting and coordination activities take place in different locations. This approach allows a company to get the benefits of stronger connections with high-priority markets without the downside of officially closing headquarters in its home country. A lot of companies are still experimenting. Several have chosen a

two-location format, usually with one site in a mature market and the other in an emerging geography: the US and Dubai or the US and India, for example. One company has created three management hubs—one in France, one in Hong Kong, and one in the US—with five of the company's most senior people located in each.

Technology helps, but these arrangements increase pressure on senior managers. One senior executive at a multihubbed company's center in China says he regularly works a "second shift" on conference calls when he should be asleep. As interactions among members of a global, multihubbed top team are often more frequent than traditional interactions between central and local teams, many companies will need to learn to manage this tension better (see an interview with Michael Cannon-Brookes on page 35 to learn how IBM is managing it).

Senior executives also must make sure that these fragments of headquarters do not exacerbate the problem of unclear decision making authorities or lines of accountability in the regions where they are located.

Step 3: Redefine headquarters staffing

Many managers see a correlation between the size of headquarters and its impact on the company. Most do not realize just how small yet powerful a headquarters can be if it combines people with the right knowledge and skills; anchors its actions in a clear set of values, guidelines, and principles that all company employees follow; and communicates adequately to the rest of the company. For instance, a large financial services company turned around its central risk unit, not by increasing its headcount but by adding experienced, recognized managers from the field and by clarifying its groupwide risk policies.

Diversity of experience is as important as intrinsic skills for headquarters roles. When building up headquarters' functions, managers should try to reflect the degree of internationalization of the company, staffing employees from diverse backgrounds and offering them an adequate environment to grow. For companies not originally based in the US or the UK, the transition to English as the internal lingua franca is often a turning point in the creation of such a globalized environment.

To cross-pollinate ideas and knowledge, headquarters must attract talent but not retain it; instead, headquarters should be the "beating heart" of the organization, constantly pumping talent to and from the business units. With adequate HR mechanisms in place, it is possible to imagine a headquarters with only the CEO and his or her direct reports as permanent staff with all other executives having fixed-term appointments and then rotating back to a business unit or function.

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Corporate centers, though often derided by the very executives they are meant to serve, play a key role in global organizations. In a more volatile, increasingly dispersed, and faster-changing world, headquarters must be the source of values and strategy and an embodiment of the company brand, while global centers of excellence and shared services can help capture economies of skills and scale across geographies. But this requires focusing on activities that truly add value to the work done in business units, frequently reassessing the business case for centralizing activities in centers of excellence and shared services, and using location choices and staffing models to increase connectedness with the rest of the organization.

Pascal Baumgarten is a principal in McKinsey's Paris office and **Suzanne Heywood** is a principal in McKinsey's London office.

An interview with Jesse Wu, Worldwide Chairman, Johnson & Johnson Group of Consumer Companies

About two-thirds of Johnson & Johnson's consumer business is now outside the US, and the company expects to see continued higher growth rates in markets outside the US than in it over the next several years. McKinsey's Martin Dewhurst and Tracey Griffin spoke with Jesse Wu. The worldwide chairman of the company's consumer group, Jesse Wu was born in Taiwan and spent most of his career in Asia and in this interview talks about how Johnson & Johnson integrates its acquisitions, how companies can ensure that more executives from emerging markets have opportunities to join global leadership teams, and why global companies are better at allocating capital than their local competitors.

Martin Dewhurst
Tracey Griffin

McKinsey: *How does Johnson & Johnson think about which products sell in emerging markets?*

Jesse Wu: Right now, I believe our products are more suitable to the middle-income consumer than the bottom of the pyramid, and we have learned over time that reaching out to middle-income consumers is actually very efficient. You can use an attractive premium brand to expand reach and grow revenue, for example, by offering the product in a smaller size to help consumers reduce out-of-pocket cash. You have to be careful, though, because once these premium brands go mass market, it can start to erode brand equity with higher-income consumers. It's also important to have a brand aimed squarely at the mass market, which is why we acquired Dabao in China; the brand has grown and become important to our business there. In the longer term, a midmarket brand will return more without the risks of expanding an existing prestige brand.

Another pitfall to watch out for is complexity—if you're not careful with complexity, you can create a less profitable business. Emerging markets add volume, but as you expand variants, you're also adding complexity to the supply chain, marketing, and other facets of the business, which can lower margins. Complexity plus lower margins can have unintended consequences if you're not very disciplined in your approach.

One important point to always keep in mind in emerging markets is that, just like consumers everywhere, emerging-market consumers are looking for good value, but they don't want "cheap." As we've expanded our lines to reach more consumers in the middle of the pyramid, we've been careful to keep product quality as high as in our higher-end brands. I always tell our new-product development teams, "Don't touch the juice." It's one thing to offer the same quality product in a smaller size, but what you don't want to do is offer a lower-quality product. That can kill brand equity quickly across the product line.

McKinsey: *How does Johnson & Johnson manage integration?*

Jesse Wu: When we do an acquisition in an emerging market, of a brand or a small to midsize company, we generally keep that operating company separate and decentralized. We try to protect its business model—large volume, fast turn, little advertising, whatever. I always remind people that the reason we bought the brand was because it was successful. The danger for an acquirer is that it's easy to come in and say, "We want better distribution. We want more advertising. We want better margins." But then you end up forcing the operating model in a different direction, which wouldn't be wise. The key is to understand fully the model you've bought into first. Only then, maybe after two or three years, can you start to think about making changes to the model. If you change the operating model too quickly, you also lose out on an important learning experience that may hold lessons for other brands and markets in your portfolio.

As for integration, we first empower the local team to manage the acquired business and follow the established business model. We normally see good results, and then we start thinking about integration. Some people argue it's more expensive upfront, but I think that knowing the intricacies of the company you acquired generates more growth down the road.

We go as far as to ask specifically for approval for visitors to the newly acquired company, particularly people from our internal functions. We do this to protect the acquired business from being overwhelmed by well-intentioned

people who want to come in to see how they might add value but who may not be adding to the immediate business priorities. I continue to believe that one of Johnson & Johnson's strengths is that we always operate better, more nimbly—and we're better informed—than our competitors on the ground because of our decentralized empowerment culture. It's important to empower the local team or region so that we don't have to give all of the instructions from the center.

However, we have also learned as a highly decentralized company that if you're not careful, you can end up with a fragmented approach—for example, different IT systems in different countries. So we've said, "OK, certain things are not going to be decentralized anymore," like strategy for the brands. We're also trying to build consensus on growth drivers for the future and determine which geographies to focus on, so that the role of the brand and role of the market become clear. You'd be surprised by how something so basic is not always as easy as it sounds.

McKinsey: *As a leader of a global company who spent most of his career in emerging markets, how do you think companies should meet the challenge of having enough leaders with local knowledge?*

Jesse Wu: The US is a very important market, but the US is not *the* market. If all the global positions are based there, over time you will be overly influenced by the US. Given that growth is going to come from Latin America and Asia, I advocate putting global positions in the growth markets or growth regions to make it easier for us to hear the voice of our future customers. For example, we've moved key global franchise and R&D heads to emerging markets. This is probably a "test and learn" model, but I think it will generate a higher level of growth and help the rest of the world understand what the challenges are.

Leaders' mindsets are very different. When you're running an emerging market, for example, you always operate under an austerity model. When you've been operating in emerging markets and come to the US, you become aware of the little things, like how much people use color printers for internal documents. All these little things add up. Everybody's happy with emerging-market growth, but there are implications for technology, investment, talent, and so on. Emerging-market growth necessitates a lot of changes worldwide, not only in emerging markets. Our job is to prepare for that, so that a couple of years from now we will have made the mindset changes to accommodate where our growth is.

Talent is an issue that anyone with a global business needs to be concerned about. On the one hand, US talent over time seems to have become less mobile than executives from Europe, Asia, or Latin America. We need this to change. On the other hand, if you look at talent in other global markets, particularly in Latin America and Asia, many leaders are very good at a local level but struggle a bit when they start to have regional responsibilities. Among the reasons for this are having to use English as a business language and having to adjust to extensive travel to conduct business. It takes dedicated training and patience to be able to put local talent into regional and global roles. But in the end it's worth it, because once you can pick someone from Russia or South Africa, you have an expanded talent pool that's much more attuned to thinking globally and that's in touch with the needs of various kinds of consumers. We've been moving talent recently between the US and other markets, in both directions, and we'll be doing more of it in the future. Only when you're proactively moving talent around the world will people realize that there isn't just one operating model that works.

Jesse Wu

Vital statistics

Married, two grown children

Education

Graduated with a major in Economics from National Chengchi University, Taiwan

Received his MBA from Duke University

Career highlights

Johnson & Johnson Group of Consumer Companies (1989–present)

Worldwide Chairman, Consumer (2011–present)

Company Group Chairman, Global Markets Organization

International Vice President, Asia-Pacific (2003)

President, Greater China (2000)

Finance Director, China

Finance Director, Taiwan

Fast facts

A recipient of the Magnolia Award from the Shanghai municipal government, given in recognition of his contributions to Shanghai's development

Sits on the board of directors of the Consumer Goods Forum, a global industry network of more than 650 retailers and manufacturers

If you aren't very, very careful with talent development it's unlikely that your growth is going to be sustainable. When I have multiple opportunities to invest in, I would choose to invest where we have a strong local team; in practice, this has directly affected our business decisions.

McKinsey: *If talent is still a huge challenge, is there any area in which you see global companies having an edge over local competitors?*

Jesse Wu: In our industry, brands are important—people in India, China, and Russia have heard of multinationals' brands and have a strong desire for them. Beyond that, I believe that multinationals allocate capital more efficiently, so long-term we compete better. Capital efficiency is critical to sustaining a company, which is why Johnson & Johnson has lasted over a hundred years while others come and go. A local company that starts small and establishes some level of success, and then all of a sudden can go public at a price-to-earnings ratio of 30 to 50, would tend to think that capital is relatively easy to get. More established companies, over the years, always look at the return on investment—whether it's an acquisition, machinery, or new technology—so we tend to allocate our capital more efficiently. I think that will continue to be a relative competitive strength for multinationals.

Martin Dewhurst is a director in McKinsey's London office and **Tracey Griffin** is a director in McKinsey's Washington DC office.

Getting ruthless with your processes

Consistent global processes add value—up to a point. New research helps companies find the right balance between consistency and flexibility

Avinash Goyal
Toby Gibbs
Suzanne Heywood

Management processes—everything from how a company manages risk to how it gets supplies for factories to how it manages and develops people—are some of the primary ways that global companies impose order and consistency on a diverse set of global operations. 85 percent of the more than 300 executives we surveyed believe that processes help them share knowledge across divisions and regions, and executives agree that seamless delivery and service processes can be central to meeting customer expectations. In a world where the pace of competition is increasing faster than ever, best-in-class processes can create competitive advantages in areas such as innovation and risk management.

But our research also shows that global companies are particularly poor at managing their processes. In our survey of executives, processes emerged as one of the 3 weakest aspects of organization out of the 12 we explored. Strengthening them is crucial. However, executives often don't know where to begin. Often, they have far too many processes: one oil company, an executive told us, had 30 different processes for the simple act of folding a seat on an oil rig. Sometimes, especially when their company has grown by M&A, executives don't even know what their processes are. Other problems include allocations of authority between central and local leaders that no longer reflect economic reality; the ways that information and communications technology, for all its help in standardizing processes, also freezes them in place; processes that don't reflect new customer needs such as product-focused sales forces that don't sell integrated packages; and, perhaps most intractable and ignored, resistance to change.

Where processes go wrong at global scale

Our research and discussions with executives in global organizations have identified three main challenges:

Challenge 1: Too many processes, too little value

Companies do not differentiate between processes that are essential to creating global value and must be globally standardized, those that are not essential but offer benefits if they are consistent, and those that do not need to be standard at all. Nor do they differentiate between processes that are crucial to customers or the creation of value and those that are not. As one executive told us, "We need to allow local managers to focus on adding value instead of forcing on them too many central processes."

Nearly a third of the 317 executives we surveyed said that their company would be more effective globally if it reduced the number of its standardized processes. The leaders at the oil company mentioned above would surely agree. One of the reasons for the sheer number of management processes is that, as companies have grown, they've built processes ad hoc to manage expanded operations. Most have tried to address this, of course—but when they try to "lean out" operations at any level, they usually focus on reducing the number of people, not the number of processes. A small number of companies do talk about "core" or "signature" processes, but focusing on those few rarely knocks out the others. Processes also proliferate and become more complex as companies add new partnerships, outsourcing arrangements, or other externally focused relationships. These deals are often crucial to success in emerging markets, but

when companies try to manage them to a global standard, they miss local nuance; when they manage to local nuance, they end up with different processes for every country.

Growth through M&A also typically leads to a company having different processes in different countries accomplishing the same goal. One global retailer conceded in our survey that it doesn't even know how many processes it has. And companies can miss hundreds of millions in savings by not standardizing back-office processes they often overlook, such as accounts payable.

Finally, companies often try to set a single, standard global process but find that various locations maintain the old processes in the background—treating them as equal to the global process to avoid having to redesign other processes to which the local ones connect. One example is a bank that tried to institute a global expense-processing system only to find that many countries retained their own system to avoid the issues with currency conversion and long lag times that plagued the global process.

Challenge 2: Overstandardizing processes

Maximizing control and reducing risk are, rightly, priorities for leaders of global organizations. But too often these concerns lead to overstandardizing processes, making them too rigid, and to a dramatic decrease in local responsiveness. Indeed, finding the right ways to be responsive in new growth markets is a major challenge for most global companies.

Financial risk and controls are one area where most companies, and particularly financial ones, must standardize; one global bank has an anti-money-laundering policy that, its leaders know, makes their services less convenient for customers. But for most processes, executives we have talked to cited a lack of balance between local and global processes that results in slow decision making or too much bureaucracy for no benefit. This is often an issue with highly centralized companies that try to apply home market processes in emerging markets—where everyone from customers to regulators to employees has different expectations from those at home. And it can raise real problems, especially as global companies try to balance competing needs in different markets, such as cutting costs in one region while investing heavily in another. (The same can be true of structures; see "Structuring your organization to meet global aspirations" on page 29 for suggestions on how companies can address this issue from that angle.) We recently surveyed the executives of 13 leading global companies based in India; only half thought that processes were tailored to local needs, and only slightly more thought that reaction time and innovation reflected local market imperatives. One executive told us, "An issue that is number 1 priority in India is number 10 in Europe—so it takes far too long to resolve issues." Another executive said there should be reasonable expectations for processes like budget submissions and that these could vary by country—executives in countries with smaller operations should have a simpler budget process than those running larger businesses.

Standardization can also create some unexpected problems. A global bank, for example, added scorecards to its employee evaluation processes, tracking detailed assessments of performance on financial and business goals. However, they found that this tended to stifle innovation because achievements outside the plan weren't counted. An executive at another global company pointed to yet another standardization problem: ensuring that a global standard, especially on people processes, works in many different cultures. This company is facing the question of whether it needs to look for

people who can adapt to the system or whether the local culture should limit the degree of global standardization that it applies. (See "Winning the talent war in local markets by staying global" on page 67 for more discussion on this topic.)

Challenge 3: Resistance to changing processes

Processes that aren't immediate pain points often fade into the background. Senior executives have a hard time making the case for spending time or money changing back-end processes, given other priorities. They even find it hard to change customer-facing processes until they face customer backlash. One global bank, for example, realized that in some local offices, corporate customers were being approached by 10 different salespeople for 10 different products because the bank was organized by product line. Senior executives at a telecommunications company were organized by country and didn't understand that some customers wanted standard global service instead of country-specific variations.

And even when a process is causing pain—such as particularly high costs in cash or time—change can create more resistance than it's worth, as a global telecommunications company found out. It spent millions trying to integrate its customer-billing processes in a single region but faced so much resistance that in the end leaders decided changing it wasn't worth the employee turmoil it would cause.

Toward better global processes

Approach 1: Catalog and prioritize your global processes

A company has to start by knowing what major processes it has, in every area from people management to factory operations and billing. Then it can figure out those processes it must standardize globally, those it can localize, and those it can stop altogether. One approach to figuring this out is to divide the processes into four categories: signature processes, enabling processes, "hygiene" processes, and processes that don't need to be global (most of which will remain local but some of which will be scrapped). A company's archetype—how and why it's global (see "Next-generation global organizations" on page 1 for a description of these)—will affect this prioritization, as will its strategy, operating model, and the countries in which it competes.

Signature processes are those that add significant value if they are global, distinctive to a company, and difficult to replicate. A company should have no more than one or two of these, however large it is, as they are costly to develop and maintain in terms of both resources and senior management attention. These processes should be linked to the company's strategy and to its value drivers and should be widely recognized as essential to the organization's "DNA."

If building market share with new products is an important part of strategy to a customizer, for example, then signature processes could be product development or customer relationship management.

Most companies find that their signature processes are best supported with one or two "enabling processes" that they should also standardize globally. These are often processes common to an industry and following standard best practice with regard to them is sufficient. They may well be linked to drivers of value but they are not central to them. In oil and gas firms and other resource-seeking companies, for example, capital-expenditure decision making is often an enabling process, given the huge expenses these companies bear. Enabling processes are often functional processes, such as

performance management or talent management, particularly in knowledge-focused businesses. A large Indian conglomerate, for example, sees its people processes, such as workforce planning, performance management, organization culture, and capability building, as a crucial support to its overall business growth goal.

Almost every company will also find that it needs to standardize a few "hygiene" processes to ensure compliance or efficiency; these might be safety or payroll, for example—topics that typically do not take up much management attention until things go wrong.

Categorizing processes this way will likely leave a company with 10 to 15 signature and enabling processes that it needs to standardize globally. Everything else can—and should—go local, or be abandoned. Local processes are likely to be most important to value creation in high-growth markets. (See "How Western multinationals can organize to win in emerging markets" on page 13 for more on innovation in those markets.)

Approach 2: Optimize your processes

Companies typically have significant opportunities to improve their processes, both global and local. Of course, deciding which to standardize will eliminate a lot of near duplicates and thus cut down on the sheer number of processes to manage. But companies can also take a few steps to make sure their global processes are maximizing value at minimal costs and complexity.

The first step is simply to figure out what value the process currently delivers and what it could deliver; if there's a gap between the two, the next step is to figure out why. For example, a capital allocation and deployment process creates value by reducing project duration and costs. If duration or costs tend to creep above estimates, one reason could be a lack of cross-functional expertise—having production, engineering, sales, and procurement experts as a group evaluating a project will make sure nothing gets missed. Once a company fills any such knowledge gaps, applying lean principles will typically help optimize the steps of any process.[1]

A key point in managing both complexity and costs is to remember that "standardization" need not mean that every business fills in the same forms in the same sequence at the same time. For example, an annual target-setting process could include only four or five key performance indicators (KPIs) and need not be a comprehensive modeling exercise. These KPIs will be then used across the organization; businesses and regions will have flexibility to choose additional KPIs to track. One executive whose company has struggled to standardize its processes noted that it's important for people to understand that hiring an assistant in a new location won't require approval from headquarters—it's just that the same fair-hiring guidelines must be followed globally. The degree of standardization left in the process should be as light as possible while remaining consistent with the value drivers.

A second important point to consider in optimizing processes is the role of technology. On one hand, technology can immediately standardize a process globally; on the other, once it's locked in, technology can make changing that process very complicated and expensive. A global retailer created significant value from standardizing supply chain processes in its home market and then built its global sourcing process on top of that and supported both through dedicated technology solutions. But now, those processes are very complicated and making even small changes in the technology that supports them is costly. So

1 To use lean to optimize process time, firms often evaluate the time spent, distinguishing between necessary steps and non-value-adding activities (e.g., paperwork, rework, and redundant steps). The results of the difference between them are often significant (e.g., planned process time of four weeks versus actual implementation time of six to seven weeks). The firm can then conduct a detailed quantitative cost assessment to calculate the cost incurred at each step of the process (e.g., IT cost and time spent). Lastly, a quality assessment provides a clear understanding of the frequency with which the process achieves its objectives.

as part of their optimization, companies must assess how quickly the value drivers underlying a given process are likely to change and what effect those changes are likely to demand from a given process. If the value drivers are likely to change soon, then the supporting technology must be designed and built as flexible as possible.

Local leaders will almost certainly benefit from going through this same optimization process for the processes they newly own.

Approach 3: Implement change from the top

Consultation is all well and good, but too often discussions of process change bring out deeply vested interests that CEOs are unwilling to tackle. As one executive told us, "Involving the regional heads in a discussion of process change adds a year." Another said that, "If you can involve people in process design, it helps, but new-process implementation requires a top-down mandate." One reason for resistance and for why mandates work is that, as the first executive

explained, "Regions are not nearly as different as they think they are."

New-process implementation is a major change that typically requires a full change management approach.[2] But at companies with global scale, our experience, and that of almost every executive we have talked to, suggests that this alone is not enough: a senior leader is required to lead the change and confront organizational inertia.

For example, the global bank that had 10 different salespeople approaching the same customers put a very senior executive in charge of assessing its processes and then gave him all the resources and authority he needed to push through change, including introducing entirely new performance metrics. The bank moved from a product-driven approach to a customer-driven approach only as a result of this leader taking on a full-time role dedicated to supporting this change.

• • •

Assessing and optimizing your processes and embedding them in the organization isn't a one-time event. Senior leaders need to review processes regularly. As an oil company executive told us, "You have to prevent people from reinventing the wheel"—that is, you cannot allow processes to proliferate without adding value, or to continue unmodified as the company's sources of value or its overall strategy change. Only by going through this process regularly can a global company ensure that, at a minimum, all its global processes are at least enabling performance rather than hindering it—and, at best, conferring real competitive advantage with strong signature practices.

2 See *McKinsey Quarterly* articles "What successful transformations share: McKinsey global survey results," March 2010, and "The irrational side of change management," April 2009, both on www.mckinseyquarterly.com.

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The authors would like to acknowledge the contribution of Rahul Varma to the development of this article.

Getting more value from your global footprint

Connections between people are the glue that holds the company together. Getting these right costs little and delivers substantial value

Gregor Jost
Leigh Weiss

Many of the companies we have studied say they get value from their global footprints, but not as much value as they would like. Product ideas and customer knowledge are trapped in "silos"—the vertically integrated structures that are necessary in global companies to manage specialization, scale, and distance. For example, it is often challenging for senior executives to get a complete picture of global purchasers' needs across different regions and businesses.

Most companies find that formal global processes (such as the planning process) are necessary but insufficient to capture all of the value that could be derived from this footprint. Therefore they turn to a host of linkages—connections between individuals, such as meetings and calls, e-mails, instant messages, formal and informal networks, project teams, liaison and integrator roles, knowledge portals, and so on—to capture the value in their footprints. (The connections to the corporate center are often different to the horizontal connections across businesses and regions and "Reinventing the global corporate center" on page 41 discusses how companies are managing these vital information flows.)

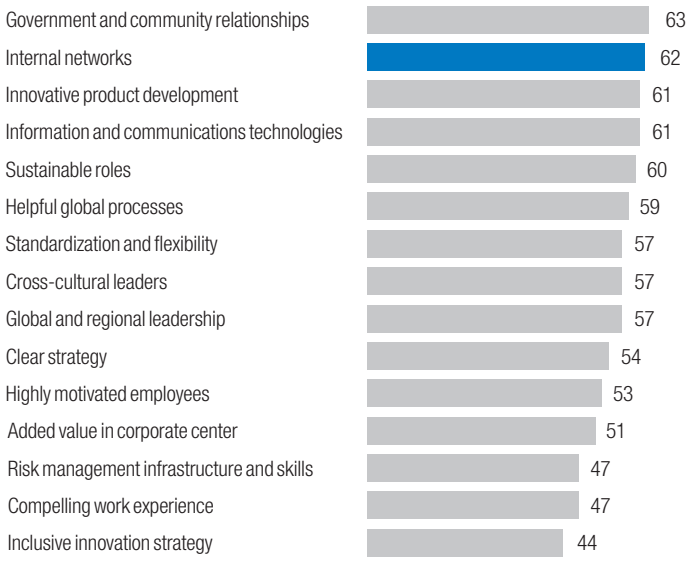
Linkages between people and groups are the glue that holds an organization together. Having the right structures and processes in place to enable growth and reduce complexity is essential, but without the right links among them even the best-structured organization with the most carefully designed processes will struggle. Two-thirds of executives at global companies surveyed by the McKinsey Quarterly recently said that their organization's ability to create links across the company was a source of strength[1] (see Exhibit 1). In addition, linkages can help

1 "McKinsey Global Survey results: Managing at global scale," *McKinsey Quarterly*, at mckinseyquarterly.com. The survey was in the field in September 2011.

Exhibit 1

Linkages rated second most important factor in managing at global scale

Percentage of respondents who agree, n=4,643



"Our ability to create linkages across divisions, functions, and regions is a source of competitive advantage"

Source: *"McKinsey Global Survey results: Managing at global scale,"* McKinsey Quarterly, at mckinseyquarterly.com; the survey was in the field in September 2011

global organizations overcome the "globalization penalty" that puts them at a disadvantage to locally focused competitors.[2]

Modern communications technologies make some linkages easy and cheap. But connecting everyone to everyone has diminishing returns. Piling on yet another videoconference or e-mail chain consumes time and energy instead of helping senior executives make decisions and lead organizations. Instead, global firms should work to establish the ideal number and kind of linkages. Getting this right will create demonstrable value for the business, as several leading companies, described below, have already learned.

Sources of business value from linkages

Organizations derive business value from linkages in three ways.

First, linkages can accelerate business impact (such as cross-selling products and services, improving the uptake of best practices, and improving customer service). Our Organizational Health Index research shows that companies with better collaborative management capabilities also have superior financial performance—top-quartile companies on average have returns on capital that are 50 percent higher than those in the lowest quartile.[3]

For instance, an oil and gas company established some linkages to share best practices, including a knowledge portal and talent rotations for field personnel. Those moves reduced costs due to poor quality maintenance and manufacturing by two-thirds and boosted new-product revenue by 22 percent and talent productivity by 10 percent (due to time saved). Similarly, one of the world's largest engineering consultancies created IT knowledge communities in major expertise areas, and new project management teams that cut across traditional geographic and business unit boundaries to focus on a few key functional initiatives (e.g., platform standardization). The improved linkages led to a 16 percent decrease in the size of the technology group. That translated to a reduction of technology costs from 5.2 percent of revenue to 3.6 percent of revenue in about 5 years.[4]

Second, linkages can improve organizational effectiveness (e.g., improving decisions about resource and capital allocation, reducing bureaucracy and interaction costs, and better integrating new hires and making them effective sooner). For example, a global consumer company's streamlined decision making for pivotal processes (e.g., strategic planning) by identifying and eliminating unnecessary interactions within and across silos and clarifying roles and responsibilities: in doing so it reduced SG&A by about 10 percent across the base of the organization, increased talent productivity by 80 percent, and improved decision making timing and outcomes (e.g., higher success rates of initiatives, higher forecast accuracy in business planning, winning advertising copy).

Third, companies can improve external stakeholder management to reduce the vulnerability that arises when only a few leaders hold the majority of relationships with external stakeholders.

Understanding your pattern of linkages

For senior executives, the linkages that drive performance are often hidden behind an opaque wall of formal mechanisms and structures. They cannot see whether they have too few linkages

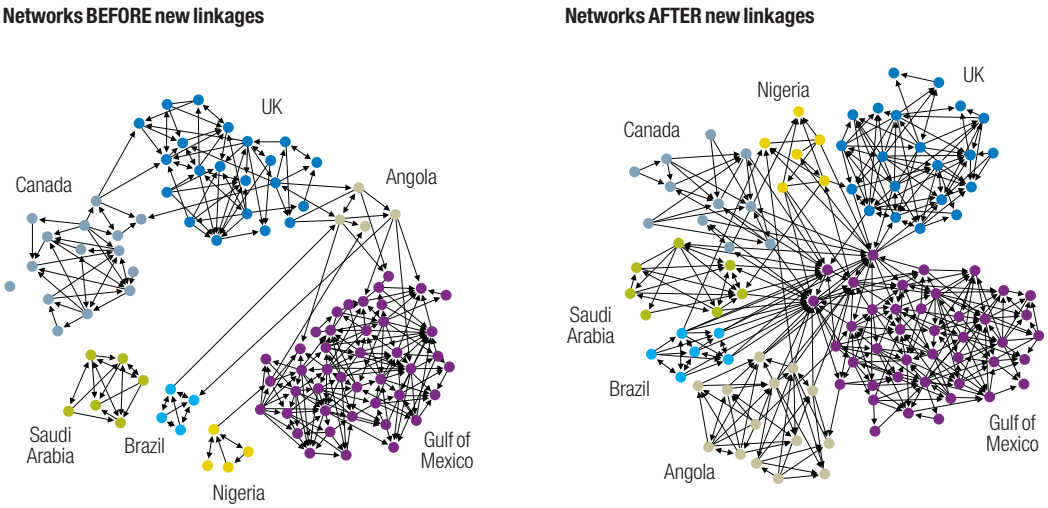
2 Martin Dewhurst, Jonathan Harris, and Suzanne Heywood, "Understanding your 'globalization penalty,'" *McKinsey Quarterly*, July 2011.

3 For more on this database, see http://solutions.mckinsey.com/ohi.

4 *McKinsey Quarterly*—"The role of networks in organizational change"; *WSJ* article—"Engineering firm charts ties."

Exhibit 2

Social network analysis shows growth in linkages at a global oil and gas company



or if the organization is overwhelmed with too many; and they cannot tell which ones add value. Three examples show how different organizations addressed these linkage challenges.

Example 1: Reducing costs by sharing best practices

Leaders of a global oil and gas company knew that operations personnel weren't sharing best practices effectively; a quick review showed that the company had more than 30 distinct ways to operate the same rig. Managers also knew that field workers facing problems such as equipment breakages or uncertainty about the local terrain did not know how to get answers quickly and effectively. When the executive leading operations studied the linkages, she found three places where links were missing. First, field workers tended to contact only those technical experts with whom they had strong personal relationships; second, the experts did not reach out unasked to the field workers to share best practices; and third, field workers facing similar problems in different geographies did not share best practices.

The oil company made improvements to the way information requests were processed and developed a thriving knowledge community, in part by designing a new knowledge portal. It also transferred a number of field workers among countries to establish new connections amongst colleagues and to build expertise on particular technical topics. Within a year, the new networks had blossomed (Exhibit 2). The adoption of new technologies boosted new-product revenue by 22 percent and talent productivity by 10 percent, and costs related to poor quality fell by two-thirds.

Example 2: Reducing bureaucracy and improving talent productivity

A global consumer company suffered from an overly inclusive culture, mired in linkages that slowed decision making and reduced employee productivity. A survey of pivotal decision making processes (such as strategic planning of new

product design) showed that nearly 45 percent of interactions added no value and 25 percent could be removed from each decision process. The company took action by "freeing up" specific individuals from decision making activities (e.g., some meetings and e-mail exchanges) and clarifying decisions roles and responsibilities. Then they rolled out newly streamlined global processes, starting with the most pivotal decisions. As a result, the company reduced SG&A by ~10 percent and improved talent productivity by ~80 percent. The company says it now makes more timely decisions and employee satisfaction has risen, as people appreciate getting out of meetings and e-mails that are not particularly relevant to them, and can dedicate the freed-up time to their real work.

Example 3: Boosting revenue through cross-selling in priority markets

A global financial services company, formed through acquisitions, had poor sales and customer "share of wallet" in several high-priority emerging markets. A review showed few linkages between product groups in these high-priority markets. It did a pilot test of a new, temporary group for the distribution of specific products from two main business units into these markets. Early success in improving cross-selling led to similar initiatives in a limited number of specific areas in which linkages would create value. These groups had their own charters, budget, support, and success metrics. The company further reinforced the new cross-selling priorities in its process to "onboard" new talent and in its training programs. The cross-sell rates between business units and geographic units improved in direct correlation to the number of linkages. The company developed a culture of better collaboration and innovation in these markets while also preserving accountability.

Getting better connected

Up to now we have discussed linkages in general terms. As companies think through their connections, more precision is needed. There are six kinds of linkages – connections between individuals – that companies use to extract more business value, such as dotted-line reporting or integrating roles, and five enablers, such as co-locating employees or job rotation, that facilitate or create these connections (Exhibit 3).

When faced with a lack of connection or collaboration, the standard reflex is to formalize linkages (e.g., adding new reporting lines or additional dimensions to the organization matrix). But these more formal linkages can be costly to operate; dual reporting lines will almost certainly double an executive's administrative burden, to take only the most obvious example.

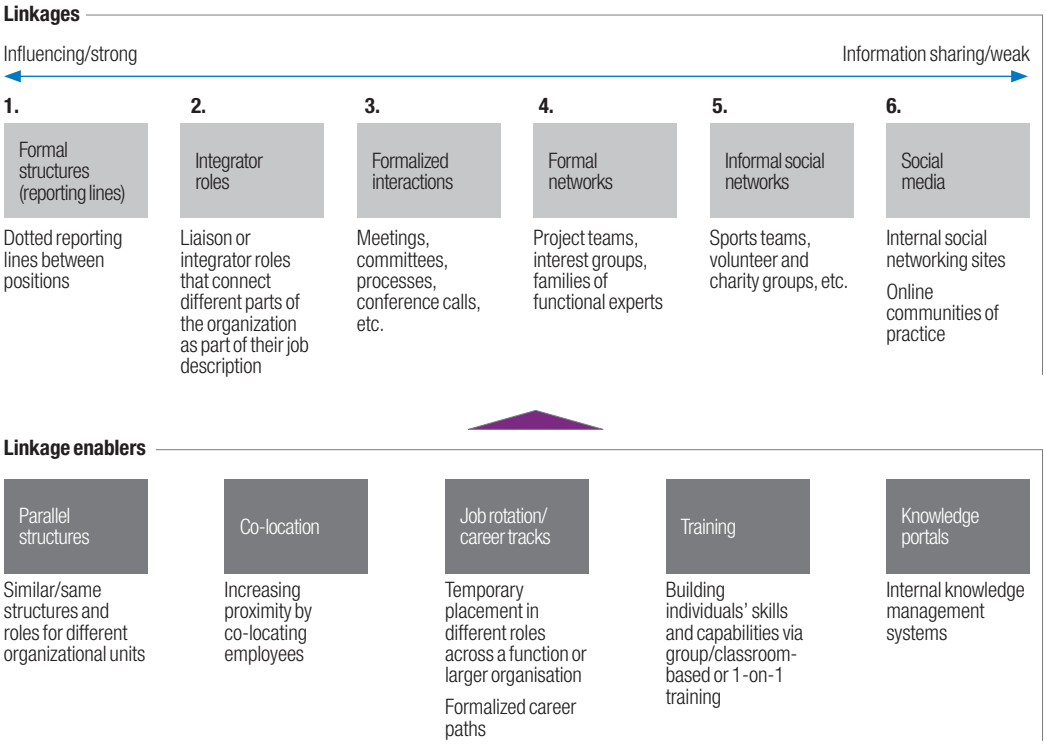
Better solutions can come from considering a wider range of linkage mechanisms. For example, some tasks and functions, such as coaching or mentoring, require strong, personal, trusting, and frequent interactions (such as via direct reporting lines). Other connections, such as those for sharing documents, can be weaker, more impersonal, and infrequent.

As the companies in the examples above demonstrated, a good first step in getting better connected is to understand whether a company has too few, too many, or the wrong type of linkages, where they are or where they are missing, and the problems arising as a result (such as missed opportunities, wasted time, or overburdened managers).

Once a company knows where it stands, its leaders can decide where to remove linkages, where to add them, and what kinds they need.

Exhibit 3

Linkages and enablers to connect the company



When there are too many linkages, structural changes such as clarifying decision rights and reporting lines will help (see "Structuring your organization to meet global aspirations" on page 29 for more on this).

If the challenge is too few linkages, as at the oil company, or linkages in the wrong places, the company will need to identify its knowledge seekers and the holders of that knowledge; it can then determine the best ways to connect them, whether through strong, collaborative, and trust-based personal connections or simpler information exchanges using e-mail or regular reports. In general, the purpose of the linkage should determine which mechanism to use.

The integrator role is one linkage that not many companies have yet explored. That's too bad as it is perhaps the best way to build strong, personal links. An integrator role links specific teams together, often temporarily, until close working relationships have been established. For example, when researchers analyzed social networks and studied e-mails among teams involved in developing aerodynamic components for Formula 1 racing cars, they found that teams that designated a relationship manager to interact frequently with peers working on related products across geographies were 20 percent more productive than teams whose managers interacted less often.[5]

5 Jacomo Corbo and Gary Pisano, "The impact of information networks on productivity," paper given at Circuits of Profit conference, Budapest, June 20, 2011.

One note of caution: companies that rely on informal links also need to ensure that the kinds of behaviors that support effective personal communication are built into performance evaluation criteria, leadership standards, and processes for measuring and developing employees' effectiveness.

To build less costly links, companies are using a number of technological tools, both as enablers to connect knowledge seekers with expert knowledge and, in the case of social media, as a platform on which people build durable, personal links. For instance, IBM's internal Beehive Web site does both. It allows users to add personal content via "status update" and "about me" features; the site also includes "hive five" lists where staff can outline business ideas and invite comments from colleagues.6 This helps foster collaboration and can even help the company develop a new, global set of values. (See our interview with Michael Cannon-Brookes, IBM's Vice President for Business Development, China and India, on page 35 for more.)

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Companies can get more value from their global footprints by using a range of linkages to tap ideas and knowledge trapped in silos. Companies that have the right linkages in place can boost revenue, lower costs, make better decisions about resource and capital allocations, accelerate innovation, and improve talent productivity.

6 Joan M. DiMicco, David R. Millen, Werner Geyer, and Casey Dugan, "Research on the use of social software in the workplace," paper presented at CSCW workshop on social networking in organizations, San Diego, California, November 2008.

Gregor Jost is an engagement manager in McKinsey's New York office and **Leigh Weiss** is a senior expert in McKinsey's Boston office.

Winning the talent war in local markets by staying global

New ideas can help global companies successfully compete for scarce talent in new markets

Matthew Pettigrew
Ramesh Srinivasan

Global organizations need to win in multiple local markets. To do so, they need distinctive local insights and capabilities. But they also need to maximize the return on their global assets: everything from brand equity and economies of scale to the ability to provide services around the clock and take a global view on talent.

This article draws on conversations and interviews with leaders of global firms, and our recent research on managing global organizations, to examine how such firms can turn a global approach to talent to their competitive advantage. It argues that to recruit and retain the best local talent, such companies need to draw on their access to a number of global talent assets that their local competitors simply don't have: large, diverse, and mobile talent pools; access to stimulating and demanding jobs across a global network, including access to regional or even global leadership roles at an accelerated rate; and a steady flow across borders of world-class capabilities from other parts of the business.

Understanding the challenges

Many global companies appear to be struggling with this agenda, particularly in emerging markets where the competition for the best talent is intense. It's not difficult to see why. It's now more expensive to hire leaders in some emerging than mature markets. Local workers are more likely than ever to leave jobs with global companies, jobs that were once highly prized. Levels of diversity at the top of many global companies remain stubbornly low. And in some major Western economies, employees are becoming less, not more mobile.

Some examples of these trends:

- HSBC acknowledged in its recent annual results that it now pays its most senior staff in China, India, and Brazil double what it pays their counterparts in the UK.

- Our client experience with pharmaceutical companies and others confirms that in China most foreign employers continue to suffer from talent shortages. One reason is that Chinese job seekers increasingly look askance at jobs with MNCs. In 2007, 33 percent wanted to work for a foreign firm, but in 2009 just 18 percent did.[1] As a result, only 13 percent of global organizations say they are confident that their talent pipeline in China is adequate.[2]

- In the US, less than 10 percent of the directors of the largest 200 firms are nonnationals, up from 6 percent in 2005 but still low when the global interests of these firms are considered. In Europe, 24 percent of the directors of the biggest companies in 2011 were nonnationals, but there is a great deal of variation, with more than half of directors in Switzerland nonnationals compared with only 10 percent in Spain.[3] A senior executive at a global company in Asia told us, "In our top 100 executive meetings, we spend more than half of our time speaking about Asia. But if I look around the room I hardly see anybody with an Asian background." Another put it bluntly "Leaders tend to promote and hire in their own image."

- Expatriate executives, whom companies would once have expected to take up the slack, are less and less eager to move, for reasons that include a reduced appetite for risk in uncertain financial times and the demands that working far from the center put on both executives' professional networks and their personal lives. A recent Manpower report suggests that in many Western countries—including the UK, Canada, the US, France, and Germany—the proportion of people ready to relocate for a job has declined substantially.[4]

1 Corporate Executive Board, as reported in "The battle for China's talent," *Harvard Business Review*, March 2011.

2 Mercer What's Working China survey, 2011.

3 Heidrick & Struggles, European Corporate Governance Report 2011; US Corporate Governance, cited in *Financial Times*, "Directors without borders," August 2011.

4 Migration for Work Survey, *Manpower*, 2011.

Making local talent global

To respond to these challenges, companies need to act at both local and global levels in a way that recognizes the interdependencies between the two. Too often companies have approached their local talent needs in an uncoordinated way. We believe that an approach starting with a global talent strategy and then extending it deeply into localized HR practices is best as it makes it easier to decide on appropriate but bold moves that will substantially change a company's talent position. Global companies need to put their people strategy on par with their business strategy, to tailor their offering to employees precisely, and to invest significantly in developing local talent.

Put people first

Winning companies recognize that they need to solve their talent strategy even as they are developing their global business strategy. One executive from a global financial services firm with a long international history told us that its commitment to people is often stronger than its commitment to the business in a given country. A good first step is to create a talent strategy that defines the skills and capacity needed at every level in each location. This exercise usually confirms that a scarcity of talent is the biggest bottleneck for growth; more importantly, it also allows companies to identify sources of talent that may have otherwise been hidden and to begin the process of matching demand with supply of talent.

Such an approach may often trigger a counterintuitive sequence of moves. The head of organizational development at a global technology company said it started securing the people it needed for a Chengdu chip assembly plant "before we had our buildings built." The company went to technical schools and universities to hire young talent that they could train and develop over time.

Figure out what local employees really value

For a long time, companies with global brands could coast in emerging markets, knowing that their brand carried more prestige for potential employees than that of any local competitor. "We still have the attitude that someone is lucky to be hired by us," one executive told us, but fewer and fewer people think that's true.

Global companies have to get the basics right: an employee value proposition that incorporates competitive compensation, good use of brand capital, attractive working conditions, and managers who develop, engage, and support their staff. Tata sets out to "make it a point to understand employees' wants—not just in India, but wherever Tata operates," according to its group vice president of HR. It has a tailored employee value proposition for each of its major markets; for example, it stresses manager quality to employees in India, development opportunities in China, and job interest in the US. (See "How Western multinationals can organize to win in emerging markets" on page 13 for more on finding the right incentives for local employees.)

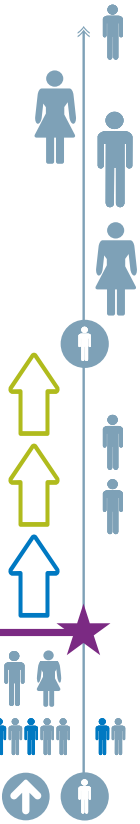
One big advantage global companies have is the ability to offer opportunities. But a recent McKinsey survey of senior multinational company executives based in India found that while their companies see locally grown managers as a source of global talent, the organizations were still not providing them with opportunities that would allow them to become global leaders.[5] This is a concern we've heard in many interviews as well. Indeed, while a few executives have moved from being an emerging-market leader to a global leadership role, such as Ajay Banga, president and CEO of

5 McKinsey Talent and Organization Imperatives Survey of 120 executives at 17 Indian country organizations within multinationals, February 2012.

MasterCard Worldwide; Indra Nooyi, chairman and CEO of PepsiCo; and Harish Manwani, COO of Unilever, global companies need to develop many more such role models if they are to convince more talented local staff to join and stay. (See our interview with Jesse Wu, Johnson & Johnson Group of Consumer Companies' worldwide chairman, on page 47 for more on this topic.)

One approach is for global firms to provide high-potential local employees with global opportunities from an early point in their career. Bertelsmann does this by bringing some high-performing employees from emerging markets into the corporate center as part of its CEO program. They are given broad exposure to the kinds of functional and geographical issues they can expect to encounter as leaders while taking on real work assignments. Having spent a couple of years at the center, recruits then have to win a senior role in a local or regional market. They move back to local markets with a strong understanding of the organization and its strategy and with trust in and strong relationships with its leaders. (Diageo is another company that has a structured talent program; read more in our interview with Nick Blazquez, Diageo's president for Africa, on page 23.)

Bertelsmann targets high-turnover employee groups, particularly those in competitive labor markets, with longer-term training programs. In India, for example, high-potential employees can apply for an INSEAD Singapore Executive



MBA; over a three-year period, this benefit sharply increased motivation and retention among all employees who attended, at a lower cost than big salary hikes.

In some markets, particularly in Asia, global organizations are working to build employee loyalty by building a relationship between the firm and an employee's family. For example, Motorola and Nestlé have tried to strengthen these links in China through their family-visits and family-day initiatives. And an Indian conglomerate webcasts its annual employee-award ceremony to all employees and their families globally.

When you can't buy it, develop it

If companies can't attract the mature talent they need, they will have to develop it. Developing raw talent into a group of global leaders can be one of the most sustainable talent-sourcing options for global organizations. An executive at Unilever Vietnam told us, "We basically just look at the top 200 graduates and hire from that pool. The real energy gets put into training, developing, and retaining talent. Our management team here is predominantly Vietnamese and all of them are homegrown."[6]

Some firms are creating developmental programs that explicitly address cultural and linguistic barriers that can make it much harder for local executives to work at the global level. In Japan, for example, Goldman Sachs launched a program in 2009 to help its local staff interact more comfortably and effectively with staff around the world, with a particular focus on improving cross-cultural communication skills. It now plans to extend this "cultural dojo" to South Korea, China, and Singapore, based on a very positive response from participants.[7]

Making global talent local

Even if they can find and retain all the local leaders they need, global companies will still want to send some executives from home markets to emerging ones to deepen the global organization's understanding of these critical markets, share expertise, and develop talent. Some leading firms are consciously rejecting an expatriate culture by replacing short-term expatriate jobs with long-term international appointments and setting an expectation that employees in these posts will stay until they can find their next position in the usual corporate cycle. This helps build expertise and eliminates a problem cited by one European car firm executive working in South America: when expatriate managers are known to be leaving soon, they become lame ducks, liable to be worked around by local managers.

Make the right moves

As noted above, many executives in developed markets don't want to move to an emerging market, however much their company wants them to. As one executive put it, when it comes to changing such attitudes, "there's no one silver bullet—it just takes time." It's crucial that employees who are asked to move have real trust in the senior leaders so that they are willing to take the personal risk of moving.

Some firms make it clear that long-term career success will require moving across businesses, functions, and regions. For example, a leading mining company expects its people to have had experience in at least two different geographic regions, two different businesses or functions, and even two different economic environments – for example, high and low growth—before moving into senior leadership roles.

6 Chairman of Unilever Vietnam, quoted in Conference Board report.

7 "Cross-cultural conversations," *Financial Times*, January 11, 2012.

When people do move, good mobility programs support employees and their families, align with established career paths, and help employees away from home retain strong links back to the corporate center. HSBC's International Management program, for example, carefully selects applicants and sends them to a location far from their current one; they can expect to rotate again after 18 to 24 months. Participants receive close mentoring and accelerated career progression opportunities, and HSBC hopes to secure a broad and diverse future leadership pool. Even accommodating something as basic as time zone differences can help, as IBM's Michael Cannon-Brookes points out in the interview on page 35.

Help executives familiarize themselves with new markets

To make sure that new executives can make the strongest contributions in new markets—and avoid errors—on-the-job training is crucial. A number of companies have set about developing local insight in innovative ways. For example, IBM sends its executives to give free consulting advice in emerging markets (even those in which it is not yet active) as a means of bolstering business in new geographies, building familiarity with new markets, and developing personal skills. FedEx and Novartis have also used a similar approach of providing free services in emerging markets, mainly to cultivate new customers, but also so that the company's executives can become more familiar with the markets.

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Winning the war for talent in global markets requires a two-pronged approach: finding more leaders in local markets and improving the ability and interest of expatriates from all over the world to work locally. Making this happen isn't easy and remains a significant challenge for all of the global companies that we spoke to in conducting this research. Doing so requires a global corporate culture that places talent and leadership at the heart of corporate strategy, which may take years to build. But companies that do this successfully will increase their chances of winning locally with a global approach to managing people.

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An interview with Santrupt Misra, Aditya Birla Group HR Director and CEO of Carbon Black

The Aditya Birla Group is an India-based multinational conglomerate. The Group has diversified business interests and is a leading player in all the sectors in which it operates such as aluminum rolling, viscose staple fiber, metals, cement, viscose filament yarn, branded apparel, carbon black, chemicals, fertilizers, insulators, financial services, telecommunications, BPO, and IT services. Some 40 years ago the company began to expand internationally. Over the past eight years, it has become five times bigger in terms of revenue and three times bigger in terms of EBITDA. Now it has operations in 40 countries and gets more than 56 percent of its revenue from outside India. McKinsey's Rajat Gupta and Suzanne Heywood talked with Dr. Misra in January 2012.

Rajat Gupta
Suzanne Heywood

McKinsey: *How do you connect employees to the company across so many different cultures?*

Santrupt Misra: We have been able to make the local people feel part of our company very quickly while preserving what is important to them. We have awards that honor individuals and teams from across the world for outstanding achievement. For example, a lady from Egypt was honored for her exemplary role in keeping the plant safe during the Egyptian revolution in the face of many threats. Similarly, a team from North America was honoured for technical innovation. We've typically held the award ceremony in India but have started holding it in different parts of the world. We bring the nominees together, even the most junior employees in the organization, whether they are Canadian or Thai or Indonesian or Korean. And we do a live Webcast to all employees and their families globally. An equally meaningful platform is our leadership center in Mumbai, where many employees attend learning programs: in the elevator, "thank you" and "good morning" are written in seven languages, so people don't feel that this is an Indian company that's only telling me in Hindi what to do. We're also global in terms of talent development. Even though many people don't move for personal or family reasons, all our internal job postings are made available to all our employees in the world. So I think they feel if they do want to, they can move. This can be really helpful. For example, we have brought young Thai engineers to work in the remote parts of India for six months on a project. They go back with tremendous experience and can talk about how they were part of the activities and festivals in India too.

As we grow further, we need to become more efficient in moving knowledge and best practice around our organization. Part of this will be accelerating the development of peer leadership. We are growing as a company more rapidly than people grow, so we need to develop more leaders at all levels. Simultaneously, we need to create a very strong employer brand so that if we do not manage to develop enough people, we can hire.

We've found that this process of connecting people with the company is a particular challenge with acquisitions. In an acquisition, you get a group of people who have a memory and a history, a pride associated with their organization, and you get their culture. To integrate your culture and that new culture of the acquired business in a globalized context, you have the national cultures *and* the organizational cultures, so in effect you're trying to combine three or four things. Weaning people away from the way they have done things or questioning what they have done in the past is very difficult, and during an acquisition you're trying to mold the whole organization at the same time, which is far more difficult. This is one of several reasons that I think inorganic growth is much more difficult than organic growth.

McKinsey: *How have you used technology to help you operate globally?*

Santrupt Misra: Our use of information and communication technology (ICT) has really helped us become global. For example, we acquired Colombian Chemicals six months ago, and the first thing I established was video connectivity between them and our locations elsewhere and mail integration so that they have access to our portal, our knowledge, our e-learning, and every other support.

We have to be careful, though, to remain very responsive locally. There has been a lot of local empowerment at one level, but with the growth of ICT we have become more headquarter centric.

This hasn't been a deliberate policy; it's just that people in the distant territories have found ICT an easy way to kick the ball upstairs. Now we need to learn to push back, to say "don't come back just because you have access to me." But we need to figure out how to make sure that empowerment is exercised within a framework where the risk issues are well understood.

McKinsey: *How do you build connections to local communities?*

Santrupt Misra: In every country we work in, we become part of the community and we try to participate physically, not just make financial contributions. Sometimes it is building physical assets, like a vocational training center in Thailand. In Egypt, there are no adequate community toilets, so I am trying to take an Indian organization that puts up cost-effective public sanitary facilities to Egypt to work with the government on public toilet facilities. And after the floods in Thailand we were providing tarpaulins from our factories and we sent our electricians to repair electric connections.

McKinsey: *How does your global scale help you with customers?*

Santrupt Misra: Whenever our customers have been in need in their country, we have been able to use our global presence to provide them support and services from other locations, sometimes at significant cost to us, just to make sure that our customers understand we are a global company. To give an example, when the Egyptian revolution happened and there was no transport and ports were on strike, we offered to bring our customers materials from Thailand and India to make sure there were no stockouts at their end. We made sure that our shipments from the factory were there, ready to be delivered whenever the port was open for a couple of hours. We were able to master the new logistics process internally very quickly. Being honest, staying in touch with customers, putting the sales and marketing people in touch with their counterparts in other regions, and moving people quickly lets us help those customers.

We have always been comfortable delivering products and customer service through our own people, our own channels, our own networks. As we expand, though, we'll need to be able to rely on third parties, partnerships, and outsourced services. So we're reimagining what we need to do within the organization and what can we deliver on behalf of the organization through a network of partners. We have to figure out how we create an integrated system that allows us to deliver the services and products to our customers efficiently.

However, we are already able to manage a lot of supply chains very successfully: for example, our pulp comes from South Africa and from Canada, gets converted into fiber in India, Thailand, and Indonesia; then the yarn is manufactured in seven other countries; and fabric is made somewhere else again. So we have been able to integrate and manage supply chains across multiple businesses. We also have strong relations with global customers and with global suppliers—people who supply us pipeline equipment, motors, and even IT. We not only deliver products but also access products and services seamlessly across the globe.

McKinsey: *How will you know when you've become a truly global corporation?*

Santrupt Misra: One metric is the proportion of our revenue that comes from outside our country of origin. Our revenue base is already fairly dispersed across different regions of the

Santrupt Misra

Education

PhD in Public Administration, India

PhD in Industrial Relations, Aston Business School, UK

Career highlights

Aditya Birla
(1996–present)

CEO, Carbon Black Business (2009–present)

Global Director, HR

Employment history with J.K. Group, Tata Institute of Social Sciences, Hindustan Lever Ltd.

Fast facts

Dr. Misra is a director on the Aditya Birla Management Corporation Private Limited Board. He is also a member of the boards of the Aditya Birla Science and Technology Company Ltd., Alexandria Carbon Black Co. SAE., Thai Carbon Black Public Co. Ltd., and Alexandria Fiber Co. SAE., which are part of the Aditya Birla Group

Dr. Misra has received several awards including the "Role Model & Exemplary Leader Award" at Asia's Best Employer Brand Awards 2010, Singapore

He also holds multiple fellowships including:

Fellowship of the National Academy of Human Resources (NAHR), US

Fellowship of the All India Management Association (AIMA)

And he is an Eisenhower fellow

Dr. Misra has published a book and several articles. His areas of interest include organization development, change management, management training, and leadership

globe and about 58 percent of our revenue comes from outside India. A second metric is diversity of employees; currently only about 28 percent of our employees are outside India. We operate in 40 countries and have people from 37 nationalities working with us, but we need to be still more diverse. I'd like to see 50 percent of our people be non-Indians by 2015. More importantly, we will know we are more global when our top 100 managers include people from at least 20 nationalities; today there are 7 or 8. The same is true of shareholders. The last and most important criterion is how widely our corporate brand is recognized by key stakeholders around the world. That is the ultimate test of the global nature of a company.

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