



EXPATRIATE MANAGEMENT: A BUSINESS MODEL FOR DIVERSITY MANAGEMENT

Programme for the Practice of Diversity Management

Department of Immigration and Multicultural Affairs in Cooperation with the
Australian Centre for International Business

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EXPATRIATE MANAGEMENT: A BUSINESS MODEL FOR DIVERSITY MANAGEMENT

2001

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Foreword

The Programme for the Practice of Diversity Management is in the process of developing several diversity-related Business Models. This Business Model addresses the role of diversity capabilities in managing expatriate success. A matching Toolkit addresses the implementation of diversity initiatives to enhance expatriate performance.

Other Resources for Diversity Management:

The Business Case:

HRM Case

Knowledge Firm Case

International Business Case

Marketing Case

Theory of Diversity and Group performance

Business Models:

Diversity Management: the Big Picture

Managing Diverse Human Resources Effectively

Expatriate Management

Capturing the Diversity Dividend

Going Global

Adding Value through HRM

Toolkits:

Attract, retain and motivate

Keys to Expatriate Success

Adding Value through HRM

Using Diversity Climate Surveys

Diversity Management in Australia – the State of Play

Capturing the Diversity Dividend

Report to Business on Aboriginal Employment

PROGRAMME FOR THE PRACTICE OF DIVERSITY MANAGEMENT

The Programme for the Practice of Diversity Management is a collaborative arrangement between the Department of Immigration and Multicultural Affairs (DIMA) and the Australian Centre for International Business (ACIB) funded through DIMA's Productive Diversity Partnership Programme.

The mission of the Programme for the Practice of Diversity Management is to meet the practical needs of business by developing a business case for productive diversity, providing Business Models for diversity management, and creating Toolkits and checklists for assessing diversity.

The Programme invites your firm to become a member of the electronic Diversity-Network, which brings Australian business together to promote good diversity practices.

Join the diversity network on-line at www.ecom.unimelb.edu.au/acib/diverse/

Executive Summary

The Business Case : Bottom-Line Benefits of Diversity Management

Expatriates and Business success

Diversity management reduces the bottom-line costs of expatriation.

Challenges of cultural complexity

One of the greatest challenges for expatriates is cross-cultural complexity. Diversity management facilitates the development of cross-cultural capabilities to manage such complexity.

Cultural diversity is a missed opportunity in Australian business

Survey results reveal that firms are not making the most of their diversity capabilities.

What is Diversity?

Diversity is all the ways in which individuals differ, both on a personal basis and in terms of organisation-related characteristics.

Understanding Culturally-Complex Environments

Mental Models: a new framework for understanding culture

Mental models reveal how people interpret their environments and understand events.

Convergent mental models: how firms understand

Expatriates who share mental models with host nationals have special cross-cultural capabilities.

Divergent mental models: conflict in firms

Divergent mental models with host nationals impose costs on firms by hindering communication.

Formal and informal institutions: why culture is important

Institutions are the 'rules of the game' that firms need to understand in order to be effective.

The Evidence: how diversity capabilities impact on the bottom line

Culture shock

Many expatriates experience culture shock and have difficulty adjusting to a new culture.

Diversity capabilities reduce culture shock

Expatriates with sound diversity capabilities overcome culture shock quickly.

Direct costs of expatriation

Direct expatriation costs range between \$200,000 and \$1,500,000 per year.

Cost of expatriate failure

When expatriates fail, firms incur both the loss of direct costs and indirect costs, such as damage to goodwill.

Diversity management: avoiding expatriate failure

By aiding expatriate adjustment, diversity capabilities reduce failure.

Diversity capabilities: Expatriates with an 'edge'

Expatriates with strong diversity capabilities benefit firms through their skills in partner selection; building personal relations; communication with host nationals; managing in corrupt environments; and navigating transitional economies

Diversity strategies: keys to success

The five key steps to expatriate success are:

1. Conduct an expatriate audit;
2. Conduct a cultural diversity audit;
3. Refine expatriate selection;
4. Provide cross-cultural training; and
5. Provide repatriation assistance

The Business Case: Bottom-Line Benefits of Diversity Management

Expatriates and business success

The management of expatriate assignments is critical to international business success. Diversity management reduces the costs of expatriation and improves expatriate success rates. Expatriates are managers and employees relocated from one country to another. Expatriate managers oversee international joint ventures (IJVs), alliances (including franchises and licensing) and overseas subsidiaries. They play a crucial role in ensuring the success of multinational enterprises (MNEs) international operations. Expatriate technicians bring specialised expertise to overseas business processes. All expatriates engage in international business activities in host environments that are often vastly different to those of the parent company.

Challenges of cultural complexity

One of the greatest challenges for expatriates is the cultural complexity of the environments in which they operate. They are confronted with new systems of values, beliefs and 'ways of doing things' that may be dramatically different to those of their home country. Such variation complicates the international business environment and expatriates are at the forefront of managing this complexity. Consequently, the development of expatriate cross-cultural capabilities is essential for international business success.

Managing diversity productively can ensure that firms can create expatriate cross-cultural capabilities. The transition of expatriates into culturally distant locations can be extremely difficult. Expatriates who originate from the country or region of their posting will adjust more readily to their assignment than those with little experience of their new cultural

environment. Such individuals will be more effective than those who struggle to adjust to foreign cultures. Their superior performance has a direct impact on the firm's bottom-line.

The cross-cultural capabilities that emerge from managing diversity for expatriate assignments contain bottom-line benefits for firms that operate globally.

Cultural diversity is a missed opportunity in Australian business

A 2000 survey conducted by the Australian Centre for International Business showed that 68 percent of CEOs ranked managing diversity for understanding the complexity of overseas cultural environments as of moderate-high importance. Seventy-one percent (71%) of CEOs ranked managing diversity as of moderate-high importance for serving new foreign buyers/consumers.

Despite the recognition of the importance of diversity management in internationalisation, only three percent of firms *always* selected expatriate managers from the same cultural background as host nationals and sixteen percent *never* sent expatriate managers from the same cultural background. The survey results show Australian CEOs are failing to capture the bottom-line benefits for expatriate assignments of diversity management.

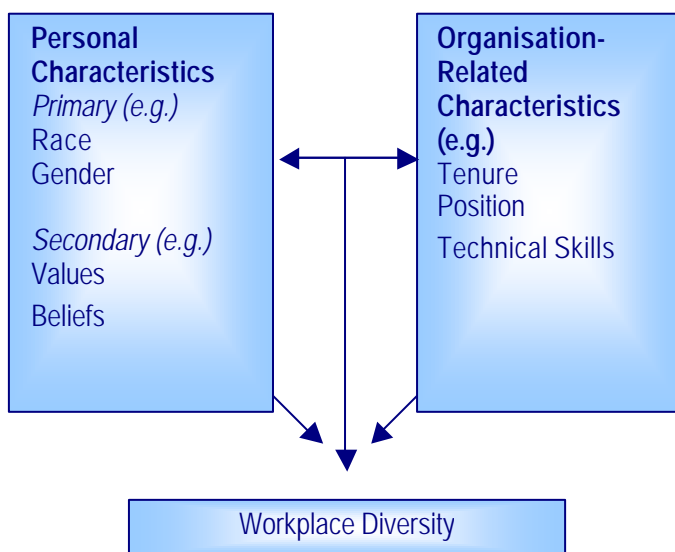
What is Diversity?

Diversity is all the ways in which individuals differ, both on a personal basis and in terms of organisation-related characteristics. Figure 1 shows that the major components of diversity comprise:

- Primary personal characteristics e.g. ethnicity, gender, sexual orientation,

- nationality, and mental and physical ability
- Secondary personal characteristics e.g. marital status, educational level, values and beliefs
- Organisation-related characteristics e.g. position in hierarchy, tenure, casual/part-time/full-time status

Figure 1. Components of workplace diversity



Understanding Culturally-Complex Environments

Mental Models: a new framework for understanding culture

Mental models provide a new framework for understanding culture that captures complexity. Mental models reveal how people understand their environments, determining the type of information they receive and the ways in which they process that information. Mental models are deeply embedded in individuals and act as software to process data. Such models are socially learned, educationally reinforced and experientially altered.

Expatriates managers who originate from the host country culture have well developed mental models to operate global alliances, subsidiaries and international joint ventures. Culturally-adept expatriates apply such mental models to interpret the business environment.

Convergent mental models: how firms understand

Mental models can converge and operate at the group level. Collective mental models emerge from shared experiences that become stored in a group's social memory'. While no two individuals have the exact same set of mental models, there are many shared mental models amongst people of the same ethnic, religious, linguistic and national groups.

The degree to which individual mental models overlap has been termed 'strategic consensus'. Strategic consensus enhances the ability of interacting parties to coordinate their activities and facilitates collaborative decision-making processes. Individuals are more likely to communicate with each other when they share common features in their mental models.

Expatriates who share a cultural background with overseas alliance partners, managers, workers and government officials reap the dividends of convergent mental models.

Divergent mental models: conflict in firms

When mental models between individuals are significantly divergent, there is considerable scope for miscommunication and conflict. Divergent mental models impose costs on business, which must invest in infrastructure to bridge communication gaps. Such gaps are a major cause of international joint venture failure.

Formal and informal institutions: why culture is important

Institutions are the 'rules of the game'. They may be formal – laws and regulations - or informal – taboos, customs and traditions. Institutions vary between countries, and informal institutions are often more important than formal institutions. This has important ramifications for international business. Firms need to understand that they may have to operate according to informal 'rules', which may be contrary to formal institutions.

These informal 'rules' are particularly important in transitional economies, where 'corruption' is present and norms and beliefs are different from Australia. Australian firms need expatriates who can navigate culturally-complex environments in foreign countries and 'play the game' according to the informal 'rules'.

The Evidence: how diversity capabilities impact on the bottom line

Culture Shock

Many expatriates experience 'culture shock'. They are unable to interpret cues from a new and uncertain environment. They are faced with the seemingly inexplicable behaviour of those around them, which is governed by a culture that they do not understand. Their lack of comprehensive mental models for understanding the local culture inhibits their awareness of what is appropriate, or inappropriate, behaviour. Expatriates discover that their past behaviours do not work in the new culture, but they have not yet learned more appropriate substitute behaviours. This is a source of immense frustration, which causes high levels of confusion and anxiety. The confusion that

they experience is often exacerbated when they do not speak the local language.

Culture shock is caused by multiple stresses – intellectual, emotional and physiological – that place individuals under severe pressure. These stresses impair the ability of expatriates to function.

Culture shock is alleviated as expatriates become accustomed to their new surroundings, learning to 'fit in'. There is a period of reduced productivity while expatriates adjust.

Australian firms need expatriate managers who can navigate culturally-complex environments

Expatriates take between four and twelve months to feel comfortable in a new culture. Some expatriates take even longer, while about five percent never adapt to the new culture. Such individuals experience their postings in an ongoing state of culture shock, constantly trying to adjust. Consequently, their productivity is permanently impaired.

Diversity capabilities reduce culture shock

Diverse organisations can reduce the impact of culture shock on their expatriates by selecting expatriates who share the cultural background of the host country. The host culture holds fewer surprises as expatriates have existing mental models to understand their surroundings. The level of uncertainty is reduced. They are able to relate to others with ease, in culturally appropriate ways and in the local language. They are already comfortable with the cultural norms of their host country co-workers. The adjustment process is relatively fast and smooth.

Diverse organisations have superior capabilities for coping with difference compared to homogeneous organisations. Managers who work in diverse organisations become comfortable with difference. Such managers are accustomed to working with people from many cultural backgrounds and with many different world views. Diverse organisations foster managers with valuable cross-cultural skills. These skills reduce the amount of time it takes expatriate managers to adjust to overseas assignments. They experience reduced culture shock followed by speedier recovery.

Reducing culture shock and enhancing expatriate adjustment benefits the firm's bottom line by boosting productivity.

Direct Costs of Expatriation

Expatriate assignments impose direct costs on firms. The cost of maintaining an expatriate manager is estimated to be between \$200,000 and \$1,500,000 per year, depending on the country of assignment, salary, housing, home leave, company cars, air fares, relocation allowances, foreign service premiums, and schooling for children. Figure 2, Estimates the annual costs of maintaining an Australian expatriate manager in Hong Kong earning a salary of \$200,000.

Figure 2. Expatriation costs

Salary	\$200 000
Housing	\$150 000 - \$300 000
Foreign service premium	\$20 000 - \$50 000
Company cars	\$8 000 - \$ 30 000
Air fares	\$6 000 - \$24 000
Relocation allowance	\$10 000 - \$80 000
Schooling for children	Approx \$20 000 per child

As a rule of thumb, the total cost per year to the firm of maintaining an expatriate is expatriate salary multiplied by three.

Cost of expatriate failure

Expatriate failure is costly. Most large MNEs have had at least some failed expatriate assignments. Expatriate failure is the failure of expatriates to meet the goals of their overseas assignments. It is usually measured as the rate of premature recall back to the home country. While large scale empirical research has not been conducted into Australian expatriate failure rates, it is estimated that around five to ten percent of Australian expatriates fail.

Workforce diversity capabilities reduce the potential costs of expatriate assignments

In addition to the resources allocated to failed expatriate assignments, there are costs of repatriation of the failed expatriate as well as finding a replacement. US research reveals that the estimated direct costs of a failed overseas assignment ranges from US\$200 000 to US\$1.2 million. Further costs may be incurred if the failed expatriate has actually caused damage to an overseas business operation. Damage to the goodwill of partners, suppliers, distributors, buyers and government officials can seriously impact upon the business prospects of an overseas venture.

Most expatriate failures are caused by the inability of individuals and their accompanying families to understand and adapt to foreign cultures. They are poorly prepared for the challenges posed by cultural complexity.

Diversity management: avoiding expatriate failure

Workforce diversity capabilities reduce the potential costs of expatriate assignments. The selection of expatriates who share the national cultural background of the country to which they are assigned means that they have minimal difficulty adjusting to the host

country's culture. Well adjusted expatriates are less likely to fail in their assignments than expatriates who struggle in 'foreign' cultures. Although expatriates from the host country culture still must adjust to the organisational culture of their new assignment, this process will be easier than for expatriates who are unfamiliar with local languages, customs and ways of operating. Selecting national expatriates translates into increased productivity, reduced time adjusting to national cultural norms and the ability to more quickly focus on organisational tasks.

Diversity capabilities: expatriates with an 'edge'

Partner selection

Diversity capabilities are particularly valuable for establishing new IJVs, especially at the initiation stage. US research has demonstrated that 'partner problems' are the greatest source of IJV problems and failures. Such problems emerge as a consequence of poor partner selection. Too often, firms rely on poorly informed second-hand information available through diplomatic and expatriate communities in their search for a foreign partner.

Expatriates with a host country background have valuable capabilities for establishing new foreign ventures

The selection of expatriates with a host country background prevents such reliance on inferior information for partner selection. Expatriates with an in-depth knowledge of host environments, including shared mental models with locals, are better placed to make wise partner selection decisions. Firms can benefit from the cultural, organisational and industry based knowledge held by such expatriate managers.

Building personal relations

Diversity management enhances the ability of business to build interpersonal overseas networks. While personal connections play an important role in business all over the world, they are ubiquitous in Chinese business, both within and outside China. The establishment of strong interpersonal relationships and effective communications is critical in maintaining the necessary trust between business partners to facilitate ongoing exchange.

Expatriate managers of the same cultural background as host country nationals have special capabilities for establishing personal overseas networks. Such expatriates share many similar personal characteristics with locals. Studies of human similarity reveal that similar individuals are likely to form favourable impressions of each other, enhancing the potential to establish strong interpersonal relationships. Consistent and reliable interactions within these networks promote trust within the business relationship.

Local language proficiency is crucial for establishing local networks. Personal relations are difficult to establish when individuals do not share a common language.

Personal connections can be particularly valuable for securing access to scarce resources, such as government licenses, permits, special loans and credit facilities, subsidies, discounted privatisations and contracts. Well connected expatriates may have access to informal information about potential sources of income that may not be publicly available. Firms that employ such expatriates have an advantage over firms lacking cross-cultural capabilities.

Communication with host nationals

Expatriates who speak the national language of the host country have an advantage over those who lack this capability. The assumption that, as the

lingua franca, English proficiency is sufficient for international business is false. Much of a nation's culture is contained within its language. Firms that wish to excel in foreign linguistic environments have much to gain from selecting multilingual expatriates, including:

- access to overseas social networks;
- understanding of foreign negotiating styles;
- knowledge of how to conduct market research; and
- an ability to quickly contact suppliers, distributors and buyers by telephone/e-mail/fax in their preferred language.

Managing in corrupt environments

Diversity capabilities assist firms in understanding [corruption](#) in foreign environments. While corruption exists, to varying degrees, in all societies the challenge for international business is to understand the different ways corruption manifests in foreign environments. Corruption, the abuse of public office for private gain, is often a problem where the development of formal political and economic institutions lags the sophistication of capital stock and where the state exerts tight control over the economy.

Expatriates with a background in the host country will have culturally derived mental models to identify and understand corruption risks to the firm. Such risks can range from pressure to pay bribes to 'grease the wheels' of state bureaucracy to 'theft by stealth' of the firm's physical and intellectual property. Once culturally skilled expatriates are aware of how corruption manifests in the business environment, they can implement appropriate strategies to manage corruption risks.

Managing in Transitional Economies

[Transitional economies](#) are the latest source of new investment opportunities, but they have unstable and ill-defined formal

economic institutions. Relative to domestic companies, Australian firms have inferior knowledge of host country political, economic and social institutions and organisations. They face costs of learning 'how things are done' that carry implications for their competitiveness. Failure to understand informal norms in transitional economies can seriously erode returns on assets.

Expatriates with a background in the host country have valuable capabilities for navigating these transitional economies. Their mental models of the business environment converge with those of host nationals, narrowing the environmental knowledge gap between Australian and domestic companies.

The political know-how of well informed expatriate managers with a host country background ranges from lobbying capabilities and knowledge of routinised processes for applying political pressure, to highly nuanced knowledge of when a 'word in the right ear' is appropriate. Such know-how can be effectively exploited by the firm. Possessing clear mental models of the informal 'rules', these expatriates can succeed in the 'game'.

Diversity strategies: keys to success

There are five key steps to expatriate success:

1. Conduct an expatriate audit;
2. Conduct a cultural diversity audit;
3. Refine expatriate selection procedures;
4. Provide cross-cultural training; and
5. Provide repatriation assistance

These steps, explained below, are the subject of an expatriate toolkit produced by the *Programme for the Practice of Diversity Management*.

Step one: expatriate audit

An expatriate audit allows firms to review their current expatriate practices. Firms can identify their expatriate failure rates and address the causes of costly expatriate failure. Equally, firms can determine sources of success for expatriates. Through compiling information about the experiences of current expatriates and repatriates, firms can create knowledge to improve future expatriate assignments.

Step two: cultural diversity audit

Diversity management requires data on firm diversity and characteristics of employees. A cultural diversity audit provides firms with the opportunity to identify the cultural diversity within its workforce. The process and aims of a the audit are similar to skill audits commonly undertaken by large organisations. A survey of all employees is undertaken seeking information on factors such as cultural identification; place of birth and education; and language skills. This provides management with a 'diversity picture', identifying skills of the firm's human resources.

A cultural diversity audit allows for the construction of an organisational diversity profile that identifies the firm's diversity capabilities for managing in culturally-complex environments. Firms can harness this knowledge for selecting expatriates with cross-cultural capabilities for overseas assignments.

Step three: expatriate selection

Having identified the diversity capabilities residing within the workforce, firms are well positioned to select top-performing expatriates. Firms need to consider the cross-cultural capabilities of potential candidates as well as their technical and managerial expertise. Expatriates who

possess clear mental models of the host country cultural environment and who are open to 'difference' make ideal candidates. Candidates with a background in the host country will have the most detailed and accurate mental models of the foreign culture.

When selecting potential expatriates to culturally distant locations, firms should emphasise the individual's 'relational abilities'. Such candidates should be accustomed to managing a diverse workforce and possess diversity capabilities that allow them to feel 'comfortable with difference'.

Step four: cross-cultural training

Cross-cultural training reduces expatriate and foreign venture failure. Such training is important for all expatriates, but especially important for individuals with little knowledge of the host environment. Cross-cultural training eases the burden of culture shock and helps expatriates to adjust to their new surroundings.

Cross-cultural training is a second best solution because it provides expatriates with neither deep understandings of the host environment nor the complex mental models needed to navigate foreign formal and informal institutions. Consequently, utilisation of cultural diversity capabilities remains a superior solution.

Family cross-cultural training

Cross-cultural training must be ongoing to ensure the best chance of ameliorating culture shock. It should also involve the accompanying family since 'family problems' are the largest cause of premature termination of expatriate assignments. Such training should include:

- pre-departure country briefing;
- some basic language training;
- on-arrival coaching (eg. mentor

Cultural diversity capabilities are superior to cross-cultural training

- programmes);
- training in cross-cultural understanding;
- and repatriation assistance.

Costs of cross-cultural training

Cross-cultural training is costly, as shown in Figure 3. A cross-cultural or country briefing course costs around \$1600 per day. In-depth training costs even more. Despite the costs of training, it is a small insurance premium relative to the much greater costs of expatriate failure outlined above.

Figure 3 Expatriate training costs

Type of training	Approximate cost
18 hours foreign language training at the Centre for Adult Education Australia	\$248 per participant
One day country briefing and cross-cultural training workshop at International Languages Australia	\$1365 fixed, plus \$235 per participant
Two day cross-cultural training seminar in Bangkok	\$900 per participant
Two day country briefing at 3C New York	\$3500 per participant

Step five: reaping repatriation rewards

Repatriation assistance is an integral component of any expatriate package. Research demonstrates major discontent with the repatriation experience. Many repatriate managers feel that the skills that they have gained overseas are not valued in the home country. They often return from senior management in the host country to a position of lesser status back home.

Poor repatriation practices may reduce the pool of potential expatriates. Where

individuals view overseas placement not only as a hardship, but as a career move that reduces their perceived value on return, they are unlikely to be willing to accept foreign postings.

Dissatisfaction with repatriation means that about half of all repatriates leave the firm within two years of their return to the home country; translating into a loss of valuable skill and experience.

Repatriation assistance is crucial for preventing the turnover of repatriates with valuable cross-cultural and international management skills. Such repatriates are a source of knowledge and learning, which can be disseminated throughout the firm. Firms that fail to assist repatriate managers may find their repatriates poached by their competitors.

The business case restated

The expatriate business case for managing diversity is simple: effective diversity management enhances expatriate performance and reduces failure. Diversity management improves the firm's bottom line by enabling international business to leverage the cross-cultural capabilities of their human resources.

Deep mental models of both the host culture and organisational processes reside within expatriates with a background in the host culture. Such expatriates will require less extensive, and less costly, training compared to those who lack such models.

Culturally-adept expatriate managers are superior international performers with special capabilities in partner selection, communications, building personal relations, managing corruption, and negotiating complex institutional environments in transitional economies.