The regional solution: an alternative to globalization

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For years, United States companies have struggled with the conflicting challenges of globalization. On the one hand, they have watched as market shares have declined in the face of Japanese competition while, on the other hand, they have faced very real obstacles in organizing subsidiaries for global effectiveness. The authors argue that a global strategy may be inappropriate for United States companies with extensive international subsidiaries. Rather, a regional approach to business represents a more effective solution to the dual challenges of efficiency and organizational responsiveness. The authors discuss the advantages of regionalization from a United States perspective and offer practical advice to both head office and subsidiary managers as they approach regionalization.

Changing patterns of international competition are pushing many companies to search for new sources of competitive advantage. The success of competitors from Japan in particular has encouraged many United States companies to globalize operations by rationalizing subsidiaries and centralizing decision-making. Not surprisingly, a growing number of subsidiary managers are balking at these changes and are instead arguing that subsidiaries represent often overlooked and untapped sources of competitive advantage. As a result of what are largely implementation difficulties, an increasing number of companies are searching for new solutions to the globalization challenge.

The authors explore how companies are responding to the challenges of globalization through the adoption of regional strategies, describe the changing pressures facing international competitors and outline distinct dif-

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ferences in the approach taken by Japanese versus other Western companies. The study is based on a multi-year research project involving almost 150 parent transnational corporations (TNCs) and 125 subsidiaries in the United States, Canada, France, Germany, Japan and the United Kingdom. Analysis suggests that United States TNCs are uniquely positioned to exploit regional strategies, but that such a move involves a considerable leap of faith for many companies. The authors describe how United States companies are coping with globalization through a regional approach to business. They argue that, for many United States TNCs, the Japanese-inspired model of globalization is both outdated and inappropriate. The basis of regionalization is described and there is a discussion of how regional strategies can be best approached by United States TNCs.

Divergent approaches to international business

International business fundamentally involves two different forms of activity: trade and foreign direct investment (FDI). At its most basic level, a company desiring to sell products abroad can either export from the home country or invest overseas and produce for international consumption. While most TNCs typically pursue some combination of both strategies, since the end of the Second World War United States TNCs have primarily relied on FDI as the preferred mode of penetrating international markets. That contrasts sharply with the experience of Japanese TNCs, which have largely pursued trade-based strategies in penetrating international markets. Those historical differences have fundamentally influenced the range of responses available to United States versus Japanese TNCs as they approach globalization.

The United States experience

As Western countries struggled to rebuild their economies after the Second World War, United States investment flowed into overseas markets. United States FDI was encouraged by a number of factors, including the Marshall Plan, the high value of the dollar and American culture, which readily accommodated the delegation of decision-making to overseas authorities. From 1950 to 1975, United States FDI in Europe increased by over 500 per cent to almost $125 billion. From 1975 to 1987, FDI increased another 350 per cent to almost $428 billion (United States Department of Commerce, 1989).[1] By 1987, United States TNCs employed more than 2

[1] Figures are for all of Europe.

million people in Europe and produced about 85 per cent of all goods and services sold by United States firms in the European Community (the remaining 15 per cent were generated from exports from the United States) (UNCTC, 1990). A similar pattern was also evident in Canada, which has become the largest host country to United States investment; by 1989, fully one quarter of Canada's largest 500 corporations were subsidiaries of United States parent corporations.[2] In 1989, Canada's manufacturing sector was almost 50 per cent foreign owned, with foreign ownership rising to 90 per cent in the automobile and rubber industries (UNCTC, 1990).

In Japan, levels of United States investment have remained low. In 1988, United States FDI in Japan totalled only $16.8 billion, reflecting various difficulties foreign TNCs have had in penetrating Japanese markets. In spite of low overall investment, however, United States TNCs have continued to favour stand-alone subsidiaries as opposed to exports. In 1988, for example, export sales amounted to only 18 per cent of total United States TNC sales to Japan; sales by United States subsidiaries in Japan produced the remaining 82 per cent of TNC sales (UNCTC, 1990a).

The Japanese experience

In contrast to the historical emphasis that United States companies have placed on FDI, Japanese TNCs have followed a much more trade-based path to internationalization. In 1989, Japanese FDI in Europe amounted to a mere $35 billion. Of Japanese sales in Europe, only 20 per cent came through local subsidiaries; fully 80 per cent of sales were generated through exports from Japan (UNCTC, 1990). In the United States, the historical pattern has remained the same: a low emphasis on FDI and a high emphasis on trade. Total Japanese FDI in the United States amounted to $53 billion in 1988, significantly lower as a percentage of GNP than investment levels of TNCs from Canada, the Netherlands, Switzerland, and the United Kingdom. In 1988, 88 per cent of Japanese goods purchased in the United States were imported; only 12 per cent were locally manufactured (UNCTC, 1990).

Culture and history have both played major roles in explaining Japan's emphasis on trade-based strategies. Following the Second World War, Japan's economy was in ruins and development was achieved by focusing on exports. To become successful internationally, the Japanese experienced

[2] According to the Financial Post 500, in 1989, 123 of Canada's largest firms were controlled by United States-based companies (block foreign ownership or wholly foreign owned).

decades of subordinating their own consumption needs to those of international customers. Trade flourished and Japan became the only country in the modern world to gain economic prosperity by copying the products and processes of other nations.

Trade-based strategies and globalization

The historical emphasis that Japanese TNCs have placed on trade development has facilitated the more recent move of many Japanese companies towards global strategies. Global strategies can be defined as the cross-subsidization of market-share battles in pursuit of world-wide production, branding and distribution advantages.[3] Under a global strategy, a world-wide perspective is maintained through tight central control and the coordination of activities across countries. High-value activities are typically located in the home country; the activities of overseas subsidiaries are rationalized with little input in decision-making coming from abroad. A global strategy is a specific type of international strategy; it should not be confused with other macro strategies for international markets, such as multidomestic or multifocal approaches to competition.

Japanese culture, which encourages homogeneity of thinking and promotes the centralization of decision-making, has done much to foster the globalization of Japanese TNCs. By promoting strong company cultures and by concentrating decision-making authority among a limited number of Japanese managers, Japanese TNCs have had a higher propensity to develop globally standardized approaches to international competition.

Matsushita provides a good example of the staged movement of a Japanese TNC from an export-based to a global strategy. During the 1960s, Matsushita pursued a low-cost strategy based on exporting standardized consumer electronics products around the world. As sales increased, economies of scale in R&D, purchasing, marketing and distribution led to further reductions in cost. Additional distribution, marketing and product development efficiencies were achieved as the company expanded into related industries such as television models, VCRs, audio equipment and office machinery. Throughout that period of growth, the company maintained a policy of locating all strategic decision-making and high-value-adding activities in Japan (Bartlett and Ghoshal, 1987). From 1983 to 1986, for example, all new products introduced in international markets by Matsushita were developed in

[3] For a more complete discussion of global strategy, see Hamel and Prahalad (1985) and Ghoshal (1982).

Japan. By maintaining primary decision-making at home, the company could more easily juggle international operations to take better advantage of changing supply and demand conditions. That tight central control relegated overseas subsidiaries to primarily downstream, low-value-adding activities where strategy implementation became a critical responsibility.

Advantages from globalization

From Matsushita's perspective, globalization represented a natural extension of its historical emphasis on exporting with several clear advantages:

- By centralizing operations at home, economies of scale can be gained in such activities as product development, production and marketing;
- Additional operational synergies can be achieved as related products are managed in the home country;
- Through tight, centralized decision-making, the integrity of a culturally dependent management system can be maintained;
- Flexibility in responding to changing world-wide demand and supply conditions can be maintained. Companies can quickly shift low-value-adding operations from country to country as host country costs change;
- With minimal foreign investment, a TNC has considerable bargaining power in dealing with countries seeking new investments.

United States TNCs: caught in the middle

In recognizing those advantages, managers of United States TNCs have often felt compelled to move in a similar manner to globalize operations. Encouraged by the success of Japanese TNCs, pundits and scholars have filled the public press and academic journals with articles calling for the wide-scale adoption of global strategies such as that pursued by Matsushita. By 1990, however, it was becoming increasingly clear that few United States companies had been successful at adopting global strategies (Morrison, 1990).[4] There are primarily two reasons for that failure: first, in spite of the predictions of standardized products for all markets, local

[4] In a study of 115 United States TNCs, Morrison found little evidence that American companies were pursuing global strategies.

demand conditions have persisted. In virtually every industry it has become evident that globalization has its limits; and second, and perhaps most importantly, many United States TNCs have run into major problems implementing a global strategy. Here, the historical legacy of FDI and culture have severely limited the ability of United States TNCs to respond as integrated organizations with common approaches to world markets.

For well over a decade, the prophets of globalization have been predicting that product demand would become standardized around the world. While demand for many products has become more homogeneous across countries, the trend towards globalization has been slowed by continued requirements for local product features, differences in technical standards and persistent tariff and non-tariff barriers to trade. While many globalization pressures are clearly at play, they are far from unified in the vast majority of industries.

The international television industry provides a clear example of the limits of globalization. The international industry remains dominated by three world-wide broadcast standards: one for Europe, one for North America and one for Asia and the Pacific and Japan. The emergence of high-definition television has encouraged efforts towards homogenizing those standards, but political pressures have put those efforts on hold. Beyond broad regional standards, intraregional differences continue unabated. Within the European Community, for example, technical standards differ across some or all member countries in seven different areas of television design. Many observers anticipate that the onset of Europe 1992 will have only a modest impact on those standards. Beyond standards, European Community duties on imported televisions—currently set at approximately 10 per cent—will stay in place after 1992, thus discouraging efforts to globalize production. Similar barriers are in place in North America, Japan and many newly industrialized countries.

Beyond those external hurdles, organizational realities have severely impaired the ability of United States TNCs to pursue global strategies. The integration of far-flung operations through tight central control has been difficult to achieve given historical patterns of subsidiary emphasis on unique products, processes, services and labour practices. After years of relative independence, many subsidiaries have developed cultures, systems and structures that are incompatible with those of the parent. Not surprisingly, integration has often been bitterly opposed by foreign subsidiaries eager to protect historical relationships. From the subsidiary's perspective, a globalization strategy directed from the United States head office is a frightening proposition. Many subsidiary managers are concerned that parent companies, historically preoccupied with United States market issues, lack the understanding and sophistication effectively to integrate operations internationally.

This study found virtual unanimity among subsidiary managers that the head office misunderstands the potential contributions of subsidiaries and should generally not be trusted to manage globalization effectively. According to one subsidiary general manager in Germany, a man with over 25 years experience working overseas, "there are no parents that I have ever seen that know what they are doing internationally". A subsidiary manager in Canada stated, "If we don't take the initiatives, we'll be dead in the water. The United States operation will push the wrong projects onto us." A subsidiary manager in France stated:

> "Headquarters has shown a considerable degree of naivety in proceeding [with globalization]. They overestimated the similarities in material markets and tried, at least in the early stages, to act very quickly. If it weren't for the concerted efforts of the major subsidiaries acting together to convince the head office to proceed more cautiously, we aren't sure where it would have ended."

And finally, the head of strategic planning of a large United States subsidiary in Japan stated: "Head-office people often make arbitrary decisions without the input of experts in the subsidiary. American management style is very top down in orientation and can be troubling for Japanese employees."

Beyond the sense that the head office may be unprepared for the subtleties of directly managing operations overseas, subsidiary managers are also apprehensive about globalization, because it necessitates a significant reduction in their autonomy. Globalization requires tight control over subsidiaries in order to rationalize facilities, coordinate production and standardize marketing. This is best managed by a strong headquarters and functionally oriented subsidiaries. In many subsidiaries, autonomy is something that has been fought for and defended for years. It has also been encouraged by Governments of host countries which recognize that autonomous subsidiaries are more prone to respond to the needs of local consumers. Globalization threatens all of that. By moving too rapidly towards globalization, the parent risks alienating and ultimately losing much of the management talent that served to distinguish effective subsidiaries in the first place. The parent company also risks losing support from Governments of host countries, worried that globalization signifies minimal commitment to local market needs.[5]

United States companies that have been effective in establishing globally integrated operations have generally begun the process with a clean slate. Even so, results have been mixed. Consider Dow's experience with globalization. The Michigan-based company's efforts to globalize operations began in the mid-1960s, when virtually all its sales and production were located in the United States. In order to both encourage and facilitate globalization, the company began a series of reorganizations that led to the formation of a three-dimensional matrix with geographic, functional and global-product dimensions. The results in terms of international growth have been phenomenal. By 1989, almost 55 per cent of Dow's sales and profits were being generated outside the United States; the company had established 180 manufacturing sites in 30 countries around the world; and resource allocations and strategies were tightly coordinated among domestic and international operations.[6]

But such efforts have had their costs and may be inappropriate for TNCs that start the globalization process with extensive overseas subsidiaries in place. According to the CEO of one of Dow's largest overseas subsidiaries, "It has clearly been a difficult company to manage" and "the matrix wouldn't work if we were to start the company today". For outsiders, the structure and related systems have proved extremely difficult to figure out. It is not uncommon for new employees to take three or more years to become comfortable with work roles, evaluation systems and reporting relationships. As a result, it is often difficult to bring new people into the company. The need for fine-tuning appears continuous. To improve responsiveness, the company is currently exploring the option of adding a fourth dimension based on specific industry segments. According to one senior executive, a move to expand the matrix "may take 10 years to figure out".

For Dow, the road to globalization has not been easy. In spite of the obstacles, however, the journey for Dow was made easier by its ability to begin the process with a clean slate. Like the Japanese, Dow had a free hand in organizing operations to maximize flexibility and encourage integration across national borders. For many United States TNCs, such flexibility may

[5] For a more complete discussion of Government policies and subsidiary bargaining power under globalization, see Doz (1986).

[6] From an address by H. Mohlmann, Vice President for Chemicals and Metals, Dow's Corporate Product Department. See Mohlmann (1990).

be unattainable because strategies of the past have saddled the company with large, self-sufficient national subsidiaries. For those companies, globalization may mean walking away from resources, skills and relationships that have taken decades to develop.

The regional solution

In finding a balance between the need for greater integration and the need more effectively to exploit existing resources, United States companies have begun to explore the use of regional strategies in Europe, North America and the Pacific Rim. Regional strategies can be defined as the cross-subsidization of market-share battles in pursuit of regional production, branding and distribution advantages. A TNC with a regional strategy locates strategic decision-making within the region; market-share battles are designed, waged and monitored within the region, and company operations are geared to regional-scale requirements. Like a global strategy, a regional strategy is a specific type of international strategy that is appropriate for certain competitors.

A regional strategy offers many of the efficiency advantages of globalization while more effectively responding to the organizational barriers it entails. Regionalization also presents United States TNCs with a unique opportunity to exploit established subsidiary strengths.

- In Europe, American Cyanamid is currently undertaking a major reassessment of its country-by-country strategy. It has manufacturing facilities in six European countries: Belgium, France, Germany, Italy, Spain and the United Kingdom. The company is currently struggling to rationalize operations on a pan-European basis. Given the historical emphasis on country self-sufficiency, restructuring will bring many changes to each subsidiary's operations. In Germany, for example, the company employs about 800 people in a large, modern office complex and state-of-the-art manufacturing facility. The subsidiary currently handles German sales of pesticides, pharmaceuticals, specialty chemicals and veterinary products. A move to regional rationalization would force the subsidiary to focus on a much narrower range of products, turning over the remainder to sister subsidiaries in other European countries.
- Motorola Inc. responded to the need for a greater regional emphasis in its communications equipment operations when it acquired Mobile

Data International (MDI) of British Columbia through its Canadian subsidiary. At the time of the acquisition, MDI was a manufacturer of mobile data communications equipment and was the largest player in the United States industry, with 39 per cent market share. MDI was a primary supplier to Federal Express, the second largest purchaser of mobile data terminals in the world. Before the acquisition, the company's largest competitor in the United States was Motorola Inc. The decision to acquire MDI was made jointly by the head office and Canadian management and provided Motorola with almost 70 per cent of the United States market. Since the acquisition, Motorola Inc. has progressively transferred control over United States mobile data activities to MDI. All top MDI managers are Canadians and MDI has been set up as a fully autonomous affiliate of Motorola Canada. In spite of those connections, only about 15 per cent of MDI sales are Canadian-based. Furthermore, while MDI maintains control over R&D, production and sales from its Canadian offices, all production is based in Puerto Rico and close linkages have been established with the communications sectoral head office in the United States. In fact, none of the products of MDI is currently being produced in Canada.

From the perspective of a TNC, a regional strategy may represent an ideal solution to the competing pressures for organizational responsiveness and global integration.

- **Regional-scale manufacturing facilities represent the limit of potential economies of scale.** In the United Kingdom, for example, Toshiba's production facilities for televisions and microwave ovens are designed for European market requirements. According to a senior subsidiary manager: "Economies of scale begin to fade out at some level and this is dealt with best through a regional-sized plant. As size increases, our experience has been that control drops. Communication and motivation become real problems when a plant is too large."

  Similarly, European-size plants have been established by Sony, Hitachi, Philips and Thompson.

- **Regionalization allows for faster delivery, greater customization and smaller inventories than would be possible under globalization.** Thompson Consumer Electronics, for example, has regionalized operations in both Europe and North America. In Europe, the company has established four separate divisions to manage the R&D and production for television. Its German subsidiary, Electronic Werke Deutschland, focuses on high-end, leading-edge, large-screen TVs. The French subsidiary, Seipel, focuses on high-volume and large-screen television sets. The Spanish subsidiary, Cedosa, and the United Kingdom subsidiary, Ferguson, both focus on low-cost, smaller sets. By producing a limited range of televisions, each subsidiary is able to respond more quickly to customer needs, shorten lead time to consumers, cut shipping costs and minimize inventories compared to producers at world-scale plants in Pacific Rim countries.

- **Regionalization accommodates organizational concerns and exploits subsidiary strengths.** As General Electric moves to regionalize its major appliance operations in North America, the role of the Canadian subsidiary, Camco, is being significantly altered. Until the mid-1980s, Camco manufactured and marketed an entire line of major appliances for the Canadian market. With the reduction of tariff barriers between Canada and the United States and the sizeable scale economies possible in manufacturing major appliances, the Canadian subsidiary's operations appeared to be a prime candidate for rationalization. In determining what role the subsidiary should play, it became apparent that Camco had specialized skills in products uniquely emphasized in Canada. Canadians, for example, are more fashion-conscious about kitchen appliances, and portable dishwashers and chest-type freezers are bigger sellers in Canada than in the United States. Those differences have encouraged Camco to develop unique production and design competencies that, in turn, influence General Electric as it determines how it will proceed on regionalization. For the subsidiary, it means the possibility of positioning itself as the "natural leader" in certain products—an important consideration if the company wants to retain and development top subsidiary managers.

The emergence of distinct regional pressures

Regional strategies in Europe and North America have also been encouraged by the economic, political and social pressures associated with the development of regional trading blocks. In North America, the Canada-United States Free Trade Agreement has already had a far-reaching impact on the integration of business across borders. In 1990, for example, almost

70 per cent of Canada-United States trade was intra-firm. Ongoing negotiations with Mexico have further promoted a regional approach to business. In Europe, 1992 is looming as a pivotal year in the elimination of trade barriers. The effects of Europe 1992 on indigenous businesses were expected to mirror those changes brought about by the Canada-United States Free Trade Agreement, including increased industry concentration, a greater number of cross-border and national mergers and alliances, and escalation in the movement to rationalize production facilities within the region.[7]

A major reason why Governments have moved to formalize regional trade has been the perceived need to discipline existing businesses without exposing them to the unfettered pressures of global competition (Stone, 1989; Crookell, 1990). To the degree that competition is moving towards regionalization, companies with strong overseas subsidiaries will have a competitive advantage over companies that have relied on exporting into the region. Here, Japan is at its weakest, particularly in North America and Europe.

The Japanese at a disadvantage

Japanese TNCs, recognizing that they are exposed geographically, have been trying to play catch-up in North American and European markets through massive new investments. By the mid-1980s, the United States had surpassed Western Europe as the world's number one recipient of FDI. Much of those flows came from Japanese companies that saw their stock of FDI in the United States grow by 40 per cent per year during the late 1980s. In Europe as well, Japanese investment climbed significantly during the second half of the 1980s. Nissan, for example, has now located all of its design, engineering and manufacturing operations in Europe and plans to begin exporting cars back to Japan. Sony has established eight manufacturing plants and two R&D facilities in six countries in Europe. Toshiba now manufactures 80 television models in the United Kingdom for the European market using components—from printed circuit boards to cabinets—manufactured in-house. Those investments suggest at least a partial abandonment of globalization by Japanese TNCs.

Despite those more public examples, however, Japanese TNCs have a long way to go before they become true insiders in Europe and North America. In 1989, for example, Japanese FDI in the European Community amounted to only $35 billion, of which three quarters was in the service sec-

[7] The impact of regional trading blocks on TNC strategy is more fully discussed in Morrison, Ricks and Roth (1991).

tor; of that amount, a full two thirds was in banking. Japanese investment in technology industries in 1988 totalled a mere $2.2 billion. In the United States, while Japanese investment has soared, in 1988 it still represented only about 16 per cent of all FDI in the country. To put this in context, in 1987, foreign firms accounted for only about 7 per cent of the total employment in the United States, suggesting that Japanese subsidiaries in the United States employed well under 1 per cent of the population (UNCTC, 1990a).

In addition to their modest presence in North America and Europe, Japanese TNCs have also been severely limited because of their emphasis on tight control from Tokyo. Tight control often leads to unresponsive local management and slow decision-making. In North America, for example, NEC recently retreated from the engineering workstation market because decision makers in Tokyo could not keep up with the rapid technological improvements made by Sun Microsystems, DEC and Hewlett-Packard (McWilliams, 1990). Subsidiaries also complain that, even if decision-making is "localized", subsidiary managers are typically Japanese, effectively minimizing input from local managers. Even expatriate Japanese managers frequently serve as "shadow executives" making few key decisions. In this position, the ability of Japanese TNCs to respond to growing regional pressures will be severely hampered.

Japanese TNCs are also vulnerable in their home region. Beginning in the early 1970s, Japanese TNCs began establishing subsidiaries throughout the Pacific Rim in an effort to globalize operations from a regional base. Many Japanese TNCs were pushed into the region by a combination of factors, including high labour costs, a soaring yen and punishing corporate taxes—up to 70 per cent in some instances. The dominant strategy was to use the Asian region as a centre for labour-intensive, low-value-added activities; almost 70 per cent of export sales from Japanese Asian subsidiaries ended up back in Japan for further work before being re-exported to North America or Europe. Although Japanese companies have clearly benefited from cheap Asian labour, Japan's future role in the region remains uncertain. By the late 1980s, for example, Japan was the dominant investor in only two Pacific Rim countries: the Republic of Korea and Indonesia. In terms of investment flows, Japan was the dominant investor in only three Asian countries: Indonesia, the Republic of Korea and Thailand (UNCTC, 1991).

Japan is held back in its home region because countries in the Pacific Rim remain distinct in terms of product demand, government regulation, cost structure and so on. In industries such as automobiles, consumer electronics and home appliances, demand patterns in many Pacific Rim countries lag years behind those in Japan. Although demand has grown rapidly in recent years, features and services demanded by affluent Japanese are still beyond the reach of most consumers in other Pacific Rim nations. As a result, the Pacific Rim remains ideally suited as a global platform, but underdeveloped as an integrated regional market. With regionalization taking off in North America and Europe, Japanese TNCs risk being left with an investment platform in the Pacific Rim that is rapidly losing its relevance.

Strategic implications

In most instances, regionalization serves the interests of United States TNCs over those of Japanese TNCs. How does a United States company best exploit the advantage? The authors recommend the following:

- **Constantly test for changes in the competitive environment.** Many companies have a tendency to drift. Policies developed years ago are often infrequently re-evaluated and assumptions rarely tested. Nowhere is this more dangerous than when a company's transnational operations expose it to diverse and often conflicting environmental pressures.

  To be responsive, strategic thinking must permeate the entire organization. When subsidiary managers are involved in overall strategy formulation of TNCs, they are in a much better position to interpret relevant changes in the environment. Subsidiaries should be at the front line in testing strategies through constant customer interactions, continual reassessments of competitive positioning and regular evaluations of government policies.

- **Develop a clear understanding of subsidiary strengths.** Many of the head-office managers who participated in the study had only a superficial understanding of the strengths and weaknesses of overseas subsidiaries. Information was typically garnered from quarterly reports and periodic field visits. Relatively few head-office managers had a good understanding of the subsidiary's competitiveness on a product-by-product basis. Parent companies often assumed that subsidiaries were uncompetitive internationally when, in many cases, they were more competitive than the parent company at home. For example, subsidiaries often have unique design or manufacturing skills related to their experience with low-volume products. Smaller subsidiaries are often uniquely qualified to produce speciality, high-value-added products for narrow regional niches.

- **Prepare the organization for strategic change.** It was found in the course of the study that parent companies that unilaterally move to integrate previously autonomous subsidiaries can expect major implementation problems. If not properly managed, opposition can get out of hand, with subsidiaries undertaking improper initiatives that bind the parent firm's hands for years to come. By preparing the organization for change, much of that opposition can be more easily assessed and controlled. Parke-Davis in Europe, for example, began working with subsidiaries three years in advance of a move to a regional strategy. Subsidiary managers in Belgium, France, Germany, Ireland, Italy, Spain and the United Kingdom were all involved in the planning that went into regionalization, even though it was appreciated early on that rationalization would force the closure of more than half of the manufacturing facilities in operation. Their involvement assured not only that better decisions were made, but that each of the subsidiaries was on board when the changes began.

- **Prepare to shift autonomy to regional managers in Europe and North America.** It was found that companies that can articulate a clear and consistent vision of how to they are going to compete had the best chance of outperforming competitors. In doing so, it was found, companies were beginning to converge on two approaches to regionalization. The first approach involved rationalizing operations vertically. Under that approach, subsidiaries focused on a limited number of vertically integrated activities for the benefit of the region as a whole. Subsidiary A may focus on design, subsidiary B on component manufacture, subsidiary C on sub-assembly and so on. The second approach involved specialization, whereby subsidiaries were given a mandate to focus on a limited range of products. With a mandate, the subsidiary controls all aspects of production, sales and distribution of the product within the region. Specialization is often preferred by subsidiaries, because it also gives them greater autonomy and control of operations.

In determining which approach to pursue, parent companies should encourage subsidiaries to become actively engaged in the process. Subsidiaries can and often do influence the outcome of decision-making by initiatives they undertake. It was found in the course of the study that specialization was primarily a function of how competent the subsidiary was in terms of managerial depth and its track record in product and process R&D. Initiatives designed to build those core competencies seemed to have the greatest impact of the roles subsidiaries play within regions.

- **Manage the organization effectively.** In organizing for regional effectiveness, our research found that a rationalization strategy required the establishment of a strong regional organization. This typically involved a regional headquarters staff with full control over strategic decision-making and subsidiaries acting primarily as cost centres. Under that approach, corporate headquarters in the United States should focus primarily on assisting each region in interregional relations. In contrast to this tight regional control, it was found that a specialization strategy was best implemented through the establishment of a more modest regional "coordination office". That option involves limited staff support, with contact between subsidiaries maintained by fax, telephone and frequent one-day meetings. The role of corporate headquarters is broadened to include supervision of regional planning, budget approval and performance evaluation.

- **Approach Japan as a special case.** For most United States TNCs, setting up in Japan provides few advantages from a regional perspective. Rather, Japan makes sense because it is a huge market in its own right and because it provides access to front-line technologies critical for success in other regions. In disposable diapers, for example, Japan's Uni-Charm Corp. first introduced super-thin technology in 1982. Procter & Gamble, which had extensive diaper operations in Japan, picked up the technology in 1985 and transferred it to North America, where the company got a jump on Kimberly-Clark, which had not been a major player in Japan.

  Many companies are finding that establishing an R&D presence helps considerably in accessing new Japanese technologies and in responding to the needs of key Japanese exporters. Pfizer, for example, has undertaken a major shift in strategy to establish a regional centre of excellence in Japan. Pfizer has typically encouraged subsidiaries to make only modest changes in product dosages, while focusing instead on country-specific packaging requirements and local marketing and distribution activities. Virtually all discovery work has traditionally been carried out in the United States.

Beginning in 1984, however, Pfizer made a decision to expand its presence in Japan. Management felt that it needed to establish better ties with local Japanese pharmaceutical houses which were undertaking major R&D efforts at the time. Initially, however, head office-management was not sure if the subsidiary could effectively manage an R&D facility so far from home and with essentially no track record. At first, a lab was set up with only a few technicians. For five years the subsidiary worked to convince the parent company that it could manage discovery work. Finally, in 1989, the parent company was won over and a decision was made to proceed over the next five years to build up the facility to 400 people. Japanese R&D now focuses on anti-inflammatory preparations and has become a major centre of R&D excellence in the company. Most customers now perceive the subsidiary as a Japanese company. With the stronger presence in Japan, major efforts are now being undertaken to harmonize pre-clinical testing in Asia and the Pacific region. The subsidiary is also increasingly serving as a management training centre for the region.

Conclusions

Faced with the task of managing global operations, many United States TNCs are reigning in foreign subsidiaries and centralizing decision-making. The research indicates that regionalization may be a better approach to improving competitiveness, particularly for companies that have historically emphasized stand-alone subsidiaries. Regionalization provides many of the scope and scale advantages of globalization, while permitting the organization to exploit existing competencies. For TNC parent companies, however, regionalization requires a considerable leap of faith because control over decision-making shifts away from head-office to regional managers.

Regionalization also has important implications for government policy. Although the Japanese are moving quickly to narrow the gap in FDI, financial scandals and changing tax laws at home may lead to a reduction in the rate of Japanese growth in FDI during the early 1990s. North American and European Governments will have to assess whether this period should be used to tighten investment laws to restrict further Japanese access to regional markets. If production efficiencies are maximized regionally, Japanese firms would be placed at a competitive disadvantage outside the Pacific Rim if North American and European Governments were to restrict Japanese FDI.

Within regions, a general tendency exists, particularly among United States TNCs, to become preoccupied with what is happening at home. Language skills and levels of overall awareness of world conditions are typically lower in the United States than in Europe and Japan (IMEDE and World Economic Forum, 1989).[8] Clearly, education requires priority attention. To be effective in the 1990s, managers will require a heightened degree of sophistication and sensitivity. In spite of those requirements, United States TNCs have a distinct advantage over many Japanese companies. The successful companies of the future may well be those that best exploit existing advantages rather than those that struggle to imitate a far-away competitor. ■

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[8] One recent assessment (IMEDE and World Economic Forum, 1989) of corporate preparedness for Europe 1992 ranked United States managers at 38 out of a possible maximum score of 100. European managers, not surprisingly, fared significantly better.

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