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Here's Why Walmart Stumbled on The Road to China

A woman walks past signage for a Wal-Mart Stores Inc. store in the Shekou district of Shenzhen, China Bloomberg via Getty Images

By **ROBERT SALOMON** February 21, 2016

Managers tend to speak optimistically about the prospects of globalization, and for good reason. Globalization has fostered an increasingly interconnected world, with more than $30 trillion in goods and services traded and more than $1 trillion in corporate investment each year. Advances in information technology and transportation have helped facilitate globalization—connecting developed and developing worlds, lifting some 400 million people out of poverty along the way.

Nations are now inextricably linked through global trade and investment. There is no turning back. Accordingly, managers often view globalization as a powerful and inevitable force, and they tend to treat it with reverence

—speaking of it as if it were a breakthrough technology, the wave of the future that will change the world, if not their companies' fortunes. And they tend to think of themselves as the champions of globalization, akin to explorers embarking on a mission to discover and conquer far-off, unexplored lands.

Managers express their optimism for globalization in terms of the profitability it can generate for their companies. They salivate at the potential for double-digit sales growth. They are seduced by opportunities that promise to slash costs by half or more, simply by shifting operations overseas. And they lead their companies on journeys to global markets in search of untapped and untold riches.

However, opportunity and reality do not always coincide. Although globalization certainly holds promise, it is also rife with hazards. It presents risks that managers fail to appreciate and that they often overlook. Sadly, in the high-stakes world of global strategy, companies regularly fail to convert potential into profits. Most companies are poorly positioned to capitalize on globalization's potential, and many are spectacularly unsuccessful in their attempts to globalize.

China provides the setting for a classic cautionary tale about globalization. Given a population of more than 1.3 billion

people and the market potential that goes hand in hand with a consumer base of that size, the prospect of expanding to China is enough to make any manager's eyes light up. The potential is seemingly limitless.

But on further inspection, it becomes clear that China poses tremendous challenges for Western companies. The first obstacle is economic. Though China has made tremendous strides and enjoyed incredible growth since opening its markets to global trade and investment in 1979, the development of its economic institutions and its infrastructure has lagged behind that in the West. The second obstacle is cultural. Chinese consumers, for example, tend to be very different from those in the West, which makes it difficult for Western companies to appeal to local consumer tastes. The third obstacle is political. Western companies struggle to skillfully navigate China's complex web of local

and national political organizations. All of these factors led G.E.'s CEO Jeff Immelt to conclude: "China is big, but it is hard."

Walmart has learned these lessons the hard way. Walmart's ongoing troubles in China, since opening its first superstore in Shenzhen in 1996, reflect a fundamental misunderstanding of China's political, economic, and cultural environments.

The American retailer has struggled to understand Chinese consumers and Chinese culture. Chinese consumers, unlike those in the U.S., differ widely from city to city in their needs. Walmart therefore struggles to find the right product mix to offer in the 117 cities and 25 provinces in which it operates. This makes it challenging to sell a core set of products nationwide.

Walmart has also suffered from troubled relationships with politicians—both local and national. The company has had its fair share of run-ins with the law. On one occasion the Chinese government fined Walmart for violating local and national laws and even forced it to close stores temporarily for purported product violations. Walmart paid the fines, even though the company believed the claims to be unfounded.

Yet the company's greatest challenge remains an economic infrastructure that is problematic and underdeveloped. China simply cannot accommodate one of Walmart's greatest strengths: an ultra-efficient and technologically advanced supply chain. The company did not anticipate that scaling up its business model there would present so many problems. Walmart's struggles highlight the difficulties inherent in transferring a competitive advantage rooted in supply-chain efficiency—that is, logistics—to a country lacking a sophisticated technological and physical infrastructure.

Although China has led the globe in infrastructure investment over the past several years, outside of its largest cities (e.g., Shanghai, Beijing, Tianjin, Guangzhou, and Shenzhen), its infrastructure remains more than problematic. The efficient transport of goods from one region to another is a challenge because of China's sheer physical size, and because its air, ground, and rail infrastructure does not meet developed country standards. Not surprisingly,

Walmart's China business has struggled to generate profits, and it has consistently underperformed in this huge and potentially lucrative market.

The lesson in all of this is that, when it comes to globalization, managers are not just optimists; all too often, they are *unbridled* optimists. They habitually overestimate the benefits of globalization and underestimate its costs. In evaluating globalization opportunities, managers often forget the other side of the opportunity equation: risk. Risk goes hand in hand with opportunity, and managers fail to accurately account for the risks they face in global markets.

Managers often make dangerous assumptions about what it takes to succeed in global markets. They tend to assume that their current business model, one they successfully and profitably exploit in their home country, will translate simply and effectively to other countries, yielding similar levels of profitability. These same managers fail to account for real and salient differences between nations, and fail to consider how those differences generate operational risks that may negatively impact their business. Unfortunately, they end up learning the hard way that the risk borne out of cross-country differences can overwhelm even the best-laid globalization plans. And Walmart is no exception.

To improve the practice of global business and to make better global expansion decisions, managers need a more sophisticated understanding of the economic, political, and cultural environments in the countries in which they intend to operate. They must appreciate how nations differ economically, politically, and culturally, and how those differences manifest as increasing risks (and costs). They then need to incorporate those risks into their existing strategy and financial decision models.

Robert Salomon is a professor of International Management and Faculty Scholar at NYU's Stern School of Business and has researched globalization and global strategy for nearly 20 years. This article is excerpted from his book, Global Vision: How Companies Can Overcome the Pitfalls of Globalization. *Published by Palgrave Macmillan; reproduced by permission.*