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Who Will Produce the Next GloCo?

We assess which industries are most—and least—likely to produce a successful global company (GloCo)

Who stands to benefit most from globalization? Last summer, in *Getting Globalization Right: Meeting the Challenge of the Century,* (Global Economics Paper No.95, 23 July 2003), we identified eight criteria that we consider vital to the success of a truly global company, or GloCo. We discussed the criteria by looking at a list of international firms selected by our equity sales force.

Building on our earlier work on globalization, we now identify which industries are most—and least—likely to produce a GloCo. These are not necessarily the industries dominating our initial list of companies, which was designed to be illustrative rather than definitive.

Looking at globalization from an industry perspective rather than a company perspective is not merely a question of seeing which sectors have moved more rapidly than others. Industries vary significantly in their ability to capitalize on the opportunities afforded by globalization.

Some—like financial services, technology, media and entertainment and perhaps retail—are well positioned to generate successful GloCos. Others—like autos and airlines—are hampered by structural problems that will prevent them from ever developing real GloCos. Many industries fall somewhere in the middle, meaning that skillful and nimble companies will stand a good chance.

What Makes a Successful Global Company?

We define globalization as the integration of capital markets, trade, production process and political and social interactions that results in the export and import of best practices.

We discuss our criteria for a successful global company, or GloCo, in detail in CEO Confidential Issue 2003/10, August 2003. This report is available at www.gs.com/ceoconfidential/ceoprev.html

To capitalize on the opportunities globalization affords, we think GloCo will need to meet most of eight criteria:

- A strategy for globalization;
- Global brand;
- Localness;
- Flexibility;
- Use of technology to integrate the business;
- Employee-friendly workplace practices;
- A strategy for China and other major developing economies; and
- Meaningful social engagement at the local level.

In thinking about which industries are and are not likely to produce a GloCo, we have divided our criteria into three pools.

Cross-sector criteria can fairly easily be achieved by a range of industries; these include social good, employee-friendly workplace practices and a strategy for key emerging markets.

Custom-made criteria, namely technology and brand, are more difficult for all industries to achieve but still possible.

Finally, strategy, localness and flexibility are **criteria specific to certain sectors.** We think they are potentially impossible for some industries to achieve**.**

Cross-Sector Criteria

Three criteria—social good, employee-friendly workplace practices and a strategy for China and key emerging markets—seem to be areas where any firm in any industry can develop a robust program.

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Take **social good.** In our earlier paper, we discussed ways in which companies can promote social good in local communities: by donating money or services to charities; by providing their own goods and services; and by using corporate expertise to address social questions directly. Examples include pharmaceutical firms providing medicine at low or no cost; financial services firms teaching financial literacy; tech firms providing computers and software to local schools and non-profits; and retail firms offering their distribution networks to spread medicine and AIDS education.

The exact content of these initiatives will vary across industries—and it should, as each industry and each company focuses its own competitive advantages. But there is no reason that even the most 'aloof' industries, like natural resources, cannot implement some kind of program. In fact, social good programs may be even more important to these industries and may help these companies make progress on other GloCo metrics, like localness.

Who Meets the Challenge of the Century: Potential GloCos'
American International Group, Inc. (AIG)
BP plc
Cisco Systems, Inc.
Citigroup Inc.
Coca-Cola Company
Dell Computer Corporation
General Electric Company (GE)
GlaxoSmithKline plc (GSK)
HSBC Holdings plc
Hyundai Corporation
IBM
Microsoft Corporation
Nestlé S.A.
Nike, Inc.
Nokia Corporation
PetroChina Company Limited
Pfizer Inc
Procter & Gamble Company (P&G)
Rio Tinto Group
Samsung Corporation
SAP
Sony Corporation
Unilever
Vodafone AG
Volkswagen AG (VW)
Wal-Mart Stores, Inc.

Note: This is a list of companies we identified in a survey of the GS equity sales force and presented in our earlier paper. We do not think these are not the only firms that stand to benefit from globalization.

Similarly, all industries can have **employee-friendly workplace practices.** Again, the specific policies will vary, but the key is that each industry can take steps to ensure that employees feel valued. This too has important spillover effects into other GloCo metrics, including localness and the perception of a firm's global brand.

We also think all industries can have a **strategy for China and other key emerging markets.** Although many, if not most, GloCos will pursue China's low-cost production facilities or its consumer markets (or both), others may, entirely appropriately, decide not to make this market a major focus.

- Pharmaceutical firms may decide that intellectual property and pricing concerns make these markets unattractive for now.
- Luxury goods firms may opt to treat emerging markets as targets for the more distant future and focus on key regional tourist markets for the foreseeable future.
- Industries offering commodity products may find that pricing pressures in developing countries severely constrain the opportunities available.

What matters for a GloCo is that the decision be rigorously made and well-executed.

Custom-Made Criteria

Two other criteria—technology and global brand—are more variable for a range of industries.

Technology is important for any would-be GloCo because it allows global coordination on an unprecedented scale, giving skillful users a clear competitive advantage. Technology can alter business processes and organizational structures to enhance productivity. This has clear advantages for industries, like tech, pharmaceuticals and financial services, which offer more or less the 'same' product around the world.

But technology may be less helpful for other industries that sell more diverse goods or services. The example of Unilever guided our thinking here. Because its products vary greatly across and even within regions, Unilever has less need for a comprehensive, granular tech systems than does a firm like Microsoft.

This is true for many firms in the food and personal care industry, which our equity research analyst thinks could well exist as a set of regional firms instead of global ones. In some cases, deep technological integration may even be counter-productive if it hinders companies from developing the flexibility to address varied market conditions.

Brand is also complicated. Conventional wisdom holds that a global brand is essential to globalization, but the reality among major global firms is more complex.

Brand does appear to be very important for would-be GloCos in the financial services and tech industries. But it is less so for food (where brands are regional, not global), pharmaceuticals (where drug names seem to matter more than company names), retail (even Wal-Mart retains some of the brand names it acquires) and natural resources (where our analysts say brand is relatively unimportant across the board).

In other industries, it seems fair to say that a strong brand is important, but that it is not essential (and in some cases not advisable) to have a uniform brand around the world. Flexibility and localness, two important GloCo characteristics we discuss below, can trump the importance of brand for some industries. Consistent global standards can be just as effective but allow more flexibility in the actual branding.

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Sector-Specific Criteria

Our final three criteria—strategy for globalization, flexibility and localness—seem to us to be the hardest for all industries to achieve. Some industries are likely to find them impossible.

A **strategy for globalization** seems an obvious criterion for GloCo, but our interviews thought leaders on globalization and equity research analysts suggest that this is anything but simple.

The most successful global companies see every facet of their business through the lens of globalization—manufacturing, distribution, pricing, hiring, workplace policies, management, etc. GloCo must be willing to adapt its strategy over time, and in some cases to radically overhaul it. Many of the most promising GloCo candidates on our original list—including Samsung and Vodafone—had gone through several strategies for globalization before settling on their current plans.

Although establishing and executing a globalization strategy is up to company management, heavily regulated industries face structural constraints on their ability to be truly global.

Airlines spring immediately to mind. National legislation prevents the consolidation and competition needed to create global airlines, forcing companies (and their customers) to make do with a series of alliances. Natural resources firms are also subject to legal and political constraints that may hinder their ability to be truly global—although this appears to be less true now than in the past.

We have stressed the need for GloCo to look and feel **'local,'** with local management and staff and products geared to local tastes. This is one of the most difficult issues for many industries.

Industries requiring extensive local distribution networks are more likely to be seen as local. Financial services, pharmaceuticals, retail, personal care and food must do extensive local hiring and tend to rely on local knowledge to market their products. Although pharmaceuticals and financial products do not differ greatly across markets, retail goods, food and personal care goods do and thus must be tailored to local tastes. Thoughtful customization boosts the chances of success as a GloCo.

Telecommunications and utilities are typically seen as local by default, primarily because of their historical development as monopolies.

In contrast, natural resources companies, operating in isolated areas, usually staffed by foreign workers and often engaged in businesses that do not touch local consumers, are unlikely ever to be seen as truly local. Airlines, with their history of national carriers, are also likely to remain 'foreign' even when they have global operations. But autos seems to be moving away from its history of national champions as production facilities spread around the world and brands become more global.

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Retail and media can both be local, by customizing their products and distribution. But too much customization runs the risk of undermining the economies of scale that make globalization attractive in the first place. Wal-Mart, one of the stand-outs from our earlier paper, has done a very good job in this, although other retailers have struggled.

We think media and entertainment firms are potentially well-placed to become GloCos. With their global reach, strong brands and technological integration, the key challenge is likely to be achieving the necessary degree of local content and image. Because local tastes matter greatly in entertainment, some customization seems essential. Too much, again, risks diluting economies of scale.

We define **flexibility** as the ability to spread best practices around the firm and to adapt business practices to diverse local contexts. Key issues include attention to spreading best practices; the degree of regulatory risk; and the willingness and ability to undertake transformational change.

Transformational change is the ultimate expression of flexibility, seen in the rise of Nokia and Vodafone. Samsung and Hyundai are undergoing similar transformations in the wake of the Asian financial crisis. It is hard to imagine many firms in industries like autos and airlines, hindered by regulation and politics, undergoing similar shifts.

Regulatory risk, which is typically higher in emerging markets, is a particular problem for the natural resources, pharmaceuticals, tech and telecom industries, as well as for those that rely heavily on intellectual property. Natural resources firms seem to regard regulatory risk as a manageable cost of doing business, but weak protection of intellectual property rights can be a major constraint for tech and media firms.

Regulation—in the form of strict employment rights or political pressure not to close down unprofitable operations —can be an obstacle to all industries seeking to shift production to lower-cost locations. Autos, aerospace and defense, financial services and pharmaceuticals are most vulnerable to this pressure. Their international acquisition plans may also face softer barriers from governments intent on bolstering national champions.

Where Will We Find the Next GloCo?

Of our eight criteria, we think strategy for globalization, localness and strategy for key emerging markets are the most important in determining which industries can and cannot produce GloCo. Financial services, technology, media and entertainment and perhaps retail seem to us the best placed on these metrics. Autos, airlines and defence face tough political and regulatory constraints that should keep them as regional players at best.

Overall, we would focus the search for GloCo on service sectors rather than manufacturers. Globalization in services has lagged manufacturing, which has been the focus of trade liberalization efforts for decades.

Now that liberalization of services is firmly on the agenda, services offer much greater potential upside in the years ahead. Political acrimony, like the recent rhetoric about stepped-up trade protectionism, may slow—but should not derail—the steady efforts of companies in the best-placed industries.

Yet globalization is probably not the best choice for all industries—at least right now. Weak protection of intellectual property rights and low disposable incomes will continue to make emerging economies unattractive to industries like pharmaceuticals, healthcare and luxury goods for several years. And some industries, like food and personal care, may find that a regional focus works better than a global strategy. ■