Exam International Business (188080)

Date: April 3, 2008 Time: 13.30 – 17.00 p.m.

This exam consists of **6 questions**. Each (sub-)question of this exam will be graded with a maximum of points, as indicated behind each question. In total, on questions 1-6 (including sub-questions) you can score a maximum of **90 points,** which equals the **grade 10**. Attached to this exam the article *Supplying auto parts to the world (McKinsey Quarterly, 2004)* can be found *(see p.3, 4 & 5).* **Carefully read this article** before answering the questions. You can make use of a dictionary. You may answer both in English and Dutch.

Question 1; introduction in International Business

In the book and during the second lecture, 7 global dimensions have been discussed. Name these dimensions and apply them to the company Wanxiang, China's largest maker of auto parts (see article p. 3-5) **15 points**

Question 2; introduction in International Business (continued)

Apply the International Business Model (p.26 of the 11th, p.23 of the 10th edition, Ball & McCulloch) on the company Wanxiang, China's largest maker of auto parts (see article p. 3-5). In case you cannot find relevant information in the article (see p.3 and further) to connect practice to theory, give fictitious examples and give arguments why you choose these examples. **20 points**

Question 3

Is the Hechscher Ohlin theory of Factor Endowment applicable on the operations of the company Wanxiang? Explain. **5 points**

Question 4; International institutions

a. What is the World Trade Organisation (WTO) about? Mention 4 focuspoints. **5 points**
b. During the 5th lecture, 5 Important policies of the WTO for business have been discussed. Name them and explain which one is the most important for Wanxiang, directly and/or indirectly (if at all). **10 points**
c. In the book and during the lectures, the role of the OPEC is discussed in line with the importance for International Business. What is this importance? Explain. **10 points**

Question 5

In what way(s) is or could Wanxiang be influenced by the BOP-deficit of the USA regarding their operations in China and the USA? Explain. **15 points**

Question 6

In chapter 8, (socio)economic forces, amongst others **Income distribution, Private consumption and Gross Domestic Investment,** are discussed.

a. mention the remaining 5 Economic (not; socio-economic) forces **5 points**
b. Which of the forces mentioned in your answer of 6a is most prominently present force in the article on Wanxiang (p.3 -5)? Explain **5 points**

End of questions; attention, page 3-5; article *Supplying auto parts to the world* (McKinsey Quarterly, 2004)

Supplying auto parts to the world

Lu Guanqiu, the founder of China's third-largest private company, discusses the future of China's automotive industry.

Thanks to a strong economy and falling automobile prices, more and more consumers in China are plunking down money for their first car. With 20 percent annual sales growth expected through 2007, China is on track to become the world's third-largest market for autos, after the United States and Japan. One company that seems well positioned to tap into this growth is Wanxiang, China's largest maker of auto parts.

Wanxiang started out in 1969, with barely $500 in capital, as a repair shop for bicycles and farm tractors. Now it is China's third-largest privately owned company. Wanxiang, based near Hangzhou, in Zhejiang province, controls or has stakes in 100 companies, both in China and overseas, e.g. in the USA and the UK, that deal primarily in auto parts. Last year, it earned $165 million in pretax profits on $1.8 billion of sales, including $380 million in parts exported or produced abroad. The company employs 31,800 people, 920 of them in the United States and Europe.

There are challenges, however. A global glut of production capacity is forcing automakers to put heavy pressure on suppliers to reduce costs. In China, seven new companies have entered the auto market since 2001, and several more have announced plans to do so. Once this new production capacity comes on line, utilization at auto factories with foreign investment could dip below 60 percent, so automakers would put even more pressure on their suppliers to reduce prices. And although Wanxiang does have a labor cost advantage over many of its auto parts competitors in the West, the competitors have strengths of their own, such as more advanced technology and much larger scale.

But Lu Guanqiu, Wanxiang's founder, continues to see opportunity in the face of difficulties. For the past several years, he has been on an acquisition spree, buying auto parts makers in the United States and Europe to plug gaps in his company's technology, markets, and brands. To tap into businesses with higher profit margins and funnel funds back into the core auto parts business, Wanxiang has also acquired stakes in several services firms. In addition, Lu is hatching plans to fuel growth and profits by building a complete automobile, with the ultimate goal of manufacturing autos bearing the Wanxiang brand. An important part of his strategy is the development of an electric car, which he hopes will help address the problems of higher fossil-fuel consumption and air pollution. Whether or not he eventually succeeds in moving his company up the value chain, Lu is still committed to his core auto parts business: "As long as cars are being made somewhere in the world, we'll be making parts."

Lu Guanqiu discussed his company's prospects in an interview with Paul Gao, a principal in McKinsey's Shanghai office.

The *Quarterly*: *What events have had the biggest impact on your business?*

Lu Guanqiu: The first occurred in the early 1980s, when Wanxiang cut the number of products it made. The whole country's manufacturing industries were restructuring. This was aimed at state-owned enterprises, but Wanxiang wasn't one of them and wasn't asked to participate. We decided to take advantage of the opportunity to change, however, and initiated our own restructuring. We discarded our diversification strategy, which had grown out of the economic shortages of the 1970s. Wanxiang was involved with so many products: castings, drills, pumps, agricultural equipment. The company took an ax to all of them.

We decided to concentrate our human, financial, and material resources on building Wanxiang into a company specializing in universal joints.[1] Costs went down, quality went up, and the impact on customers was enormous. Of the 56 makers of universal joints at the time, Wanxiang is 1 of only 3 that survived. Building on this base, we gradually developed our technology, products, and markets and became an industry-leading company that produced everything from auto parts to system parts. The second major event occurred in 1984, the year Wanxiang entered the US market. That was a turning point for us. It was then that we began the process of exploration and experience that I describe as "stepping out and bringing in." We brought our products and our people into the world, and in learning about the world we discovered our own shortcomings.

At the time, government policy strictly forbade us to operate outside of China. It absolutely would not allow us to take money out of the country. Nor could our people leave. And we couldn't export products. We thought of every way we could to create a shortcut that would allow us to get into international markets. We borrowed money from friends. We used various channels to export our products. Once we made it to the outside world—once we saw just how big the gaps between us and the outside world really were—we were just stunned.

The *Quarterly*: *How did you respond?*

Lu Guanqiu: We eliminated our most unsophisticated products, outdated equipment, and underperforming employees. We imported high-precision equipment, developed a pool of high-quality talent, and focused on producing high-quality products. By improving the overall quality of Wanxiang, we built the foundation for our future progress. Today we've acquired, merged with, or established 30 companies in eight countries, including the United States, England, Germany, Canada, and Australia. We have sole ownership or control over 18 of these. We sell our products to world-class automakers like General Motors and Ford. We have established strategic alliances with companies like Bosch and Delphi.

The *Quarterly*: *What are your long-term aspirations for Wanxiang, and what management approaches do you follow to achieve your goals?*

Lu Guanqiu: Wanxiang's corporate credo is, "Create value for the customer, create profit for the shareholders, create a future for the employees, create prosperity for society." To realize these aspirations, we've defined our company's mission as a "struggle to add a zero every ten years." In the 1970s, we earned 10,000 renminbi[2] a day in profits. The most any worker earned in a year was 10,000 renminbi. In the 1980s, we earned profits of 100,000 renminbi a day. The most any worker earned was 100,000 renminbi. In the 1990s, we earned profits of 1,000,000 renminbi a day. The highest-paid worker also earned 1,000,000 renminbi. In 2009, when the company turns 40, we plan to earn profits of 10,000,000 renminbi a day, with the highest-paid worker earning 10,000,000 renminbi a year.

Above all, this is an easily understandable goal. It's also a way to link the interests of our employees tightly to those of the company. The employees can see and touch our company's goals and therefore believe in them. If all of the company's employees hold these goals close to their hearts, they will be able to think like owners, live like owners, take responsibility like owners, and, finally, experience the enjoyment of being owners.

I believe in speaking the truth and being practical in business. Seek truth from the facts, don't spout slogans about being able to do more than you really can, don't do things that exceed your ability. Take it one step at a time. As Chairman Mao once said, "Produce an inch and improve your life by an inch." You need to be consistent in word and deed when dealing with employees. When you speak, follow through with action; when you take action, it must produce a result. Once a company loses its reputation, even the best will collapse like a house made of twigs, no matter how good its products or how great its technology.

The *Quarterly*: *What is your view of the new investment pouring into China's auto industry and of the potential for oversupply?*

Lu Guanqiu: You might have oversupply in total production volume, but total demand is still growing. It's just a matter of how fast or slow this rate of growth is. A period when supply can't keep up with demand might conceal some of the problems of the weaker companies. When there is oversupply, the companies that really get hit hardest are the weaker ones. For the strong companies, there will never be the problem of oversupply. It's when supply exceeds demand that you find out which companies can really compete. As long as cars are being made somewhere in the world, we'll be making parts. If some companies fail, at least I'll be the last one to go.

The *Quarterly*: *How do your acquisitions fit into your growth strategy?*

Lu Guanqiu: The companies we've acquired overseas aren't simply acquisitions. It's really about pooling international resources. We'll combine whatever resources we can find to become a company that operates on a multinational basis, using the most advanced technology and playing in the key markets of the world. For instance, we acquired Schiller, Universal Automotive Industries, and Rockford Powertrain, among other companies, because they have what we lack most: markets, technology, and brands. The weakness of these companies is rising labor costs. Our strengths lie in our labor. We use a lot of labor for low-value-added products. We can bring these companies' low-value-added products to China and make them here while keeping the high-value-added goods over there. So by combining with these companies, we bring costs down and improve efficiency. This is how we could penetrate GM, Ford, and other major companies and markets so successfully. Everyone wins in the process.

Wanxiang will combine with companies in industries related to auto parts. Perhaps we'll take these companies' market share, add it to ours, and combine our resources in an optimal way. It's our way of contributing to society by providing jobs and supporting economic growth while building the base for a stronger company. Alliances are the fastest, lowest-cost way to grow.

The *Quarterly*: *But you've also made domestic and foreign acquisitions in areas, such as finance and insurance, beyond your core business. Could Wanxiang lose focus again?*

Lu Guanqiu: There are examples of successful diversification and examples of failures. There are examples of successful specialization and examples of failures too. The answer is to look at your company's abilities and understand what you're best suited to do. If we continued to diversify as we did in the 1970s and early 1980s, we would have ended up with nothing. And if Wanxiang today had only a single product, we wouldn't have built up our company to the scale it has reached today.

The industry we're in—auto parts—is really hard these days. It's a capital-intensive, labor-intensive, technology-driven business with very thin profits. You can't get rich in this business. If you want to do really well in it, you must expand volume, you must specialize, you must become more professional. But relying entirely on your own strength as an auto parts company will limit you. There's no way you can continue on your own to grow each year by more than 25 percent. So I've cultivated a group of talented professionals to bring the company into other businesses. This is Wanxiang's biggest resource. Through these talented individuals, we can get into services businesses that ultimately serve the auto parts business. If we can make a little money in them, we'll do so. But they are not my primary business. We'll plow the money we earn from them back into our core auto parts business.

The *Quarterly*: *How do you attract and cultivate talent?*

Lu Guanqiu: In the past, investing in "software" always took second place to investing in "hardware." So while we put a lot of investment into factories and equipment, we invested little in developing our human resources. The failure to prepare enough high-quality talent constrains our growth today.

In the early 1980s, we sent 44 people to college for training. We also recruited heavily. This group now forms the core of our leadership. But it's not enough. We have capital; I can buy technology; I can buy management. We've got a complete line of products. Sales—we can't supply enough products to keep up with demand. Given such rapid growth, the biggest bottleneck to our development has become human resources. It's the one factor that works against our development. You can't see the effects in a year or so; you definitely need 10, 15 years or even longer. Outstanding people can develop new products. We don't have enough outstanding talent, and that slows down the pace of our development.

The *Quarterly*: *How do you manage the relationship between family managers and professional managers?*

Lu Guanqiu: When you manage a business, it all comes down to the quality of your people. In Chinese we have a saying that goes something like, "Keep an open mind when deciding whether to nominate your son or an outsider for a position." When I recommend hiring someone, the key thing I look for is ability. It doesn't matter whether it's your own son or a relative—I don't care. If you are using a really outstanding person, you can't go wrong. If you make a mistake, it doesn't matter whether it's a relative or an outsider; the person will have to step down.

I'm always practical in business. I have a son. Between two candidates, if one is an outsider and one is my son, and they are more or less the same, I'll use my son. I once read that of the top 500 global companies, family companies make up 40 percent. In family-run companies, you have professional managers, but aren't they all family too?