

**University of St.Gallen**

# **CONTEXTUAL INTELLIGENCE: CHINA**

## **HQ-Subsidiary Relationship Design**

**Prof. Dr. Roger Moser**

*Assistant-Professor of International Management &  
Director, ASIA CONNECT Center, University of St.Gallen*

# HQ-Subsidiary Relationship Design

## Introduction

- China is a highly dynamic market that offers a lot of uncertainty and ambiguity to anybody operating there.
- For Western executives, it is very difficult to understand which rules really apply in China.
- Draft & Weick (1984, p. 287) explain this situation in China with the following story:

*Let's imagine a game with 20 questions («20 Questions»), where one person/group leaves the room while the others who stay in the room choose a word that the person/group needs to find when he/she/they return. The only hint given is whether the word describes an animal, mineral or vegetable. The questions the person/group asks can only be answered with YES or NO. In this game, each question should be well chosen to provide new information.*

Draft & Weick link this concept to how companies operate. Executives have limited time and a lot of questions but only limited resources to find answers.

*If we now take another situation where the people left in the room change the rules of the game and decide that they will not choose any word. Instead, they will just answer with YES or NO as it pleases them; provided that the answers don't contradict with each other. In such a situation, the person/group that comes back into the room is trying to identify a word that actually has never been chosen. E.g. if the person/group finally believes the chosen word is «A» then the group will simply confirm that it actually is «A». The person/group then thinks they actually won the game but actually they never played the same game as the group providing the answers.*

This story often mirrors the reality in China when Western companies believe they are playing a game with a set of rules while they actually do not even know the rules.

# HQ-Subsidiary Relationship Design

## Introduction

- Western companies need to consider the following if they consider to operate in China:
  - Individuals in China need to give priority and loyalty to families and close friends first because the pressure from parents, spouses and the extended family is much stronger than in Western countries.
  - This implies that a supervisor's decision is mostly interpreted according to an employee's personal priorities – whether it is to provide better financial stability to parents or his/her personal status in order to give face to the family.
  - It might also happen that an employee supports a manager whose goals differ from a company's priorities – for example, if the manager is a close friend of the family or if the employee has some sort of social or professional debt.
  - In most cases, the loyalty of a Chinese employee can be associated with the direct supervisor – not with a more senior executive or the company as a whole.
- In order to put these considerations into practice, we have developed a morphological box that allows executives to take numerous aspects into consideration in order to design their relationship between HQ and its Chinese subsidiary.

# HQ-Subsidiary Relationship Design

## Criteria Description

Criteria	Option 1	Option 2	Option 3	Option 4	Option 5
<b>Size of Company</b>	Traditional differentiation between multinational companies (MNCs), medium-sized companies that have some assets in foreign countries and small companies with most or all resources in the domestic/regional market				
<b>Function</b>	Traditional classification of departments in a company that are often essential in operations between HQ and subsidiary (not exhaustive).				
<b>HQ Philosophy towards Subsidiaries</b>	Description of the general attitude and expectations of HQ towards the subsidiary in China. The attitude can vary from a negative feeling of having made a mistake to invest in China to a situation where the subsidiary carries the hopes of the company for future financial health – along with the respective attention from HQ and pressure to perform.				
<b>Target for Subsidiary in China</b>	It can vary from early expansion to maximising profits or increasing market share growth as well as finally also downsize/merge offices or outsource operations from China.				
<b>Employee's main Task in Subsidiary</b>	This parameter refers to the main objective of the employee. Some employees are hired to solely increase the sales of a company while others are hired to improve the management practice standards or ensure compliance or improve the innovativeness of the local staff in China.				
<b>Primary Focus of Subsidiary in China</b>	The primary activity focus of a subsidiary varies not only depending on strategies but also depending on industries. E.g. luxury brands will mostly be in China for sales while the textile industry might have a strong focus on sourcing. Manufacturers might focus on local production for local/global markets while the pharma industry might not only push sales but also R&D capabilities.				
<b>Decision Process</b>	The decision process includes the flexibility and autonomy given to the subsidiary. E.g. some HQs try to maintain a high level of control including HR staff budgets or marketing content while others leave all decisions to the local management team.				
<b>Compliance &amp; Transparency</b>	Compliance refers to the importance of respecting the internal compliance policies of a company and its enforcement (e.g. reporting but also ethics and transparency in conducting business in China). This parameter is also linked with the decision process parameter: E.g. if HQ has a «laissez-faire» attitude, the enforcement of compliance will not be considered important.				
<b>Employee's major Competence</b>	The major competence is a way to judge the seniority and the type of work that will be performed – from decisions on regional strategies in China/Asia to detailed strategy implementation tasks through junior managers with local partners.				
<b>Chinese Language Skills</b>	Language refers to the ability to communicate in Chinese. In the case of foreigners, it refers in particular to the oral communication as learning to write Chinese characters is even more challenging for non-natives.				
<b>Employee Profile</b>	The profile refers to the type of employee that will ensure the objectives for the subsidiary and implement its specific targets. The type of employee can vary from foreigners with no prior China experience sent from HQ to locally hired mainland Chinese. Hong Kong, Taiwan, Singapore and mainland China returnees (from Europe or US) are summarized in this assessment. Although all of them have direct or historic links with China there are huge differences between those profiles. However, the focus in this assessment is to highlight their communication style and especially their understanding of a Western management approach.				

# HQ-Subsidiary Relationship Design

## Options per Criterion


Criteria	Option 1	Option 2	Option 3	Option 4	Option 5
Size of Company	SMALL	MEDIUM	MNC		
Function	Finance	Logistics	Manufacturing	Marketing & Sales	Human Resources
HQ Philosophy towards Subsidiaries	Priority Market	Important among other Markets	«Must Have» because its China	Not important	Past error to have invested
Target for Subsidiary in China	Profit	Growth	Early Expansion	Downsizing / Closing	
Employee's main Task in Subsidiary	Profit	Management	Compliance	Innovation	Change Management
Primary Focus of Subsidiary in China	Sourcing	Manufacturing	R&D	Revenue Generation	Not relevant
Decision Process	Done by HQ / regional HQ	Done locally with reporting to HQ	Laissez-faire		
Compliance & Transparency	Not important	As long as nothing backfires	Important but flexible	Outmost important	
Employee's major Competence	Strategy	Supervision	Implementation	Contact to local partners	
Chinese Language Skills	Fluent	Working Knowledge	Limited Knowledge	None / Beginner	
Employee Profile	Foreigner sent by HQ, no China experience	Foreigner sent by HQ, solid China experience	Locally hired Foreigner, solid China experience	HK, Singapore, Taiwan, mainland returnee	Mainland Chinese


# HQ-Subsidiary Relationship Design


## European-Chinese Case Example


### Branding & Reputation Management

Criteria	Option 1	Option 2	Option 3	Option 4	Option 5
Size of Company	SMALL	MEDIUM	MNC		
Function	Finance	Logistics	Manufacturing	Marketing & Sales	Human Resources
HQ Philosophy towards Subsidiaries	Priority Market	Important among other Markets	«Must Have» because its China	Not important	Past error to have invested
Target for Subsidiary in China	Profit	Growth	Early Expansion	Downsizing / Closing	
Primary Focus of Subsidiary in China	Sourcing	Manufacturing	R&D	Revenue Generation	Not relevant
Employee's main Task in Subsidiary	Profit	Management	Compliance	Innovation	Change Management
Decision Process	Done by HQ / regional HQ	Done locally with reporting to HQ	Laissez-faire		
Compliance & Transparency	Not important	As long as nothing backfires	Important but flexible	Outmost important	
Employee's major Competence	Strategy	Supervision	Implementation	Contact to local partners	
Chinese Language Skills	Fluent	Working Knowledge	Limited Knowledge	None / Beginner	
Employee Profile	Foreigner sent by HQ, no China experience	Foreigner sent by HQ, solid China experience	Locally hired Foreigner, solid China experience	HK, Singapore, Taiwan, mainland returnee	Mainland Chinese

 Parameters set by situation

 Parameters that are inconsistent given the blue parameters

 Parameters that are consistent with blue parameters


 Parameters that are consistent with blue parameters but of secondary importance or relevance compared to dark green parameters


# HQ-Subsidiary Relationship Design


## European-Chinese Case Example


### Factory Expansion & Compliance

Criteria	Option 1	Option 2	Option 3	Option 4	Option 5
Size of Company	SMALL	MEDIUM	MNC		
Function	Finance	Logistics	Manufacturing	Marketing & Sales	Human Resources
HQ Philosophy towards Subsidiaries	Priority Market	Important among other Markets	«Must Have» because its China	Not important	Past error to have invested
Target for Subsidiary in China	Profit	Growth	Early Expansion	Downsizing / Closing	
Primary Focus of Subsidiary in China	Sourcing	Manufacturing	R&D	Revenue Generation	Not relevant
Employee's main Task in Subsidiary	Profit	Management	Compliance	Innovation	Change Management
Decision Process	Done by HQ / regional HQ	Done locally with reporting to HQ	Laissez-faire		
Compliance & Transparency	Not important	As long as nothing backfires	Important but flexible	Outmost important	
Employee's major Competence	Strategy	Supervision	Implementation	Contact to local partners	
Chinese Language Skills	Fluent	Working Knowledge	Limited Knowledge	None / Beginner	
Employee Profile	Foreigner sent by HQ, no China experience	Foreigner sent by HQ, solid China experience	Locally hired Foreigner, solid China experience	HK, Singapore, Taiwan, mainland returnee	Mainland Chinese

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# HQ-Subsidiary Relationship Design


## European-Chinese Case Example


### Improving weak Sales & Managing local Teams

Criteria	Option 1	Option 2	Option 3	Option 4	Option 5
Size of Company	SMALL	MEDIUM	MNC		
Function	Finance	Logistics	Manufacturing	Marketing & Sales	Human Resources
HQ Philosophy towards Subsidiaries	Priority Market	Important among other Markets	«Must Have» because its China	Not important	Past error to have invested
Target for Subsidiary in China	Profit	Growth	Early Expansion	Downsizing / Closing	
Primary Focus of Subsidiary in China	Sourcing	Manufacturing	R&D	Revenue Generation	Not relevant
Employee's main Task in Subsidiary	Profit	Management	Compliance	Innovation	Change Management
Decision Process	Done by HQ / regional HQ	Done locally with reporting to HQ	Laissez-faire		
Compliance & Transparency	Not important	As long as nothing backfires	Important but flexible	Outmost important	
Employee's major Competence	Strategy	Supervision	Implementation	Contact to local partners	
Chinese Language Skills	Fluent	Working Knowledge	Limited Knowledge	None / Beginner	
Employee Profile	Foreigner sent by HQ, no China experience	Foreigner sent by HQ, solid China experience	Locally hired Foreigner, solid China experience	HK, Singapore, Taiwan, mainland returnee	Mainland Chinese

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 Parameters that are consistent with blue parameters but of secondary importance or relevance compared to dark green parameters



# HQ-Subsidiary Relationship Design

## European-Chinese Case Example

### Market Entry for Swiss SMEs

Criteria	Option 1	Option 2	Option 3	Option 4	Option 5
Size of Company	SMALL	MEDIUM	MNC		
Function	Finance	Logistics	Manufacturing	Marketing & Sales	Human Resources
HQ Philosophy towards Subsidiaries	Priority Market	Important among other Markets	«Must Have» because its China	Not important	Past error to have invested
Target for Subsidiary in China	Profit	Growth	Early Expansion	Downsizing / Closing	
Primary Focus of Subsidiary in China	Sourcing	Manufacturing	R&D	Revenue Generation	Not relevant
Employee's main Task in Subsidiary	Profit	Management	Compliance	Innovation	Change Management
Decision Process	Done by HQ / regional HQ	Done locally with reporting to HQ	Laissez-faire		
Compliance & Transparency	Not important	As long as nothing backfires	Important but flexible	Outmost important	
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Chinese Language Skills	Fluent	Working Knowledge	Limited Knowledge	None / Beginner	
Employee Profile	Foreigner sent by HQ, no China experience	Foreigner sent by HQ, solid China experience	Locally hired Foreigner, solid China experience	HK, Singapore, Taiwan, mainland returnee	Mainland Chinese

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