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The Thought Leader Interview: Zhang Ruimin

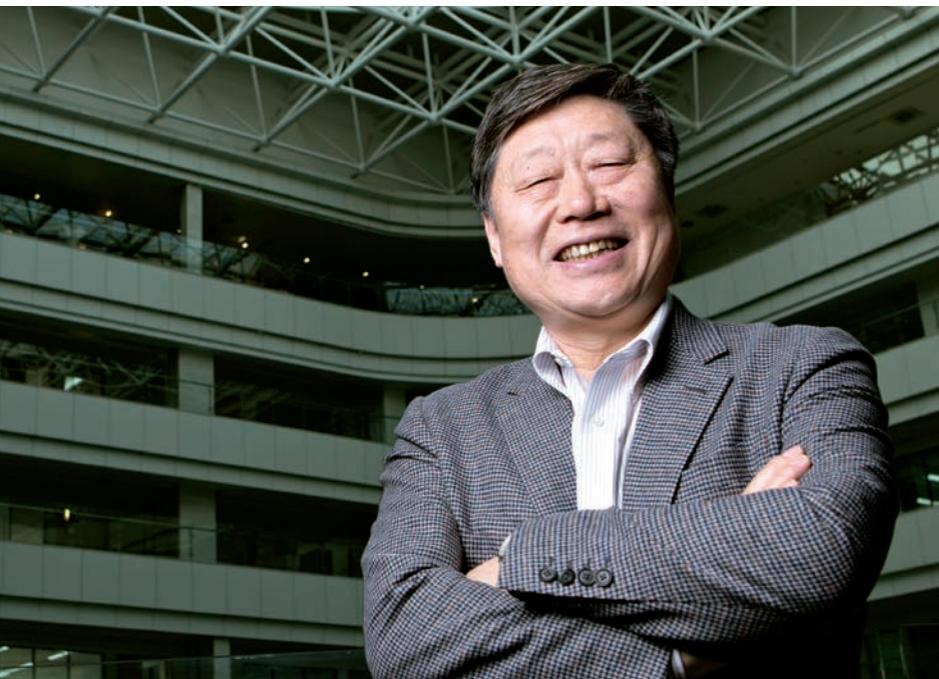
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BY ART KLEINER

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Each year, the Academy of Management recognizes one of the world's most influential chief executives by inviting that person to keynote its annual meeting. When Zhang Ruimin gave the address in 2013, it was a signal that China had produced its first philosopher-CEO. Like Jack Welch and A.G. Lafley, Zhang is recognized not just for leading a high-performing and truly entrepreneurial global business, but also for organizing that company around a conceptual framework that has guided its de-

velopment for years—in Haier's case, practically since its founding. The Haier Group is the world's fastest-growing appliance maker, and the company with the largest market share in “white goods” worldwide—about 14 percent of a market with at least seven other major competitors. It is also a world leader in business innovation and one of the largest non-state-owned enterprises in China. That's not bad for a company that was once in such desperate straits that the CEO had to borrow money to pay workers' salaries,

and many of the products it was selling needed to be repaired before they could be used for the first time.

But Zhang has never accepted limitations—including the definition of Haier as just a manufacturing firm—as permanent. Today, the company is repositioning itself as a provider of solutions to consumers' problems, selling not just home appliances (refrigerators, washers and dryers, entertainment electronics, and air and water conditioners are among its major lines) but also services including water safety information and other guidance designed to improve the quality of life for consumers in China and other emerging economies. To maintain that identity, Zhang has steadily initiated shifts in the company's structure, moving consistently toward participative management, decentralized decision making, and autonomous but accountable work teams and platforms.

Haier's prowess in business innovation has yielded a continuous stream of products and services that serve distinctive consumer needs. For example, it makes large washing machines for Pakistani robes, small ones for Chinese delicates, and durable ones with large hoses for

Photograph by Wang Zhao

washing vegetables on Chinese farms. Its product line is also increasingly tailored to customer specifications, and its water purifiers are designed to remove the specific pollutants in each of 220,000 communities across China. (Haier jointly holds more than 20 water purification patents with Dow Chemical.) Every appliance that Haier sells today is custom-crafted; each individual purchaser specifies colors and features that are sent directly from the Internet to the factory floor.

Zhang took the helm of Haier in 1984, when he was 25. At that time, it was a troubled company partly owned by the city of Qingdao, one of China's first enterprise zones. Zhang was an assistant city manager, instructed to find a managing director who could turn the company around; he found no one willing to tackle the job, so he took it himself. He quickly educated himself in business management, and used his new insights to establish Haier as one of China's preeminent producers of quality goods—first for that country's burgeoning consumer population, and then for the rest of the world.

As Haier becomes a platform-based business, every part of the organization has its own P&L, makes autonomous decisions (including which other parts of Haier to work with), and can reach out independently to customers, potential employees, and collaborators. R&D projects now often reach beyond Haier's walls to include academics, independent designers, and even competitors. Zhang sees this as a natural evolution for all major companies, particularly those focused on business innovation in the Internet age. He is determined to make Haier one of the first to bring

this type of management to fruition, even if people inside the company (and, for that matter, everywhere else) still feel uncertain about how to implement it day-to-day.

Zhang Ruimin sat down with *strategy+business* at Haier's headquarters in Qingdao as part of a broader inquiry into how companies compete with their distinctive capabilities (see "Haier's Capabilities System," page 6). The conversation, which was conducted in Mandarin and English through interpreters, shows how the thinking of a gifted CEO can lead a company to greater innovation and global influence.

S+B: When we ask people to name companies that consistently succeed, year after year, through their distinctive capabilities, Haier is often mentioned. How have you been able to do this?

ZHANG: Over time, some companies perform relatively better than others. You could say these are outstanding enterprises, highly capable

and it's extremely difficult to stay abreast of them. Second, from an internal perspective, companies lose their entrepreneurial spirit. As soon as a company grows large, its employees learn to work in accordance with the company's rules. As regulations multiply and companies control their employees more tightly, everyone becomes really good at following orders. Their sensitivity to the market decreases accordingly.

The top leaders of any major company are also susceptible to this loss of entrepreneurial spirit. Jim Collins and Jerry Porras wrote in *Built to Last: Successful Habits of Visionary Companies* [HarperCollins, 1994] that many great chief executives are "time tellers." They create great products and services, but their value lasts only as long as they are personally present. Senior executives should be more like "clock builders": focused on making a great company—a company where people think as entrepreneurially as the leaders do, even after those leaders

“An enterprise must evolve into a system that stands on its own, and does not depend on the whim and fancy of its current leader.”

companies. But most of these companies today—and this includes many big international firms—will have an extremely hard time maintaining their outstanding position indefinitely.

At Haier, we have a saying: “Successful companies move with the times.” There are two reasons we believe this. First, from an external perspective, times change quickly

are gone. An enterprise must evolve into a system that stands on its own, and does not depend on the whim and fancy of its current leader.

Lack of entrepreneurial spirit is a major reason for the decreasing competitiveness—and even the eventual collapse—of big enterprises. It is an extremely difficult problem for Chinese companies in particular. In the past, business leaders

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in China would tell workers that they should love the factory and treat the company as they would their home. That's how the relationship was framed. Today, a successful enterprise must be less of a home and more of an entrepreneurial platform: a base for pioneering work where employees can realize their personal value. This shift is difficult for many workers to accept.

An Entrepreneurial Spirit

S+B: Haven't you maintained an entrepreneurial platform since the company was founded?

ZHANG: Not to the extent we do today. To be sure, we have felt a sense of urgency at Haier ever since we began to rebuild the company in 1984.

Haier's previous incarnation was an enterprise on the brink of collapse. At that time, the overall quality of the staff was extremely low—the entire factory had only about two college graduates. From the start, we've felt like there was an extremely large gap between us and more established international companies, a gap we would have to overcome. The only way to survive was to pursue a path of constant self-improvement.

After we got on our feet and started making money, we looked up and noticed that many companies around us—some that performed even better than we did—were shutting down. That just reinforced our sense of urgency. We saw that we weren't facing just a one- or two-day challenge. To survive and be competitive would always be a company-wide, long-term challenge for us. That's why we have a culture of self-questioning. Everyone is always challenging their own ideas and continuously surpassing themselves.

In 1999, we ventured overseas, opening factories in places like the

we have another saying: "When looking for a chess partner, find a grandmaster."

S+B: What have you specifically done to foster an entrepreneurial spirit at Haier?

ZHANG: Most recently, we reorganized. We used to have a pyramid-style structure for our sales in China. The people in charge of sales had to manage business at the national, provincial, and city level.

After the arrival of the Internet age, we realized that under this triangular hierarchical structure, people had a difficult time adapting to the requirements of the times. So we

"If a home appliance can't communicate with the Internet, it shouldn't exist."

United States. At that time, we used GE as our yardstick. It's as if the industry were a boxing ring, and we were some barely known upstart taking on Mike Tyson. Of course, by conventional standards, we didn't stand a chance. But in the company

reorganized ourselves as an entrepreneurial platform. We flattened everything out, taking out all the middle management. We decentralized the structure to one with more than 2,800 counties. Each county organization has seven people or fewer.

This transition has been extremely challenging. As part of this change, in an instant, more than 4,000 employees who worked for the company were unemployed. [Many of them were quickly invited to reapply, but this time for entrepreneurial positions where they could build businesses under the Haier brand.] We know of no other Chinese company of our size that has done this.

Cultivating Consumer Insight

S+B: How has Haier's flattened structure affected the people inside the company?

ZHANG: Whenever you pursue reform, there are always a significant number of employees who are unhappy because you've begun messing with their interests. Some may not be able to adapt, but if they leave and go somewhere else, they may not be able to find a decent job, so of course they complain. This is a really difficult nut to crack. The only thing we can do is provide employees with a level playing field, where they can compete on an equal footing for opportunities within the company. In reality, however, even this isn't good enough; many em-

ployees just don't have the necessary skills. So what do we do? This is an issue we have yet to fully resolve.

Another major challenge has to do with making the enterprise truly borderless. We are using digital technology to connect everyone. In your question, you said "inside the company," but in fact, we believe that there is no "inside" the company versus "outside" anymore. As a Haier executive, my goal is no longer to be a maker of home appliances, but to be an agent of interaction and networking among people who might be anywhere. I want to turn the company into an Internet-based company, a company unrestricted by borders. Whoever is capable, come and work with us.

We now have a lot of entrepreneurs at Haier who don't work inside the company. Some aren't interested in joining, preferring to stay outside in society, partner with the company, and use our platform for pioneering work. Those inside the company are also free to leave at any time, and still use the Haier platform for their work, though they would no longer actually work for the company. In the long run, there won't be any company employees to speak of—only the Haier platform.

We involve customers in a similar way. In the past, users would hear through advertising which Haier products were good, then they'd go buy those products. Now we bring in users to participate in the whole process of product development. It's not like in the past where we designed things behind closed doors. For example, the Air Box [a smartphone-controlled intelligent device introduced by Haier in 2014 for monitoring and managing the climate inside a building by connecting to other heating, filtering, and air conditioning devices] is the result of a significant amount of user input. This guided us on issues like whether the AC unit should be able to test the cleanliness of the air and be controlled intelligently. We then brought in Samsung and Apple to help us meet users' requirements. The resulting product is different from those of the past. The Air Box can control any company's AC unit, not just Haier products. This is completely a result of interaction and cooperation.

All of our products are integrated with the Internet. If a home appliance can't communicate with the Internet, it shouldn't exist. And to make that happen, we need to facili-

tate a relationship of constant interaction with the appliance itself and with our customers. [See “A Strategist’s Guide to the Internet of Things,” by Frank Burkitt, *s+b*, Winter 2014.]

S+B: Why does building the company around platforms give Haier an advantage?

ZHANG: The idea of the platform represents a stark contrast from how we used to manage the enterprise in the past. First, it should allow us to bring in and integrate greater quantities of resources—all contributors will be able to enter unhindered. Before, there were always borders and barriers. Second, all who join the platform as a resource should see their returns maximized. Before, maximizing the benefits for the company took precedence. This limited us in what we were able to accomplish.

Now that we operate in this fashion, we at Haier are no longer the ones directing things. We are the glue binding everything together. Being the glue is a difficult task; we have to come up with myriad ways of managing resources.

For example, we have an interactive platform devoted to solutions for water quality and treatment. Instead of inventing everything we sell in this domain ourselves, we are now like a binding agent, incorporating insights and efforts from water treatment companies around the globe, if possible, into this one platform. We also want to learn about and resolve users’ needs through direct interac-

tion with them. Our team tasked with the water solution interactive platform now has to do all of this.

S+B: How did you develop your high level of customer insight?

ZHANG: Around 2010, we realized that we had a lot of products for which we had put forth great effort in order to understand and meet the demands of users—but which seemed to be giving only half the returns for double the work. In the Internet age, when people continually identify new needs and demands, the rapid evolution of user preferences represents a huge source of pressure. We had products we thought were ready to go, flawlessly researched and developed. When they hit the market, however, results were lackluster.

That got us thinking: How can we make the transition from the past, when we learned about users’ needs via questionnaires and telephone calls, to the present age, when we can interact with users more directly?

So we put forward some new concepts. For some appliances, we designed a group of various modules and invited users to select, for example, the colors and designs they wanted. In one day, we sold more than 10,000 television sets online. This made us realize that our old ways of thinking and conducting business needed an overhaul.

Many employees, especially those in management, had a hard time accepting this approach. When we started requiring that products

be developed in cooperation with users participating in the front-end design, employees felt like they didn’t know how to go about it. Some flatly refused, whereas others were [passively] unwilling. As an entry point, we started with the Dizun and Tianzun air conditioner series. [These products include temperature precision, smartphone-based controls, and, in the case of Tianzun, lights that change color with the air quality in the room.]

In the beginning, we told our employees in these groups that it wasn’t a big deal if they failed, that it was meant to be a process of trial and error. The employees accomplished it successfully. As a result, we now require that all products be developed in this way, with users as interactive partners. At that point, we told all of our traditional advertising partners that we weren’t doing direct ads anymore. A lot of advertising firms were extremely unhappy about this, complaining that if we didn’t do ads they wouldn’t be able to earn a living. But it was far better to change, and meet consumers directly online.

Differentiation through Ideas

S+B: How do you decide which aspects of the company should be open, with an entrepreneurial spirit, and which elements—core elements of the company’s identity—should remain unchanged?

ZHANG: That’s an extremely difficult question, and we are still work-

ing out the answer. [We have decided] that many areas that were previously closed off and untouchable now must be opened up. For example, when dealing with patents in the past, new technologies and products were kept strictly confidential until the day when the new products were unveiled. Nowadays, we make users part of the R&D pro-

cess. Even after the product is successful, we go back for constant revisions, in which we also invite users to participate, and competitors as well. For example, in the research and development of the Haier “cordless home appliance,” we invited industry competitors from across the globe to participate.

This was very hard to adapt to

at first. It means we don’t keep absolute secrets like we did in the past. One can only succeed, even temporarily, if all parties perceive they will benefit. That wasn’t completely true in the past; but this is how things are today. [See “The Sharing Company,” by Robert Vaughan, *s+b*, Winter 2014.]

Haier’s Capabilities System

Haier is one of 12 companies that were studied closely in a Strategy& research project on distinctive capabilities and coherence.

Value Proposition: Haier’s “way to play” in the market (its value proposition) has gradually broadened since Zhang Ruimin became CEO in the mid-1980s. The company first took the role of a category leader, maintaining top market share because of its reputation for quality in China. Then it became a customizer (adapting its products to customer demands) and a solutions provider (helping consumers manage issues like water quality and home design). Haier now sells not just home appliances but related services, adapted to consumer demand in China, and, increasingly, other markets. Haier delivers its way to play by excelling at four differentiating capabilities.

<p>Consumer-responsive innovation (called “customer service leadership” within the company), rapidly tailoring products and, increasingly, services for local markets and specific customer needs—most recently, the needs of China’s emerging middle class</p>	<p>Operational excellence, geared to produce high-quality products at very low cost through the company’s continuous improvement, zero-defect, and internal competition culture</p>	<p>Management of local distribution networks, a capability honed in China’s highly decentralized value chain, applied to emerging markets and other locales</p>	<p>On-demand production and delivery, incorporating a pull-oriented distribution system and zero-inventory logistics, allowing immense variety at minimal cost</p>
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Source: The Strategy& Capable Company research project; *The Essential Advantage: How to Win with a Capabilities-Driven Strategy*, by Paul Leinwand and Cesare Mainardi, Harvard Business Review Press, 2011

S+B: What do you see as the primary differences between Haier and other companies?

ZHANG: One of the biggest differences is our ability to remake and overhaul ourselves. Many companies’ ways of thinking and operating have ossified and become hard to change, especially their organizational structures. At Chinese companies, it’s exceptionally hard to remove an executive who is not performing well, especially if they’re in the mid to high levels of management. At Haier, however, we can make fast changes. We have responded to the changing environment by eliminating or adjusting more than half of the vice-president-level executive positions.

The main factor enabling this difference is our culture. Those inside Haier, especially managers, understand that it’s crucial that we adapt to the evolving needs of users and the changing market environment. A few people who have gone from Haier to work for other companies have written to me telling me that the biggest difference between Haier and their new company is Haier’s transparent interpersonal re-

lations. They say that this is unheard of at other companies.

S+B: What differences do customers and users perceive?

ZHANG: Before we embraced the Internet age, the biggest difference between us and other companies was our commitment to honesty. We had an advertising slogan, “Forever honest.” Users may have felt that other companies weren’t paying enough attention to some of their needs, but that Haier was able to address those needs immediately. Especially in the area of after-sales services, there was a widespread feeling among users that this was the biggest difference between Haier and other companies. This has been an important reason that Haier has been able to grow so quickly and for such an extended period of time.

Today, we hope that users enjoy an outstanding experience from beginning to end. We’re still working on this concept. Customers still don’t feel that it’s anything extraordinarily special. We know they are relatively happy with our distribution. We have a guarantee, for example, that if goods don’t arrive within 24 hours in China, they are free. No other company has been bold enough to make this kind of promise. On the same note, Haier is the only producer of large appliances that has been able to synchronize delivery and installation. This is one of the reasons for our cooperation with [the e-commerce site] Alibaba. These examples are all possible because of our back-end platforms. In the front-end area of information exchange, we still need to pick up the pace.

S+B: You are known for personally paying close attention to trends in

management theory. What theories or ideas have most influenced the direction you’re taking the company?

ZHANG: For me personally, the most influential person in management theory has been Peter Drucker. A lot of what he said can be summarized with two major focal points. First, the only correct and effective way to increase the value of a company is the creation of customers. Second, employees should not be implementers; they should be individuals able to realize their value by making decisions. Throughout our company’s history, roles have been organized according to Drucker’s theories.

With the advent of the Internet age, the people with the most influence on us have been American experts such as Chris Anderson with his theories of the long tail and “maker” culture [related to digital fabrication], and Clay Shirky with his book *Here Comes Everybody: The Power of Organizing without Organizations* [Penguin Press, 2008]. There have been many ideas coming out of the U.S. regarding the Internet that have had a huge influence on our reforms.

We try to implant these concepts into everyone’s thinking. For example, every Saturday, when we hold our weekly management meeting, we disseminate these ideas and encourage people to change how they think about things. We also try to put these concepts into practice. To avoid big mistakes, we always implement a small pilot test at first. Only after the pilot has been shown to be successful will we initiate things on a larger scale.

S+B: In this context, how do you think about the growth and development of your employees?

ZHANG: In the past, we had a large-scale select-and-train approach to

recruiting employees, like many Western companies. This cookie-cutter method of training employees led us to cultivate people who identified with the culture and whose implementation abilities were incredibly strong—but who lacked creativity. The recruits weren’t required to have any skill with innovation, which was a major problem.

Employees today should be encouraged to think for themselves. They should be cultivated to have an entrepreneurial, innovative spirit, and not just to implement orders. From now on, enterprises such as Haier will be like ecosystems. You might find yourself working together with a group of people you didn’t know yesterday, and after tomorrow you’ll all go your separate ways. People come together for specific projects, after which they disperse. It’s become a very fluid, dynamic type of arrangement.

S+B: Will this wave of innovation take you as far as you need to go?

ZHANG: That’s the eternal question. I’ll say just one simple thing: Never follow only a single road. [In his 1939 book *Business Cycles: A Theoretical, Historical, and Statistical Analysis of the Capitalist Process* (McGraw-Hill)] Joseph Schumpeter defined innovation as the reorganization of the factors of production. You and your rivals have access to virtually all the same resources. Only by constantly thinking of new ways to reorganize these factors can you differentiate yourself. It’s like poker. Everyone has the same number of cards. It’s how you play your hand that matters. +

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