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Why Ignoring Cultural Differences Causes Production Relocations, PMIs, Company Acquisitions, or Private Equity Investments to Fail

Ignoring cultural differences is a crucial factor when it comes to the question of why production relocations or the integration of acquired companies fail in practice.

Technical processes are plannable and can be copied according to best practices. Machines and equipment are installed identically – no problem. Quality standards are defined and clearly verifiable in the form of drawings – also no problem. But what about the human factor? With their lived understanding of delivery date reliability, quality, and best practices? Read here how the consideration or disregard of cultural differences determines the success or failure of a production relocation or integration.

What's It About?

Production relocations, merger PMI scenarios, or the acquisition of companies by private equity investors always have one thing in common: It's about integrating parts of companies or outsourcing production processes or entire productions. To prevent this contribution from expanding into a small dissertation, I'll limit myself here to the essential factor – the maximum economic success of the project.

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Mergers, PMI Scenarios, or Company Acquisitions

It doesn't matter which of the three scenarios we're specifically dealing with – almost always the same mistake is made: The company to be taken over or integrated is completely examined with the help of an auditing firm as part of a due diligence. This must and should be done in order to:

- agree on the purchase price,
- demonstrate the economic viability,
- expose any financial risks, and
- identify and derive further measures to make the transaction economically more attractive.

But What About the Cultural Due Diligence?

Apart from figures, data, facts (FDF)? Apart from economic and accounting key figures? Cultural differences in takeover scenarios simply cannot be expressed in FDF and, in the best case, only lead to considerable additional costs, often to interrupted supply chains or the failure of the entire transaction.

Very often, a technical due diligence is also not carried out, or only superficially. This often leads not only to significant, unplanned investments, but also to disrupted supply chains and a greatly reduced ROI.

The disregard of cultural differences or the failure to conduct a cultural due diligence is by far the biggest mistake. You're wondering why this is the case?

Here's the explanation:

Cultural differences can be so severe that they cause projects to fail completely, lead to significant delays in implementation, completely interrupt supply chains, and jeopardize customer relationships. The economic benefit is often gone or reduced to absurdity. Different understandings of business processes and values, as well as seemingly simple language barriers and culturally conditioned different behavioral patterns, endanger the implementation of the project and do not stop at management:

Global Cultural Differences

Language barriers: Except for the plant manager and perhaps the production manager, nobody speaks or understands English (let alone German). So how do you communicate on the shop floor? How do you convey details on drawings that have English or German annotations? How do you secure quality-relevant issues on the shop floor? How do you discuss and implement process issues

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on the shop floor? Sure, all of this can be solved somehow! But it costs time, money, and leads to instability in the supply chain.

Regional management culture: Eastern European countries are often the focus when it comes to relocations. Experience shows that changing views on historically/politically shaped standards, processes, and communication patterns often takes generations. This explicitly includes top management. This can certainly be solved as well, but it also costs time, money, and leads to instability in the supply chain.

Country-specific cultural differences may sound trivial at first, but in practice, they are a real stumbling block:

- Start at 2:00 PM. It's 2:00 PM and participants are gradually trickling in – completely normal in other cultures.
- Projector? Doesn't exist.
- Binding agreements are not considered binding because they simply haven't been lived by until now.
- Overtime or extra shifts? Almost impossible to implement, as the compensation is so unattractive that additional working time brings no economic benefit for the individual worker. A second job is more likely.
- 'Just now' means 'sometime'.
- The willingness to take (personal) responsibility or proactively plan the next process or action step is often not present – also due to the compensation model: Exactly what one is paid for is done – and nothing more.
- The team concept does not exist; working in silos and personal reputation are in the foreground. This is also often due to the compensation system.
- 'Leadership' often means a strongly hierarchical leadership culture in which the collective plays a subordinate to no role at all: In practice, this means that all processes can only be implemented through top management. If there are (culturally conditioned) resistances here, this leads to enormous time loss and significant economic disadvantages.

Operationally and in practice, this means:

Management Structure:

The organizational and operational structure differs fundamentally and cannot be integrated as is. Contact persons are missing, responsibilities are organized completely differently or are non-existent. This also sounds simple at first, but in practice, real issues arise here with an impact on supply chains and customer relationships.

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Entrepreneurial Scope:

The focus is on one's own, location-specific economic result. The interaction within a group, with the goal of strengthening the group, is not understood and the actions (of management) are accordingly inward-oriented. This means that decisions are blocked, which in turn has negative effects on the desired economic result.

Shopfloor:

There are often unique, location-specific processes that affect absolutely relevant topics such as quality (tolerances regarding drawings, inspection instructions, welding specifications, etc.), production standards (frozen zone, lot sizes, test equipment, sampling, documentation, etc.) or production key figures (KPIs). In practice, this leads to considerable discussions with enormous time delays and irritations regarding the supply chain and the customer.

Location-specific Sub-Culture:

Often there are decades-old location or company-specific sub-cultures whose origin is not rooted in country-specific differences. These established and lived, location-specific structures shape the social behavior of people locally in the company, the social behavior among each other, the communication culture – internally and externally, as well as the hierarchically shaped pyramid of responsibility. From my experience, changing this local and site-specific culture is only possible over years. It is therefore absolutely necessary to recognize these differences and adapt to discrepancies in order to avoid a time delay of the project and thus avert economic damage.

What does this mean now?

A decision to relocate production, acquire a company, or carry out a merger should never be made solely on the basis of purely economic factors. A decision in the context of economic viability (ZDF) to cultural differences to technical parameters is essential to derive the full benefit from the deal. Neglecting one of the factors leads, based on experience, to the failure of the project or at least to a significantly reduced economic benefit.

What do we learn from this?

Whether merger, company acquisition or production relocation – the classic due diligence or the decision of production relocation **without thorough consideration of cultural differences** carries an immense risk. For smaller SMEs, without financial strength, this can mean downfall (keyword: production relocation). Certainly, not all details necessarily come to the surface during a **Cultural Due Diligence**. However, risks can be derived and measures can be set up in advance through the **Cultural Due Diligence**. A risk analysis can be made and measures to minimize the risk (Risk Mitigation) can be determined.

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The decisive factor for the success or failure of a project is therefore NOT only the purely economic consideration – but the inclusion of cultural differences in the deal.

The 'dear' technology - Can it even do that!?

Technical Due Diligence

Now let's assume the **Standard Due Diligence** and also the **Cultural Due Diligence** have been carried out. However, there is another aspect that has a severe impact on the economic success of the project: the **Technical Due Diligence**.

In practice, a **technical due diligence** is often implemented half-heartedly at best. The CTO examines the processes, including existing machines and equipment, without delving deeper. However, this is precisely where the 'crux of the matter' lies: Are the technical requirements actually feasible with the existing machines and equipment? The details are crucial here:

- Tube profile bending machines: present. However: what tolerances can they maintain?! Is that even suitable?
- Welding robots: present. However: are they laser-guided?! Or just tactile?
- Welding equipment: present. However: pulse or not?! Parameters adjustable at the nozzle or not?
- Press brakes: present. However: what is the maximum width?!
- Measuring equipment: present. However: does the existing equipment in the measuring room meet the parameters required by the customer? Are the existing measuring devices compatible?
- Paint shop: present. However: what is the maximum capacity?! Grandfathering?!
- Assembly line: present. However: are the existing stations sufficient?! Can the assembly line be extended?! Are the corresponding aids available?!

All these points – and in reality, many more – can lead to necessary investments that were not budgeted for in advance as part of the deal. Furthermore, in addition to the extra costs, delays occur due to delivery times from suppliers of the required machines and equipment. This, in turn, leads to a delay of the entire project – including endangering the supply chain to the customer plus loss of credibility for the customer. Not to mention the time needed for commissioning any new machines and equipment plus initial samples and PPAP and… and… and…

My experience from conducted production relocations and PMI shows that evaluating the technical feasibility with existing machines and equipment plays a crucial role. In the worst case, substantial investments need to be made, which call into question the economic success or set back the ROI of the project by years. For some SMEs, this simply means the end.

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In a nutshell …

The combination of disregarding cultural differences (Cultural Due Diligence) AND failing to consider the technical parameters (technical due diligence) before the actual deal or project start is definitely negligent and often leads to project failure in practice. For a smaller SME, this is a threat to its existence – for a group or an investor, it means economic failure – in other words: burning money.

André Krings

I am available for an exchange of experiences with an operational focus! As an Interim Manager, I bring leadership strength, strategic competence, and a goal-oriented, hands-on approach.

My focus is on increasing process efficiency and profitability through pragmatic Lean Management. I am a value-oriented, empathetic leader with strong communication skills, social competence, and intercultural experience.

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