

Why Do Regional Headquarters Live and Die?

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Introduction

Across the globe, multinational companies' headquarters employ thousands, if not millions, of managers, who have a constant pressure to manage better their complex and ever-changing organizations. For many years I was one of those managers, contemplating the same issues. That in-depth experience provides a background for my dissertation, which investigates regional headquarters (RHQ) and their dynamism in the context of the organizational structures of multinational companies (MNCs).

MNCs face the dual challenge of managing their operations in a globalizing world and answering a simultaneous need for local responsiveness (Prahalad & Doz, 1987). MNCs often respond to these challenges by adopting increasingly complex organizations (Ghoshal & Westney, 1993). *Regional* organization structure is a model where a layer of regions is introduced between the corporate headquarters and the country subsidiaries (Heenan & Perlmutter, 1979).

Regional structures have received increasing attention recently (Rugman & Verbeke, 2004, Piekkari et al., 2010), and the first of my four essays uncovers what we currently know of the RHQ phenomenon and what remains unknown. Using systematic literature review, covering a period from 1967 to 2014, the analysis served as a foundation to develop a framework for an enhanced understanding of the RHQ phenomenon. The prior research on RHQ has focused predominantly on the roles that RHQ perform and the location selection and relocation of RHQ. This dissertation focuses on the largely uncharted area of RHQ dynamism, i.e., how and why RHQ changes and evolves over time. Such changes can relate to the role, location, or geographic scope of RHQ, but more fundamentally, dynamism also includes the birth and death of RHQs (Lasserre, 1996). The focus is on the factors and processes that affect the evolution of RHQ within the MNC organizational structure. Following from the discussion above, in my dissertation I address a simple, yet fundamental research question: *Why do regional headquarters live and die?*

The Real Survival Game of Regional Headquarters: Add Value or Die

Regional headquarters will continue to live only if it adds value to its parent, to its subsidiaries or to both. RHQ will survive if it provides a cost effective alternative in comparison to other structural options available in the MNC. Furthermore, RHQ seem to be flexible structures that are able to adapt to different needs in the multinational organization, thus increasing their chances of survival.

How do RHQ may then lose its mandate over time? My longitudinal study shows that while RHQ may evolve through a life cycle, it is most likely to lose its mandate due to a disruptive change in the MNC or due to external developments. These reasons account for two thirds of the mandate losses in the data, while natural death remains in a clear minority. Such natural death is

most often caused by the parent losing its trust on the RHQ or by the simple fact that it is no longer adding enough value to cover its cost.

The empirical analysis in my three empirical essays is based on a unique, longitudinal data set of RHQ in Finland. The first round of data collection was made in 1998-99, when 375 RHQ were identified. In 2010 our research team followed them up, and with an excellent response rate, we were able to track 97 % of these firms. As a number of the subsidiaries were no longer there due to ownership changes, ended operations, or other reasons, we interviewed 224 subsidiaries, of which 131 still were RHQ and 93 had lost that status over the 12 year period. In the third phase, we interviewed and examined nine RHQ more thoroughly in order to capture especially revealing stories of their evolution.

The second of the four essays in my dissertation, is a multiple case analysis which explains when RHQ adds value to MNC management. This essay applies parenting theory (Campbell et al. 1995) in building the notion of added value and in constructing a process framework. The process outputs are characterized in terms of delivered parenting value, perceived parenting value, and required parenting value, hence including the effect of MNC management's perception in the model. The evolution of parenting values typically follows one of four evolutionary patterns, which then may lead to mandate retention or to either abrupt or gradual mandate loss.

The third essay presents a quantitative study on what explains the survival or demise of a RHQ within an MNC. This essay draws on agency theory (Jensen and Meckling 1976) to consider RHQ units as involved in principal-agent relationships with both CHQ (as agents) and subsidiaries (as principals). The study reveals that in order to sustain its mandate over longer periods of time, the RHQ must enjoy trust from its parent (CHQ) and have a short geographic, cultural, administrative, and economic distance to the units within its geographic scope. Intermediate HQ will survive if the combined agency costs of the relationships between the CHQ and the intermediate HQ and the intermediate HQ and the subunits are lower than the agency costs that would have been incurred had the CHQ controlled the subsidiaries directly.

Finally, the fourth essay takes another perspective looking at an entire population of RHQ embedded in three environments, namely host and home country and MNC environments. The ecological analysis shows that the processes of variation, selection, and retention played a pivotal role in the evolution of the RHQ population from its inception to ultimate decline. Since RHQ are facing forces from three different environments, they are therefore especially prone to change.

Contributions

A key theoretical contribution of my dissertation is to integrate previous research into an analytical framework and offer an overarching definition of RHQ, based on both theoretical and empirical findings.

The new definition of RHQ positions it as “an intermediate organizational unit with a mandated role, geographic scope, and location, which is triple-embedded, terminable, and sensitive to change.” This trichotomic construct (see Figure 1) interlinks the key attributes of RHQ in a novel way and also takes into account the geographic scope, which has previously been ignored despite its high practical relevance (Ambos & Schlegelmilch, 2010). Furthermore, this novel definition grasps much of the dynamism of RHQ, through the identification of the four characteristic attributes of RHQ, namely intermediacy, terminability, triple-embeddedness, and sensitivity to change, which together distinguish RHQ from other types of organizational units and provide its unique features.

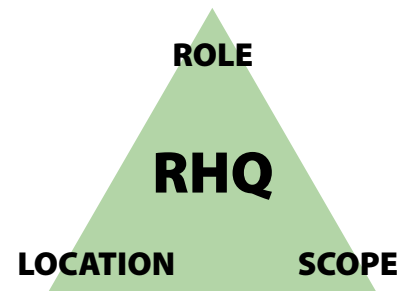
Another key contribution is the longitudinal field study which covers a complete set of RHQ in a given country, Finland. This unique dataset is one of the largest ever collected in the context of RHQ and the only large dataset with longitudinal data. Research on RHQ is short on quantitative studies and this dissertation provides an important addition to the field in that respect.

The dissertation also contributes by suggesting a future research agenda drawn from the systematic literature review and the empirical studies. The future research could take better benefit of the special characteristics of RHQ in order to generate theories from the headquarters dynamism. Moreover, such topics as geographic scope of RHQ, inherent dynamism of intermediate headquarters, and the role of people in headquarters merit more attention. This would support us in meeting two key goals, namely generating more relevant organizational theories with the help of the unique phenomenon of complex MNC organizations, and providing more relevant knowledge for the MNC managers with their daily management challenges.

Having been one of those MNC managers myself, I see my research having important implications also for the business practice. Following my framework, such implications could be seen from the eyes of a CHQ manager, a RHQ manager, and a subsidiary manager. For example, a CHQ manager could apply my framework to create an organizational design that best fits the firm’s needs, taking benefit of the capabilities they have in various locations and matching those with the roles given to each headquarters unit and assigning them a suitable geographic mandate. For a RHQ manager, my findings would highlight the importance of trust in the relationships with both the CHQ managers and the subsidiary managers. The more trust the RHQ manager can build in these relationships, the more likely her RHQ will be to survive in the long run. Subsidiary managers, on the other hand, could get a better understanding of the role and the processes RHQ apply to add value to the subsidiary operation.

Finally, my research makes contributions also towards policy makers. In fact, much of previous literature on RHQ location characteristics is due to the policy makers’ needs to attract headquarters into their cities and countries. MNCs govern a significant amount of economic activity in today’s world and hosting RHQs within its national borders will help any government to benefit from this economic activity. With the increased complexity of MNC organizations and introduction of RHQ mandates and sub-RHQ, practically any country can host a RHQ as long as the location-specific characteristics meet the firm-specific needs. Therefore, any government should ask themselves, what they can do to attract more such headquarters.

Figure 1. Conceptualization of RHQ



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Perttu Kähäri has 20 years of managerial experience in multinational companies. He has held roles at corporate headquarters, regional headquarters and country subsidiary management. Having defended in October 2014, his work has been nominated for various international and national awards and has attracted exceptional media attention in Finland. While currently pursuing a business venture, Kähäri remains affiliated with Aalto University School of Business. His research focuses on MNC organizational design, headquarters and international entrepreneurship.