Globally Dispersed Startups

by

Avner Halperin

M.Sc., Applied Physics
Tel Aviv University, Tel Aviv, Israel (1993)

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Signature of Author: _____
Alfred P. Sloan School of Management
May 4, 2001

Certified by: _____
Janice A. Klein
Senior Lecturer, Management Science
Thesis Supervisor

Certified by: _____
D. Eleanor Westney
Society of Sloan Fellows Professor of International Management
Thesis Reader

Accepted by: ____ _____
Stephen Sacca
Director, Sloan Fellows Program
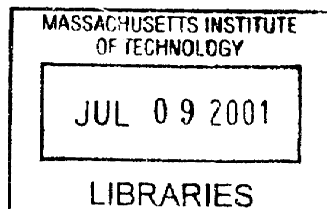
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ABSTRACT

Managing a hi-tech startup in the USA is a difficult challenge. Managing a startup based in a peripheral country is next to impossible. It requires setting up a strategic operations office in a different country and managing a startup that is globally dispersed.

This thesis analyzes Israeli startups as a case in point in managing globally dispersed startups. In depth interviews were conducted with several Israeli startup companies that have globally dispersed operations. Wide coverage interviews were conducted with members of Israel's Venture Capital community, and Social Network Analysis was done to provide qualitative measure of organizational unity.

It was shown that the keys to a dispersed startup success are balance and trust. These can be achieved through some best practices that are described in this work.

Thesis Supervisor: Janice A. Klein
        Title: Senior Lecturer, Management Science

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Introduction and Executive Summary

This work analyzes the organizational challenges faced by startups originated in peripheral countries. Peripheral countries are those whose domestic markets cannot support a technology product business plan. Startups in peripheral countries must target foreign markets. Therefore they locate their strategic operations (marketing and business development functions) in their target markets. Thus, they face the organizational challenge of managing a startup whose organization is split into two parts R&D in the home country and strategic operations in the target market country.

This research used Israeli startups as a case study. Israel's recent high tech boom generated thousands of startups whose target market is in the USA. These startups have opened strategic offices in the USA while maintaining their R&D department in Israel. They face the challenges of a globally dispersed operation in an extremely fast paced and low budget constraint.

In order to evaluate best practices in globally dispersed startups, this research used multiple interviews with managers of Israeli startups and veteran Venture Capital professionals located on both sides of the Atlantic Ocean. Further, available theory of global teams and Israeli startups were analyzed. Finally, a Social Network Analysis tool called InFlow Software was used to qualitatively analyze the effectiveness of different organizational layouts.

The interviews and analysis uncovered two critical success factors:

1. Balance between the two locations. Neither one should become dominant. Neither should feel neglected.

2. Trust must be built between the two locations.

To achieve the above criteria the following is required:

- Founders must be split between locations. Having them all in one site, limits cross-site trust level and generates a feeling of neglect in the other site. Splitting the founders develops high trust relationships between the two locations (See diagrams in Appendix C). Trust can be further enhanced by crossing over R&D engineers and marketing people into both locations.

- CEO must be balanced in closeness between USA and Israel. Unlike common wisdom, hiring American CEOs has not proven successful for Israeli startups. In most cases, it is advisable to hire an Israeli CEO (preferably with US employment or education experience) and locate her in the USA.

- Cultural differences must be celebrated and learned. Careful use of cultural differences and stereotypes can turn cultural differences into a competitive advantage.

- Conflicts must be proactively watched for and funneled to be resolved through high trust relationships.

- The selection of location of the USA office has a dramatic effect on the capacity to build trust between the two organizations. It is substantially more difficult to build trust level between Israel and the West Coast (Silicon Valley) than the East Coast, due to the larger time difference and geographical distance. Unless there is a dramatic advantage for business efficacy of being located in the West Coast, the East Coast should be preferred.

These strategies helped the companies analyzed work as a unified unit instead of a group of factions. Though, the ultimate business success of a peripheral country startup is determined by many business factors, optimizing the globally dispersed operation of those startups can significantly affect its chances of success.

Preface

The classic All-American startup is located in the garage. The visionary founder, the geeky engineer and the sleek salesman all work in the same clammy room sharing ideas, eating pizzas and yelling at each other the top of their lungs, as needed. This is the usual story for an American startup and it is a tough survival battle.

Lately however, a rapidly growing number of hi-tech startups are springing up in countries outside the USA. A large percentage of those are in countries where the domestic markets cannot support a viable hi-tech business model. In these, so called peripheral countries, the magical combination of venture capital firms, universities, established companies, and startup companies is blended together to form the "Venture Capitals" of the future: Bangalore, India, Oulu, Finland, Sao Paulo, Brazil, and Hsinchu, Taiwan[1]. Several of them even invented for themselves a niche namesake similar to Silicon Valley such as: Silicon Wadi in Israel, Silicon Bog in Ireland, and Silicon Island in Taiwan[2], for a total of 105 such namesakes[3]. They all boast the Siliconia names and enjoy lower costs of development and higher degree of loyalty of human resources than Silicon Valley. But, their remoteness from target market poses crucial challenges in their development. So in addition to huge challenges facing a domestic startup in the USA, startups in these locations have to contend with the physical and cultural distance from their target markets.

"Where I live, everything is so small! Straight ahead of him, nobody can go very far."

The above quote from the book The Little Prince was used by a CEO of a hi-tech startup in a peripheral country to emphasize her approach to her domestic market. In such a situation, these companies must reach out beyond their domestic markets.

"So companies set up U.S. operations to strike partnerships and expand the business, allowing the Little Prince to become the Great Global Player."[4]

To have any chance of success, the peripheral startups must set up remote strategic operations (marketing, sales and business development) close to their target market, in the USA. The leadership of such a startup must learn to manage then a globally dispersed garage operation.

Why Research Startups?

Globally dispersed teams have been researched for years. In 1994, several key works described the challenges in maintaining trust relationships and motivation in globally dispersed teams[5]. In the same year, Kostner's amusing allegory of King Arthur as a management mentor suggested that the balanced and equal treatment of all team members was key to high-trust and high motivation work[6]. However to date, the specific challenges involved in managing globally dispersed startups have not been studied. As the Internet revolution continues around the global it is to be expected that the number of startups in peripheral countries will constantly grow and with them the challenges of

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managing globally distributed startups. Such globally distributed startups pose a few key challenges that are different from globally dispersed teams in larger companies:

1. Startups tend to change business directions quite often. In the companies interviewed, key strategic changes happened 3-6 times a year.

2. Startups operate under extreme time and financial constraints, often not experienced by teams within large organizations. Often, large organizations will attempt to assign quick turnaround projects to collocated teams, if possible.

3. Startups tend to operate in more extreme budgetary and time constraints than large companies.

4. Startups in peripheral states will tend to compete with domestic American startups that are collocated and thus tend to communicate well internally. In global teams within large organizations, they usually compete with other large organizations that are also globally dispersed and thus face similar challenges.

Therefore, some of the practices used by large companies with globally dispersed teams cannot be directly imported into startup operations.

Why Research Israeli Startups?

In studying startup operations in peripheral countries, it is valuable to look at countries that have developed a significant hi-tech startup industry. Further, to make timely learning it is instrumental to turn to Charley Fine's concept of Clockspeed[7]. Different industries have different clockspeeds. In his book Charley Fine, suggests that in the same way that geneticists use Drosophila fruit flies to speed up the learning for human genetics, business researchers can use industries that have high clockspeeds. The highest clockspeed industry according to Fine is computer software in which product life cycle is about 6 months. Thus the ideal research subject for this research is a peripheral counter that has developed a cluster of hi-tech startups focused on software applications.

"Indeed, outside of Silicon Valley, Israel's Silicon Wadi is now the most dynamic producer of Internet technologies -- notably Internet security systems -- in the world."[8]

In an attempt to learn how global startups deal with the distance challenge, Israel is an excellent case study. Over the past decade, Israel has gone through an incredible hi-tech boom. It boasts over 2000 hi-tech startups[9] and about 100 companies traded on Nasdaq, more than any other country outside North America[10]. According to the Clockspeed analysis, Israeli companies have gone through 20 product cycles in the last decade.

Practically all Israeli hi-tech startups operate a strategic operations (Market, Business Development, and Sales) business entity in the US starting at a very early stage in their development. According to a recent report by the Israel Democracy Institute, an independent think tank, 90 percent of Israeli high-tech companies incorporated abroad last year. A large percentage of the companies register as American companies and many hire Americans as their top executives.

An Israeli Entrepreneur: *"Israelis like to think they know everything, but the smart ones have finally realized they don't know anything about marketing, So the solution for many Israeli companies has been very un-Israeli: hand over control to others."* [11]

Israeli companies have learned to bring in foreign talent for their strategic management. Most hire mainly American professionals for many of the strategic operations positions who interact with a few Israeli expatriates.

The challenges posed by the integration of cultures, locations, and professions in these startups is the core of this research that can be applied to startups worldwide.

## Differences between Countries:

When analyzing the challenges posed by managing globally dispersed startups, several variables affect the specific difficulties:

- Language barriers

- Cultural differences

- Time zone differences

- Geographic distance

For the sake of visualization, these can be roughly summarized as follows:

Culture/Language

Differences vs. USA

Geographic/

Timezone
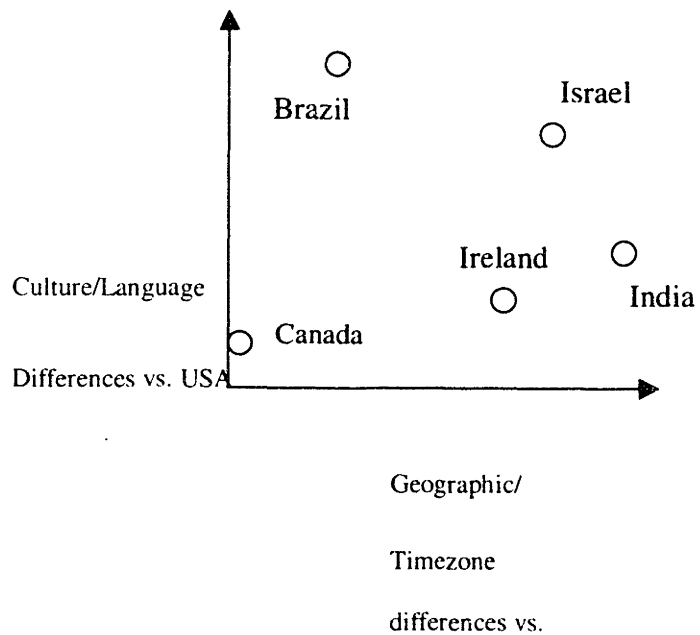
differences vs.

Israel represents a location with significant time zone and geographic distances as well as a totally different language and some cultural differences with the USA[12]. Other locations may have different mixes of the challenges but many of the same lessons may apply. Further research is required as to the effects of the differences between the different peripheral countries on the best practices to overcome the challenges.

The Challenge:

The latest fashion in Israeli Startup management is to say that the only thing that counts in a startup is the marketing. But, as a rough generalization, a startup originating in a peripheral country will find it difficult to excel in its marketing capability in the USA and make that into a competitive advantage[13]. At best marketing will not be a competitive disadvantage. The key success will probably be maintaining a technology edge in tune with professional level marketing. Anecdotal evidence brought up in my interviews suggests that the great majority of Israel's hi-tech success stories had a unique technology advantage compared to their competitors. Very few Israeli startup success stories boast marketing capability as their key competitive advantage.

Thus, a key success factor is to balance and align between marketing (or strategic operations) R&D. This is not easy to do in a collocated American startup. In an Israeli startup, R&D and marketing are located 5,000 miles apart, have a seven to ten hour time difference, and literally speak different languages. The task of making these two units operate as one organization is the key challenge analyzed in this research.

How The Research Was Done?

This research integrated the following sources:

- Interview with several veterans of Israel's hi-tech industry, including a few Venture Capital (VC) professionals that gave a general overview of the issues involved in managing globally dispersed Israeli startups.

- In depth interviews with ten Israeli hi-tech startups.

- Analysis of existing literature on corporate culture, US and Israeli culture, globally dispersed teams, and the Israeli hi-tech industry.

- Social Network Diagram analysis was performed using the data assembled in the interviews in order to get a qualitative evaluation of different organizational structure choices.

The startup companies that interviewed in depth were selected according to the following criteria:

1. The company is a hi-tech startup with less than 200 employees.

2. The company was founded in Israel by Israeli founders.

3. The company must have at least one site in Israel and one site in the USA.

4. In each site of the company, a critical part of the company's value generation takes place (i.e. at least one of the following functions is managed from this site: R&D, Marketing, or Sales).

Founders, executives and mid-level managers were interviewed. The interviews took place in both the USA and Israel locations. Interviewees were both American and Israeli. Similar questions were presented to all interviewees. In total, twenty-eight interviews were performed.

Key findings:

In more than a decade of hi-tech R&D and marketing management experience I have been taught several rules for managing Israeli startups. The following have become generally accepted guidelines for managing a dual headed Israel/USA startup. This research has shown these not to be the best practices:

- × Hire an American CEO as early as possible.

- × Keep the founder's team collocated.

- × Prevent redundancies between the two halves of the organization.

- × Open communication lines between the remote locations on all levels for all issues.

- × Don't bring out cultural differences; emphasize the common values to avoid conflicts.

Through the integration of the cross-cultural interviews and available theoretical research, I came to the following guidelines for managing the Israeli – American dispersed startup, which can probably be applied to startups in other peripheral countries as well:

1. Divide the company into two parts as equally as possible and maintain balance between the parts.

2. Try to avoid being located in Silicon Valley

3. Do not hire an American CEOs to manage the company from the USA.

4. Proactively look for conflicts and funnel them through high trust relationships.

5. Use stereotypes: make culture differences an issue and invest time and effort in it.

Organizational Structure – Solomon's Trial:

"The king therefore said: Bring me a sword. And when they had brought a sword before the king, Divide, said he, the living child in two, and give half to the one, and half to the other."[14]

The Biblical King Solomon's seemingly heartless decision to cut the baby in two was never executed. But does it specify the optimal structure for a globally dispersed startup? Should the different parts of the organization be cut in two and split between the two locations?

The organizational structure is key to overcoming the challenges of the globally dispersed garage operation. The typical Israeli startup begins with an Israeli only operation (though it is usually incorporated in Delaware). After 6-9 months on average, with 10-30 employees, the company opens a strategic office in the USA that will cover Sales, Marketing and Business Development. At this point the startup's management faces a crucial choice point:

- How to split the company into two.

- Which jobs in the USA should be filled locally and which should expatriates from Israel fill?

There are several possible approaches:

- Build a completely new US operation without sending any executives from Israel.

- Send the whole management team from Israel to the USA, and recruit the missing spots (usually marketing and/or business development executives)

- Split the management team.

The purpose described by all startups that opened a USA office is to become literally and figuratively closer to their customers, partners, and capital market. The ideal situation would be to have the organization act as one integrated unit that is not collocated but is closely aligned and integrated.

Which is the best approach? The literature on globally dispersed teams clearly suggests that a key criterion for that decision is which structure maximizes the level of trust between the two halves of the organization.

"The key to build high performance across distance is to build trust"[15]

For distributed teams, trust has to substitute for local control[16]. *"Managing people you do not see requires trust"*[17]. Or as Kostner's King Arthur teaches: *"When trust flourishes, people do magical, wonderful things together – like create Camelot."*[18]. The challenge for startups is that building trust requires time and time is the scarcest resource of all. The question becomes which model builds trust between the two sites most quickly.

Below is an analysis of the possible structures based on the previous available research, interview results, and outcome of the Organigraphs using Social Network Analysis tool called InFlow[19].

Hiring a New Team to Manage the Strategic Operations:

One strategy employed by a few Israeli startups is to keep in Israel the original management team and recruit a fresh new, American team to manage the strategic operations in the USA. The team that manages the strategic operations is then typically well networked into the target market. But, there is very little integration between the USA team and the Israeli team. All VC experts interviewed described that as a disastrous strategy.

One of the companies interviewed that tried this approach, found that there was practically no trust built between the two offices. The managers in the two offices hardly knew each other and knowledge was not transferred. In fact they described a situation where mistakes that were previously done in the Israeli office in initial sales attempts were repeated when the American office started its sales operation

This approach clearly creates a low level of trust between the two sites. Further more, the low level of connection and trust limits the transfer of tacit knowledge defined as knowledge that is mainly in the heads of people and requires personal interaction to transfer[20]. This was evident from the examples in the interviews of mistakes being repeated between sites. The tacit knowledge about how to sell the company's products

was not transferred from one site to the other. The Social Network Diagram (see Appendix C for explanations) shows that the teams in both sites are quite distant from each other and the high trust links between the two sites are minimal. If, as was the case in the companies analyzed, the employees hired in the USA are all American, the members of the USA site are separated from those in Israel by culture, language, time zone, geographic distance and lack of acquaintance. There is much more that keeps the two organizations apart than holds them together, as can be seen in Appendix C. The lack of trust and of tacit knowledge transfer makes this the least effective model of those examined. A startup cannot afford to make the same mistake twice.

Sending the Management Team to the USA:

The second organizational approach is to move practically all the top management including founders from Israel to the USA. Typically, a hired R&D manager is the only executive who stays in Israel to manage the R&D team. This popular approach is was explained to me by one entrepreneur:

"Once the initial product development is done, the key to business success is Marketing and Business Development. Since this is done in the USA, we needed to move all possible management talent to the USA."

The Key Function of Founders

This research showed that the key consideration in this respect is the location of the founders of the startup. In most of the startups interviewed, the founders maintained a special status. In the companies interviewed, not all the founders who initiated the company survive the very early stages. But those that remain in the company, even if not holding the top leadership positions, hold influential positions. In most cases, the founders are members of the Board of Directors, setters of the cultural tone, and/or a just a close-knit core team. They usually have a long joint history (often having previous experience together in the Israeli Defense Forces or a previous "startup life"). Together they went through the challenges of starting up a company, getting initial funding and defining the company culture. In most companies, their unquestionable personal commitment to the company allows them to have a direct, open and frank communication with each other.

In the companies where all founders move from Israel to the USA, the issue of transferring knowledge from the Israeli site to the American one is resolved. The founders in the companies analyzed were walking encyclopedias of company history and know-how. In that respect this approach is better than the previous one described. The founders are also well acquainted with company employees in Israel. They bring their network with them to the USA office. However, in the companies I visited, the ties between founders and non-founders were not as strong as within the founders' team. By moving all the founders to the USA, the companies did not set up high trust relationships between the Israel and USA offices. See Appendix C for the Social Network Diagram that shows the result of the headquarters moving to the USA. When the whole group of founders moves to the USA, the company faces two problems in the operation of its two sites:

1. The Israeli site feels deserted. People feel they have no access to power. For example, an Israeli product manager I interviewed described: *"when all the management left for the USA, I felt abandoned. I used to be able to knock on the door of the CEO and express my opinions or get the latest corporate news. Now I can hardly get five minutes of his time during his bi-monthly visits to Israel."*

2. The human links between the two sites are few in number (see Appendix C). Those that exist are low trust relationships and many are cross-cultural as well. High trust is key for remote communication[21] and without it communication often breaks down and conflicts over trivial matters loom large. One manager left behind in Israel described his feelings: *"Whenever I try to report a problem to my*

boss in the USA, I feel he does not believe that the problem is so difficult and feels

that I am just not doing the right things to solve it. He usually replies by telling

me that this is no problem and he will fix it for me on his next visit to Israel. That

makes me feel quite frustrated."

Splitting the Founders:

This research shows that the most effective organizational approach is to split the founders between the two locations. Just as King Solomon originally declared, the baby must be cut into two equal parts. Unlike the Biblical story, in this case it should actually be executed. Cutting the infant company into two equal and well balanced parts will maximize its chances of success.

The most critical group to be cut in two is the founders' group. In many companies, the founders prefer to stay together just because they know each other well and enjoy working together. By splitting their group between the two locations, the founders will be distancing themselves from their best friends. But, by virtue of the close relationships within themselves, they will be bringing their two locations closer together. Doing that provides the following benefits:

- The high trust relationships between the founders on the two sides of the ocean increase the general level of trust between the two sites. The Social Network Diagram shows that the two sites move closer together and operate more like one unit than two separate ones. See Appendix C.

- Those founders that move from Israel to the USA will bring with them a real life database of company history, network and culture. Thus facilitating the development of site culture in the USA that integrates well with the company culture developed in Israel. Tacit knowledge is also be better transferred through the founder's know-how and their access to other know-how in Israel through their network in the Israeli site.

- The fact that some of the founders stay 'behind' in the Israeli location, will give the people in that location a sense of being valued and of having access to top management.

In one company interviewed the founders on either side talked to each other several times a day, often from home at ungodly hours. Thus they were practically always in sync with each other and through them the two locations worked more closely together. The Israeli R&D team used the founder as its information channel to the rest of the management team in the USA. This structure made them feel listened to and important.

Cross-Over Model:

The literature shows that cross-cultural communication is prone to more problems than communication within the same culture[22]. Misunderstanding between marketing departments and other key operations of a company are the rule rather than the exception[23]. In my interviews and observations of startup activities, it was evident that people communicate best with those that are similar to them. Especially when the communication is not face to face, but through electronic means. The results of the interviews as well as the Social Network Diagrams show that the two locations work best when management minimizes Trans-Atlantic communication lines that are also cross-cultural. Some examples observed:

- One startup had product managers in both sites. Though this introduced some redundancy (previously thought to be wasteful), I found that they were able to communicate better with each other than with R&D engineers overseas. One product manager told me: "*I like to look an R&D engineer in the eyes when he tells me that something can or can't be done. If I don't have the luxury of doing that, I prefer to talk on the phone with a fellow product manager who will look the engineer in the eye and report to me.*"

- Another startup moved senior R&D engineers from Israel to the USA. The engineers brought with them to USA office their understanding of the R&D operation and the communication capability with the engineers back in Israel. These relocated engineers served as translators between the marketing and R&D people. They

improved the understanding of R&D issues in the USA marketing office and the understanding of marketing issues in the Israeli R&D center. However, the startups that did that paid a price for it. The R&D center in Israel was not happy about losing some of its key people to the USA office.

- Having a mix of Israelis and Americans in both sites helps communication tremendously. I witnessed a Trans-Atlantic teleconference in a startup company where on both sides there were Americans and Israelis. When an Israeli engineer in Israel did not understand what an American marketing person was saying, an Israeli engineer on the USA side quickly switched to talking Hebrew and explained the situation in Israeli slang. The misunderstanding was resolved in seconds. Similarly, the American marketing manager was able to gain a better understanding of the emotions on the Israeli side by the subtle explanations of the American Product Manager that was located in Israel. Today, it may be difficult to have Americans move to Israel, but it is critical that key functional people in the USA office be willing to travel to Israel extensively. One product manager in Israel told me: *"Usually when we get visitors from the USA, we get into a marathon of meetings. But, I get much more value from just having my American counterparts share an office with me while we are both going over our e-mail"*.

The value of crossing over cultures and functions in the two sites can be seen in the appropriate Social Network Diagram in Appendix C.

Building Trust:

"The more virtual the organization, the more its people need to meet in person. Meetings are more about process than task. Work, and play therefore alternate in many of the corporate get-togethers. These are not perks for the privileged; they are the necessary lubricants of virtuality."[24]

The previous sections analyzed ways of maximizing the value generated by existing high trust relationships. Another way to bring the two sites closer together is to engage in activities that build trust. Two practices that were observed:

- One company had a routine of setting up short-term special purpose teams to analyze product opportunities or solve a specific problem. The teams were cross-cultural as well as Trans-Atlantic. The people who took part in those teams reported that they build their trust in each other and their confidence that effective work can be done between the two sites.

- Most companies do offsite activities that are intended to build teamwork. Unfortunately, due to budget constraints these activities are generally confined to the local teams of each site. From the Social Network Analysis, it seems that there would be great value on doing joint offsite activities for the management of both sites.

The severe budget and time constraints of a startup may make it difficult for managers to justify investment in processes that build trust and do not contribute directly to day-to-

day operation. However, managers should consider this a capital investment in Social Capital, "the component of human capital that allows members of a given society to trust one another and cooperate."[25] Investment in Social Capital generates economic value in bringing people closer together and making them work more effectively as a team[26], as can also be seen from the Social Network Diagrams in Appendix C.

Split External Stake Holders:

Other key stake holders can help bridge the divide between the two locations. The investors and Board of Directors can be used to bring the two halves of the company closer together. Several of the leading Israeli VC organizations have imitated the structure of their portfolio companies. They have set up split operations between Israel and the USA. One veteran venture capitalist told me he decided open a USA office in order to support both halves of his portfolio companies. The VC employees in both locations can then work with the half of the company closer to them. The internal communication within the VC about the company becomes another channel of transferring strategic knowledge about the company and its market between Israel and the USA. The Board of Directors member who represents that VC in Board meetings can then provide the Board with an integrated outlook on the company's situation on both sides of the Ocean.

Selection of board members is also a way to build a bridge between the two halves of the company. It is also a key way to built credibility in the USA. Recruiting board members

that have management experience in the USA has been shown to correlate directly with the value of Israeli startup companies that had their Initial Public Offerings[27].

The CEO and the Board of Directors

Qualifications of the CEO and the Board of Directors:

Most Venture Capital (VC) Firms and Boards of Directors (BOD) aspire to bring an American CEO to manage their Israeli startups as early as possible. It is a generally accepted notion that an American CEO will deliver better strategic execution and will interact better with the American capital market.

How does the c re brought in by the American CEO integrate with the organization that is originally Israeli? No rigorous statistical data is available as to the effectiveness of American CEOs in these startups. But, the anecdotal evidence is overwhelming. Over the past few years, there have been a few hundred success stories defined by an "exit" event either through an IPO or an acquisition[28]. Yet, in all the interviews I conducted, my interviewees were not able to name one single company out of these hundreds that had employed an American CEO before the "exit" event. Yet, each of my interviewees was able to name several failure stories of companies that hired an American CEO and due to the lack of cultural fit, the CEO and/or the company failed.

With no exception, my interviews showed that American CEOs of Israeli startups are located in the USA. The American CEO is then distanced from the Israeli operation by all 3 levels of culture: national, site, and occupational (she is generally has a Marketing background)[29]. She will generally not be acquainted with any of the key R&D people in

Israel and will not have the time to get closely acquainted with them as she focuses on marketing and business development activities.

Furthermore, several veteran entrepreneurs and VC professionals described the following phenomenon. For an American CEO it will not be regarded as a prestigious job to work for an Israeli startup with a mostly Israeli Board of Directors. Therefore, as a broad generalization, those interviewed suggested that American professionals who will be willing to work for an early stage Israeli startup will not be the most proficient and experienced. On the other hand, for an Israeli executive, to be the CEO of an early stage hi-tech startup with a possibility of relocation to the USA is an extremely lucrative opportunity. The best talent in the Israeli job market is available for such a position.

On the other hand, as a general rule, an executive with American business experience generally has a stronger network within the target customer and capital markets in the USA. Israeli executives, as described by VC professionals, generally have a less intuitive understanding of the American market and less of a network in the USA. Clearly, there are theoretical advantages to hiring an American CEO. But, the evidence is quite clear that such a CEO is less likely to succeed in this setting.

One option that is worth further exploration is a dual leadership of the company (co-CEOs) shared by one Israeli and one American executive. In one of the companies that I analyzed, the CEO position is being shared by an Israeli founder that moved to the USA and an American CEO that was hired. Both are located in the American office. As expected, the American CEO has minimal interaction with the Israeli operation. His

Israeli counterpart has a close personal connection to the Israeli R&D center. Through his close relationship with the second founder who remained in Israel, the Israeli Co-CEO facilitates the cross-site communication and cooperation. The management is thus ultimately balanced between cultures.

Another option is to hire as CEO an Israeli that has previous executive management experience in the USA or has done an MBA in the USA. Statistical analysis that was done of valuations of IPO of Israeli hi-tech startups shows this to directly correlate to lowering the under pricing of Israeli startups[30]. Companies that employed Israelis with such a background suffered significantly less under pricing than those who did not. As more and more Israeli professionals now relocate to the USA to work for hi-tech companies or study for an MBA, the pool of professionals with such a background is constantly growing[31].

Another key point in balancing the operation is through the Board of Directors. The above-mentioned statistical analysis of Israeli IPO under pricing also showed that recruiting seasoned American executives to Israeli Startups BODs reduces under pricing significantly. To some extent, bringing in Americans with strong networks in the target business generates similar advantages to those gained by hiring an American CEO:

1. Knowledge of the target market.

2. Knowledge of the practices in hiring top personnel.

3. Network in the American target industry.

Yet, bringing this capacity at the BOD level seems, from my interviews, to generate less of the day-to-day friction due to cultural differences.

Location of the CEO and the Board of Directors:

In the analysis of King Arthur's Camelot, Kostner suggests that a key reason for the decline of Camelot was King Arthur's apparent favoritism towards Sir Lancelot[32]. Kostner suggests four key guidelines for preventing this trust breaking phenomenon in globally dispersed teams:

1. Be scrupulously fair in treating all team members near and far, equally.

2. Appearances or suggestions or favoritism break trust.

3. Avoid the temptation to rely more on those on-site with you than those at a distance.

4. Balance the needs of team members near and far.

Human nature makes it extremely difficult to treat equally those near and those far away. One possible solution to this challenge is to take a broader view of distance. Distance, could be measured not only in physical distance, but also in the level of cultural difference ("distance") in site, occupation and national cultural perspectives. This opens up a possible way to overcome the natural human tendency to favor those who are closer. It is possible balance the physical closeness with cultural "distance" and vice versa. For example, an Israeli CEO that locates herself in the USA offices balances her physical closeness to the mostly American employees in USA office with the cultural closeness to

the mostly Israeli group located in Israel. It serves the balance to locate an Israeli CEO in the USA. As can be seen in the Social Network Diagrams in Appendix E, while the cultural link and perhaps acquaintances will keep her closer to the Israeli group, the physical location and the daily interaction with the USA location will make her better attuned to the USA side.

Further more, within the USA offices, that CEO must make sure not to show any preference to interacting with the few Israeli employees located there. One of the Israeli CEOs in the USA that I interviewed would not speak to other Israelis in that office in Hebrew, only in English. This was a symbolic gesture to clarify his efforts of giving equal access to all his employees. Similarly, CEO who is an engineer by background may best be located by the marketing people and vice versa.

A mix of BOD members cultural and occupational backgrounds (R&D and Marketing) will also help bridge the chasm between the two halves of the company. It is also a good idea to alternate the location of board meetings between Israel and the USA. This signals to all involved that both sides are crucial for the company's success.

Conflict

One of the key roles of management is to handle conflict. Effective managers must identify conflict and resolve it quickly and effectively.

Identifying Conflict:

Identifying conflict in a globally dispersed operation is more challenging than in a collocated operation.

"[In a globally dispersed team,] *you have to have a sensitive ear and be very precise with the questions you ask people. It can be hard to hear a cry for help from an overburdened team member, and if you miss it, you could have problems down the line* "[33]

Indeed, the interviews showed that identifying conflict in non face-to-face communication is quite challenging. This is especially true when the communication links do not rely on previous acquaintance and trust. Further more, the interviews showed that higher-ranking people in the organization are often less aware of conflicts than lower ranking ones. For example, one of the CEOs interviewed claimed that his US operation and Israeli operation were working very closely together. His reports gave a widely different view of the situation and cited numerous examples of failures due to miscommunication between the two sites. Many of these failures were not reported to the CEO or were reported at a late stage and were attributed to external sources (bad markets, difficult customers, etc.).

Conflicts are an inevitable aspect of doing business in globally dispersed startups, just like conventional ones. But identifying conflicts at an early stage often requires a focused, proactive effort in the dispersed startup.

Handling Conflict:

Effective management of conflicts requires high trust relationships as a holding environment.[34] The interviews helped identify three issues that make conflict management more difficult in the Israeli startups:

1. Cultural differences: Israelis and Americans handle conflict differently[35].

2. Lower level of trust between people that are not collocated.

3. Conflict are often managed through electronic media such as e-mail which tends to generate paranoia[36]

Thus in most of the companies interviewed I found examples where small misunderstandings or even attempts at humor got out of control and severely affected the capacity of the Israeli and USA offices to work together effectively.

In managing a conflict between individuals that are not collocated, the following must be balanced:

1. The level of trust between the two individuals.

2. The context level of the communication method to be used (face to face being the highest context, e-mail being the lowest).

I saw founders who trusted each other completely and were therefore able to resolve delicate conflicts via e-mail. On the other hand people who did not know each other well and had a low level of trust between them, needed a face-to-face meeting to resolve their conflicts. The effective balance, and appropriate selection of the two points above is required for each conflict. Often, in the high paced startup environment, there is no time to wait for face-to-face meetings to resolve conflicts. Effective handling of the conflict then requires the funneling of these conflicts in both offices to be handled by the few people who have Trans-Atlantic high trust relationships. In one startup, for example, the two founders in each office called the other daily to go over all open conflicts between the two organizations. Though this approach is not scaleable, it seems extremely effective in the early days of startup operation. At a later point in time, effective operation requires the balance of trust level and communication medium to effectively resolve conflicts.

Culture

Cultural Differences:

"If a man does not keep pace with his companions, perhaps it is because he hears a different drummer. Let him step to the music which he hears, however measured or far away" [37]

The cultural differences between the Israeli and American sites of the startups examined can be analyzed via three cultural lenses: national culture, occupational culture, and site culture[38]. The US site of the startups is mainly occupied with American marketing and business development people, while the Israeli site has mainly Israeli engineers in it. So there are cultural differences that fit into all three lenses in this situation. On the other hand, the traditional, collocated startup has to deal with mainly the occupational cultural difference between marketing and R&D departments, which in itself often creates difficult challenges[39]. When national and site cultural differences are added to that, cultural differences in the organization become a key leadership challenge.

Israelis live in a modern, Western society. But, drinking Coca-Cola does not make Israelis think like Americans any more than eating sushi makes Americans think like Japanese[40]. In fact, my interviews led me to believe that the cultural differences between Israelis and Americans have as powerful an effect on doing business as the cultural differences between Japanese and Americans. For example, in the famous comparative cultural study of global IBM operations[41], the cultural differences in the ranking of

Israelis and Americans in power distance were as large as those between Japanese and Americans.

Cultural differences generate conflicts. In general, my interviews showed that Israelis blame the Americans of their company for demanding too much budget and spending it all, for not working long enough hours, and sticking to procedures in the face of an ever-dynamic situation. The Americans blame the Israelis for being impolite, politically incorrect, undisciplined, disorganized and generally unprofessional[42]. This significantly amplifies the normal collocated startup's challenge of aligning marketing and R&D.

One revealing simple anecdote uncovered in this research: An Israeli engineer presented a suggested course of action to his American CEO. The CEO said: "I don't think you should do that". A month later the CEO found out that the engineer nevertheless continued with his proposed course of action. When the CEO asked the Engineer why he disobeyed him, the Israeli engineer answered: "you thought one way, I thought another. So I did as I thought best". This little anecdote has probably happened many times, it exemplifies the differences in cultures in both power distance and directness of speech.

The diagrams in Appendix B capture the process that leads to misunderstandings between people of different cultures. It is captured by the phrase:

You don't see the world as it is; you see it as you are.[43]

The normal difficulties of electronic communication are thus amplified by the inevitable bias of cross-cultural communication (through all three lenses).

Managing Stereotypes:

Most Israeli startups find cultural difference a crippling problem that reduces their effectiveness. But, most companies pay little attention to cultural differences, and prefer to pretend that they do not exist. This research clearly shows that the most effective method of handling cultural differences is to celebrate them. Leaders that constantly discussed cultural issues made their teams aware of the challenges involved. It became politically correct to discuss cultural stereotypes and conflicts that arose from them. People could then use the stereotypes to better understand how listeners from another culture interpreted their messages. In the context of the diagram of Appendix B, this helps the speaker understand how the listener "decodes" his message. The "encoding" can then be done in a more culturally sensitive way, resulting in less miscommunication. Stereotypes are thus an effective tool in understanding how one is interpreted by his cultural counterparts.

Self-deprecating humor can be an effective tool in discussing and disarming cultural issues. For example, one Israeli CEO openly told his people before giving them their reviews: "I am Israeli so expect me to be insensitive, abrupt and sometimes insulting...". That same CEO was also able to build task teams that would have synergetic effects due to the combination of the Israeli quick reaction capability and the American efficient process focus.

Some of the theoretical work suggests that cultural differences can be made into a competitive advantage. Managers should:

- Openly talking about cultural biases.

- Ask members of different cultures to teach each other different ways of doing things.

- Don't let culture become an excuse for poor performance.

Thus, by casting aside political correctness, culture can become a powerful management tool[44]. In fact, the process of learning on the job about the cultural differences can become a fun, unifying experience that generates improved performance. Further more, as seen in one of the companies interviewed, a team of Americans and Israelis can leverage the Israeli capacity to improvise and the American capacity to implement an efficient process in order to create an efficient, reliable and adaptive work process. The synergies of cultural diversity can thus overshadow the inefficiencies of cultural conflicts.

Culture Curiosity as a Recruitment Parameter:

"Successful leaders are invigorated by the differences around them. They are driven by a sense of adventure and a desire to see and experience new things." [45]

My interviews as well as the literature show that effective leaders in cross-cultural environments must be inquisitive and eager to learn. "Team leader must be intellectually and socially curious"[46]. Managers, who did not have those traits, generally tend to create repetitive cultural conflicts with minimal learning. Unlike traditional startups, in the globally dispersed startups, inquisitiveness and curiosity must be key recruitment

parameters. My interviews showed that those who fit this description, found the cross-cultural experience gratifying. The cultural differences made them want to stay in the company and enhance their learning of foreign cultures. For others, who were not interested in learning about foreign cultures, this environment was frustrating. Some indication about a person's willingness to learn about new cultures can be gained from a person's mastery of foreign languages, international travels, and history of assignments requiring cross-cultural work.[47] It is my recommendation to use inquisitiveness as a key recruitment decision factor.

Location, Location, Location

One of the dilemmas facing a startup company from a peripheral country is where to open its strategic operations office. Israeli companies generally tend to choose between Silicon Valley and the East Coast. In the interviews conducted, this came out as a critical point. Locating company offices in the East Coast as compared to the West shortens the flight time to Israel by about six hours and the time zone difference by three hours. Employees located on the West Coast share no working day times with their colleagues in Israel, while those on the East Coast share two to three hours a day. A weekly flight from the East Coast usually generates a loss of one working day, while the journey from the Silicon Valley costs two full days plus a stronger jet lag effect.

In the past, almost all Israeli companies were attracted to Silicon Valley, because of the powerful network externalities of being located close to other hi-tech companies and VCs. Today more and more companies are locating in the East Coast citing the closer location to Israel as well as the vicinity of leading hi-tech giants such as Nortel and EMC. Over 100 Israeli hi-tech startup companies are now located in Boston alone[48].

This research showed that at some point, there are diminishing returns in moving physically closer to customers as compared with increasing alignment costs of increasing distance between the R&D and marketing. There is a substantially bigger alignment challenge for Israeli operations with West versus East Coast US locations. Only in rare cases can the advantages of Silicon Valley location overshadow that difficulty. In most cases, East Coast location leads to a more effective overall operation.

Summary

Managing a globally dispersed startup is an extreme cross cultural leadership challenge. Startups operate under heavy time and budget constraints in an environment that requires constant strategic changes. Alignment of the R&D and strategic operations is key to success in such an environment. But, national cultural differences enhance organizational and site cultural differences that are prevalent in any startup.

This research showed that the key to successful management of a globally dispersed startups are: balance and trust. Balance is required to keep both sites feeling that they are crucial to the success of the operation. Trust is required to overcome distance in the physical as well as the cultural perspectives. Below is a list of tips for success that summarize the findings of this research:

Tips for Managing a Globally Dispersed Startup:

1. Balance the management makeup and attention between USA and Israel, Americans and Israelis, Marketing and R&D.

2. Split the founders between locations.

3. Cross over R&D engineers, marketing managers, Americans, and Israelis to the "other" side.

4. Make cultural differences an issue. Learn them, laugh about them, use them in building synergetic teams.

5. Invest in off site (preferably outdoor) team building activities to be attended together by employees from both locations.

6. Set up fixed communication time slots for teleconferences between both sites' managers. Hold the teleconferences even if there is no clear agenda. In that case they can serve as casual "water cooler" chats.

7. Use technology to help:

    a. Videoconferences are effective for small teams (e.g. product reviews with no more than 2 people on each side).

    b. Instant messaging software is provides the immediacy of a phone call with the receiver control of e-mail.

    c. Web database of links to people with tacit knowledge.

8. Hire culturally inquisitive people managers for cross cultural work. Identify cultural curiosity by knowledge of foreign languages, foreign travel and previous international assignments.

9. Maximize face-to-face time between people of the two locations. Have people travel just to get aquainted with the other team. When traveling, people should not

spend the whole time in meetings. Spend time just working next to each other and going to the water cooler together.

10. Initiate small ad-hoc short-term teams that are cross cultural and Trans-Atlantic.

11. Have your investors and board imitate your company structure. Select VC investors that have offices next to the company offices in both countries.

12. Make sure people in both offices feel they are treated equally on the professional level and on the human services level. They are part of one company.

This research analyzed Israeli startups as a case study for any peripheral country startup. However, different countries face different mixtures of cultural differences, physical distance, time zone difference and language differences with their target market. Further research is required into the effects of this parameters on the optimal operation of startup operation. Further more, this research did not analyze deeply the effects of government policies in peripheral countries on these issues. This too would warrant further research.

Appendix A - Use of Technology:

Technology will not solve the management issue of geographically split startups. In all my interviews, no one suggested that these problems could be solved by technology. Several interviewees mentioned bad experiences with e-mail, voice and videoconferences. Misunderstandings and clashes caused by language, cultural, distrust barriers were numerous. The key point that came out was the need for alignment between communication channel and communication purpose. Some key results:

- E-mail is an extremely effective for transferring data. It enhances productivity by overcoming time zone differences effectively and effectively transferring factual data.

- E-mail is ineffective in transferring emotional data and motivating people. It is often disastrous in trying to resolve conflicts.

- Videoconference can be very effective if it is of high quality and used for small group meetings of up to 2 people from each side. Several companies interviewed used this tool for product status reviews involving product managers and key engineers to transfer softer issues and make priority decisions. Most interviewees suggested that with groups video conferencing had limited added value and was often distracting.

- Instant messaging software (e.g. ICQ) is a tool that is used very effectively by one company interviewed. It is a compromise between e-mail and phone. It is

quicker and more lively than e-mail, but less intrusive than phone. Some examples of uses:

- o A sales person in the USA does a product demo on his laptop to a customer. His laptop is connected to the Internet and runs an instant messaging software. He can see which of the top engineers and tech support people in Israel are available at the time. When asked a tough technical question by the customer, he can instantly relay that question to one of the engineers online and get an answer within less than a minute. This both amazes the customer as to the level of global support and gives both the product manager and engineer a feeling of operating on one team.

- o In Israel, Sunday is a working day. A group of engineers is having a heated discussion on prioritizing different technical software implementations. They need input from an American product manager who is at home. Americans are much more sensitive than Israelis to being disturbed at home by a work phone call. But on the other hand, the product manager may well be sitting by his computer working. The engineers can immediately tell which of their colleagues are currently online at their computer and can ask their question or set up a conference call within seconds without interrupting anyone who is not working.

- Though startups are small companies, finding the people who have the right knowledge is often hampered by geographical distance and cultural differences.

So another important tool is an employee database with pictures of all employees and their areas of expertise and hobbies. This helps people find tacit information available in someone else's head. The personal information about each employee adds the human touch, which improves interaction.
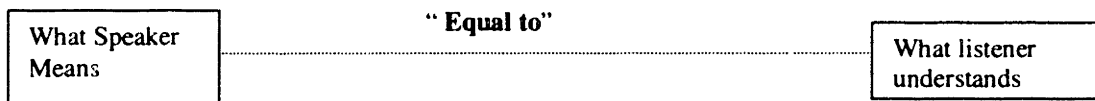
- Electronic company newsletter: focused on making people on both sides of the ocean feel they are part of the same company. This materializes for many people the fact of being on one team. The use of a digital cameral in that to put "faces" on peoples names is often very effective.

- The tool that is missing: there is still a need for an interactive tool that will allow people to be accessed at home, outside their work hours, but only if they allow themselves to be accessed. The instant messenger provides this solution, but a more generally accepted solution may yet be required.

Appendix B - Miscommunication

This appendix attempts to depict graphically the challenges of cross communication in a multi cultural environment. In globally dispersed teams, a listener's misconceptions of a speaker's culture create significant differences between what was the speaker meant and what was understood by the listener.

Communication Assumption versus Reality

ASSUMPTION:

```
┌──────────────┐           " Equal to"          ┌──────────────┐
│ What Speaker │                                 │ What listener │
│ Means        │.................................│ understands   │
└──────────────┘                                 └──────────────┘
```

REALITY: What speaker means to say is "encoded" by his mood and by his cultural background. It is then "decoded" by the listener's perception of what the speaker's mood and culture are. In a perfect world (first diagram below) the encoding and decoding are perfectly symmetric and what the listener means is what the listener understands. In the real world these can be very different. The normal communication problems are clearly aggravated by the listener's misconceptions of the speaker's culture.

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Fig. 1: Perfect world: Listener perfectly "decodes" speakers "codes":
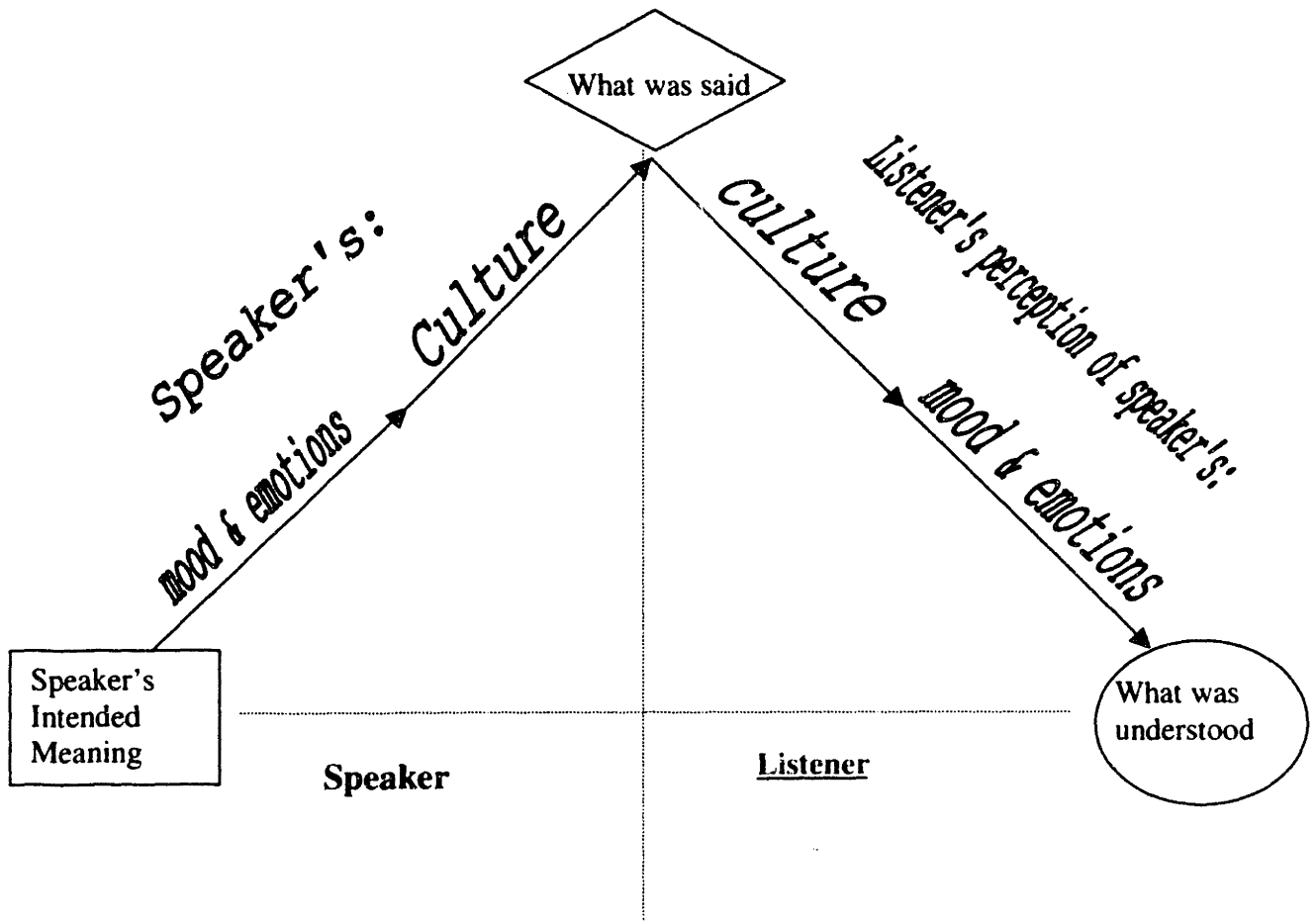
Real world in multi cultural settings: Listener's misconceptions of speaker's culture create significant difference between what was meant and what was understood. The decoding is different from the encoding resulting in miscommunication.
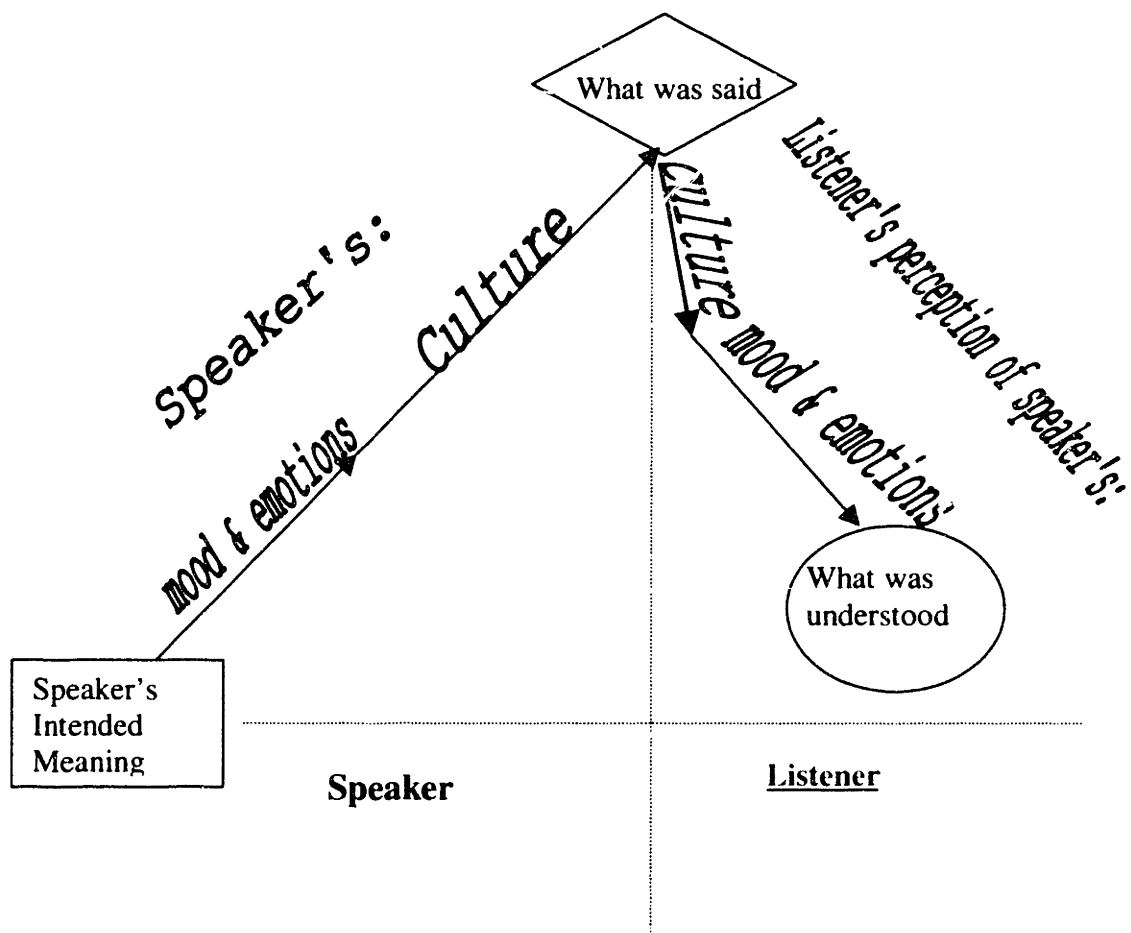
Appendix C – Social Network Diagrams

The diagrams in this section are called Social Network Diagrams or Organigraphs. Their purpose is to provide qualitative analysis of the effectiveness of networks[49]. The input to the Inflow software that calculates these diagrams is a series of nodes with links between them. The links can be attributed a parameter of strength and a parameter of direction. Some anchor nodes are defined and displayed in fixed locations. The anchor nodes are used in this case to signify physical location and cultural background of each person in the startup. The anchor nodes are fixed in position all the rest of the nodes are free to move. The software calculates for each node the optimal location which has the lowest "potential energy" based on the different pull and push forces applied on this node.

The nodes are depicted in two colors: Yellow for those located in the USA and blue for those located in Israel. Based on my interviews I created graphs that depict the different organizational structures I saw. I took the key team of three founders, one CEO, two R&D people, and two marketing people. I defined the level of the communication links and trust between different people in the organization according to my best judgment. I also attributed to each person his cultural background and his physical location. The software then calculated the resulting diagram for each case. The two qualitative measures to look for in each diagram are:

1. How far apart are the yellow and blue nodes, signifying how big is the divide between the two offices of the startup.

2. How many lines go between the two groups and how thick are those lines. This signifies the human links between the two groups and the level of trust between the groups.
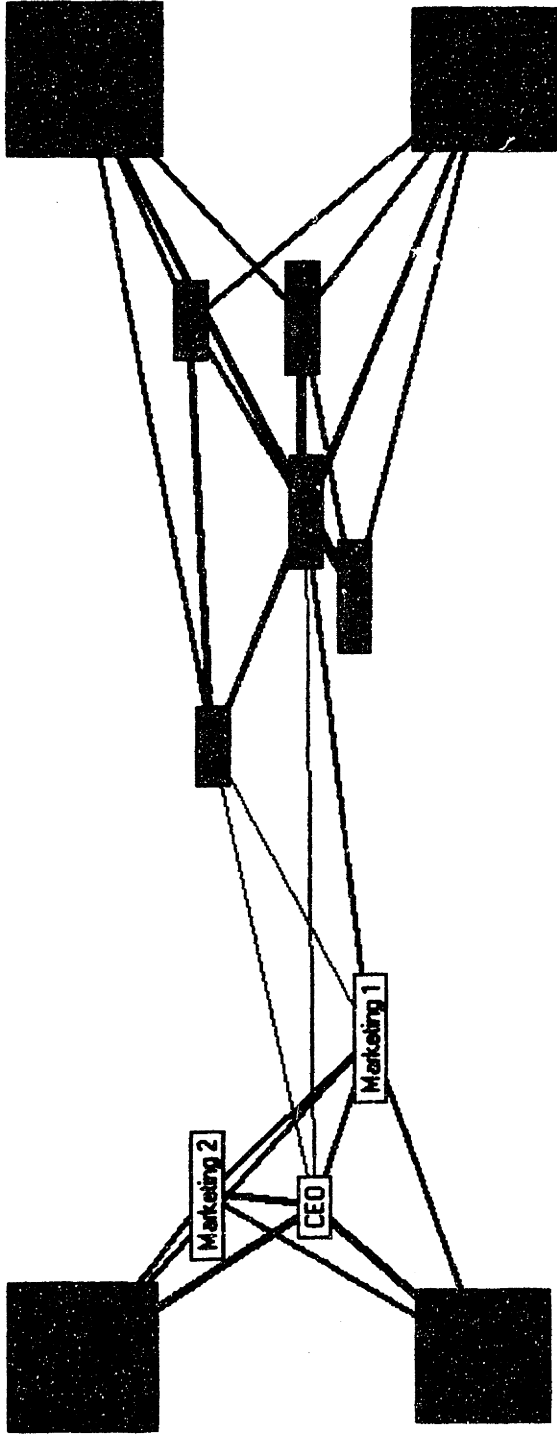
Fig. 3: Founders remain in Israel, new management team hired in the USA.
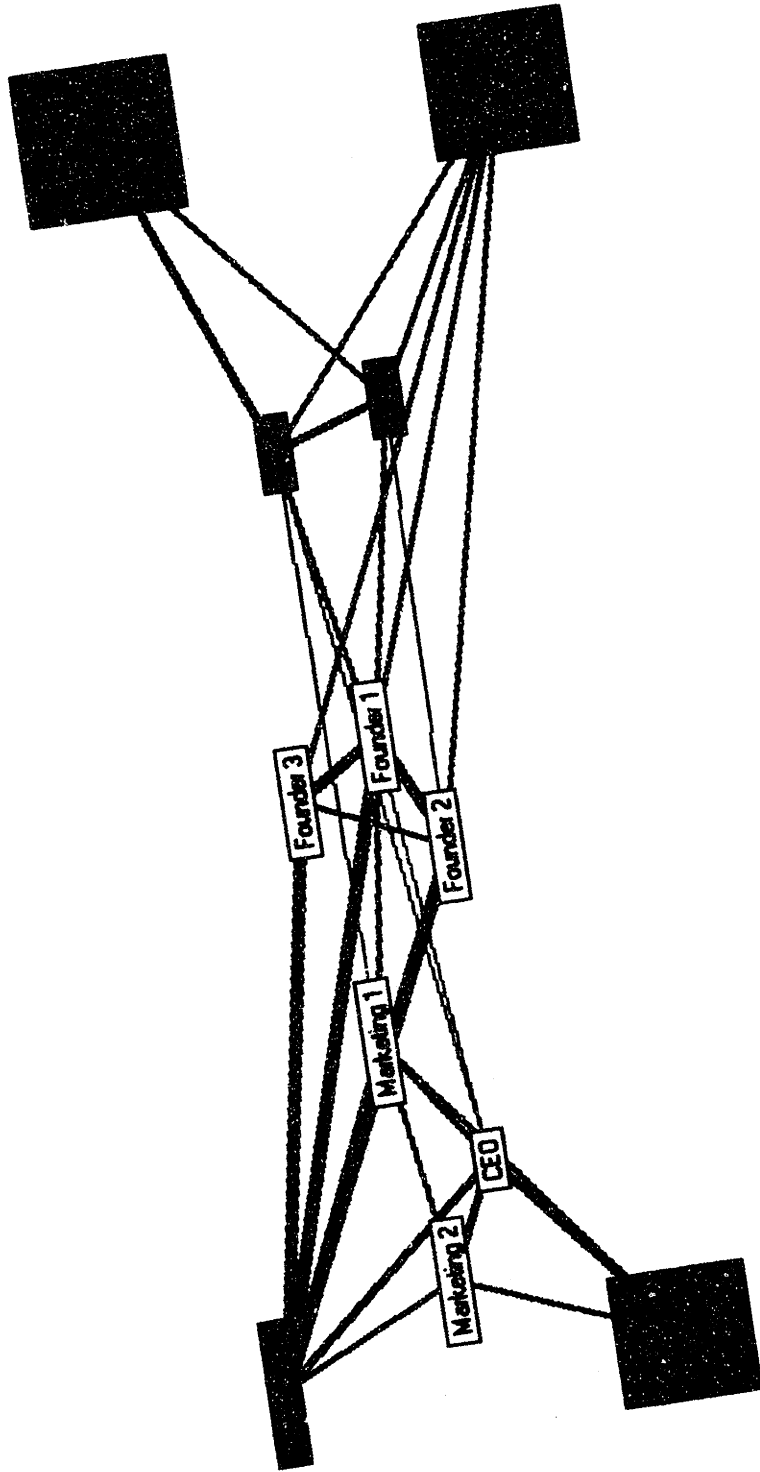
Founder 3
Founder 1
Founder 2
Marketing 1
CEO
Marketing 2

Fig. 4: Founders move to USA, only R&D remains in Israel.

59
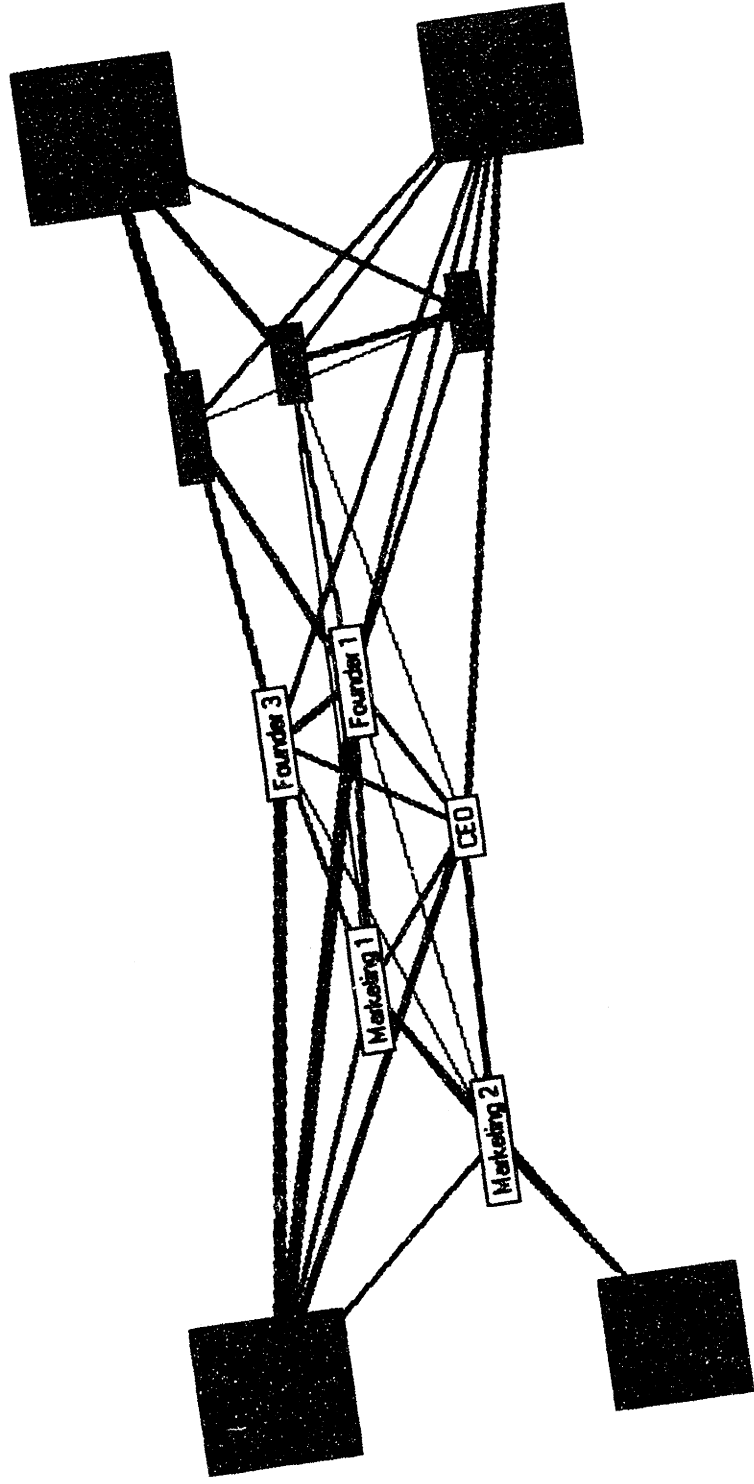
Fig. 5: Founders split between two sites.

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