

# Haier: The world's biggest Producer of White Goods<sup>12</sup>

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## Introduction

When people in the Western world think of white goods brands, they often think of major American manufacturers such as GE and Whirlpool or maybe the German company Bosch and the South Korean LG Corporation. To many, it may come as a surprise that the world's biggest producer of white goods is a Chinese company by the name Qingdao Haier. In only 30 years, Haier went from a single worn-out factory in the Chinese city of Qingdao to being a multinational company with a global market share in white goods of 10.2 percent in 2014<sup>3</sup> and a workplace for more than 60,000 people. Its CEO, Zhang Ruimin, has become known for his rigorous focus on customers and quality management. Originally inspired by Western and Japanese management techniques, he has since explored new ways of managing and organizing a global corporation which has led to some people referring to him as 'the Oracle of Qingdao'.

## The Continuing Challenge for Haier

Rumor has it that Zhang is currently planning his succession after more than 30 years as the person in charge of Haier. A large part of Haier's success has been ascribed to Zhang's abilities as a leader and an innovator, and time will tell whether or not Haier will be able to stay ahead of its competitors and keep its position as market leader, even if it will be under new leadership.

Recently Haier has gone through a major restructuring. It is still too early to say whether or not the grand restructuring has been successful. Some business analysts believe that the new structure has weakened Haier and may lead to great conflicts inside the organization. At the same time, growth in the Chinese market for consumer electronics have been slowing down, while Haier is facing an increasingly tougher competition from Chinese rivals, who are starting to threaten Haier's success in the consumer electronics market<sup>4</sup>.

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<sup>1</sup> The case was developed and written by Mathias Pihl, Richard M. Burton, Børge Obel and Dorthe Døjbak Håkonsson from public materials.

<sup>2</sup> The case has been written as a basis for class discussion. The case cannot be used as an endorsement for organizing the Haier group or illustration of effective or ineffective management.

<sup>3</sup> <http://uk.reuters.com/article/2014/12/31/cn-haier-market-share-idUKnPn9hz95F+81+PRN20141231>, accessed 27/3-2015

<sup>4</sup> "Haier to axe 10,000 jobs this year" by Tetsuya Abe. Published 17/6-2015 by Nikkei Asian Review

Looking forward: will the new structure and strategy be successful? Will Zhang continue or will Haier have new leadership? If so, what should that leadership mean to this new structure and strategy? As you read this case, you should keep these questions in mind. At the end, there are more questions, which will help you develop a deeper understanding of the challenges that Haier faces and will face in the future. To understand Haier, we continue the history of Haier and how it became the world's largest white goods manufacturer.

## The History of Qingdao Haier

Haier started as a refrigerator factory founded in the 1920's in the city of Qingdao, Eastern China. The factory was later taken over by the Chinese government, following the Chinese Communist Revolution in 1949.

By the early 1980's, the factory, then known as Qingdao Refrigerator Co., suffered from several problems including poor infrastructure and a lack of proper quality control. The poor infrastructure was a common problem in many parts of China at the time making it difficult and time-consuming to transport goods between the factory in Qingdao and the rest of China. The factory was incurring losses of RMB 1.47 million (USD 0.24 million) and was struggling to pay its workers, who were rarely able to produce more than 80 refrigerators per month<sup>5</sup>. A change was needed at the Qingdao factory. In 1984, the former managing director left the firm and was replaced by the 35-year-old Zhang Ruimin. He had previously been working as an assistant city-manager. He had a great interest in the Western and Japanese management philosophies. With China's new openness in the early 80's, Qingdao Refrigerator Co. entered a partnership with Liebherr-Haushaltgeräte, one of Germany's leading manufacturers of home appliances. Zhang personally went to Germany in 1984 to visit Liebherr to compare products and exchange thoughts and ideas. Zhang ended up feeling embarrassed about the low quality of the Chinese products; he knew that something had to be done about the culture and organization of his company. New technology alone would not be enough.

The big shock came in 1985, when a customer wanted to return a faulty refrigerator. Zhang took the customer into the inventory to look for a functioning replacement. He discovered that out of the 400 refrigerators in their inventory, 76 were in some way of an unacceptable quality. This was equivalent to a failure rate of about 20 %. Zhang then had the 76 refrigerators lined up on the factory floor while distributing sledgehammers to his employees. He ordered them to destroy the faulty products. Many of the employees were hesitant, considering that the price of a refrigerator was worth about 2 years of salary for a factory worker. Zhang finally convinced them proclaiming that, "If we pass these 76 refrigerators for sale, we'll be

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<sup>5</sup> <http://www.fundinguniverse.com/company-histories/haier-group-corporation-history/>, accessed 23/3-2015

continuing a mistake that has all but bankrupted our company". This event is a well-known history in the Haier Corporation; it marked the start of what Haier themselves have called their 'Brand Building Strategy'.

## **The Creation of the Haier brand**

In the early 1980's, the demand for refrigerators in China greatly outweighed the supply. Many producers had a sole focus on quantity of production without considering the quality of their goods. Zhang was convinced that this would soon change, and he wanted to make sure that his firm would have an early advantage over their competitors when the market changed. He had a vision of the company as a late starter with high starting point<sup>6</sup>. Quality became a main priority at Qingdao Refrigerator Co. and a new and rigorous quality management system was implemented. Managers became responsible for attributing each task to a specific employee, which made it possible for Zhang to introduce a new reward system where employees were evaluated based on their output. Poorly performing employees were made to stand on a pair of yellow painted footsteps on the factory floor at the end of the day, and explain to their bosses and colleagues what went wrong, in an effort to promote personal accountability.

In 1986, only 2 years after Zhang joined the company, Qingdao Refrigerator Co. had turned from a debt-ridden company to a profitable business with sales rising with an average of 83 percent per year. A growth that would eventually lead to an increase in sales from RMB 3.5 million in 1984 to RMB 40.6 billion in 2000. The increased focus on quality was also acknowledged in 1988 when Qingdao Refrigerator Co. was awarded a gold medal for their products by the National Refrigerators Appraisal, which helped the company to acquire a position as market leader among Chinese manufacturers of refrigerators.

Zhang Ruimin's predictions about the Chinese market were right. In 1989, the market for refrigerators finally hit a point of over-supply. While their competitors were experiencing falling sales numbers and engaging in price wars, Qingdao Refrigerator Co. had no problems selling their products, even with a 15 % premium - due to their advantage in quality and customer service.

## **Diversification of activities**

Following the newfound success of the refrigerator company, the Qingdao government encouraged the company to take over other of the failing house appliance manufactures in the city. The Qingdao government hoped that the culture and management style of Qingdao Refrigerator Co. could help these failing houses to become profitable businesses. Qingdao Microwave Electric Appliance Factory was the first in 1988, followed by Qingdao Air Conditioner Plant, and Qingdao Freezer in 1991. With the expansion of activities, Haier became the new company name in 1992. Why Haier? It is the phonetic spelling of Liebherr,

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<sup>6</sup> [http://www.haier.net/en/about\\_haier/history/](http://www.haier.net/en/about_haier/history/), accessed 24/3-2015

(pronounced ‘Li-bo-Hai-er’ in Chinese) the German company where Haier had imported their refrigerator technology initially.

By 1997, Haier had acquired a total of 18 companies (some from the government pressure). In addition to a wide range of white goods; they were now producing consumer electronics such as televisions, mobile phones and personal computing systems. Zhang described this as the “Stunned Fish”-strategy where the purpose was to identify and take over firms (“fish”) who had promising products as well as good facilities and distribution channels, but who were “stunned” due to a lack of proper management. Haier would then turn the company around by implementing their own corporate culture and quality management system. Only then would they start marketing the new product line using the Haier brand.

The diversification strategy made Haier a major player in the Chinese market for white goods and other products. The success was clear in 1998 when sales topped RMB 14.29 billion; Haier had reached impressive market shares in China: 40 percent for refrigerators, 36 percent for washing machines, 47 percent for freezers and 37 percent for air conditioners<sup>7</sup>.

Not all the companies, that the government asked Haier to take over, could be said to satisfy Zhang’s idea of “stunned fish”, but Haier often had enough power to turn down these offers. One exception was when Haier was pressured to take control of a pharmaceutical company - despite having no former experience or knowledge with production or distribution of pharmaceuticals<sup>8</sup>. The synthesis of pharmaceutical drugs has little in common with the production of white goods, with the pharmaceutical industry being known as one of the most research-intensive and science-driven industries in the world. The capabilities that had helped Haier become a major player in the market for white goods were very different from the capabilities necessary to succeed in the market for pharmaceuticals and as a result of this the acquisition ended up as a disaster. Why do you think the Haier model was a disaster for the pharma firm?

## Entering the global market

In 1992, Haier achieved the ISO 9001 quality certification for their refrigerators enabling them to export their own products to foreign markets. They began with Indonesia but quickly spreading to other countries in East Asia where they quickly became known for the quality of their products. This brand awareness became a valuable asset for Haier a few years later when they started to enter the East Asian markets directly through joint-ventures. Haier’s first entry was a production plant in Indonesia in 1996 through a venture with

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<sup>7</sup> “Chinese Entrepreneur Striving to Create Global Brand Name”. Published 24/12-2000 by People’s Daily Online

<sup>8</sup> “Business: A Jack Welch of Communists”. Published 8/5-2005

the Sapporo group, followed by Malaysia and the Philippines in 1997. By the year 2000, Haier's market share of freezers in Indonesia had reached 28 percent<sup>9</sup>.

Parallel to their expansion into the East Asian markets, Haier had begun the entry into the U.S. market with exports in 1994. Haier knew that they would have a hard time competing with well-known American brands such as Whirlpool and GE. Many consumers had a preconceived view that a Chinese produced good would be of a lower quality than an American produced equivalent. Haier chose to look for smaller niche markets that were underdeveloped and easier to compete in; they found two. One was small-sized refrigerators made for business offices, hotels and students living in small college dorms; the second was electric wine coolers. The first Haier products in the US market were compact refrigerators imported by the New York-based company Welbilt Appliances in 1994. They sold under the Welbilt name, capturing a 10 percent share of the U.S. market for compact refrigerators within a year, and growing to around 30 percent after 3 years.

In 1999, a joint venture selling products in the U.S. under the Haier brand was formed. The joint venture was called Haier America and had its headquarters on Manhattan. The success of their niche products helped Haier build brand awareness and establish Haier as a trustworthy name in the U.S. market. In 2000, Haier opened its first manufacturing plant in the U.S., a \$40 million industrial park in South Carolina designed to produce 500,000 refrigerators per year. This was their 6<sup>th</sup> production plant overseas. Regarding Haier's strategy to establish itself as a global brand, Zhang Ruimin had said:

*"We can't be considered a success unless overseas consumers no longer regard Haier as a Chinese brand name but a global one,"*<sup>10</sup>

And further,

*"You can't be an international company if you only make things at home and export them"*<sup>11</sup>

In 1997, Zhang had announced his "three thirds" goal: one third of revenue should come from goods produced and sold in China; another one third should originate from goods produced in China and sold overseas; and the last one third should be from products both produced and sold overseas.

The plant in South Carolina was later followed by a design center in Los Angeles and a trade center in New York. Haier hoped that the expansion into the U.S. would not only prove itself a platform for increased sales and revenues (with the economic growth of China slowing down in the late 1990's) but also as a platform for learning and gathering experience. Supplying the world's most demanding consumers in competition with

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<sup>9</sup> "Internationalization and technological catching up of emerging multinationals: a comparative case study of China's Haier group" by Duysters, Jacob, Lemmens and Jintian. Published 2009 by Oxford University Press

<sup>10</sup> "Chinese Entrepreneur Striving to Create Global Brand Name". Published 24/12-2000 by People's Daily Online

<sup>11</sup> "Chinese Entrepreneur Striving to Create Global Brand Name". Published 24/12-2000 by People's Daily Online

big American brands such as GE, Frigidaire, Maytag and Whirlpool, who together had a market share of 98 percent for full-sized refrigerators in the U.S. at the time, Haier would learn a great deal.

By 2002, Haier's revenues from the U.S. topped \$200 million dollars. In 2005, its market share reached 26 percent for compact refrigerators, 17 percent for air conditioners, and over 50 percent for electric wine coolers. Haier was a player in the American market.

Haier's international expansion was in no way limited to the North American market; it had been exporting to the European market since the early 1990's - starting with Italy and the UK and later France and Italy. In 1997, their first direct investment in Europe, a manufacturing plant in Belgrade was established as a joint venture with a Yugoslavian company. Haier's products were especially successful in Germany, where they were marketed by the Liebherr Group from whom Haier had bought the refrigerator technology 15 years earlier<sup>12</sup>. Three years later, in the year 2000, Haier Europe was established in Italy to handle sales and marketing in the European market, followed by the acquisition of an Italian refrigerator plant in 2001. Haier later moved into the Middle East with a production facility in Pakistan in 2002 and a plant in Jordan just a year later.

## Product differentiation

A big part of Haier's success, can be attributed to their market responsiveness and focus on satisfying the demands of their consumers. When the success that Haier had with their small-sized refrigerators became apparent, other companies began to enter the market to compete for sales and profit. Haier's response was to send product designers to visit students, living in college dorms, to better understand the needs of their customers. They noticed that many of the students were placing wooden boards across two refrigerators to use as desks in order to save space in the, often cramped, dormitory rooms. Soon after, Haier developed and introduced a new compact refrigerator model, which had a built-in fold-out table that could function as a desk<sup>13</sup>.

When a customer, from the rural Chinese region of Sichuan, called Haier's service center to complain about his washing machine constantly becoming clogged, Haier sent a technician to have a look at the machine; he soon discovered that the large amount of dirt did not come from the clothes. The Sichuan region is known for its production of sweet potatoes, and the farmer and his family would often use the washing machine to clean their harvest clogging the pipes with dirt and pebbles. Instead of telling customers only to use their washing

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<sup>12</sup> "Haier: Taking a Chinese Company Global" by Palepu, Khanna and Vargas. Published 2005 by Harvard Business School

<sup>13</sup> "The art of innovating on a shoestring" by Donald N. Sull and Alejandro Ruelas-Gossi. Published 24/9-2004 by Financial Times

machines for cloth, Haier realized that this family was probably not the only one in the region using their machine to wash potatoes. So, Haier decided to change the design of the washing machines, sold in the Sichuan region, to handle the unusually large amount of dirt and then marketed the machines as being able to clean both clothes and vegetables<sup>14</sup>.

There are many stories about the changes that Haier made to their products to adapt them to different countries and regions. As of 2009, Haier had 96 product lines with a total of more than 15,100 product varieties. To accommodate the high degree of innovation, Haier provided a flat organizational structure with the end goal of creating an organization without borders. Zhang stated in 2006, that the purpose of this structure was to:

*“(...) enable every staff member [to] face the global market as a strategic business unit. This way we can make everyone a source of information: No matter where in the world they are they can be the first to find out customers’ needs and respond the most quickly, continuously using innovation to create new customers.”*<sup>15</sup>

Specifically, the Haier organization consisted of four layers: At the top was group headquarters, with headquarters consisting of four centers; human resource center, capital center, center research academy and project development center. The subsequent level was formed by the different departments, which were then divided into the different department branches<sup>16</sup>.

## Re-organizing for the Internet Age

The 2000’s had been a great decade for Haier, who had experienced large growth rates in global market share, from 3.1 percent in 2003 to 9.6 in 2012, while revenues increased from less than \$10 billion to \$26 billion.

In 2012, Haier felt ready to announce the implementation of their new Networking Strategy, meant to enable the company to stay responsive and competitive upon the arrival of the Internet Age and its effect on business organization. The new Networking Strategy was characterized by three main elements:

- Border-free enterprise
- Manager-free management

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<sup>14</sup> “Why It’s Okay to Wash Potatoes in a Haier Washing Machine and Other Lessons From Philip Carmichael” by Normandy Madden. Published 3/2-2010 by Advertising Age

<sup>15</sup> “2016: What’s Next for Asia? – Building Asian Brands” by Zhang Ruimin. Published in Far Eastern Economic Review; Nov 2006; 169, 9

<sup>16</sup> “Internationalization and technological catching up of emerging multinationals: a comparative case study of China’s Haier group” by Duysters et al., published in Industrial and Corporate Change; Feb 2009; 18, 2

- Scale-free supply chain<sup>17</sup>

Whereas the company previously consisted of traditional departments responsible for production, marketing etc., the employees were now divided into about 2,000, so called, *zi zhu jing ying ti* (ZZJYTs). These ZZJYTs can be described as self-managed teams, each being responsible for their own profit and loss and with individuals being paid according to their performance. Employees were able to propose ideas for a new product or service, and to vote for and to decide, which idea should win. The winner then formed his own ZZJYT consisting of team members they selected from across the corporation. According to Zhang Ruimin, the purpose of this approach was to develop “a free market in talent, so the cream rises”. The person, in the vote for the new product or service, would also be placed in the team and have the opportunity to take control of the group if the original leader was unable to perform satisfactorily. This is part of the so-called “catfish management” approach, meant to promote a culture with a high degree of competition and tension. The need for middle-management would be greatly reduced with the Networking Strategy since the ZZJYTs were allowed to act independently as long as they were able to contribute value to the firm - bringing down costs while empowering employees. Some people have been skeptical about the lack of management and the risk of an uncontrollable and unproductive chaos. Zhang himself said that “We don’t need to balance. An unsteady and dynamic environment is the best way to keep everyone flexible”<sup>18</sup>.

A recent development of the Networking Strategy was the implementation of an internal social platform that provide a quick overview of the employees available for new projects and keeps track of their performance in previous project groups<sup>19</sup>.

The restructuring of Haier led to a reduction in the workforce of 16,000 jobs, in 2013, equivalent to 18 % of its workforce, and again in 2014, 10,000 jobs were cut, resulting in a company with around 60,000 employees<sup>20</sup>. Some of the layoffs were among semi-skilled workers, due to automatization of the production lines through the installation of industrial robots, while others were middle-level managers, partly due to the implementation of the ZZJYT structure<sup>21</sup>.

However, some of these laid-off workers have been able to find new jobs close to the Haier organization; the company has recently started moving towards a new step of the Networking Strategy by outsourcing an increasingly large number of tasks to new micro-enterprises that sub-contract to Haier. These micro-enterprises are often started by either former or current employees at Haier and therefore have a close

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<sup>17</sup> [http://www.haier.net/en/about\\_haier/haier\\_strategy/network\\_strategy/](http://www.haier.net/en/about_haier/haier_strategy/network_strategy/), accessed 26/3-2015

<sup>18</sup> “Haier and higher”, published 12/10-2013 by The Economist

<sup>19</sup> “Look East For Management Innovation” by Jeff Sampler. Published 2/7-2014 by Forbes

<sup>20</sup> “Haier to axe 10,000 jobs this year” by Tetsuya Abe. Published 17/6-2015 by Nikkei Asian Review

<sup>21</sup> “A Chinese business model for the Internet Age”, published 3/12-2014 by China Daily

connection to the company. For example, Beijing Haihengfeng Commercial Consulting Co. Lt., a private consulting firm led by Wang Xiaoqiang who started the firm together with eight former colleagues at Haier Beijing Industry and Trade Co., one of Haier's regional sales divisions<sup>22</sup>. Zhang Ruimin's vision of Haier is not as a traditional manufacturer and marketer of home appliances, but rather as a business platform that provides capital and support for a network of different micro-enterprises. As of late 2014, there were around 200 micro-enterprises working for Haier but this number has been fluctuating a lot due to a large number of turnovers among the micro-enterprises.

## Questions:

- For which of the 26 dimensions in Burton, R. M., Obel, B., & Håkansson D. (2015). *Organizational design: A step-by-step approach*. Cambridge University Press. Third edition are you able to determine the scores for the Internet Age at Haier?
- What are the scores on these dimensions?
- What should the scores be for those dimensions that you couldn't find a score for in the case description?
- What misfits, if any, does Haier have?
- Where should Haier be located in the design space? That is, what should Haier do to fix its misfits?
- If Zhang were to leave as CEO, can you develop a leadership profile for the new CEO of Haier? The new leader might be very much like Zhang, or would a very different leader be more appropriate for the new Haier?
- Why do you think Haier's structure, task design, culture, leadership, incentives, would be a disaster for the acquired pharmaceutical firm? Can you suggest a better approach for the pharma firm? Apply the model in Burton, Obel and Håkansson. Do two analyzes – one for Haier and one for a pharma company. Then do a fit analysis comparing the two companies. Then examine the misfits for each and compare them as well. Explain why Haier did not do well with the pharma company. Can you anticipate other companies for which a merger into Haier is not likely to work well?
- The Internet Age Haier can be compared with Valve. You can find a description and analysis of Valve in the Organization Zoo, Journal of Organization Design, v. 4, n. 2, 2015. What are similarities and differences between Haier and Value?

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<sup>22</sup> "Haier's New Look: 'Micro-Enterprise' Platform" by He Chunmei and Chen Lu. Published 27/8-2014 by Caixin Online

## **Timeline**

### **Turnaround**

1984: Zhang Ruimin is appointed managing director and Haier starts importing technology from Liebherr

1985: The destruction of faulty refrigerators, symbolizing the turn-around for Haier

### **Diversification phase**

1988: Haier assumes control of Qingdao Electroplating Company

1991: Haier takes over Qingdao Air Conditioner Plant and Qingdao Freezer

1992: Haier adopts its current name

### **Global expansion**

1992: Haier acquires ISO 9001 quality certification for its refrigerators

1996: Haier opens a production facility in Indonesia

1997: Haier opens a production facility in the Philippines and Malaysia

1997: Haier moves into television manufacturing with the acquisition of Huangshan Electronics Group

2000: Haier opens a production facility in the U.S., in order to compete in the North American market

2002: Haier opens a production facility in Pakistan

2003: Haier opens a production facility in Jordan

2008: Haier surpasses Whirlpool as the world's largest producer of refrigerators, with 12 million refrigerators sold worldwide, equivalent to a global market share of 6.3 percent

2011: Haier acquires the Japanese Sanyo White Goods

2012: Haier buys the New Zealand appliance manufacturing company Fisher & Paykel

### **Restructuring**

2012: Adoption of the Networking Strategy

2013: Haier starts to reduce its workforce by cutting 16,000 jobs

2014: The Haier brand has the largest share of the market in white goods, with 10.2 percent



Exhibit 1: The different stages of Haier's business strategy. Source: haier.net



Exhibit 2: Group chart for Qingdao Haier. Source: haier.net