

# The Rise of Global Champions: Impact of Country, Industry & Company Effects

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*The rise of global champions is neither a universal nor a random phenomenon. It is not universal in the sense that not every aspiring or large Indian company will be able to grow into a significant global competitor. At the same time, it is not random either in that one can systematically lay out the factors that will distinguish a firm that becomes a global leader from one that tries to but fails. The authors present here a conceptual discussion of the factors that enable new players to emerge on the global stage and to challenge the established positions of incumbents.*

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## Emergence of New Global Champions

The emergence of new global champions from emerging economies has been well documented (See Kumar, Mohapatra & Chandrasekhar 2009, Ramamurti & Singh 2009, M. Zeng & Williamson 2007). In this article, we present a conceptual discussion of the factors that enable new players to emerge on the global stage and to challenge the established positions of incumbents. Our core premise is that the rise of global champions is neither a universal nor a random phenomenon. It is not universal in the sense that not every aspiring or large company from India will be able to grow into a significant global competitor. At the same time, it is not random in that one can systematically lay out the factors that will distinguish a firm that becomes a global leader from the one that tries to but fails.

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As depicted in Fig. 1, there are three dominant factors that determine the likelihood that a company from any country, developed or emerging, will end up as a global force within its industry: (i) the country effect, (ii) the industry effect, and (iii) the company effect.

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**Fig. 1: Factors That Drive the Emergence of Global Champions**

### Country Effect

In the early stages of globalization, the only place where most companies have any significant operations is the home country. Thus, it is critical that, as it spreads its wings abroad, a company be able to leverage country-specific comparative advantages. Without these advantages, the aspiring globalizer has

little to build on as it prepares to enter foreign markets and take on incumbent players on their home turf.

Country-specific advantages can be of many different types. We highlight below some of the most prominent ones (for a detailed analysis of country-specific advantages see Porter 1990):

- *Labour costs:* Much lower labour costs for both blue and white collar work in their home countries have proven to be a major source of global advantage for companies such as Suzlon Energy from India and Chery Auto, a car company from China.
- *Cost of raw materials and other inputs:* For Tata Steel, which acquired the much larger Anglo-Dutch Corus in 2006, access to India's low cost iron ore has been a major source of competitive advantage. Similarly, access to abundant and lower cost feedstock was the major advantage that Saudi Arabia's Sabic (Saudi Basic Industries Corp.) leveraged when it purchased GE's plastics business for \$11 billion in 2007.

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- *Cost of capital:* Indian companies have generally faced a disadvantage on this factor. In contrast, abundance of capital in China and the oil rich nations has made it much easier for state-owned or state-supported

companies in these countries to access capital at a much lower cost than would be feasible for companies based in many other countries including India.

- *Talent pool:* Access to a large, well educated, and relatively lower cost talent pool has been a major source of global advantage for technology-intensive companies such as Tata Consulting, Wipro, and Infosys.
- *Domestic scale:* A mega-sized domestic market is one of the primary reasons why a sizeable number of companies based in the U.S., Japan, and Germany have historically dominated their industries worldwide. A large domestic market gives the globalizing company home-grown scale economies that it can leverage against competitors in other markets. The large and rapidly growing size of the domestic market within India is now playing a similar role for companies such as TVS and Mahindra & Mahindra.
- *Innovation:* A country's unique challenges can also serve as a driver of leading edge innovation by companies embedded there. Think about why Japanese companies became world leaders in manufacturing innovations such as just-in-time and total quality management. Given Japan's very high population density and thus very expensive real estate, operating a U.S. style plant would have been simply prohibitive. In order to

survive and succeed even in the domestic market, companies such as Toyota had to invent new approaches to manufacturing that dramatically reduced the need to devote factory space to any task other than direct production. Once created, these innovations served as global rather than merely local advantages. Companies such as Tata Motors and Bharti Airtel are playing an analogous game. The per capita buying power of the Indian customer is extremely low. Thus, if you want to sell a car or a cellular phone service, you either skim the surface or you push the envelope to create and deliver products and services that are ultra low-cost. Tata Motors and Bharti Airtel have chosen the latter path. The resulting innovations in technology, product/service design, operations, and even the entire business model are likely to be highly fungible across borders.

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*Public policy:* Country effects can also take the form of public policy that encourages and facilitates exports and foreign direct investment by domestic firms. Unlike in India, the role of public policy is particularly evident in the case of China where the national government has pursued an explicit "Go Global" policy in recent years. As Vice-Minister

of Commerce Ma Xiuhong noted in her remarks at a conference in 2006: “The Chinese government supports those domestic companies with the strength to invest in the rest of the world to jointly develop business with their international counterparts” (Caixiong 2006: 10) President Hu Jintao even included a reference to the importance of “go global” strategies in his report to the 17<sup>th</sup> Party Congress in October 2007. Some of the planks in this policy include direct exhortation to state-owned enterprises, a helping hand by the Export-Import Bank of China in financing project outlays by foreign customers, co-investment by China Investment Corporation (a sovereign wealth fund), and encouragement to state-owned enterprises to set up Overseas Economic and Trade Cooperation Zones in countries and regions which have a favourable investment climate.

Despite the major role that country effects can play in giving local players a foundation for global advantage, it is important to remember two other facts. One, these advantages are equally available to almost all domestic companies. Yet, not every domestic company becomes a global champion. Thus, other factors such as industry and company effects (that we examine below) also play a critical role. Two, in this era of open borders and a globally integrated world economy, most of the country-specific advantages are available not just to domestic companies but also to those from abroad. IBM has built almost as large a staff in India as the Indian IT giants. Thus, whether or not country

effects become a source of competitive advantage depends also on the company’s ability to internalize them.

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### Industry Effect

Industries differ in the extent to which the strengths from one country can be leveraged across other countries. The three most important industry characteristics that can facilitate (or impede) the emergence of global champions are as follows.

- *Economies of global scale:* In some industries (such as semiconductors and mobile phones), global scale in R&D, sourcing, and/or operations is very important. In others (such as nursing homes), what matters is local, not global, scale.
- *Economies of global scope:* In some industries (such as supply chain management software), most customers are multinational companies who prefer suppliers with the capability to provide the needed products/services on a worldwide basis. In others (such as food retailing), virtually all customers are local who place no value on whether or not the supplier is global.
- *Economies of global delivery:* In some industries (such as athletic

shoes and call centres), goods and services can be produced in the most cost efficient location and distributed/delivered worldwide. In others (such as restaurants or home repair services), the product or service must be produced locally near the customer.

These three factors – economies of global scale, economies of global scope, and economies of global delivery - drive some industries to become very “globally integrated” (e.g., semiconductors, mobile phones, and IT or IT-enabled services), for some others to remain “multi-domestic” (e.g., housing construction, food retailing, and consumer banking), and for the rest to fall somewhere in between (e.g., Internet retailing and legal services).

Whether or not an industry is of the globally integrated or the multi-domestic type has a major bearing on the likelihood that an emerging global player will be successful in realizing its aspirations. In a multi-domestic industry, it is extremely hard (although not impossible) for an aspiring global champion to leverage its home-based advantage into other markets. Thus, established players in other countries have little to fear from such new entrants. Even a giant such as Wal-Mart faced miserable failures in Germany and South Korea precisely because of industry structure. Given the inherently multi-domestic structure of the discount retailing industry, the local market leaders in Germany and South Korea could easily defeat Wal-Mart.

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On the other hand, if the industry is globally integrated, then an aspiring global player faces very low industry-level structural barriers to global expansion. This does not, however, imply that such expansion would be either easy or successful. This is so because globally integrated industries also make it easier for incumbent multinationals to leverage their global scale and scope to attack the aspiring global champion in its home market. This is what IBM and Accenture have attempted to do by aggressively building very large footprints in India. But for IBM and Accenture’s aggressiveness, the Indian IT majors would probably have grown at an even faster pace.

The case of Nokia versus domestic competitors in China’s mobile phone market is also very instructive. By every measure, the mobile phone industry is a very global industry. Thus, bulk of the worldwide market has long been shared by a small number of global players (primarily Nokia, Samsung, LG, and Sony-Ericsson). In 2003-2004, within the Chinese market, which had already become the world’s largest, the global players came under serious attack from domestic challengers such as TCL and Ningbo Bird. Within short order, the domestic champions had captured over 51 percent of China’s mobile phone

market. To its enormous credit, Nokia decoded the developing scenario accurately and responded with all its might against the Chinese challengers. Among other moves, Nokia's actions included the introduction of much cheaper cell phone models and a rapid expansion in its distribution system. By 2007, the combined market share of the Chinese players had been reduced to 25 percent and was declining.

In short, aspiring global champions as well as the established multinationals must never forget that industry structure matters and must be factored into the design of strategic moves.

### **Company Effect**

Today, Infosys in IT services and the Chinese company Haier in home appliances are well known and highly respected names within their industries worldwide. As of mid-2008, Infosys' market cap stood at \$26 billion, second only to that of IBM in the worldwide IT services industry. And, Haier was the fourth largest home appliance manufacturer in the world, with not just the leading position in China but also growing market shares in other large markets such as the U.S. and Europe.

In understanding how Infosys and Haier became what they are, it is important to note that the explanation goes well beyond country and industry effects. In the mid-1980s, Infosys was just one of several hundred tiny IT

services companies based in India. In 1991, ten years after its founding, the company's revenues were less than \$2 million and its market value was estimated to be only about \$1.5 million. Similarly, look at Haier in 1984. Known at that time as the Qingdao Refrigerator Factory, the company was one of several hundred appliance manufacturers in China. More critically, it was teetering on the verge of bankruptcy and Zhang Ruimin, the newly appointed director, was the fourth boss in one year.

Why did Infosys leave most other Indian IT companies in the dust and emerge as the global giant that it is today? Why did Haier emerge from the ruins not merely to survive but to become one of China's most respected global companies? The answer lies in what we call the "company effect" i.e., the company-specific core capabilities, mindset, and organizational culture that distinguish the emerging champion from its peers within the home country. Leaders such as N.R. Narayana Murthy at Infosys and Zhang Ruimin at Haier were relentless in their passion to transform their companies into world-class organizations. Consider first the rise of Infosys:

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- In 1991, the Indian government commenced economic liberalization and multinationals such as IBM began planning to re-enter India. Many observers predicted that Infosys was basically “as good as dead.” They doubted that it could withstand the expected war for talent, the company’s key asset. Infosys’ response was brilliant and highly atypical. Even though they did not need the cash, its leaders decided to do an IPO and used the capital to build a world-class campus (that would rival that of Microsoft or IBM in the U.S.) in what was still third-world Bangalore. They also decided that Infosys salaries would be in the top 85-90 percentile of the companies in its peer group. Critically too, Infosys became one of the first companies in India to issue stock options to all employees. A top engineer from one of the Indian Institutes of Technology could now see that he/she had a better chance of becoming a millionaire at Infosys than at IBM.
  - As the U.S. government started to reduce the number of visas that could be granted to foreign workers doing projects in the U.S., Infosys became one of the first companies in India to develop global delivery capabilities whereby the work could be done in Bangalore and exported from there instead of having to be done at the customer site in the U.S. In order to assure customers that quality standards would continue to be met, Infosys became one of the first companies in India to receive ISO 9000 certification.
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- In the mid-1990s, rather than bow to intense pricing pressure from GE which accounted for 40 percent of its revenues, Infosys’ leaders decided instead to let GE go and vowed to significantly improve the company’s marketing capabilities so that it would never again be so dependent on any one customer.
  - In 1998, Infosys became the first Indian company to achieve CMM-Level 4 certification from Carnegie-Mellon’s Software Engineering Institute (SEI). In 2000, it again became the first Indian company to achieve CMM-Level 5 certification, the highest awarded by SEI. Until then, only 40 companies in the world had achieved CMM-Level 5 certification.
  - In 1999, Infosys became the first Indian company to undertake an IPO on a U.S.-based stock exchange. Like the IPO in India in the early 1990s, this IPO too was done for not just financial but also strategic reasons. The company’s leaders believed that an IPO on NASDAQ would help build name recognition and credibility with the CIOs and CEOs of major U.S. corporations, all potential clients. By now, the company had “arrived.”

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### Consider now the rise of Haier

- Just a few months after becoming the CEO in 1984, Zhang Ruimin pulled 76 newly built refrigerators from the production line, gathered all workers outside the factory, and asked them to join him in destroying these defective products. Such an act was unheard of in China and was highly symbolic. Many of the defects were minor and each refrigerator would have sold for four times the average annual salary of a worker. The message hit home: the company would no longer produce substandard products. The CEO was convinced that better quality products would command a higher price, even in the then very poor China. By 1988, Haier was widely regarded as the producer of the best quality refrigerators in China. Even though the company charged a premium price, its market share was growing. Haier's track record on all fronts – product quality, brand image, profitability, and cash flow – made it the obvious leader in consolidating the fragmented white goods industry in China.
- Haier entered into strategic alliances with several leading multinationals to build technological capabilities in both product design as well as manufacturing. The alliances included a technology licensing agreement with Germany's Liebherr, imports of production technology from Denmark's Derby and Japan's Sanyo, and joint ventures with Japan's Mitsubishi and Italy's Merloni. As Zhang Ruimin explained the logic behind these moves: "First we observe and digest. Then we imitate. In the end, we understand it well enough to design it independently."
- Haier became a pioneer in market segmentation and product innovation to meet the unique needs of different segments. The discovery that rural customers were using Haier washing machines to clean vegetables and sweet potatoes led the company to redesign its machines for rural customers so that they would no longer get clogged with mud. At the other end of the market, Haier introduced a tiny machine for customers in Shanghai. This machine could clean just a single change of clothes and was a hit with customers who lived in a hot and humid city and had tiny apartments.
- Haier cultivated a culture of delighting customers with the quality of its after-sales service. Tales of Haier's dedication to customer service were legendary and many observers regarded Haier as the leader in after-sales service across all companies in China.

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- As is clear, these capabilities (a mania for product quality, a disciplined approach to building technological capabilities, an obsession with market responsiveness and product innovation, and a commitment to after-sales service) became the defining features of Haier's DNA. They had little to do with the fact that Haier was a Chinese company or that it was an appliance manufacturer. Zhang Ruimin and his team built these capabilities because they wanted Haier to become a world-class company, whether in China or outside China. This obsession with building world-class capabilities paid off handsomely as Haier ventured into markets outside China, especially in highly competitive markets such as the U.S. and Europe where established incumbents ruled supreme and entry barriers were relatively high.

To sum up, large country-specific advantages can present significant potential opportunities for many home-grown companies to become global champions. However, this potential is likely to become a reality only for those companies which figure out how to build leading edge capabilities in a systematic manner. Even then, we are much more likely to see global champions in only those industries whose underlying economics make them globally integrated than in those which are destined to remain largely multi-domestic.

### **Indian Tigers vs. Chinese Dragons**

We conclude by applying some of the conceptual ideas discussed in this paper to interpret and explain important differences in the rise of global champions from India versus China. Since this analysis focuses on country-level comparisons, our explanation rests primarily on country-level effects.

The *first* major difference pertains to the fact that, on average, Chinese companies are far ahead of India's in globalization through exports of manufactured goods. In turn, Indian companies are far ahead of China in globalization through exports of remotely deliverable services. These differences derive directly from the historically differing strengths of the two economies. China is far ahead of India in manufacturing. In turn, India is far ahead of China in IT and IT-enabled services.

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The *second* major difference pertains to the fact that a much larger number of Chinese (as compared with Indian) companies are emerging as global giants in the supply of equipment and project management services for infrastructure projects such as the

construction of highways, electric power plants, ports, and the like. Having built more infrastructure over the last 15 years than has ever happened in any other country in the world, Chinese companies bring well-developed and much lower cost capabilities to these tasks. Take, for example, the construction of hydro-electric dams. China is home to almost half of the world's 45,000 biggest dams. Chinese companies such as Gezhouba Co. (an engineering firm) and Sinohydro Corp. (a dam builder) have recently won multi-billion dollar orders for dam projects in other developing countries. Often, these projects are financed by the Export-Import Bank of China, a state-owned enterprise. (Oster 2007:B1)

The *third* major difference pertains to the much stronger capabilities of Indian companies (relative to their Chinese counterparts) at playing the cross-border acquisition game, especially when it comes to making large acquisitions in developed countries. Obviously, there are exceptions such as Lenovo's purchase of IBM's PC business in 2005. However, as a general statement, it is valid to claim that Indian companies are far ahead of their Chinese peers at making large cross-border acquisitions and integrating them successfully. Let us look at the reasons why.

The two key requirements for success in globalizing through the M&A mode are: strong financial skills (to do the deal on the right terms) and strong post-merger integration skills (to make the deal work). In general, emerging global champions

from India have an edge over their Chinese counterparts on both dimensions.

Given an abundance of capital in China and a well-recognized propensity on the part of China's state-owned enterprises to put national policy goals ahead of shareholder value maximization, Chinese corporate leaders are still at a relatively early stage in developing world-class finance skills. In contrast, Indian business leaders are probably at the leading edge on this dimension.

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Indian business leaders also have an edge in post-merger integration skills. China's is a command-and-control economy embedded in a culture which respects hierarchy. In addition, China is a relatively homogenous society in terms of race, religion (or lack of it), and language. In contrast, India is a ferociously democratic country with one of the largest intra-country diversities in the world on almost any dimension that matters. Thus, the cultural DNA of Indian business leaders makes them more adept at horizontal integration and managing horizontal organizations than is currently the case with most Chinese business leaders. Finally, Indian corporate leaders have the well-known advantage of fluency in English so crucial to cross-border integration.

In globalizing through acquisition of companies in the developed economies (especially the U.S.), another advantage that Indian companies appear to enjoy pertains to the significantly lower political sensitivity of acquisitions by companies from India relative to those from China. The reasons are multifaceted and perhaps rooted in the similarities or differences in the cultures, political systems, and dominant languages between various countries. Any sizeable bid (say, above \$1 billion in deal size) by a Chinese company to acquire a controlling stake in a U.S. company would almost certainly be a front page story in *The Wall Street Journal* and is likely to invite negative comments from U.S. politicians. In contrast, even large acquisitions by companies from India are treated by the media and the politicians as relatively routine commercial events. As a recent case, consider the agreement by India's Essar Steel to buy the U.S.-based Esmark Inc. (a steel producer and distributor) for \$1.1 billion in cash. It was a relatively small news item on page B5 of *The Wall Street Journal*. (Matthews 2008: B5).

Chinese companies are responding to their relative disadvantage at playing the cross-border M&A game by adopting a learning mode. In concrete terms, this is reflected in the willingness of Chinese companies to take a minority stake rather than outright control. Recent examples include a \$5.6 billion investment by the Industrial and Commercial Bank of China to acquire a 20 percent stake in South Africa's Standard Bank, a \$2.7 billion investment by Ping An Insurance

to acquire a 4.18 percent stake in Fortis, a Belgium-based banking and insurance company, and a \$14.05 billion investment by a partnership between China Aluminum and Aluminum Corporation of America to acquire a 12 percent stake in Rio Tinto, an Anglo-Australian mining company.

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Looking ahead, we anticipate that, as both China and India continue to grow and develop more diversified strength, there will be convergence in the strengths and weaknesses of the dragons and the tigers. In the meantime, globalizers from both the economies have a lot of learning to do. Considerable opportunities also exist for entrepreneurs who can figure out how to combine an abundance of capital in the Middle-East with an abundance of manufacturing capabilities in China and an abundance of organizational and managerial capabilities in India.

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