

Think differently, or think of the differences

In globalization, recognizing local biases and regional differences can help unlock strategic opportunities for companies at home as well as abroad.

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Yes, there's a local bias in business. Even global cities like New York, London, and Tokyo are more embedded in their local contexts than many believe.

This local bias and other challenges to global connectedness are not just the concern of multinationals doing business abroad. Professor [Pankaj Ghemawat](#) argues that four key propositions he has made regarding international business also apply to *intranational* business — that is to say, what is going on within national borders.

Contributing a chapter to the 2015 book [Emerging Economies and Multinational Enterprises](#), Ghemawat, a globalization and strategy expert, turns his attention to domestic markets. Citing evidence from the United States (by state), China (by province), Spain (by autonomous community), etc., Ghemawat argues that domestic business could benefit from his international frameworks and theories.

Proposition 1: "Most markets are far from completely integrated internationally intranationally."

For more than a decade now, Ghemawat has devoted much of his research to exposing the state of "semiglobalization" he finds us in.

For example, "[Benchmarking Globalization to Boost Business Connections](#)" describes the [DHL Global Connectedness Index](#) (GCI), a tool to separate facts from "globaloney," to quote its creator. Measuring the depth, breadth and direction of global connections, GCI

levels from 2005 through 2013 indicate that there is still a surprising amount of integration work to be done — even before the Brexit challenge to the European Union.

So, the world is not yet integrated internationally, but how about domestic markets? Looking at four key variables — product, labor, capital and knowledge — Ghemawat finds evidence of home bias within domestic markets for all of them. For example, China's trade within its provinces has been estimated to be several times as intense as trade *between* provinces, even when controlling for distance. A similar phenomenon is seen within and between the states of Brazil.

And while more developed nations may be expected to have higher levels of integration, the United States and Spain both also exhibit product market fragmentation. For example, prices for the same product available in different U.S. locations can vary widely. Ghemawat cites a 2011 study by economist Anthony Landry that found McDonald's Big Mac prices varied more *within* New York City than they did internationally across the 15 countries sampled. To update a quote from "Pulp Fiction," a Big Mac may be a Big Mac, but what you pay for it is different from the Bronx to Queens.

Wage variations within the United States (Massachusetts versus Mississippi, for example) also speak to domestic differences, even after controlling for employees' skills and the state's occupational mix. It's seen in China, too: wages in Beijing are roughly double those found in Guangxi.

Proposition 2: "Geographic distance dampens international intranational business."

A number of studies show that the number of kilometers (or miles) matters. This is true for product, capital, information and people. It also flies in the face of the myth that global cities — like New York, London, Paris, Los Angeles, Tokyo and Sao Paulo — are more connected to other global cities than to their domestic hinterlands, because really they are more embedded in their regional contexts.

Proposition 3: "In addition to geographic distance, cultural, administrative, and (often) economic distances also dampen international intranational

business."

How to measure distance? The CAGE framework captures Cultural, Administrative, Geographic and Economic dimensions of differences across countries. And, with the exception of some administrative elements, Ghemawat argues that this model helps describe domestic distances as well.

The two countries Ghemawat currently calls home — the United States and Spain — offer illustrative examples. For instance, a map of major U.S. cities' trade relationships shows New York trading with Europe and Los Angeles trading with China. This figure "explicitly highlights the influence of cultural and geographic proximity," Ghemawat notes. That's half of his CAGE framework right there.

In Spain, the CAGE framework also helps predict the connectedness (or distance) between autonomous communities. For example, Catalonia, home to IESE Barcelona, and its two biggest trade partners — neighboring Aragon and Valencia — were united under the Crown of Aragon for centuries and speak Catalan (and Valencian), along with Castilian Spanish. Again, multiple CAGE dimensions matter, even within national borders.

Proposition 4: "The dimensions of distance suggest an expanded set of strategies for dealing with international intranational differences."

The first three propositions present evidence that countries (or domestic economies) are far from perfectly integrated. But to go deeper, the author looks at how this applies to business strategies. In other words, how does thinking about domestic business with available international business tools help inform decisions for a competitive advantage?

The CAGE framework is one way to think differently about differences and how to address the domestic context. Another is the author's "AAA triangle," which summarizes three effective strategic responses to manage distances: "Adaptation, Aggregation and Arbitrage." In brief, "adaptation" means being locally responsive and making adjustments as warranted. A very different approach to the same situation is to create economies of scale, an "aggregation" to minimize the impact of local quirks and overcome them. And the third approach is to exploit selected dimensions of local differences, finding "arbitrage" opportunities. For example, within Spain, Zara tends to hire in Galicia for domestic production work at relatively low wages. Over in the United States, over half of U.S. publicly traded companies are

incorporated in the small state of Delaware, which boasts relatively low taxes and business-friendly legal protections.

It bears repeating that the world is *not* flat. Neither are the many domestic markets within it.

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