

## Q&A

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**PANKAJ GHEMAWAT**  
PROFESSOR OF GLOBAL STRATEGY AT IESE

ANTHEA MILNES DISCUSSES  
DISTANCE AND DIFFERENCE WITH  
PROFESSOR PANKAJ GHEMAWAT,  
AUTHOR OF “REDEFINING GLOBAL  
STRATEGY”.



**Q** Why do you take issue with the thesis Thomas Friedman expresses in his book “The World is Flat”?

**A** I take issue with “The World is Flat” for two basic reasons: one is, it isn’t so; and second, if it were, most of the problems

that managers face in crossing borders wouldn’t exist. So “the world is flat” can’t possibly be a helpful prescription for how to do international strategy.

When you look at trade that could occur either within countries or across country borders, and look at the cross-border component as a percentage of the total, you typically end up with figures in the 10 to 20 per cent range, rather than the 90 to 100 per cent range you might expect if borders didn’t matter at all.

**Q** What kinds of mistakes have companies made by assuming the world is flat?

**A** What’s interesting to me is the extent to which excessive belief in the flatness or openness of the world economy can lead to problems, even in companies that are very sophisticated along other dimensions.

Take Wal-Mart. A couple of years ago when Lee Scott, the CEO, was asked what made him think Wal-Mart could be

successful internationally, his response was effectively, “If we can move from Arkansas to Alabama, how different can Argentina be?” And if you juxtapose that against Wal-Mart’s profitability in 2004 in its foreign markets, you see almost a perfect negative correlation between distance from Bentonville, where Wal-Mart is based, and profitability.

Another example is Microsoft. On Bill Gates’s first visit to China, he went to the Great Hall of the People and gave a lecture arguing that it was wrong and irresponsible for governments to select standards, and that the market should decide. This didn’t go down well, and Gates later admitted it took them ten years and cost them a couple of billion dollars in losses to figure out they need to work differently with the Chinese government than with the US government.

It sounds trite to say countries are different, but these notions of the flattening of the world, the death of distance, the end of the nation state, and so on, are deeply embedded in our psyches.

**Q** What do you mean by semi-globalisation?

**A** If the world were completely composed of isolated countries, obviously you wouldn’t need global strategies, individual country strategies could work just fine; and if the world were

completely integrated, we would have one giant country, and presumably all our single market frameworks would continue to apply. It’s precisely because we inhabit the messy middle ground between these two polar extremes, that some thinking is required.

**Q** Can you explain your concept of the four different types of distance that strategy-makers should consider?

**A** Borders clearly matter, but not all borders matter as much as each other. Hundreds of statistical studies have been done identifying the impact of factors like language, religion, or the legal system, on cross-border interactions. What I’ve been trying to do, rather than come up with a list of 30 variables, is to group them into categories that are helpful to my students.

So I talk about the CAGE framework for thinking about distance – that is an acronym for “cultural distance”, “administrative (political) distance”, “geographic distance”, and “economic distance”. All these factors have been shown to have significant negative impacts on overall cross-border activity. In terms of applying these notions of distance to strategy, the first thing to do is to start with your industry and figure out which of these generic categories matter the most.

**Q** Which companies are combining local sensitivity with global scale successfully?

**A** I think Procter and Gamble is a very interesting balancing act. They’re trying to tap more scale economies than Unilever but without entirely ceding the high ground to Unilever in terms of local sensitivity. I would use them to demonstrate that there are different mixes of emphasis possible, even within the same industry.

This trade-off between local responsiveness and global scale economies is probably the most widely established strategic dichotomy in international business. We’ve had it for more than 40 years now, and it’s a somewhat limiting way of thinking about international strategy.

Local responsiveness is the idea of adjusting to differences, while global scale economies is the idea of aggregating by overcoming differences. But differences aren’t just constraints to be adjusted to or overcome, they can sometimes be enormous sources of value creation.

**Q** How has the recession affected regionalisation and globalisation?

**A** The crisis has really affected the conversation in the sense that there are far fewer people who argue, as Friedman did in “The World Is Flat”, that government is withering away. So, there’s less need to convince people that the world isn’t flat, and there’s much more interest in trying to figure out what to do about differences.

Companies have figured out that, given the changing macroeconomic picture, emerging markets are going to account for an even greater share of global growth than they were projected to before the crisis. So, if you look at the foreign direct investment projections for this year, for developing countries they are down, but not nearly as much as for developed countries. So, proportionately markets like China and India look much more interesting than they did a year or two ago.

**Q** Has there been a move towards protectionism?

**A** There’s a group called Global Trade Alert based out of London that compiles statistics on this. Their data show that we’ve seen some protectionism, but what I’m really worried about is that what we’ve seen is not nearly as bad as things could get. The real economy, as opposed to the financial economy, continues to look very problematic, particularly in terms of the unemployment statistics.

I have a very simple forecasting model about protectionism; the key variable is unemployment. There is a point past which, if unemployment stays above that level for a certain length of time, all bets are off in terms of policy measures that might be taken – including protectionism.

**Q** Do you have an ethical stance on globalisation?

**A** If we focus on the real economy, as opposed to the financial economy, what will pull us out of this depression that we’re in, is more rather than less integration. What would certainly compound the agony would be moves towards protectionism. So I’m a believer in globalisation; I’m also a believer in protecting people, but the point is, you protect people and not jobs.

**Q** Are business schools teaching strategy the right way?

**A** Business schools talk a great deal about globalisation, but when you look at what schools are doing, there’s a very heavy emphasis on diversity – on attracting people from around the world, and a very heavy emphasis on mobility – taking them to different locations, but without any corresponding specificity on what the content of actual courses should be.

Pankaj Ghemawat gave a McKinsey seminar at the Saïd Business School on 26 November 2009 on the subject of crossing borders in a world where difference still matters.