

The Benefits and Challenges of Globalization: An Economist Intelligence Unit executive summary in co-operation with EquaTerra and World 50

Introduction

In a world with few constants, sustaining growth and outpacing competition are key concerns for just about every company, regardless of industry, geography or size. Globalization places both issues in the cross hairs, raising the potential for new ideas, new markets and new sources of competition. Little wonder then that the subject receives so much attention. As Jack Welch, former chairman and CEO of General Electric put it, “Globalization has changed us into a company that searches the world, not just to sell or to source, but to find intellectual capital—the world’s best talents and greatest ideas.”

This report, conducted by the Economist Intelligence Unit on behalf of EquaTerra and World 50, examines corporate attitudes to the risks and opportunities presented by global competition and the challenges that come with expanding one’s global footprint. The main findings of the survey are outlined below.

- Executives see globalization as an inevitable but largely positive force, the pace of which is accelerating. Respondents are optimistic about the prospect of increased sales and are eager to capitalize on new branding opportunities.
- They also feel that organizations must adapt traditional ways of doing business to the new global environment by streamlining processes, expanding markets, and hiring and retaining qualified local staff.

A 30,000-foot view

“We sometimes say that we’re a 747 at 30,000 feet and we’ve got to change one of the engines. That’s a pretty complicated job. What makes it more complicated is that we’re not allowed to land the plane. Because the market is relentless and targets need to be delivered, we can’t stall. Therefore, we’re going to use best-in-class people to help change our engine, to help redefine what’s core to us and what’s non-core to us.”

— Chris Halbard, CFO, BT
Global Services

- Executives in the developed world must respond to global competitors that can bring products to market quickly and cheaply. As they do, companies must remember that local players do not always play by the same rules as developed countries, and must understand how to respond in those situations.
- Respondents believe that the opportunities created by globalization outweigh the risks and view the trend as having a long-term positive impact on their business. As they gear up, executives will focus internally on making their business processes more efficient and externally on investing in new foreign markets.

Globalization gathers pace

While they might argue about its ultimate shape and impact, nearly all survey respondents agree on one point: globalization is here to stay. Close to 90 percent believe that continued movement toward globalization is inevitable (see Figure 1), and three-quarters (77 percent) believe that the pace of globalization is picking up (see Figure 2). More than one-third (36 percent) of respondents say that they expect the rate of globalization to increase rapidly over the next three years.

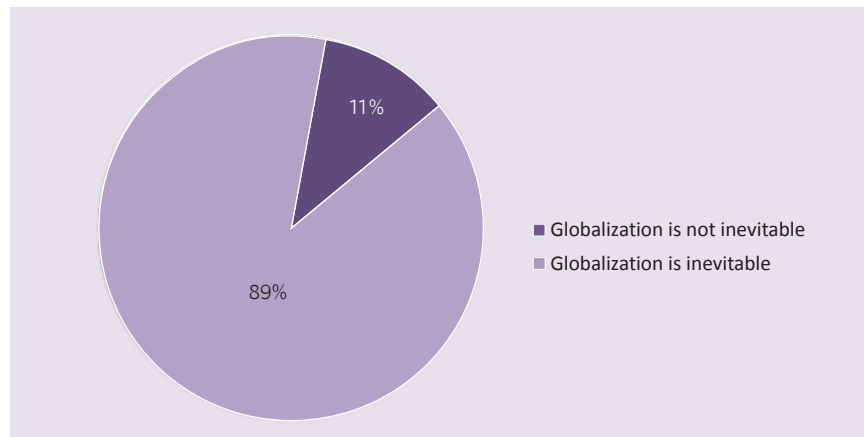


Figure 1: Globalization's Inevitability

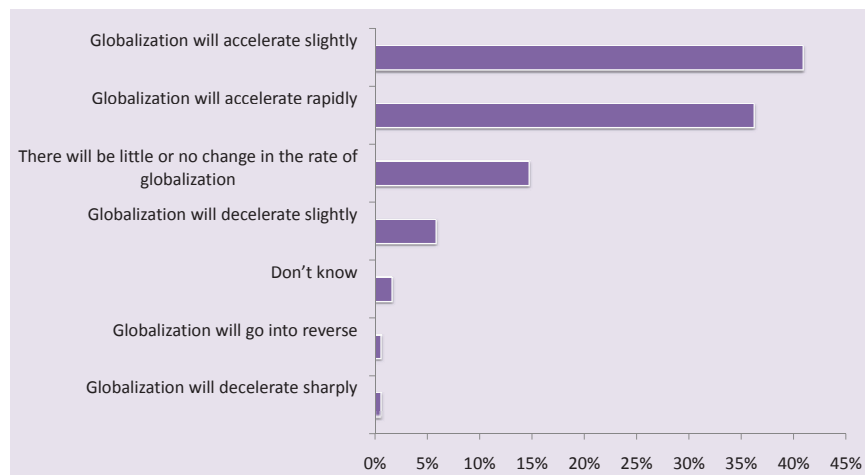


Figure 2: Globalization Growth

Helping to accelerate globalization is a combination of information technology, strong capital flows and liberalizing markets that gives firms greater access to capital, raw materials and resources, and new markets around the world. These factors appear to underlie executives' confidence about the opportunities that globalization will generate for their firms over the next three years.

Sixty-one percent of executives cite expansion into new markets as the most significant new opportunity created by globalization (see Figure 3). Ranking a distant second (39 percent) was the opportunity to improve company brand exposure and sales. New direct investment opportunities (31 percent) and access to lower-cost skilled labor (29 percent) took third and fourth places, respectively. These findings held true across all demographic groups, C-suite and non C-suite, and respondents from all three regions.

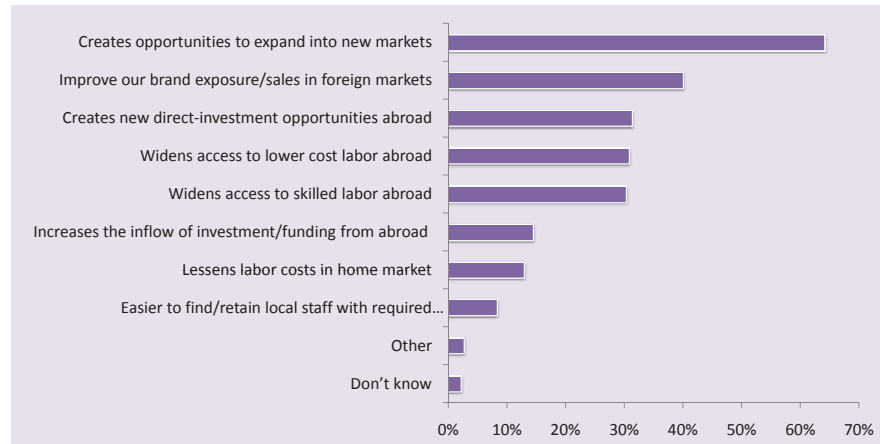


Figure 3: Opportunities from Globalization

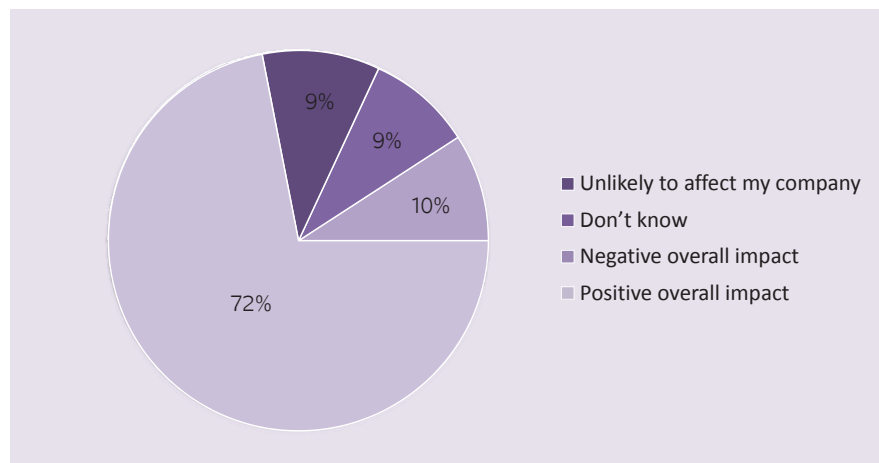


Figure 4: Impact of Globalization

While a few respondents feel that globalization will have a negative (10 percent) or neutral (9 percent) effect on their company, most (72 percent) believe that the overall impact will be positive (see Figure 4). Asian respondents, although optimistic about the impact of globalizing markets, are slightly less enthusiastic than their peers in other parts of the world.

Mini Case Study: World Economic Forum

As companies expand into foreign markets, they should consider the cultural fit between those markets and their organizations, says Simon Mulcahy, head of the World Economic Forum's (WEF) Information Technology industry group, based in Geneva. "On the basis of McKinsey's work (a strategic consultancy and WEF partner), when comparing high and low performance companies, culture is a key differentiator—more important than such factors as strategy and idea generation." To examine the influence of local culture on innovation, Mr Mulcahy brought together a diverse group of executives focused on technological innovation. "The overall intent," he says, "is to identify what factors most influence innovation and discover where these factors are concentrated around the world."

Mr Mulcahy worked with many leading organizations to create an interactive online tool they call the "Innovation Heat-map." The tool, he explains, "gathers innovation data from all sources, visualizes it through a Heat-map, and exposes it to a community of leading innovation minds to gain insights. It is designed to be as open-source as possible, aiding researchers, students and decision makers at all levels." A sample of the insights gleaned so far show that at a local level, the presence of top management schools and access to risk capital play surprisingly little role in the innovation output for most segments of the high-technology industry. With respect to Asia, the Heat-map also revealed that China and South Korea have advanced their research capacity more quickly than previously thought, and are now catching up with the technical sophistication of longer-established innovation hubs. The hope is that such intelligence will one day help companies understand the leading indicators to innovation and which local markets are better suited to supporting specific business needs.

Access to new sources of innovation is also causing some firms to re-think their strategies. Many multinationals now choose to play a "fast follower" role rather than being a leading innovator. "In the past," Mr Mulcahy says, "large companies set the game themselves. But advances in technology, such as open source and web 2.0, and the emergence of innovation hubs in India and other developing markets are changing that pattern." Today, many multinationals get some of their most interesting business ideas from outside sources. Mr Mulcahy says that with respect to emerging markets, the big players, are tracking new developments closely—"so closely that many are moving important parts of their operations to these locations." Through joint ventures, acquisition or the establishment of their own in-country R&D units, some of these large companies believe that it is more effective to piggy-back off the innovation around them rather than grow such entrepreneurship organically.

Meeting new challenges

Across the board, respondents say that finding and retaining high-quality talent is their number-one concern over the next three years (see Figure 5). Forty-four percent of all participants put this issue ahead of other organizational goals such as enabling process improvement (25 percent) or organizational innovation (23 percent). This is true amongst survey participants at all levels of the organization and across all geographic regions. Without question, the talent issue sits at the top of the management agenda.



Figure 5: Biggest Overall Challenges



Figure 6: Challenges from Globalization

As executives tackle these issues, they remain aware that globalization is creating other new challenges. Chief amongst them is the emergence of new, lower-cost competitors (see Figure 6). Nearly half (48 percent) of all participants highlighted this as one of the main challenges posed by globalization. Others cited the difficulty of navigating markets where weaker regulatory, governance and legal regimes prevail. Thirty-seven percent of respondents said that they felt challenged by the differing rules that exist in some local markets, which allow some competitors to benefit unfairly from government subsidies, trade dumping, currency manipulation or

intellectual property violations. In fact, more than half of respondents (56 percent) said the potential rise in trade protectionism is the most serious threat to the spread of globalization over the next three years, even more serious than a global economic downturn or geopolitical risks (see Figure 7).

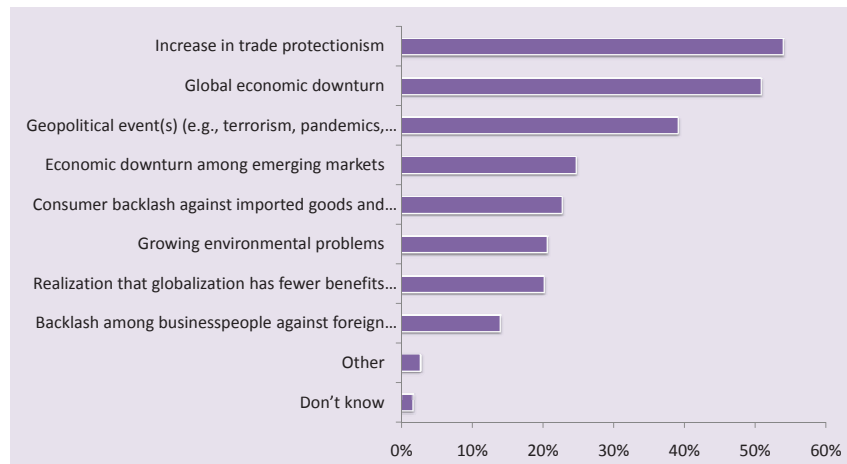


Figure 7: Potential Limiting Factors Impacting Globalization

While the degree to which protectionism will increase is uncertain, companies need to make contingency plans in case it does. Such plans could involve developing flexible sourcing arrangements that draw on multiple countries and regions, as well as owning captive operations in new markets. It also helps to establish relationships with local and state authorities, a strategy used by Caterpillar Corporation, a global manufacturer of construction equipment. “Our approach in countries like China is to go in through state-owned enterprises and form alliances and relationships,” says CIO, John Heller. “We work very closely with the governments in these respective countries to ensure that we’re not going to market in an opposing direction to the way these governments want their economies to grow.”

After trade protectionism, CEOs and other C-suite executives say that a global economic downturn is the second-greatest risk, cited by nearly half of C-suite respondents (49 percent).

Mini Case Study: BT Global Services

With growth comes added scale and complexity, two factors that Chris Halbard, CFO of BT Global Services (BTGS), the London-based subsidiary of British Telecom, deals with every day. BTGS operates digital and fiber-optic networks around the world. Revenue has doubled in recent years through a combination of organic growth and acquisitions, and is expected to reach nearly £8bn (US\$16.1bn) this year.

With so many new businesses and processes to integrate, Mr Halbard is constantly focused on ensuring that the business remains scalable. “We are at risk of our infrastructure becoming so layered, that it takes too long to release new products globally,” he says. “Too much money goes into getting things done instead of investing in how to service our customers in new and better ways.”

To offset this risk, Mr Halbard and his team identify core processes across the company’s global operations and work to standardize as many as possible. To reduce the number of online sites for such things as HR, training and collaboration, BTGS created one of the world’s largest consolidated intranets, a centralized system for document and content management. To bring order to a tangle of IT network technologies, BTGS streamlined overlapping systems to create an automated network. In an organizational culture built on personal networks, these are not easy undertakings. “Our biggest asset is the quality and responsiveness of our people. They know who to go to [in order] to get things done. Yet it can also be one of our biggest weaknesses as we look to change processes and create scalable delivery on a global basis,” he says.

Many multinationals face similar challenges. The solution often requires a bit of honest self-reflection to assess one’s true competencies. Sometimes it is easier to experiment with business model changes in emerging markets where the organizational culture may be more entrepreneurial and open to change than back at headquarters. “You can often be more radical deciding what’s core or non-core in an emerging market than at home because you haven’t got entrenched culture and working practices,” says Mr Halbard. The right conditions help as well. At BTGS, Mr Halbard relies on “low-cost economies, globalization, and labor arbitrage to drive hubs that foster standardization more naturally.”

To sharpen its customer focus, BTGS outsources many back-office processes. “We rationalize the back office to pay for investments in the front office because we know that’s what will give us sustainable growth,” Mr Halbard says. This transformation is modular, and Mr Halbard hopes that it will spread to the way his systems work—and how BTGS employees think. “In the face of an acquisition or significant organic growth, we’ll be able to integrate far better than we do today,” he says. In this way, standardization may be as much about changing the way people work as it is about changing the processes that they use.

Gearing up for success

Regardless of their size or industry, firms around the world recognize that new markets and new forms of competition require new ways of doing business (see Figure 8). As such, companies plan to focus internally on making their business processes more efficient (54 percent), and externally on investing and expanding in foreign markets (46 percent). Far fewer cite moving operations to lower cost markets (29 percent) or outsourcing/offshoring (11 percent) as their primary response to globalization. While 61 percent of West European respondents say that business process efficiency is the most important area to address, the need to enter foreign markets and expand their presence there was a slightly higher priority for Asian (67 percent) and North American respondents (47 percent).



Figure 8: Reacting to Globalization

These shifts in focus are working their way into corporate strategy (see Figure 9). Forty percent of respondents say that they are actively redesigning their company's product or service development process to create more flexible offerings tailored to different global markets. At the same time, 39 percent say that management is speeding up plans to capture opportunities in emerging markets. These plans include establishing wholly owned operations in new markets, creating alliances with



Figure 9: Globalization's Impact on Corporate Strategy

local businesses, and the option to source products and services from established providers in those markets. “You go where your market is,” says Mr Mulcahy, leader of the WEF’s Information Technology industry group. “But keep in mind what stage of the innovation process you’re sourcing—idea generation, implementation or commercialization—as different markets will be better suited for some than for others.”

Mini Case Study: Caterpillar Corporation

John Heller, CIO of Caterpillar Inc., the US\$45bn global heavy equipment manufacturer based in Peoria, Illinois, believes that IT can change the way his company competes. He sees it not as a support tool but rather as a core strategic function. “We have a strong realization within the company that IT will change the principles and rules that govern how we go to market,” he says.

Caterpillar has been a global player for decades and today sells into nearly 200 countries. This legacy has given management wide exposure to the benefits and challenges of globalization. Acknowledging Caterpillar’s explosive growth (company revenue has doubled since 2002), Mr Heller is quick to point out that the company had to stretch all aspects of its supply chain to make such growth possible, a shortcoming he is now addressing. “We are an introspective company and we’re never satisfied with where we are,” he says.

Caterpillar enters few markets directly, instead doing business through its vast dealer-distributor network. The arrangement spares Caterpillar the cost of direct investment and provides advantages in the form of established local infrastructure, relationships and knowledge. This provides flexibility and scale: Caterpillar can enter and leave markets relatively quickly, and use its dealer network to increase or spread capacity as demand changes. Keeping roughly 200 separate entities aligned can be a challenge, however. To overcome that obstacle, Caterpillar deployed its Vision 2020 corporate strategy to all of its dealers and strategic suppliers. That strategy lays out the firm’s near-, mid-, and long-term agenda in a series of three five-year plans.

Strategy is one thing, execution another; this is where IT comes in. Mr Heller’s Process Excellence Council brings together production, HR, global purchasing and finance, and after-market support. “Our mission is to find the right balance between what processes to standardize versus what decisions to leave with the local business unit,” he says. “We believe the customer should dictate whatever choices we make. If they require differentiation, we’ll recognize it. If not, our default is common.” To deviate from global system standards, local units must submit a business case explaining why they can’t be “common” rather than why they need to be unique. “When you have as much vertical integration as we do, having disparate processes creates challenges,” says Mr Heller. “Globalization makes us better. We don’t just survive it; we embrace it.”

Conclusion

Information technology, trade and economic liberalization have combined to create greater access to more markets than ever before. This creates new opportunities, but also a much broader surface area for executives to manage. While eager to leverage an expanding foreign presence, survey respondents acknowledge that they will have to redesign many internal processes in order to keep up with the rate of change. With such a remit, the job of managing a global company may be the biggest challenge for developed and developing companies alike. Leaders of tomorrow must stay on top of best practices—whether marrying process to strategy or helping a people-based culture to automate its knowledge base. In the midst of so much change, one thing is clear: in a globalizing economy, talent may be the most important competitive differentiator of all.

Methodology

This survey, conducted by the Economist Intelligence Unit on behalf of EquaTerra and World 50 in February 2008, polled 217 C-level and other senior executives from 19 industry groups worldwide about the benefits and challenges of globalization. Forty-six percent of respondents came from North America, 39 percent from Western Europe, 5 percent from Asia-Pacific, and 10 percent from the rest of the world. Sixty-two percent worked for organizations with annual revenue greater than US\$1bn, 19 percent for organizations with annual revenue below US\$500m. Board members and chief executive officers (CEOs) made up more than one-third of all respondents (35 percent); chief financial officers (CFOs), chief technical officers, and other C-level executives made up an additional 28 percent. The remaining sample was divided among a range of senior- and middle-management titles.

About EquaTerra

EquaTerra sourcing advisors help clients achieve sustainable value in their IT and business processes. Our advisors average more than 20 years of industry experience and have supported over 2000 transformation and outsourcing projects across more than 60 countries. Supporting clients throughout the Americas, Europe, Middle East, Africa and Asia Pacific, we have deep functional knowledge in Finance and Accounting, HR, IT, Procurement and other critical business processes. EquaTerra helps clients achieve significant cost savings and process improvement with internal transformation, shared services and outsourcing solutions.

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About World 50

World 50 provides executive peers from globally respected organizations a trusted forum for candidly sharing ideas, solutions and collaborative discovery free from competition or solicitation. World 50 operates Marketing 50 for chief marketing officers, Human Resource 50 for chief human resource officers, Global 50 for enterprise leaders, Supply Chain 50 for supply chain officers and Sustainability 50 for corporate social responsibility officers. Each private community provides its members intimate access to industry-leading peer practitioners, extraordinary business and world leaders, and facilitated knowledge sharing on topics members deem most critical to their business and their careers.

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