Need for multi-national companies to identify and evaluate the risks associated with national culture when formulating their risk management strategies and tactics

Excellence in global corporate competition demands certain success-enabling organizational characteristics, attributes that of course must be introduced and/or supported by management. HBS professor Rohit Deshpandé has discovered that, in order to make themselves globally competitive, successful companies strive to achieve certain characteristics, even if those desired traits are not necessarily found in, or are contrary to, the native business culture of the firm’s home country. Thus, while average companies in France, Germany, and Japan may all look quite different from each other, those countries’ best-performing multinationals look quite similar. “When you consider the top-quartile companies across multiple sectors — such as B2B, B2C, services, political systems, or cultures — you’d be hard-pressed to tell their nationality,” says Deshpandé. “Among other distinguishing characteristics, these firms tend to have intrapreneurial cultures that encourage and reward risk. They are quick to market and invest a lot in customer insight. A commitment to being customer-centric tends to be deeply embedded throughout the organization”.

Deshpandé’s observation that in top international firms, “corporate culture trumps national culture,” is in line with what other studies show. They indicate that as high-performing global companies implement transnational strategy and strive to achieve competitive advantage, decision making by those firms and their individual managers seems to rise above national influences and toward a commonality shared by other top firms in the international arena.

In their study of the software industry in India, HBS professors Tarun Khanna and Krishna Palepu detect signs that globalization in the product and labor markets can, in some cases, cause corporate governance to draw closer to international standards as well. Khanna and Palepu stress, however, that their research also indicates that there is a limit to such convergence and that national influences and systems remain powerful and distinct. With that caveat, Palepu observes, "In general, world-class companies facing global competition do appear to benchmark themselves with global best practices and performance standards". He defines those aspired-to benchmarks as sound corporate governance, transparency, an orientation to quality, and a performance-driven, high-standards organizational culture.

As the best international companies exhibit similarities in certain standards and practices, managers within these firms, despite national and cultural differences, are finding common ground where they can work together. "In a truly multicultural corporate environment, people strive to strike a balance between their own cultural core and being open to other value systems, communication styles, and decision-making processes," observes Irina Gaida (HBS MBA '03). Gaida, a Russian national who has worked in London with United Technologies (in a department whose fifteen members represented seven countries) and in Paris with Bain, is currently in Moscow with BCG (Boston Consulting Group). "People are willing to adjust their behavior to facilitate teamwork, but they expect others to make a similar effort", Gaida notes. "This mutual adjustment eventually becomes the norm within an organization."

Understanding international differences in perceptions of management control is very important to the management of risk within multinational companies (MNCs). Different perceptions of what constitutes risk, and of how risks can be managed, lead to differences of opinion about the effectiveness of control. These can hinder the international transfer of corporate control systems. Different perceptions lead to misunderstandings, which can lead to the failure of management control.

Differences in perceptions of management control are also potentially important to the regulation of management control and risk management. A variety of national and international regulations affect MNCs in their control of worldwide operational risks, and there are growing demands for further management controls and for best practice, often of an Anglo-Saxon provenance, across the world.

As Hofstede (1980) and Schneider (1989) show, national culture can impact on the culture of an organization by selecting and framing the particular sets of organizational values, behaviours and norms that managers perceive as being consistent with their own basic assumptions that have been developed in their particular cultural context. In this way, cultural assumptions also influence the process of organizational decision-making. There is still a persistent belief that social, political and cultural differences between countries will continue to supersede the forces of globalization emanating from technologically driven markets or supranational agreements (Sparrow and Hiltrop, 1997). Furthermore, "those in favour of the divergence thesis would even oppose the possibility of delayed convergence, since they argue that national, and in some cases regional, institutional contexts are not only slow to change, partly because they derive from deep-seated beliefs and value-systems and partly because major re-distributions of power are involved, but, more importantly [. . .] even when change does occur this can only be understood in relation to the specific social context in which it occurs" (Gooderham and Brewster, 2003: 8).

Culture Differences and Organizational Changes

Organizational change inevitably generates resistance (Deetz, Tracy, and Simpson 2000; Poole et al. 2000; Zaltman, Duncan, and Holbok 1973). In even the best of circumstances, change creates uncertainty and ambiguity, and employees respond to those anxieties in myriad ways, many of which undermine the organization's objectives (Ashford 1988;

Menzies Lyth 1988; Noer 1993). Some changes also carry tangible threats to the status, self-esteem, incomes, or job security of particular groups of workers (Mulder 1977). As a result, even changes that on the surface seem to promise enhanced rewards or working conditions are resisted. When the changes are sudden; significant; imposed from the outside; involve employees from multiple, different cultures and subcultures; and/or are mishandled by management, the likelihood of resistance increases substantially.

Resistance to change

Resistance to change is related to national culture in two ways. First, cultural assumptions influence the way in which multinational corporations approach expansion into a new country or market. There are many possible forms of expansion. In terms of potential cultural integration, the two extremes are (1) "greenfield" starts and (2) acquisitions. In the former situation, a multinational company sends a small group of expatriates into an area to hire locals and gradually build a business. The potential for cultural clash is minimized, and the opportunity for the expatriates to learn the nuances of the new culture is maximized.

At the opposite extreme are foreign acquisitions, in which a multinational firm purchases a local company or plant. Acquisitions are quick but are fraught with potential for culture clash. In the worst-case scenario, the acquiring firm blindly imposes its own way of doing things on members of a very different culture with little consideration of those differences or for the values of employees of the acquired firm: "Culture clashes are resolved through brute power: Key people are replaced by the corporation's own agents. In other cases, key people do not wait for this to happen and leave on their own account. Acquisitions often lead to a destruction of human capital, which is eventually a destruction of financial capital as well." (Hofstede2001,p. 45).

As a result, cross-cultural acquisitions tend to fail significantly more often than other forms of expansion, especially when the cultures of the acquiring and acquired firms/plants are substantially different (Barkema, Bell, and Pennings 1996; Kogut and Singh 1988; Li and Guisinger 1992). For a variety of reasons, most of which are related to the political, legal, and economic situation that characterizes the society in which a multinational is based, national culture and mode of intervention are strongly correlated. U.S. firms tend to acquire foreign firms or plants, as occurred in this case study, and tend to place the burden of adaptation on members of the acquired firm/plant rather than accepting that burden themselves (Hofstede 2001; Laurent 1978). In addition, U.S. managers tend to operate on a “one-size-fits-all” approach to day-to-day operations, insisting on using the same strategies and practices that have proven to be successful in other operations (Newman and Nollen 1996). When workers do resist change, supervisors tend to attribute their opposition to inadequate training and/or education, even when change is based on insightful analysis of problems with the new program or the way it is being implemented.

Although there are notable examples of U.S. firms successfully overcoming these tendencies, albeit often after an initial period of cross-cultural conflict and communication breakdown (e.g., Mann 1989), and there is also evidence that past experience operating in the culture of the acquired firm (or in similar cultures) increases the potential for a successful acquisition, U.S. firms face a unique set of culture-related challenges when they acquire firms or plants in different national cultures.

The potential for resistance is increased by differences in cultural assumptions within organizations. Hofstede (2001) and others have argued that the most important dimension that differentiates national cultures is Uncertainty Avoidance (UA), the intensity with which each culture's members feel a need to avoid uncertainty and the means through which they do so. Unlike fear and risk, which are focused on specific, known threats, anxiety and uncertainty are diffuse feelings of concern for the future.

In general, "technology" (broadly defined as any human artifact) protects people against uncertainties caused by nature, law defends against uncertainty caused by other people, and religion defends people against uncertainties they cannot understand. Organizations manage uncertainties in their environments by taking a short-term, reactive orientation and by attempting to negotiate protective arrangements with sources of environmental uncertainty (e.g., becoming a monopoly or part of an oligopoly, encouraging the creation of protective tariffs or restrictions on competitors). Organizations manage internal sources of uncertainty through the creation of rules of behavior, bureaucratic structures, and rituals (Cyert and March 1963). Cross-cultural differences in either the intensity of feelings of uncertainty avoidance or in terms of mechanisms for managing uncertainty are especially difficult to manage (Hofstede 2001). For example, rules are used to manage uncertainty in all cultures. But if rules mean different things in different countries, it is difficult to keep the organization together. In cultures like the United States managers and nonmanagers alike feel definitely uncomfortable with systems of rigid rules, especially if it is evident that many of these rules are never followed. In cultures like most of the Latin world, people feel equally uncomfortable without the structure of a system of rules, even if many of the rules are impractical. At either pole of the uncertainty avoidance dimension, people's feelings are fed by deep psychological needs related to the control of aggression and to basic security in the face of the unknown (Hofstede 2001, p. 442).

Change may be very destabilizing, especially if it is unstructured, unclear, ambiguous, or makes employees' futures with the organization more tenuous. Even the act of planning for change is negatively valued because it increases uncertainty.

The second important cultural difference involves "Power Distance" (PD), the extent to which members of a society view inequalities in power, wealth, and influence as inevitable, just, and positive in that they foster social stability or as a social problem that needs to be minimized or overcome. The United States is a relatively low PD society; Mexico has one of the highest PD scores among the nations that Hofstede and his successors have studied. Moreover, the PD scores of relatively uneducated Mexican workers in routine jobs are significantly higher than the Mexican average (Hofstede 2001, pp. 88-90). At first glance, this relationship suggests that Mexican workers would readily accept changes imposed from the top of their organizations. However, research using the PD concept has found more complex relationships. First, in high-PD societies, employees' primary ties are to groups with which they are highly familiar and closely affiliated. These 'in-groups' include other people from their families or with the same backgrounds, training, class, and experience (Zurcher, Meadow, and Zurcher 1965). Security stems from these relationships, not from organizational rules or structures. Consequently, change is acceptable if it is supported by dominant members of workers' in-groups; it is likely to be resisted if imposed by members of "out-groups", especially if the out-group is composed of foreigners or members of a different race. Organizational policies and practices must be legitimized in terms of the values of the workers' in-group, and must be accepted by ranking members of that group (Hofstede 2001, p. 97). Decision making is expected to be personal and political, rather than "strategic" or "rational", and filtered through dominant in-group members.

Organizational theorist Stewart Clegg (1989) (also see Hobbes 1962) has pointed out that as early as the Renaissance Western society grappled with two very different views of social power. One view, based on the ideas of Thomas Hobbes, depicts power and decision making as unemotional, scientific processes. Decision makers function as dispassionate legislators, making rational choices among alternative courses of action. Described in mechanistic terms, decisions, and the inevitable exercise of power that accompanies them, are legitimate if they fulfill the standards of science. When applied to organizations, this perspective suggests that managers should think strategically, rather than politically, and act via plans that are guides by formal rules. Subordinates will be persuaded to accept managers' decisions through rational processes of bargaining and reasoning based on practical considerations. When policies or programs fail, the outcome is attributed to systemic factors.

Alternatively, a Machiavellian perspective views power and decision making as inherently political, strategic processes. Decision makers take on the role of an interpreter of multiple, conflicting political pressures. Power is located in patterns of coalitions and interpersonal relationships, and its exercise is legitimate if doing so successfully manages those pressures. Managers persuade their subordinates through relational appeals and rely on interpersonal ties with their subordinates to obtain support for their decisions. In high-PD, Machievellian societies, when policies or programs fail, the person(s) at the top of the organization is assumed to be responsible for those failures (Hofstede 2001, p. 382). Over time, Hobbesian views of power came to dominate the low-PD cultures of Britain and northern Europe; Machiavellian perspectives were more acceptable in high-PD cultures such as those of southern Europe and the Mediterranean (Hofstede 2001, chap. 3).

Consequently, the acquisition of the particular plant by a U.S. multinational promised to be exceptionally challenging. Typical methods of managing acquisitions, while consistent with U.S. cultural norms, are very much incongruent with the interpretive frames of employees in the acquired firm. Those differences, and the standard acquisition process, are likely to create high levels of uncertainty and anxiety for employees whose national culture makes uncertainty avoidance paramount. There are, however, cultural characteristics that the acquiring company could use to facilitate the transition. For example establishing a more personal relationship between supervisors and workers is particularly important to establish loyalty between them. Also, everyone works mainly to get the money to live a life they can enjoy; hence, if the company relates the system objectives with an economic benefit to the employees, they are likely to work harder to achieve them. Training is fundamental for the implementation of new systems. Companies should invest heavily on training if they want to succeed. For instance, relative to Americans, Mexicans are initially more reluctant to work with a stranger; however, once trust is developed they will be very loyal to the team. This suggests the importance of team training, in particular on team formation stages, when dealing with foreign companies.

Cultural differences do not doom acquisitions to failure; instead, the differences suggest that cultural sensitivity and cultural adaptation by both parties is especially important to the success of the venture.

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